

RISK RETENTION GROUP (E) TASK FORCE

Risk Retention Group (E) Task Force Sept. 21, 2009 Minutes

New or Revised Models Impacting the Part A Accreditation Standards (Attachment One)

Letter from Peter Raymond (VT) to Julie Glaszczak (NAIC) regarding Comments on Part A Accreditation Standards, dated Sept. 10, 2009 (Attachment Two)

Risk Retention Group (E) Task Force Sept. 3, 2009 Minutes (Attachment Three)

Memorandum from Julie Glaszczak (NAIC) to Risk Retention Group (E) Task Force dated June 13, 2009, regarding Part B Accreditation Standards Summary Memo (Attachment Three-A)

Memorandum from Julie Glaszczak to Risk Retention Group (E) Task Force dated June 13, 2009, regarding Part C Accreditation Standards Summary Memo (Attachment Three-B)

Letter from Michael Bemis (Vermont Captive Insurance Association) to Members of the Risk Retention Group (E) Task Force dated July 6, 2009, regarding Comments on Part B: Regulatory Practices and Procedures and Part C: Organizational and Personnel Practices Accreditation Standards (Attachment Three-C)

Memorandum from Julie Glaszczak (NAIC) to Risk Retention Group (E) Task Force Members dated Aug. 21, 2009, regarding Recent Changes to Part A Accreditation Standards (Attachment Three-D)

Risk Retention Group (E) Task Force
Washington, DC
September 21, 2009

The Risk Retention Group (E) Task Force met in Washington, DC, Sept. 21, 2009. The following Task Force members participated: Scott H. Richardson, Chair, represented by Leslie Jones (SC); Christina Urias (AZ); Steve Poizner represented by Jill Jacobi and Louis Quan (CA); Gennet Purcell represented by Sean O'Donnell and Dana Sheppard (DC); J.P. Schmidt represented by Paul Yuen (HI); Glenn Wilson represented by Jaki Gardner (MN); Scott J. Kipper represented by Brett Barratt (NV); James J. Wrynn represented by Larry Levine (NY); Kim Holland represented by Michael Ridgeway (OK); Joel Ario represented by David DelBiondo (PA); Kent Michie represented by Ross Elliott and Neal Gooch (UT); and Paulette Thabault represented by Peter Raymond (VT).

1. Receive Update on Work of Other NAIC Groups Related to Captives

Julie Glaszczak (NAIC) provided an update regarding the ongoing work of other NAIC bodies on risk retention groups (RRGs). A subgroup of the Financial Examiners Handbook Technical Group was developed to draft additional examination guidance for RRGs. This subgroup is specifically looking at how the new risk-focused approach might apply to exams of RRGs. The subgroup is also determining whether any additional exam procedures should be included in the *Financial Condition Examiners Handbook* to address RRG-specific issues (e.g., deferred acquisition costs). The subgroup has directed NAIC staff to draft information on various RRG examination items.

Based on a referral from this Task Force, the Capital Adequacy Task Force developed a sensitivity tool, which is not part of the initial RBC calculation. This tool, which would be used as an analysis tool only, could be utilized by regulators to "statutorize" certain generally accepted accounting principles items that are specific to RRGs. Because this would be an analysis tool only, no action could be taken by the domiciliary regulator based on it. The Financial Analysis Handbook Working Group made revisions to the captive guidance in the *Financial Analysis Handbooks* (Handbooks) to indicate that the tool may be used for analysis purposes. The changes to the Handbooks indicate that the sensitivity test is just an analysis tool. Because these changes are nominal, they are expected to appear in the next printing of the Handbooks.

The Property and Casualty Insurance (C) Committee adopted corporate governance standards for RRGs as best practices. The Committee has developed a subgroup to address how the standards could be implemented by the states and required of RRGs. However, there has been no strong desire by the states to participate on that subgroup. Ms. Jones said many of the Task Force members initially expressed interest in being on that subgroup. As such, the following jurisdictions volunteered to participate: Arizona, California, District of Columbia, Nevada, South Carolina, Utah and Vermont.

2. Adopt Minutes from Interim Conference Call

Director Urias moved and Mr. Quan seconded a motion to adopt the minutes from the Task Force's Sept. 3 conference call (Attachment Three). The motion carried unanimously.

3. Discuss New or Revised Models Impacting the Part A Accreditation Standards

Ms. Jones said the Task Force had previously discussed some of the models impacting the Part A accreditation standards that had been revised since the Task Force's initial Part A deliberations. She said Ms. Glaszczak had developed a matrix (Attachment One) that compared the sections impacted by the 2006 revisions to the Annual Financial Reporting Model Regulation (#205) regarding audit committees to the corporate governance best practices standards. Ms. Glaszczak provided a summary of the information in this document. Ms. Jacobi asked if any states are currently enforcing the corporate governance standards. Ms. Jones said there were none.

Ms. Jacobi asked if there are any RRGs that currently report more than \$300 million in direct written and assumed (D&A) premium. Ms. Glaszczak responded that NAIC staff had verified that there are currently no RRGs with at least \$500 million in D&A premium, although NAIC staff did not check to see if any RRGs have D&A premium between \$300 million and \$500 million. This information will be provided prior to the Winter National Meeting.

Ms. Jones asked if this matrix covered all of the conflicts between the items in model #205 and the corporate governance standards. Mr. Raymond responded in the affirmative. Ms. Glaszczak said NAIC staff would provide suggestions as to

whether the key sections in model #205 should apply and what related revisions would then be needed to the corporate governance standards.

4. Discuss Previously Adopted Part A Matrix

Ms. Jones said some implementation questions had been raised by Mr. Raymond regarding the Part A standards the Task Force has already adopted (Attachment Two). Mr. Raymond briefly discussed his comment regarding RBC. Ms. Glaszczak said that RRGs are not required to file RBC for accreditation purposes; however, domestic regulators may require RRGs chartered in their state to file RBC. Ms. Jones said the Task Force had previously agreed that some method for assessing an RRG's capital and surplus was necessary, which was the reason for the initial referral to the Capital Adequacy Task Force.

Skip Myers (National Risk Retention Association) said a domestic regulator is free to use RBC as an analytical tool if it wants. He asked if the Task Force was now considering imposing something different. Ms. Jones responded in the negative and said an RRG's RBC filing could be utilized by the regulator for analysis purposes only; however, no action would be taken by a state.

Mr. Sheppard asked if Ms. Glaszczak could explain how an accreditation team reviews a state's analysis of a company's RBC filing. Ms. Glaszczak responded that if the RBC calculation falls below a certain percentage, a review team will only make a determination as to whether it felt the state took appropriate action regarding that situation.

Mr. Raymond said he was comfortable that Vermont can assess the adequacy of an RRG's capital and surplus position utilizing a variety of other NAIC tools without the RRG needing to file RBC.

Ms. Jones suggested that this issue be tabled for further discussion on an upcoming interim conference call, and there was no objection from the Task Force.

Having no further business, the Risk Retention Group (E) Task Force adjourned.

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Regarding Audit Committees:

Acronyms:

AC	Audit Committee
BOD	Board of Directors
CPA	Certified Public Accountant
Corp Gov	NAIC Governance Standards for Risk Retention Groups
MAR	Annual Financial Reporting Model Regulation (#205), often referred to as the Model Audit Rule
RRG	Risk Retention Group

MAR Section	Requirement of MAR	Related Info in Corp Governance?	Conflict between MAR and Corp Gov?
4D	Every insurer shall designate an AC (can be full BOD). Hardship waiver included in Section 14J.	Yes. Section 4 indicates that the RRG shall have an AC. Hardship waiver included in Section 4B.	No
7J	All auditing and non-audit services shall be preapproved by AC. Preapproval of non-audit services may be waived in certain circumstances.	Section 3D indicates that the BOD is required to review and approve all amounts paid to <u>material service providers</u> . Section 3Eiii indicates that the BOD will review and approve, at least annually, the continued engagement of material service providers. Note: It is being assumed that the approval will happen prior to the work begins (thereby being pre-approval).	1) MAR is slightly stronger because requires pre-approval of all audit services (not just material ones). MAR does allow waiver on some non-audit services. If complied with MAR, they would be complying with Corp Gov. 2) Conflict between if BOD or AC approves payments. 3) Waiver requirements for non-audit services in MAR may not be allowed in Corp Gov. if it is a material services provided. Solution: In Corp Gov definition of material service provider, specifically exclude auditors and note that specific requirements related to audits is in the MAR.
14A	AC responsible for appointment, compensation and oversight of CPA, who reports directly to AC.	Section 3iii indicates that BOD is required to review and approve, at least annually, the continued engagement of material service providers.	1) CPA may not be a material service provider 2) Conflict between if BOD or AC is responsible

		Section 4Ai indicates that AC must assist BOD oversight of qualifications, independence and performance of the CPA	Solution: In Corp Gov definition of material service provider, specifically exclude auditors and note that specific requirements related to audits is in the MAR.
14B	All AC members should also be BOD members	Section 4 indicates that RRG shall have an AC composed of at least three independent BOD. Non-independent BOD members cannot be AC members.	No.
14C	In order to be independent, may not accept consulting, advisory or other fee from insurer.	“Independent” is defined in Section 1.	MAR independence is based on compensation and affiliation. Corp Gov independence allows affiliation and is based on compensation and other business or familial relationships.
14D	If cease to be independent outside member’s reasonable control, can remain AC for a period of time.	Corp Gov standards are silent on this issue.	No.
14E	Guidance for exercising election of designating AC of an entity’s controlling insurer as insurer’s AC	Corp Gov standards are silent on this issue.	No.
14F	AC must require auditor to report certain items to the AC	Corp Gov standards are relatively silent on this. Section 4Aiii just notes that AC must discuss financials with CPA and Section 4Avi indicates that the AC must review any audit problems with the CPA.	No.
14G	Guidance for proportion of AC that must be independent	Section 4 indicates that the AC shall be composed of at least three independent board members. Non-independent BOD members cannot be AC members.	No, except for what is considered “independent.” This is discussed in 14C above.
14H	Instructions for insurer to apply for waiver of	Section 4B indicates that regulator may waive	No.

	Section 14 requirements based on hardship. No specific guidelines on when such applications for waivers should be approved or denied.	independence requirements, but not all AC requirements.	
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Securities: 1-877-550-3907

September 10, 2009

Julie Glaszczak, CPA, FLMI, ARA
National Association of Insurance Commissioners
Senior Accreditation Manager
Kansas City, MO 64108

Re: Part A Accreditation Standards

Dear Julie:

As discussed on the most recent Risk Retention Group Task Force conference call, please find a few follow up questions regarding the Part A Accreditation Standards:

2. Capital and Surplus Requirements

Risk-Based Capital – Vermont has always used RBC only as an analytical tool, although we have required our RRG's to file RBC with VT and the NAIC. The Task Force has since agreed that RBC is not applicable to RRG's. If my memory serves me correctly, the intention of the Task Force was to still require RRG's to file RBC, domiciles will use it as an analytical tool, and RRG's will continue to file it with the NAIC? Or is RBC no longer a required filing for RRG's?

6. Holding Company Systems

Does an RRG need to file Holding Company filings only with its state of domicile, or with other states?

The Part A Summary Memo states "During its discussion of the Part B accreditation standards, the Task Force will address the issue of communication to other states as it relates to items such as exemptions to the model requirements based on disclaimer of affiliation. It should be discussed whether this communication should just indicate that an exemption was granted or also indicate why an exemption was granted." If we discussed this during Part B, I can't remember what we decided?



Banking
802-828-3307

Insurance
802-828-3301

Captive Insurance
802-828-3304

Securities
802-828-3420

Health Care Admin.
802-828-2900

I'm also having a little trouble figuring out when an RRG would file for an exemption with a "disclaimer of affiliation". Would the following hypothetical example be a candidate for filing for a disclaimer of affiliation exemption?

An RRG is owned equally by 5 different hospitals. Each hospital owns 20%. Since ownership is greater than 10%, the Holding Company rules apply. Since all owners have an equal share, no one hospital can exercise any undue influence over the RRG. Each hospital has only one board member, all board members have an equal vote, the board runs the company, and therefore no one person can exercise control.

Any other hypothetical examples the Task Force could provide would be helpful.

10. Reinsurance Ceded - Reinsurance Guidelines for Risk Retention Groups

1.C. "Credit for reinsurance may be permitted if the reinsurer maintains an A- or higher A.M. Best rating, or other..."

I assume that if a domicile permits credit for reinsurance based on a reinsurer being A rated, and the rating subsequently drops below an A rating, that the reinsurance credit would not automatically be removed. The reinsurer may still meet the criteria under 1.D. If the reinsurer subsequently fails to meet the criteria under 1.D., the RRG could not place any new reinsurance with the reinsurer. Reinsurance credit could still be permitted on the past business if the reinsurance continued to be deemed collectable?

On that same note, if a RRG is currently using a reinsurer that may not meet the new guidelines effective 1/1/2011, the reinsurance credit would not automatically be removed effective 1/1/2011. The RRG could not place any new reinsurance with the reinsurer. Reinsurance credit could still be permitted on the past business if the reinsurance continued to be deemed collectable?

IV. "Any such waiver of a section I.D. requirement constitutes a change in the risk retention group's plan of operation in each of those states."

Was the intention of this to require the RRG to file the waiver, or change in plan of operation, with all the states that it is registered in?

11. CPA Audits

Requires audited statements to be filed before June 1. Vermont requires the audited financial statements be filed by June 30th. If I remember correctly, the Task Force agreed that June 30th would be considered "substantially similar"?

Thank you for the opportunity to ask further questions regarding the Part A Accreditation Standards. Feel free to call me at (802) 828-3304 should you have any questions.

Sincerely,



Peter Raymond, CFE, CPA
Director of Captive Insurance
Vermont Captive Insurance Division

cc: David Provost, Vermont Deputy Commissioner

w:/data/sep09/tf/risk_retention_Group_E_TF/VT Comments on Part A.pdf;

Draft: 9/15/09

Risk Retention Group (E) Task Force
Conference Call
September 3, 2009

The Risk Retention Group (E) Task Force met via conference call Sept. 3, 2009. The following Task Force members participated: Scott H. Richardson, Chair, represented by Leslie Jones (SC); Jim L. Ridling represented by Sean Duke (AL); Christina Urias represented by Steve Ferguson (AZ); Gennet Purcell represented by Dana Sheppard (DC); J.P. Schmidt represented by Judy Nako and Sanford Saito (HI); Glenn Wilson represented by Jaki Gardner (MN); Neil N. Jasey represented by Steve Zalewitz (NJ); Scott J. Kipper represented by Brett Barratt (NV); James J. Wrynn represented by Larry Levine (NY); Joel Ario represented by David DelBiondo (PA); and Paulette Thabault represented by Peter Raymond (VT).

1. Discuss Comment Received and Vote on Applicability of Part B: Regulatory Practices and Procedures and Part C: Organizational and Personnel Practices Standards

Ms. Jones provided a brief summary of the progress made to date by the Task Force on the Part B and Part C accreditation standards. She reminded the Task Force that the two summary memos (Attachments Three-A and Three-B) had been released for a 30-day comment period, which ended July 24. One comment letter was received (Attachment Three-C). Molly Lambert (Vermont Captive Insurance Association) provided a brief synopsis of the letter.

Ms. Gardner moved and Mr. Raymond seconded a motion to adopt the Part B summary memo and the Part C summary memo and present them to the Financial Condition (E) Committee for consideration and subsequent referral to the Financial Regulation Standards and Accreditation (F) Committee. The motion passed unanimously.

2. Review Previously-Adopted Part A Accreditation Standards Summary Memo

Ms. Jones reminded the Task Force that Vermont requested that a quick review be performed of the previously-adopted Part A Summary Memo. Mr. Raymond said he had some questions to ask the Task Force and/or NAIC staff regarding how certain Part A items might be handled on an accreditation review. For example on the Holding Company standard, he asked with whom the filings would be made, would those filings be maintained as confidential, etc. Ms. Jones suggested that a list of questions be drafted for discussion at the Fall National Meeting. It was agreed that regulators and interested parties should send any questions to NAIC staff by Sept. 10 so that they could be summarized and distributed prior to the meeting.

Julie Glaszczak (NAIC) said an initial draft of the "Self-Evaluation Guide/Interim Annual Review" form would also be provided as part of the advance materials for the Fall National Meeting. This draft will include explanatory language for some of the standards to facilitate the Task Force's discussions at that meeting.

3. Discuss Recent Changes to the Part A Standards

Ms. Jones said there have been revisions to some of the Part A standards since the Task Force began its deliberations of these particular standards. A memo from Ms. Glaszczak dated Aug. 21 (Attachment Three-D) discusses the recent Part A changes. Ms. Jones concurred with Ms. Glaszczak's recommendation that the 2006 revisions to the Risk-Based Capital for Insurers Model Act (#312) should not apply to captives licensed as risk retention groups (RRGs). There was no objection from the Task Force.

Ms. Jones also concurred with Ms. Glaszczak's recommendation that the 2001 revisions to the Actuarial Opinion and Memorandum Regulation (#822) should not apply to captives licensed as RRGs. Again, there was no objection from the Task Force.

Ms. Jones discussed the new Property and Casualty Actuarial Opinion Model Law (#745), including the four significant elements that would be added to the Liabilities and Reserves standard. There was no discussion from Task Force members or interested parties regarding any of the four significant elements, and it was agreed that each of these elements should be applicable to captive RRGs.

Ms. Jones discussed the 2001 revisions to the Annual Financial Reporting Model Regulation (#205), including the one significant element that would be added to the CPA Audits standard. There was no discussion from Task Force members or

interested parties regarding this item. As such, it was agreed that this significant element should be applicable to captive RRGs.

Ms. Jones discussed the 2006 revisions to model #205. Mr. Raymond said the corporate governance standards that have been adopted but not yet applied by the Risk Retention (C) Working Group state that the commissioner can waive the audit committee requirement. Ms. Glaszczak said the definition of “audit committee” in model #205 noted that an insurer can default to having its board of directors constitute its audit committee. She further noted that a detailed comparison of the model language to the corporate governance standards has yet to be drafted to determine if there are similar conflicts. Ms. Glaszczak suggested that a comparison of these two documents be drafted by the Task Force and NAIC staff prior to the Fall National Meeting; therefore, any of the elements related to an insurer needing an audit committee could be addressed at that meeting. The Task Force concluded that the first, third and sixth elements would be deferred for further discussion until the Fall National Meeting.

Ms. Jones discussed the second significant element in this standard. Ms. Glaszczak provided a brief summary of what constituted “certain non-audit services” in this item. There was no discussion from Task Force members or interested parties regarding this element. As such, it was agreed that it should be applicable to captive RRGs.

Ms. Jones discussed the fourth significant element in this standard. Ms. Glaszczak provided a brief summary of the restrictions placed on certain CPA employees from accepting employment with their audit clients for a one-year period. Mr. Raymond said he had no issue with the item, except that the language read a bit different from what the model requires. Ms. Glaszczak said NAIC staff could revise the wording to be more concise. There was no discussion from Task Force members or interested parties regarding this element. As such, it was agreed that it should be applicable to captive RRGs pending minor revisions by NAIC staff.

Ms. Jones discussed the fifth significant element in this standard. Ms. Glaszczak provided a brief summary of this item. There was no discussion from Task Force members or interested parties regarding this element, and it was agreed that it should be applicable to captive RRGs.

Ms. Jones discussed the seventh significant element in this standard. Ms. Glaszczak provided a brief summary of what type of conduct was prohibited by the insurer in Section 15 of model #205. There was no discussion from Task Force members or interested parties regarding this element, and it was agreed that it should be applicable to captive RRGs.

Ms. Jones discussed the eighth significant element in this standard. Ms. Glaszczak provided a brief summary of the requirements for insurers (depending on premium volume) regarding management’s report of internal control over financial reporting. She suggested that clarification language could be added to this element to indicate it is currently not applicable, because no RRGs had more than \$500 million in direct and assumed (D&A) premiums as of Dec. 31, 2008. However, a state would need to have this requirement if it did have an RRG with more than \$500 million in premium volume. Ms. Glaszczak said NAIC staff could insert clarification language to indicate that if a state can demonstrate that it does not have any RRGs writing more than \$500 million in D&A premiums at that time, it does not have to adopt this element. There was no discussion from Task Force members or interested parties regarding this element. As such, it was agreed that it should be applicable to captive RRGs pending the additional verbiage from NAIC staff.

4. Discuss How New Accreditation Guidance is Addressed Going Forward

Ms. Jones asked the will of the Task Force regarding addressing new accreditation guidance going forward. Mr. Raymond said he felt the Task Force should remain in existence and meet on as an-needed basis. Ms. Glaszczak said the Financial Condition (E) Committee would ultimately decide whether the Task Force should remain intact or be disbanded. She said NAIC staff support of that committee would be notified that it is currently the Task Force’s desire to remain in existence.

Having no further business, the Risk Retention Group (E) Task Force adjourned.

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To: Risk Retention Group (E) Task Force
From: Julie Glaszczak, Senior Accreditation Manager
Date: Updated for the June 13, 2009 Meeting
Re: Part B Accreditation Standards Summary Memo

Listed below are the Part B: Regulatory Practices and Procedures Accreditation Standards and the related Review Team Guidelines (RTG). The purpose of Part B is to identify baseline regulatory practices and procedures required to supplement, and support enforcement of, the states’ financial solvency laws in order for the states to attain substantial compliance with the core standards established in Part A.

Important Note: Part B applies to all multi-state insurers and currently includes captive risk retention groups (RRGs). Therefore, the standards and guidelines below are currently being applied to captive RRGs during accreditation reviews. To the extent that an item noted in the RTG is not required by a state’s captive laws, the RRG would not be required to follow that guideline or the applicable portion thereof. For example, if a state’s captive law does not currently require the filing of a MD&A, the RTG requiring an analysis of the MD&A would not be applicable.

1. Financial Analysis

a. Sufficient Qualified Staff and Resources

Standard: The Department should have the resources to review effectively on a period basis the financial condition of all domestic insurers.

General Guidance: Identified personnel who have the time and experience necessary to perform this function should be assigned to the analysis tasks, and the tasks should be satisfactorily completed in a timely manner.

Review Team Guideline	Task Force Consensus
<i>Qualification Guidelines</i>	
1) The Department should have analysts or qualified contractual resources with appropriate experience levels to perform necessary tasks. Such experience should match the sophistication of the domestic industry. For example, if the domestic industry consists of reinsurers, the analysis staff should have significant experience dealing with the impact of reinsurance on financial results and trends.	Applicable to captive RRGs
2) Although not required, credentials such as Accredited Financial Examiner (AFE), Certified Financial Examiner (CFE), Certified Public Accountant (CPA), Chartered Property Casualty Underwriter (CPCU), Fellow of the Life Management Institute (FLMI), Associate in Insurance Accounting and Finance (AIAF), Associate of Reinsurance (ARe), Member, American Academy of Actuaries (MAAA) may demonstrate expertise in insurance and/or financial analysis.	Applicable to captive RRGs
3) Staff should have an accounting, insurance, financial analysis or	Applicable to captive RRGs

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<p>actuarial background. If their background is insurance, it should be financial in nature. College degrees should focus on accounting, insurance, finance or actuarial science.</p>	
<p><i>Timing Guidelines</i></p>	
<p>1) The Department should begin its analysis review of priority multi-state domestics very shortly after the annual statements arrive. The Department should be essentially finished with the analysis of the annual statements (both by the primary analyst and the analyst's supervisor) and the actuarial opinions of priority, multi-state domestics by the end of April. It is acceptable if a reasonable number of reviews of companies carry over into May. The Department should be essentially finished with its analysis of the annual statements and actuarial opinions of the rest of its multi-state domestics by the end of June. Once again, it is acceptable for the analysis to carry over into July, so long as the companies carried over are the lowest priority companies. The date by which the Department should finish its analysis of the annual statements depends in part upon the size and complexity of the domestic industry. For example, if the Department has only 5 multi-state companies to analyze, it will likely finish its review of all companies (priority and non-priority) within a few weeks. But if the Department has 300 multi-state domestic companies to analyze and many of these are large, complex entities, it may take the Department several months to finish its review of domestics even though it starts right away and progresses very diligently.</p>	<p>Applicable to captive RRGs</p>
<p>2) Analysis of other supplemental filings (MD&A, CPA Audit, Holding Company Filings, Quarterly Financial Statements, etc.) should be completed within 60 to 90 days from receipt. Again, highest priority multi-state domestics should be analyzed well before the 60 to 90 day timeframe.</p>	<p>Applicable to captive RRGs</p>

b. Communication of Relevant Information to/from Financial Analysis Staff

Standard: The Department should provide relevant information and data received by the Department which may assist in the financial analysis process to the financial analysis staff and ensure that findings of the financial analysis staff are communicated to the appropriate person(s).

<p style="text-align: center;">Review Team Guidelines</p>	<p style="text-align: center;">Task Force Consensus</p>
<p>1) Procedures should be established such that information material to the financial analysis process is communicated to the analysts. Examples would include significant complaint data, legal actions taken against the company, material rate changes, results of market conduct and financial condition examinations, significant changes in the company's agents, MGAs or reinsurance intermediaries, and regulatory actions taken by other states. Some information may be effectively analyzed in a summary fashion (e.g. summary analysis of a complaint register including all domestic insurers).</p>	<p>The Task Force noted that such inter-departmental communication may not be applicable to all departments because relevant information regarding captive insurers is held within a department's captive area, instead of within different sections of a department (as is the case with traditional insurers).</p>

	<p>NAIC Staff has drafted the following language that may be added to this Guideline: Because of the organizational structure of some state insurance departments, other sections within the department may not receive or have significant information related to captive insurers as all business related to the captive occurs within the Captive unit. To the extent that sections outside of the Captive unit have information relevant to the financial analysis process of a captive, such information should be communicated to the captive financial analyst. To the extent that upper management in the Captive unit has significant information relevant to the financial analysis process of a captive, such information should be communicated to the captive financial analyst.</p>
<p>2) Analysts should comment in the analysis file with respect to significant information obtained from other units.</p>	<p>Applicable to captive RRGs; however, because of various organizational structures of state insurance departments related to captives, NAIC Staff suggests adding the following language to the end of this guideline: "...or other individuals within the Captive unit, if applicable."</p>
<p>3) Evidence of communication (e.g. minutes of meetings, memos or notes to the file, printouts, etc.) when problems or concerns are identified should be included in the department's analysis files or binders. To a lesser extent, oral verification may provide such evidence.</p>	<p>Applicable to captive RRGs</p>
<p>4) Financial solvency information, particularly adverse findings or significant unresolved issues, obtained as a result of the financial analysis procedures performed should be communicated to examiners, management and other Department staff as needed.</p>	<p>Applicable to captive RRGs</p>

c. Appropriate Supervisory Review

Standard: The Department’s internal financial analysis process should provide for appropriate supervisory review and comment.

General Guidance: An analyst’s conclusion and work files regarding the financial condition of any company should be reviewed by experienced personnel with supervisory review responsibility. Supervisory review may be conducted by the analyst’s supervisor or a senior level analyst whose job functions include such review duties.

Review Team Guidelines	Task Force Consensus
1) At least one level of supervisory review should be performed on each company analysis.	Applicable to captive RRGs
2) Evidence of such review should be documented via sign-off and dating by the reviewer.	Applicable to captive RRGs
3) Supervisory review should be timely, usually within 2-3 weeks of completion of the original analysis.	Applicable to captive RRGs
4) Supervisory review should include a review of all significant worksheets and evidence of the analysis performed. The supervisory review should also include at least some review of the source documents, the level of which should be based on the experience of the analysts. For very experienced analysts with a solid understanding of complex insurance issues including the accounting and reporting implications thereof, the supervisory review of the source documents may be more limited.	Applicable to captive RRGs
5) The supervisory review should be an in-depth and challenging review of the analyst’s findings. Some Departments may demonstrate in-depth and challenging supervisory review by maintaining supervisory review notes. Regardless of whether supervisory review notes are kept, however, the supervisory review shall be presumed to be sufficient if the analysis appears to be complete and no material matter remains unaddressed.	Applicable to captive RRGs
6) The supervisory review should encompass any written responses received by the primary analyst from the company, which contain significant information.	Applicable to captive RRGs

d. Priority-Based Analysis

Standard: The Department’s financial analysis procedures should be priority-based to ensure that potential problem companies are reviewed promptly. Such a prioritization scheme should utilize appropriate factors as guidelines to assist in the consistent determination of priority designations.

Review Team Guidelines	Task Force Consensus
1) General factors used to develop the priority system should be documented by the Department and consistently applied. The regulator should exercise reasonable judgment in the application of these factors to specific insurers.	Applicable to captive RRGs

<p>2) Domestic companies with the highest priority should be analyzed first. For example, if the Department rates companies from 1 to 4, with 1 being the highest priority, companies rated as 1's should generally be analyzed prior to analyzing lower priority companies. For states with few domestics, an informal prioritization system can be considered adequate.</p>	<p>Applicable to captive RRGs</p>
<p>3) Justification for priority ranking and any change to the priority ranking should be included in the analysis file. For example, if a company has historically been a troubled company receiving high priority and shows signs of improvement in the current year with the analyst rating them as low priority, a proper discussion of why the rating is appropriate should accompany such rating.</p>	<p>Applicable to captive RRGs</p>
<p>4) Any change to a priority ranking should be approved by the appropriate supervisor, and evidence of that approval should be apparent.</p>	<p>Applicable to captive RRGs</p>

e. Appropriate Depth of Review

Standard: The Department’s financial analysis procedures should ensure that domestic insurers receive an appropriate level or depth of review commensurate with their financial strength and position.

Review Team Guidelines	Task Force Consensus
<p>1) Depth of the analysis will depend on the complexity and the financial strength of the insurer and the existing or potential issues and problems found during review of the financial statements. Those companies with the highest priority should receive the most in-depth review. For those companies with the lowest priority, a less detailed review can suffice. This review can be conducted cooperatively with other experts, such as actuaries, where necessary or indicated.</p>	<p>Applicable to captive RRGs</p>
<p>2) At a minimum, the following information should be analyzed, to at least some extent, by the Department for all domestic multi-state companies:</p> <ul style="list-style-type: none"> • Annual Statement • Actuarial Opinion • Management’s Discussion and Analysis • Annual Audited Financial Statements • Holding Company Filings • Quarterly Statements (key financial data) • Financial ratios such as IRIS, FAST or other similar ratios 	<p>The Task Force agreed that the analysis of most of this information is applicable to captive RRGs.</p> <p>However, some of the financial ratios currently utilized for traditional insurers may not be appropriate for captive RRGs. To address this, the following could be added to the last bullet: (Some ratios or financial analysis scoring tools may not be appropriate for captive RRGs primarily because of the accounting method utilized. If it is found that some of the tools are not appropriate, the analyst</p>

	should explain why.)
<p>3) Departments may wish to use checklists developed by the Department or obtained from the NAIC <i>Financial Analysis Handbook</i>, and these checklists may be tailored to the particular needs of the analyst and the insurer under review. When using the NAIC <i>Financial Analysis Handbook</i>, the Level 1 Procedures Checklist and significant areas included in the Annual Statement General Checklist should be completed. The remainder of the checklists may be used to the extent the complexity of the insurer’s operations warrants such use or to the extent that procedures in the checklists provide a practical learning tool for less experienced analysts. The use of the Department-developed checklists or those from the NAIC <i>Financial Analysis Handbook</i> for the supplemental filings (Actuarial Opinion, MD&A, CPA Audit, Form B Holding Company Filings, Quarterly Financial Statements) is encouraged, especially for those analysts who are less experienced.</p>	<p>The Task Force generally agreed that some type of checklist should be utilized to analyze captive RRGs.</p> <p>The Task Force noted that the Financial Analysis Handbook (E) Working Group is currently developing additional analysis guidance applicable to captive RRGs.</p>
<p>4) <u>For captive RRGs, the following procedures should also be performed and documented in the analysis file in conjunction with the review of the annual statement and/or the audited financial statement:</u></p> <ul style="list-style-type: none"> • <u>Review the business plan to ensure that it is unchanged from the prior year.</u> • <u>Ensure that all changes in the plan of operations have been approved.</u> • <u>Review the reconciliation in Note 1 and ensure that it appears accurate and can be relied upon by others.</u> • <u>Review question 13.1 (largest net amount insured) and ensure that the amount agrees with the approved plan of operations.</u> • <u>Ensure that the financial projections on file accurately reflect the operations as presently conducted</u> • <u>Ensure that the “Notes” relating to the operation of the company agree with the approved plan of operation.</u> 	<p>This is a new guideline developed by the Task Force that would be applicable to captive RRGs only.</p>

f. Documented Analysis Procedures

Standard: The Department should have documented financial analysis procedures and/or guidelines to provide for consistency and continuity in the process and to ensure that appropriate analysis procedures are being performed on each domestic insurer.

General Guidance: The Department should develop an analysis manual or otherwise document its analysis process to provide a reference guide and training tool for the analysts. The use of the NAIC *Financial Analysis Handbook* or sections thereof is considered acceptable.

Review Team Guidelines	Task Force Consensus
1) All analysis work performed should include initials of the preparer and the dates of completion.	Applicable to captive RRGs
2) Worksheets designed to document the analysis process should be	Applicable to captive RRGs

properly completed as set forth by the Department's procedures.	
3) Procedures and worksheets should be of sufficient detail to uncover potential concerns addressing all material areas of the financial filing being analyzed. For example, financial analysis procedures, which ignore reinsurance transactions, would not be considered sufficient.	Applicable to captive RRGs
4) Any unusual item, fluctuation from established norms, or other issue raised during the analysis of a company, should be properly addressed and documented in the analysis file. For example, if the Department establishes a premiums to surplus ratio of 3 to 1 and the company being analyzed is writing 6 to 1, the issue should be addressed in the analysis file, as to why it is acceptable, or if not, what action the Department will require the company to take to remedy it. Also, if an analyst indicates that a fluctuation or ratio result is unusual, there should be evidence of follow-up and a conclusion as to whether the analyst considers the unusual fluctuation or ratio result to be a concern and why.	This is applicable to captive RRGs; however, some of the financial ratios currently utilized for traditional insurers may not be appropriate for captive RRGs. To address this, the following could be added to the end of the guideline: Some ratios or fluctuations from established norms may not be appropriate for captive RRGs primarily because of the accounting method utilized. If this is the case, the analyst should explain why the ratio or fluctuation is not applicable.
5) Any follow-up (e.g., memo to the file, letter to the company, etc.) should be properly documented. Any letter received from a company should show proper analysis by the Department, signing off and concluding that the response is adequate. For example, if the Department discovers that a company is not filing its securities with the SVO and sends a letter to the company requesting that such filings be made, a copy of the Department's letter and a copy of the company's response, including evidence that the analyst has determined that the company's final response is adequate, should be in the analysis file.	Applicable to captive RRGs
6) The financial analysis process should include a summary discussion of the analysis findings including a general discussion of the company's strengths and weaknesses.	Applicable to captive RRGs
7) Conclusions should be reached as to whether any action should be considered as a result of the analysis. For example, the worksheets could have a write-in section at the end, which would enable the analyst and supervisor to comment and make recommendations for action, monitoring and plans for follow-up.	Applicable to captive RRGs

g. Reporting of Material Adverse Findings

Standard: The Department's procedures should require that all material adverse findings be promptly presented to the commissioner or an appropriate designee for determination and implementation of appropriate regulatory action.

General Guidance: A material adverse finding is defined as a finding made by a Department with respect to an event, trend, transaction or series of transactions, fluctuation, agreement, arrangement, operating results or violation of law, which either has, or reasonably could have, a significant negative impact on a company's financial position.

Review Team Guidelines	Task Force Consensus
1) The Department should have a policy or procedure to require that all material adverse findings be promptly presented to the commissioner or an appropriate designee. This policy or procedure should be in written form and should be formally communicated to individuals capable of taking appropriate regulatory action via inclusion in the Department Handbook or through some other formal communication channel such as department bulletin, memo, etc. The policy or procedure should define a material adverse finding and to whom the finding should be communicated, as described in Guideline (3), and require findings to be promptly reported.	Applicable to captive RRGs
2) Financial analysis files should contain evidence that material findings were promptly presented to the commissioner or appropriate designee.	Applicable to captive RRGs
3) Material adverse findings should be reported to individuals who are capable of taking appropriate regulatory action. For example, if as a result of the material adverse finding the company need only be contacted to get further information on the finding, then reporting to the analyst's immediate supervisor would be considered adequate. However, if as a result of the material adverse finding the company needs to be placed in liquidation, contact at the highest levels of the Department is expected.	Applicable to captive RRGs

h. Action on Material Adverse Findings

Standard: Upon reporting of any material adverse findings from the financial analysis staff, the Department should take timely action in response to such findings or adequately demonstrate the determination that no action was required.

General Guidance: Material adverse finding is defined in the guidelines in g. above. The review team will accept the ultimate action of the regulator as appropriate as long as the logic of the decision is clearly documented and the decision is reasonable based upon what other regulators would commonly understand to be appropriate in that scenario and given the information available at that time.

Review Team Guidelines	Task Force Consensus
1) The Department should have a policy or procedure to take timely action in response to material adverse findings or adequately demonstrate and document that no action was required.	Applicable to captive RRGs

2) Department files should contain evidence that timely action was taken on material adverse findings or adequately demonstrate and document that no action was required.	Applicable to captive RRGs
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2. Financial Examinations

a. Sufficient Qualified Staff and Resources

Standard: The Department should have the resources to effectively examine all domestic insurers on a periodic basis, which is commensurate with the financial strength and position of each insurer.

General Guidance: Identified personnel who have the time and experience necessary to perform this function should be assigned to the examination tasks, and the tasks should be satisfactorily completed in a timely manner.

Review Team Guidelines	Task Force Consensus
<i>Timing Guidelines</i>	
1) Conduct a full-scope examination on each domestic company in accordance with the respective state law regarding the frequency of examinations or at least once every five years, whichever is less. Companies that redomesticate should be examined by the new domestic within five years of their last examination. Rare exceptions to the requirement to examine such redomesticated companies are permitted if adequately documented and communicated to all states in which the company is licensed <u>or registered</u> , but in no case shall the examination of a redomesticated company exceed six years. Domestic companies under court-ordered supervision, rehabilitation and receivership are excluded from this examination requirement. Companies classified as under administrative supervision, supervision, dormant, in run-off, or other similar designations are not excluded. Efforts to coordinate examinations with other states are not considered an acceptable allowance for non-compliance with this examination frequency requirement. The Department should be current with its statutory examination timetable.	Applicable to captive RRGs. Note, the Task Force will recommend that the phrase “or registered” be included, as noted to the left.
2) The Department should have sufficient staff to perform necessary target and limited scope exams.	Applicable to captive RRGs
<i>Qualifications Guidelines</i>	
1) The Department should have examiners or qualified contractual resources with appropriate experience levels to perform necessary tasks. Such experience should match the sophistication of the domestic industry. For example, if the domestic industry consists of reinsurers, the examination staff should have significant experience dealing with the impact of reinsurance on financial results.	Applicable to captive RRGs
2) Although not required, credentials such as Accredited Financial Examiner (AFE), Certified Financial Examiner (CFE), Certified Public Accountant (CPA), Chartered Property Casualty Underwriter (CPCU),	Applicable to captive RRGs

<p>Fellow of the Life Management Institute (FLMI), Associate in Insurance Accounting and Finance (AIAF), Associate of Reinsurance (ARe), Member, American Academy of Actuaries (MAAA) may demonstrate expertise in insurance and/or financial examinations.</p>	
<p>3) Staff should have an accounting, insurance, financial analysis, financial examination or actuarial background. If their background is insurance, it should be financial in nature. College degrees should focus on accounting, insurance, finance or actuarial science.</p>	<p>Applicable to captive RRGs</p>

b. Communication of Relevant Information to/from Examination Staff

Standard: The Department should provide relevant information and data received by the Department, which may assist in the examination process to the examination staff and ensure that findings of the examination staff are communicated to the appropriate person(s).

Review Team Guidelines	Task Force Consensus
<p>1) Procedures should be established such that information material to the financial examination process is communicated to the examiner-in-charge (EIC). Examples would include results of the financial analysis process, significant complaints data, legal actions taken against the company, material rate and form changes, results of market conduct examinations, significant changes in the company’s agents, MGAs or reinsurance intermediaries, and regulatory actions taken by other states.</p>	<p>The Task Force noted that such inter-departmental communication may not be applicable to all departments because relevant information regarding captive insurers is held within a department’s captive area, instead of within different sections of a department (as is the case with traditional insurers).</p> <p>NAIC Staff has drafted the following language that may be added to this Guideline: Because of the organizational structure of some state insurance departments, other sections within the department may not receive or have significant information related to captive insurers as all business related to the captive occurs within the Captive unit. To the extent that sections outside of the Captive unit have information relevant to the financial analysis process of a captive, such information should be communicated to the captive financial examiner. To the extent that upper management in the Captive unit has significant information relevant to the</p>

	financial examination of a captive, such information should be communicated to the captive financial examiner.
2) The EIC, or other appropriate examination staff member, should comment in the examination file with respect to significant information obtained from other units.	Applicable to captive RRGs; however, because of various organizational structures of state insurance departments related to captives, NAIC Staff suggests adding the following language to the end of this guideline: "...or other individuals within the Captive unit, if applicable."
3) Evidence of communication (e.g. bi-weekly reports, memos or notes to the examination files, examination reports, etc.) when problems or concerns are identified, as part of the examination process should be included in the examination files. To a lesser extent, oral verification may provide such evidence.	Applicable to captive RRGs
4) Financial solvency information, particularly adverse findings, obtained as a result of the financial examination procedures performed should be communicated to the EIC, chief examiner, Department management and other Department staff as needed.	Applicable to captive RRGs

c. Use of Specialists

Standard: The Department’s examination staff should include specialists with appropriate training and/or experience or otherwise have available qualified specialists, which will permit the Department to effectively examine any insurer. These specialists should be utilized where appropriate given the complexity of the examination or identified financial concerns.

General Guidance: The Department should have on staff or be able to contract the requisite expertise to examine effectively any insurer. The requisite expertise should be determined by the character and nature of the domestic industry and may include, but is not limited to, computer audit, reinsurance, actuarial and investment expertise. The Department should demonstrate that its use of specialists is appropriate.

Review Team Guidelines	Task Force Consensus
<i>Computer Audit Expertise Guidelines</i>	
1) The Department should have access to a person with expertise to conduct computer audits.	Applicable to captive RRGs
2) The Department should be utilizing software such as ACL, which enables the Department to test and understand company data. For those companies where use of such software is not feasible, the Department should document proper testing “around the computer.”	Applicable to captive RRGs

<p>3) To determine if reliance upon an insurer's Information Systems (IS) control system is appropriate, the Department may utilize such things as the IS Control Questionnaire from the NAIC <i>Financial Condition Examiners Handbook</i>, CPA Workpapers, etc.</p>	<p>Applicable to captive RRGs</p>
<p>4) Determination to rely or not to rely upon an insurer's IS controls should be made by an appropriate department representative consistent with the Department's procedures.</p>	<p>Applicable to captive RRGs</p>
<p><i>Reinsurance Expertise Guidelines</i></p>	
<p>1) Reinsurance contracts should be reviewed to address requirements contained in state law and to determine proper accounting treatment as set forth in the NAIC <i>Accounting Practices and Procedures Manual</i>, utilizing the version effective January 1, 2001 and all subsequent revisions adopted by FRSAC and the NAIC <i>Financial Condition Examiners Handbook</i>, including, but not limited to, transfer of risk. <u>For those captive RRGs filing under GAAP, the reinsurance contracts should be reviewed to determine proper accounting treatment under GAAP.</u></p>	<p>This is applicable to captive RRGs filing under statutory accounting principles. For those captive RRGs filing under GAAP, the reinsurance contracts should be reviewed to determine proper accounting treatment under GAAP. The Task Force added a sentence to the guideline to indicate this.</p>
<p>2) Complex and sophisticated reinsurance contracts may require review by persons with greater reinsurance experience or expertise. This experience or expertise may be provided by persons on staff, under contract, or as otherwise available to the Department, e.g., through consultation with the NAIC reinsurance specialist.</p>	<p>Applicable to captive RRGs</p>
<p><i>Actuarial Expertise Guidance</i></p>	
<p>1) Persons with appropriate experience to evaluate reserves should be involved on all examinations.</p>	<p>Applicable to captive RRGs</p>
<p>2) Credentialed actuaries should be involved on all life and health company examinations where the company has a substantial amount of interest-sensitive business and on all property/casualty company examinations where the company has a substantial amount of long-tail lines of business. The Department may demonstrate that non-credentialed actuaries have appropriate actuarial expertise to perform an evaluation of these types of reserves.</p> <p>For purposes of the above guideline, it should be noted that long-tail property/casualty lines of business have no definitive classification system. Certain lines are generally considered to be long-tail in nature, e.g., workers' compensation, medical malpractice, commercial general liability, and some other types of liability coverage; however, due to the historic development pattern in any particular case, a line often considered to be long-tail may in such case be medium- or short-tail, or vice-versa. As one example, losses for a long-tail line of business would not generally reach 95% of the ultimate loss development until after five years from incurral date. Other relevant factors may be considered in the determination of long-tail lines of business.</p>	<p>Applicable to captive RRGs</p>

<p>3) Coordination between examiners and actuaries should be evidenced in the examination files, especially in the planning file. For example, this would include identifying underlying data testing to be performed by the examiner and the methodologies to be used for determining reserve adequacy by the actuary.</p>	<p>Applicable to captive RRGs</p>
<p>4) Appropriate documentation should support actuarial findings.</p>	<p>Applicable to captive RRGs</p>
<p>5) The actuarial workpapers should be kept in the Department's files or otherwise be made available for review.</p>	<p>Applicable to captive RRGs</p>
<p><i>Investment Expertise Guidelines</i></p>	
<p>1) Investment policies and investment holdings should be reviewed to address requirements contained in state law and to determine proper accounting treatment as set forth in the NAIC <i>Accounting Practices and Procedures Manual</i>, utilizing the version effective January 1, 2001 and all subsequent revisions adopted by FRSAC. <u>For those captive RRGs filing under GAAP or in accordance with state prescribed methods, the investment holdings should be reviewed to determine proper accounting treatment under the method utilized.</u></p>	<p>This is applicable to captive RRGs filing under statutory accounting principles. For those captive RRGs filing under GAAP or some other method, the investment holdings should be reviewed to determine proper accounting treatment under the method utilized. The Task Force added a sentence to the guideline to indicate this.</p>
<p>2) Complex and sophisticated investment policies and holdings, that are material, may require review by persons with appropriate investment experience or expertise. This experience or expertise may be provided by persons on staff, under contract, or as otherwise available to the Department.</p> <p>For purposes of the above guideline, some examples of when an investment specialist may be necessary include: the insurer has a sophisticated derivatives program, material holdings of collateralized mortgage obligations with high flux scores, unusual real estate or limited partnership holdings, high or unusual portfolio turnover, material asset movements between related parties or unusual securities lending activities.</p> <p>If the Department does not have on staff persons with appropriate investment expertise, this investment expertise may be provided by persons associated with actuarial firms, commercial rating agencies, CPA firms, federal and state securities agencies, investment banking firms, investment brokerage firms, portfolio managers, the SVO, or other professionals experienced in analyzing investment activities.</p>	<p>Applicable to captive RRGs</p>

d. Appropriate Supervisory Review

Standard: The Department's procedures for examinations should provide for supervisory review of examination workpapers and reports to ensure that the examination procedures and findings are appropriate and complete and that the examination was conducted in an efficient and timely manner.

Review Team Guidelines	Task Force Consensus
<i>Guidelines for Supervisory Review of Workpapers</i>	
1) All workpapers, including work performed by the EIC, should receive at least one level of supervisory review. In addition, work of specialists should be reviewed by the EIC for familiarity and understanding. The reviewer should be looking to see that the specialists' reports and, if necessary, workpapers evidence all procedures that are expected to be performed. In addition, the workpapers should be consistent with the examiner's conclusions and the examination report.	Applicable to captive RRGs
2) Supervisory review should be evidenced by sign off and dating by the reviewer. Supervisory sign-off and dates on every single workpaper is not required.	Applicable to captive RRGs
3) Supervisory review should be timely in nature. <ul style="list-style-type: none"> • Planning should be reviewed before significant fieldwork begins. • Supervisory review of workpapers should occur within a reasonable period after completion of the item being examined (generally 2-4 weeks). 	Applicable to captive RRGs
4) Supervisory review should ascertain whether the form of examination workpapers is consistent with Department standards.	Applicable to captive RRGs
5) Supervisory review should be an in-depth and challenging review of the examiner's findings. The occurrence and sufficiency of supervisory review may be verified through discussions with department staff, including but not limited to, the EICs. The Department may demonstrate in-depth and challenging review by maintaining supervisory review notes. Regardless of whether supervisory review notes are kept however, the supervisory review shall be presumed sufficient if the examination procedures appear to be complete and no material matter remains unaddressed.	Applicable to captive RRGs
<i>Guidelines for Supervisory Review of Examination Reports</i>	
1) The examination report should be reviewed by at least one person other than the preparer. The commissioner or the commissioner's designee should approve the report prior to final issuance.	Applicable to captive RRGs

e. Use of Appropriate Guidelines and Procedures

Standard: The Department's policies and procedures for the conduct of examinations should generally follow those set forth in the NAIC *Financial Condition Examiners Handbook*. Appropriate variations in methods and scope should be commensurate with the financial strength and position of the insurer.

General Guidance: The Department should demonstrate that examinations have been generally conducted in accordance with the NAIC *Financial Condition Examiners Handbook*. Examination procedures should produce

reports of examination, which provide information needed by regulatory personnel involved in the admission and regulation of companies as well as specific information needed for any disciplinary or other regulatory action.

Review Team Guidelines	Task Force Consensus
<p>1) The Specific Risk Analysis (SRA) approach should be utilized in establishing priority of accounts or operational areas. Such approach should include completion of the SRA workpapers and internal control questionnaires. On those examinations where the SRA approach is not utilized, planning documentation should include rationale for not utilizing such approach and evidence that the cycles identified in the SRA approach have otherwise been considered and properly addressed in the exam work.</p>	Applicable to captive RRGs
<p>2) A memorandum should be prepared that summarizes the examination planning process. The memorandum should adequately discuss, but is not limited to, the following:</p> <ul style="list-style-type: none"> • Results of SRA or alternative analysis • Reliance on work completed by accredited states <u>(If applicable)</u> • Review of independent auditor’s workpapers and reports • Staffing and Time Budgets • Management assessment • Analytical review results • Materiality assessment 	Applicable to captive RRGs. Note that the Task Force added “if applicable” to the second bullet for clarification purposes. The “if applicable” would apply to both RRGs and traditional insurers
<p>3) Examination work programs should be utilized to document work performed. Such work programs should encompass steps identified in the NAIC <i>Financial Condition Examiners Handbook</i>. All work performed should be properly referenced from the work program to the workpaper(s) where the examination and analysis were performed. Such workpapers should fully document work performed and should include the initials and date of the preparer. Where work of the independent auditor is used or relied upon to supplement the work of the examiners, such reliance should be documented and limited re-testing of the CPAs work should be performed where appropriate.</p>	Applicable to captive RRGs
<p>4) States electing to rely on examination work completed by another state should review the planning memorandum of the testing state related to the area of planned reliance, review the related examination program prepared by the testing state, and communicate any concerns with the testing state about the examination approach. Additionally, the relying state should review the testing state’s conclusions after the examination work and a detailed review has been completed by the testing state. The relying state may also review additional working papers at the sole discretion of the relying state. For example, the relying state may choose to review working papers related to significant findings and material adjustments. A memorandum shall be included within the workpapers of the relying state describing the communication between the testing state and the relying state, information on the relying state’s actual review of the workpapers and how this review and reliance will</p>	This guideline would not typically be applicable to RRGs. However, if work of another state is used during the examination, this guideline would be applicable. The Liability Risk Retention Act of 1986 (the LRRRA) does allow for the coordination of examinations to avoid unjustified duplication and repetition.

<p>impact the relying state’s examination. The relying state should also have a copy of the pertinent workpapers completed by the testing state within their examination file.</p> <p>a. If relying on the work of a state that was accredited at the time of the review/reliance, the accreditation review team will not review the examination workpapers completed by the accredited testing state, but will review the memorandum documenting the review and reliance to determine compliance with this accreditation guideline. If a significant portion of the examination work was completed through reliance on another state’s workpapers, the accreditation review team may choose to select another examination to supplement the overall accreditation score on examinations.</p> <p>b. If relying on the work of a state that was not accredited at the time of review/reliance, the relying state must assume ownership of the work completed by the non-accredited testing state. This requires the relying state to conduct a review of the examination work performed by the non-accredited testing state. The relying state should use professional judgment in determining the extent of the review to be performed. However, since the relying state assumes ownership of the work, the accreditation review team will review the examination workpapers completed by the non-accredited testing state as if they had been completed by the relying state. If the relying state does not have the workpapers from the non-accredited testing state, this will result in an interpretation that the examination procedures were not completed. The accreditation review team is encouraged not to select other examination files to review if the documentation within a file in which reliance on a non-accredited testing state was lacking.</p>	
<p>5) Data supplied by the company or an outside source (such as the insurer’s independent auditor) on which material reliance is placed, should be tested for both accuracy and completeness. As stated in the NAIC <i>Financial Condition Examiners Handbook</i>, such tests may be substantive and/or compliance in nature.</p>	<p>Applicable to captive RRGs</p>
<p>6) Sampling techniques used should conform to guidance set forth in the NAIC <i>Financial Condition Examiners Handbook</i> or other appropriate authoritative guidance. These techniques should conform to the Department’s policy, be clearly documented, and be consistently applied on all examinations.</p>	<p>Applicable to captive RRGs</p>
<p>7) The Department should utilize qualified examiners-in-charge (EICs). The NAIC <i>Financial Condition Examiners Handbook</i> provides guidance on the authority, responsibilities and credentials for a qualified EIC.</p>	<p>Applicable to captive RRGs</p>
<p>8) If a Department elects to utilize contract examiners the Department</p>	<p>Applicable to captive RRGs.</p>

<p>should demonstrate significant involvement of appropriate Department personnel during the course of the examination to assure that the examination is generally conducted in accordance with the NAIC <i>Financial Condition Examiners Handbook</i> and the Department's policies and procedures.</p>	
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f. Scheduling of Examinations

In scheduling financial examinations, the Department should follow procedures such as those set forth in the NAIC *Financial Condition Examiners Handbook* that provide for the periodic examination of all domestic companies on a timely basis. This system should accord priority to companies, which exhibit adverse financial trends or otherwise demonstrate a need for examination.

Review Team Guidelines	Task Force Consensus
1) The Department should prepare a flexible yearly examination schedule identifying the company being examined, priority of the company, projected period of the examination and the EIC scheduled to perform the exam.	Applicable to captive RRGs.
2) The criteria used to establish the examination schedule should encompass the criteria found in the NAIC <i>Financial Condition Examiners Handbook</i> . Any additional criteria used should be properly documented in the Department's policies and procedures and should be consistently applied.	Applicable to captive RRGs.
3) The Department should be utilizing the NAIC Examination Tracking System for calling association examinations, <u>as directed by the <i>Financial Condition Examiners Handbook</i></u> .	<p>The use of the NAIC Examination Tracking System for calling examinations is applicable to captive RRGs, although the following supplemental information should be noted:</p> <p>Examinations of captive RRGs are not considered "association examinations" as the LRRRA does not specifically require other states' participation. However, the LRRRA does allow for coordination of examinations in specific situations, although it does not require that the domestic regulator coordinate an examination if it has already begun or initiated an examination. This guideline merely requires that captive RRG examinations be called on the ETS system. It does not require the domestic regulator to allow other</p>

	states to participate on the examination.
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g. Examination Reports

Standard: The Department’s reports of examination should be prepared in accordance with the format adopted by the NAIC and should be sent to other states in which the insurer transacts business in a timely fashion.

Review Team Guidelines	Task Force Consensus
1) The Department should demonstrate that reports of examination have been prepared in accordance with a format outlined in the NAIC <i>Financial Condition Examiners Handbook</i> .	Applicable to captive RRGs.
2) Reports should be prepared and distributed in a timely manner as set forth in statute. Exceptions to these timing requirements should be properly documented. As a general rule, examination reports should be issued no more than 18 months after the “as of date”; however, exceptions to the general rule are possible as noted in the guidance included in the Accreditation Interlineations. Exceptions are permissible provided contemporaneous documentation highlights mitigating circumstances, which balance timeliness issues or provides reasonable justification for delays due to unforeseen circumstances. The documentation should indicate the nature of the exception, such as staffing constraints, lack of cooperation on the part of the insurer, complexity and size of the insurer, awaiting completion of actuarial support, and due process issues. Documentation should identify both the cause of the exception and the regulatory response; for example, the steps taken by the Department to keep other States informed concerning the financial condition of the insurer. Ultimately, all timeliness exceptions should be considered in the aggregate to determine whether the Department is administering its Examination Authority to ensure examination reports are useful in describing the insurer’s financial condition.	Applicable to captive RRGs.
3) Examination reports may be mailed in hard copy form to the other states, may be sent in an electronic format, or may be posted to the Internet. If the Department has the company mail out the reports to other states in which it does business, the Department should have an established procedure to obtain evidence from the company that such reports were mailed. If the report is posted to the Internet, the state must proactively communicate the availability of the report to the other state insurance departments. If a state requests a hard copy of the examination report, such must be sent to the state in a timely manner. <u>Some state laws or regulations may require that examination reports are confidential documents, but this does not preempt the examining state from sharing examination reports with other states. The examining state may request confirmation from other states that they have the ability to maintain the confidentiality of the report.</u>	Applicable to captive RRGs. Note, the Task Force added language regarding confidentiality of examination reports.

h. Reporting of Material Adverse Findings

Standard: The Department’s procedures should require that all material adverse findings be promptly presented to the commissioner or an appropriate designee for determination and implementation of appropriate regulatory action.

General Guidance: A material adverse finding is defined as a finding made by a Department with respect to an event, trend, transaction or series of transactions, fluctuation, agreement, arrangement, operating results or violation of law, which either has, or reasonably could have, a significant negative impact on a company’s financial position.

Review Team Guidelines	Task Force Consensus
1) The Department should have a policy or procedure to require that all material adverse findings be promptly presented to the commissioner or an appropriate designee. This policy or procedure should be in written form and should be formally communicated to individuals capable of taking appropriate regulatory action via inclusion in the Department Handbook or through some other formal communication channel such as department bulletin, memo, etc. The policy or procedure should define a material adverse finding and to whom the finding should be communicated, as described in Guideline (3), and require findings to be promptly reported.	Applicable to captive RRGs.
2) Examination workpapers should contain evidence that material findings were promptly presented to the commissioner or appropriate designee.	Applicable to captive RRGs.
3) Material adverse findings should be reported to individuals who are capable of taking appropriate regulatory action. For example, if as a result of the material adverse finding the company need only be contacted to get further information on the finding, then reporting to the examiner’s immediate supervisor would be considered adequate. However, if as a result of the material adverse finding the company needs to be placed in liquidation, contact at the highest levels of the Department is expected.	Applicable to captive RRGs.

i. Action on Material Adverse Findings

Standard: Upon the reporting of any material adverse findings from the examination staff, the Department should take timely action in response to such findings or adequately demonstrate the determination that no action was required.

General Guidance: Material adverse finding is defined in the guidelines in h. above. The review team will accept the ultimate action of the regulator as appropriate as long as the logic of the decision is clearly documented and the decision is reasonable based upon what other regulators would commonly understand to be appropriate in that scenario and given the information available at that time.

Review Team Guidelines	Task Force Consensus
1) The Department should have a policy or procedure to take timely action in response to material adverse findings or adequately demonstrate and document that no action was required.	Applicable to captive RRGs.
2) Department files, examination workpapers and examination reports should contain evidence that timely action was taken on material adverse findings or adequately demonstrate and document that no action was required.	Applicable to captive RRGs.

3. Information Sharing and Procedures for Troubled Companies

a. Information Sharing

Standard: States should allow for the sharing of otherwise confidential documents, materials, information, administrative or judicial orders, or other actions with the regulatory officials of any state, federal agency or foreign countries providing that the recipients are required, under their law, to maintain its confidentiality. States also should allow for the sharing of otherwise confidential documents, materials, information, administrative or judicial orders, or other actions with the NAIC providing that the NAIC demonstrates by written statement the intent to maintain its confidentiality. The Department should have a documented policy to cooperate and share information with respect to domestic companies with regulatory officials of any state, federal agency or foreign countries and the NAIC directly and also indirectly through committees established by the NAIC which may be reviewing and coordinating regulatory oversight and activities. This policy should also include cooperation and sharing information with respect to domestic companies subject to delinquency proceedings.

Review Team Guidelines	Task Force Consensus
1) The Department should demonstrate that it is authorized to share confidential documents, materials, information, administrative or judicial orders, or other actions with the regulatory officials of any state, federal agency or foreign countries and the NAIC provided that the recipients are required to maintain its confidentiality.	Applicable to captive RRGs.
2) The Department should demonstrate that it is authorized to keep confidential documents, materials, and information provided by the regulatory officials of any state, federal agency or foreign countries and the NAIC, which is considered confidential in their jurisdiction.	Applicable to captive RRGs.
3) The Department should have a documented policy to cooperate and share documents, materials, and information on domestic companies with the regulatory officials of any state, federal agency or foreign countries and the NAIC. For example, the Department's policy could be	Applicable to captive RRGs.

to share critical information on a financially troubled company with the regulatory officials of any state, federal agency or foreign countries when requested as long as confidentiality is maintained.	
4) The Department should make reasonable efforts to respond to inquiries from the NAIC Analyst Team, the Financial Analysis Working Group, and any other appropriate NAIC body.	Applicable to captive RRGs.

b. Procedures for Troubled Companies

Standard: The Department should generally follow and observe procedures set forth in the NAIC *Troubled Insurance Company Handbook*. Appropriate variations in application of procedures and regulatory requirements should be commensurate with the identified financial concerns and operational problems of the insurer.

Review Team Guidelines	Task Force Consensus
1) Once the Department has identified an insurance company as troubled or potentially troubled, the Department should take steps such as those set forth in the NAIC <i>Troubled Insurance Company Handbook</i> to address the identified concerns. This shall apply from the point the Department identifies the insurance company as troubled, or potentially troubled, to the point the company has been placed into receivership.	Applicable to captive RRGs.
2) In most instances, examinations of those insurance companies that the Department has identified as troubled or potentially troubled should occur more frequently than once every five years as outlined in the NAIC Model Law on Examinations. Limited scope examinations are acceptable in meeting this guideline; however, the Department is still required to complete a full-scope examination in compliance with statutory requirements.	Applicable to captive RRGs.
3) Once the Department has identified an insurance company as troubled or potentially troubled, the Department should, within a reasonable amount of time, make efforts to communicate proactively with other state insurance regulators where the insurance company has a significant amount of written, assumed or ceded insurance business and with states in which affiliates of the troubled company are domiciled or those states where the troubled company has significant market share. Department files should contain written evidence of such communication(s). To a lesser extent, oral verification may provide such evidence.	Applicable to captive RRGs.

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To: Risk Retention Group (E) Task Force
From: Julie Glaszczak, Senior Accreditation Manager
Date: Updated for the June 13, 2009 Meeting
Re: Part C Accreditation Standards Summary Memo

Listed below are the Part C: Organizational and Personnel Practices Accreditation Standards, as discussed by the Task Force at its June 13, 2009 meeting. It is important to note that the Part C standards are not a “scored” section during accreditation reviews and cannot directly cause a state to fail the review. If deficiencies are noted, such will be included in the accreditation team’s management comment letter to the state.

Standard	Task Force Consensus
<p>1. Professional Development</p> <p>The Department should have a policy that encourages the professional development of staff involved with financial surveillance and regulation through job-related college courses, professional programs and/or other training programs.</p>	<p>Applicable to captive RRGs.</p>
<p>2. Minimum Educational and Experience Requirements</p> <p>The Department should establish minimum educational and experience requirements for all professional employees and contractual staff positions in the financial regulation and surveillance area, which are commensurate with the duties and responsibilities of the position.</p>	<p>Applicable to captive RRGs.</p>
<p>3. Retention of Personnel</p> <p>The Department should have the ability to attract and retain qualified personnel for the positions involved with financial surveillance and regulation.</p>	<p>Applicable to captive RRGs.</p>

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July 6, 2009

Members of the RRG (E) Task Force
ATTN: Julie Glaszczak, Senior Administrative Officer
NAIC
Kansas City, MO

Dear Members of the Risk Retention Group (E) Task Force,

Thank you for the opportunity to comment on the exposure draft dated June 25, 2009 related to the Part B: Regulatory Practices and Procedures and Part C: Organizational and Personnel Practices accreditation standards and their application to Risk Retention Groups (RRGs) licensed as captive insurers.

The Vermont Captive Insurance Association (VCIA) is the largest captive insurance association in the world representing the captive insurers and RRGs licensed in the State of Vermont. The State of Vermont is home to more RRGs than any other US domicile.

As such, the VCIA has been an active participant in the discussions during the last several months about Part B and C standards and their potential application to the regulation of RRGs. We have diligently worked with our Director of Captives and member of the task force, Peter Raymond, to understand the implications of the proposals on RRGs.

Throughout the process, our comments have been encouraged and given respectful consideration. As a result of the ability to participate in this effort, and the subsequent response to our concerns, the VCIA supports the draft document dated June 25, 2009 as written. Further, we express our thanks to the Task Force members and staff of the

NAIC for conducting a thorough and fair review of the Part B and C standards and the application of these standards to the regulation of RRGs.

Sincerely,



Michael Bemis, Chair
Board of Directors

cc: David Provost, Deputy Commissioner – BISHCA
Pete Raymond, Director of Captives – State of Vermont

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To: Risk Retention Group (E) Task Force Members
From: Julie Glaszczak, Senior Accreditation Manager
Date: August 21, 2009
Re: Recent Changes to Part A Accreditation Standards

The purpose of this memo is to discuss the Part A: Laws and Regulation Standards that have changed since the Risk Retention Group (E) Task Force (the Task Force) first began addressing the Part A Standards in 2003. The following are the Part A standards with recent changes:

1. Capital and Surplus

In June 2009, the Financial Regulation Standards and Accreditation (F) Committee (the Committee) voted that the 2006 revisions to the Risk Based Capital for Insurers Model Act (#312) should be required for accreditation, effective January 1, 2012. These revisions incorporate a new trend test that may trigger a company action level for property/casualty insurers. As the Task Force has previously voted that the RBC Model Act should not apply to risk retention groups (RRGs), the 2006 revisions should also not apply.

2. Liabilities and Reserves

Effective January 1, 2009, two new significant elements were added to this standard. The new elements are from the 2001 revisions to the Actuarial Opinion and Memorandum Regulation (#822) and require assets adequacy testing for all applicable companies and the filing of a regulatory asset adequacy summary by March 15 of each year. Since the Model Regulation only applies to life/health companies, the revisions are not applicable to RRGs.

3. Liabilities and Reserves

The Property and Casualty Actuarial Opinion Model Law (#745) will become an accreditation standard, effective January 1, 2010. Sections 2A, 2B, 3A and 3B(1) of the model are considered significant elements and will be required for accreditation. See page 2 for a matrix that includes the new significant elements.

4. CPA Audits

Effective January 1, 2008, a new significant element was added to this standard. The new significant element is from the 2001 revisions the Annual Financial Reporting Model Regulation (#205) and indicates that a qualified independent certified public account may not enter into indemnification agreements in regard to the audit of an insurer. See page 2 for a matrix that includes the new significant element.

5. CPA Audits

In June 2009, the Committee voted that the 2006 revisions to the Annual Financial Reporting Model Regulation should be required for accreditation, effective January 1, 2010. The revisions made to the model are numerous and are related to auditor independence, corporate governance and internal control over financial reporting. See pages 2-3 for a matrix that includes the new significant elements.

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Property/Casualty Actuarial Opinion Model Law – NEW

Significant Element	Task Force Consensus or Comments
(1) Requires annual submission of a “Statement of Actuarial Opinion” similar to Section 2A of the model?	
(2) Requires annual submission of an “Actuarial Opinion Summary” similar to Section 2B of the model?	
(3) Requires that the Statement of Actuarial Opinion is provided with the Annual Statement and is treated as a public document similar to Section 3A of the model?	
(4) Includes requirements that various documents related to the Actuarial Report or Actuarial Opinion Summary are confidential by law and privileged similar to Section 3B(1) of the model?	

CPA Audits – 2001 Revisions to the Annual Financial Reporting Model Regulation

Significant Element	Task Force Consensus or Comments
Prohibits CPA from entering into an agreement of indemnity or release from liability similar to Section 7A of the model rule?	

CPA Audits – 2006 Revisions to the Annual Financial Reporting Model Regulation

Significant Element	Task Force Consensus or Comments
(1) Requires that every insurer required to file an annual audited financial report under the model shall designate a group of individuals as constituting an audit committee similar to that discussed in Section 4D	
(2) Prohibits a certified public accountant that performs an audit on an insurer from also providing certain non-audit services to that same insurer as discussed in Section 7G.	
(3) Requires audit committee pre-approval of all auditing services and non-audit services provided by the certified public accountant similar to that discussed in Section 7J.	
(4) Prohibits certain certified public accountant employees who performed the audit of an insurer from accepting certain employments	

positions with the insurer for a period of one-year as discussed in Section 7L.	
(5) Requires communication of internal control related matters noted in an audit similar to Section 11.	
(6) Includes requirements for audit committees similar to that discussed in Section 14.	
(7) Includes requirements for conduct of the insurer in connection with the preparation of certain reports and documents similar to Section 15.	
(8) Includes requirements related to management's report of internal control over financial reporting similar to Section 16.	

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