SAN FRANCISCO, CA — Outside, the smoke from forest fires about 200 miles away made the air quality in the streets of San Francisco briefly the worst in the world. As this stark reminder of the need for insurance raged, inside the conference rooms regulators held sometimes contentious sessions that ended a national meeting with fewer accomplishments than expected.

When the year began, it may have been reasonable to expect that by its last national meeting of 2018, the NAIC might have addressed the most serious and potentially difficult issues facing state regulation. Last-minute concerns stalled the adoption of new reinsurance credit models consistent with the EU–US Covered Agreement. On the plus side, the new models are still scheduled for adoption at a special session of the plenary in late December.

The fate of changes to the Annuity Suitability Model Act is less immediately obvious. That response to the vacated US Department of Labor (DOL) fiduciary rule was expected to create new standards for annuity sales based on the best interest of the consumer. A revised version was exposed until February 15 over the objection of some large states in the working group. Many stakeholders expressed concerns for various reasons, and as of now, there is still clear potential for fragmentation, leaving the future as hazy as those San Francisco streets.
There was positive news. November congressional election results strengthened the possibility that a federal data security law would not be imposed on insurance, and even if such a law were to be approved, it would not preempt state insurance regulation. But the banner headlines and big decisions usually associated with the final meeting of the year were absent.

The next meeting will see new faces. The term-limited host Commissioner Dave Jones is handing the baton to his successor, and turnover may be more than usual, given some statehouse election results. Perhaps by the April meeting in Orlando, we will be able to ascertain the impact of political changes on the NAIC’s agenda.

When the year began, it may have been reasonable to expect that by its last national meeting of 2018, the NAIC might have addressed the most serious and potentially difficult issues facing state regulation.
Revised draft of annuity sales standards model moves forward

New requirements make this an improved regulatory framework with better protection for consumers, according to chair Dean Cameron, Director of Insurance in Idaho, who told the Annuity Suitability Working Group about the latest draft revision of the Suitability in Annuity Transactions Model Regulation (#275). The goal of the revised regulation is to create new standards for annuity sales, most likely moving from a suitability standard to a best interest standard.

Cameron outlined remaining questions about the draft. These included whether it should be applied to in-force contracts, whether it should be applied to life insurance applications, whether it should cover products already covered under the Employee Retirement Income Security Act of 1974 (ERISA), and if or how it should integrate with a proposed best interest regulation created by the US Securities and Exchange Commission (SEC).

Cameron said his hope was that the preliminary draft would be exposed for comment by the Life Insurance and Annuities (A) Committee.

An Ohio regulator praised the draft and wanted to differentiate it from what the regulator referred to as the currently nebulous SEC best interest standard and from a fiduciary standard. Various motions to address language changes followed. New York led the opposition to proposed changes that they saw as allowing the producer’s interest too much importance. NAIC consumer representative Birny Birnbaum expressed agreement with New York, saying the proposed change would allow the producer’s interest to be considered. “Why should the producer’s interest be involved in recommendations?” he asked. Birnbaum said the result was a lack of clarity as to whether producers should make recommendations in the consumer’s interest.

Iowa noted that the change was proposed in order to avoid favoring recurring fee-based charges over connections. New York and California opposed Iowa’s proposal. Iowa also wanted to change certain language on compensation, and that was approved unanimously. There were discussions about changing language relating to what constituted individualized recommendations.

Concerns were expressed that the proposed change would narrow the scope of the regulation. A representative of the American Council of Life Insurers (ACLI) noted that his organization had recommended that language be included so that marketing material, for example, would not be considered individualized recommendations. New York agreed with the ACLI on how to define recommendations.

The working group planned to report its progress to the A Committee and expose the amended draft for comment.

The goal of the revised regulation is to create new standards for annuity sales, most likely moving from a suitability standard to a best interest standard.
Annuity sales suitability model work causes internal dissent

Ongoing differences among regulators concerning new standards for annuity sales were at the center of a lively discussion at the Life Insurance and Annuities (A) Committee meeting.

Annuity Suitability (A) Working Group Chair Dean Cameron reviewed the history of the current suitability model and the work on its potential replacement. Cameron said that it was important to set the framework, as the current model had been protecting consumers for 15 years. Thirty-nine states have adopted that model since 2010, and the issue of change was not driven by weakness but by the since-vacated DOL fiduciary rule.

His working group, he said, had received more than 400 pages of comments. Its goal was to elevate the standard of care by ensuring producers acted with reasonable diligence, care, skill, and prudence, putting the consumer first and disclosing any compensation or other conflicts. Cameron said they were waiting to see what the SEC does, and he understood the DOL was also working on the issue again. He recommended that the current draft be parked and exposed for comment at the A Committee until February 2019 to allow interested parties and regulators to comment.

In response to a question from California as to whether there had been a vote in the working group on this draft, Cameron said that from his perspective there had been more votes than he could imagine. He added that he did not feel this was the final draft, and he was waiting to see what, if anything, the SEC or DOL would do. He called the draft a work in progress and said there were shortcomings right now, and that was fine. He told the committee that there is not a mechanism to hold the work at the working-group level, and after discussions with counsel and the NAIC, it was felt that it would be more appropriate to refer the draft to the A Committee.

New York agreed with California, opposing having a draft exposed that had not been voted as final in the working group. New York’s Superintendent Maria Vullo said she did not understand what the benefit of this committee exposing the draft would be, and she very much objected. She noted the committee had not had a substantive discussion. As for harmonization with the SEC and DOL, the NAIC should lead and not wait, Vullo said. She advocated the working group’s continuing its work. Vullo made a motion that the committee accept the report but not the draft for exposure. That vote failed, and the original report was accepted in full.

Annuity Disclosure (A) Working Group Chair Mike Yanacheak told the parent company that his group had been unable to reach consensus on model 245, which sets minimum disclosure standards for annuity sales. He asked the A Committee for additional time to review possible revisions. NAIC consumer representative Birny Birnbaum said this reinforced the issue of whether relaxation of disclosure standards is being sought. He said some products are being approved by the interstate compact, without sufficient consumer protections. The working group received an extension until the next national meeting.
LTC insolvency divides health, life insurers

The Receivership and Insolvency (E) Task Force was told that an IAIS working group had finalized drafting of the first application paper on ICPs 12 and 16, and those had been exposed for comment. ICP 12 covers market exit and resolution powers, and ICP 16 addresses enterprise risk management for solvency purposes. Any NAIC comments on the drafts will be directed through the G Committee.

A resolution paper is expected in January 2019, attendees were told. On the principles expressed by the IAIS Macroprudential Drafting Group, attendees were told that the United States has most of the powers enumerated in ICP 12 on resolution under the Insurance Receivership Model Act (IRMA). The task force will continue its evaluation to see if states needed additional powers, given that many had pre-IRMA laws in place. The task force will review to see if new resolution powers should apply.

The task force noted that it had already discussed a number of comment letters received on the Warrantech decision. This is a Pennsylvania decision relating to when claims made against a company in liquidation are valid, and the issue is its possible application to long-term care insurance. Some stakeholders have urged the NAIC to become involved in pending litigation in that state.

“We do not believe that action is necessary at this time,” said a representative of the health insurance group. He urged the task force to instead hear from people involved in the current Warrantech negotiations.

Calling it “a critical issue,” representatives of the ACLI expressed concern about what they call recent attempts by some health insurers to have this property-casualty framework adapted for Penn Treaty or other liquidations related to life or annuity products. Penn Treaty provided long-term care insurance and has been in liquidation since early 2017.

It was “a policy protection issue,” an ACLI representative said. He said the policyholder is already bound by guaranty association limits and should not be denied because they had filed claims more than 30 days after receivership. The policyholder should have access to the remaining estate assets, they said, and suggested that to do otherwise could create reputational risk.

The task force will continue to monitor the Penn Treaty situation, looking at the laws of other states to see if there are similarities to Pennsylvania law and considering how big of an issue this could potentially become.
The Qualified Jurisdiction (E) Working Group has some work to do. Stakeholders attending the meeting of the Reinsurance (E) Task Force heard that the current list of qualified non-US jurisdictions would only be good up until December 31, 2019. Current NAIC model laws require an assuming insurer to be licensed and domiciled in a “qualified jurisdiction” in order to be eligible for certification by a state as a certified reinsurer for reinsurance collateral reduction purposes. Qualified jurisdiction status must be reviewed at least every five years. This is particularly important in light of the EU–US Covered Agreement on reinsurance collateral. The NAIC is exploring extending the terms of that agreement to the designated qualified jurisdictions. The review will begin soon, and the working group will also examine whether the process itself could be streamlined.

The task force also adopted the report from the Reinsurance Financial Analysis (E) Working Group (ReFAWG). In that report, ReFAWG said that 29 reinsurers were certified for passporting and were being monitored. An increase in that number was anticipated. There was also a discussion on changes in surveillance of non-US reinsurers in certain qualified jurisdictions.

The revised Credit for Reinsurance Models (Act and Regulation) incorporating the standards of the Covered Agreement were a major topic of discussion. The Covered Agreement requires that US states conform to its terms within five years of the 2017 effective date of the agreement or risk federal preemption.

A September draft of the revised models had been exposed, and 13 comment letters were received. Working Group Chair Maria Vullo, superintendent of New York’s Department of Financial Services, thanked the 10 states on the drafting group. She said most comments received were similar to the comments on the previous draft. Comments received from the European Commission (EC) focused on whether the draft was consistent with the Covered Agreement.

The NAIC staff is in discussions with the EC and the Federal Insurance Office to explain that “the current draft revisions are fully consistent with the bilateral agreement.” A representative of the Association of Bermuda Insurers and Reinsurers said his sense was that editing of the draft was now complete. A representative of the Reinsurance Association of America (RAA) opened by saying, “I’d like to applaud the work done by the NAIC and the state commissioners.” He asked that an amendment defining each state as a jurisdiction to provide US reinsurers with identical access and identical rights as international reinsurers be added. He said RAA supported the draft as it was but asked the task force to work to amend it.

Vullo said the draft was intended to provide parity for all companies, and the task force would work through ReFAWG to address the issue. A speaker representing Insurance Europe told the task force that good regulation is way better than collateral but suggested that one sentence was problematic and inconsistent with the Covered Agreement language. The language in question referred to when losses would be covered in a dispute (paragraph 7, section 7, second sentence).

Vullo responded that the drafters had taken the language from the bilateral agreement and the US policy statement. If there were any ambiguity, she said, it was in the bilateral agreement or the signing statement. Vullo said she had never seen a model that did not have some interpretation issues—it was the nature of the beast.

A UK regulator expressed agreement with the representative of Insurance Europe, saying they did have concerns about paragraph 7, section 7, second sentence. Identified by the Insurance Europe speaker. Referring to the impending Brexit, the speaker said they looked forward to the United Kingdom having the same benefits as the European Union (EU).

Representatives of the ACLI and the National Association of Mutual Insurance Companies (NAMIC) expressed thanks to the NAIC for its work and pledged to work together on a state-by-state basis. The representative of a major US insurer said they wanted the jurisdiction of the worldwide parent of an insurance group used. Concerns expressed included that a literal reading of the language could take a subsidiary of a Canadian parent, for example, out of the Canadian regulator’s oversight. One US regulator pointed out that nothing in the Covered Agreement would compel the EU to recognize Canada.
A representative of another major US insurer asked when, in determining the amount of collateral in a solvent scheme, should the ceding company’s liabilities be applied as opposed to the assuming company’s liabilities? A Bermuda regulator said they would like to see reciprocity enshrined in the model. Vullo noted that there are plans to consider it for qualified jurisdictions.

The task force resisted requests for more time for the expressed concerns to be addressed and adopted the draft to be sent to its parent committee. Massachusetts, Texas, and Oklahoma opposed the adoption. Later an agreement was reached during the parent Financial Condition (E) Committee meeting to have technical revisions made to the draft reflecting comments received before a vote for adoption by the plenary.
Cannabis insurance group continues study

The Cannabis Insurance (C) Working Group is off to a great start, according to its chair, California Commissioner Dave Jones. Its charge is to look at each state’s markets for insurance for the cannabis industry and prepare a white paper to provide useful information.

The working group formed a white paper drafting subgroup with lots of progress made, Jones said. The cannabis industry associations have provided a lot of information, and the working group’s aim is to provide meaningful information on the architecture of the industry, what insurance is available, and what gaps there may be both in admitted and surplus lines.

One issue that surfaced near the end was the relationship between banking and the cannabis industry. One speaker said the biggest risk that the industry faced was not the product but the cash it generates. With significant amounts of cash that are sometimes difficult to bank, the risk of robbery is high.

A representative of the American Bankers Association (ABA) said it was a big misconception that banks did not want to participate. It’s not about a moral compass, he said, but that it is illegal. The ABA wants it legal, and not money laundering, for banks.

A New York regulator disagreed with the notion that it was illegal for banks to accept this green cash and said she did not think it was a great idea for the ABA to keep going around saying that it is illegal. A Michigan regulator disagreed with both, saying that banks in its state are extremely reluctant to participate. An Ohio regulator said that a few banks were in the market there, and the state examined them in conjunction with the Federal Deposit Insurance Corporation (FDIC), so there was appropriate oversight.

There were various panel discussions on different aspects of the business. Discussing gaps in coverage, an industry member said workers’ compensation insurance was particularly challenging, with every state requiring really high limits. Auto insurance for deliveries and transport is also a problem. The industry would like to see options at all price levels (for the mom-and-pop stores).

A Pennsylvania regulator said they were not seeing pricing as a problem but strict underwriting guidelines. One industry representative agreed, saying that carriers added additional barriers or requirements that exceed what is required by state law (e.g., insurance companies require a security system far more sophisticated than what is required by the laws).

Another industry trade group representative said people are willing to pay a premium in this market, but if the premium is too high, it could be cost prohibitive. If you continue to tax the golden goose, the system will fall in on itself, he warned.

A discussion on California as a cannabis insurance case study revealed the availability of insurance in both surplus lines and the admitted market. Claims so far have primarily been for theft or fire, although the possibility of the plaintiff’s bar filing other claims is still a concern. Data are being gathered to develop actuarially sound pricing. For admitted insurers, the biggest concern for now is competing with surplus lines.
Complex models, big-data use cause regulatory discomfort

Big Data (EX) Working Group Doug Ommen told his group that states are talking to life carriers about the data and analytics used by those carriers. This was part of a discussion on data accuracy and company validation methods in accelerated/nontraditional life insurance underwriting. Ommen said one question was whether regulators have sufficient tools to evaluate the appropriateness of data use (e.g., data from wearables to predict mortality). The accuracy and validity of the data also raise questions.

There were also questions about whether states should examine vendors, and do vendors offer the same models to competing insurers? A regulator from Alaska said they admittedly struggled with the tools, not knowing where to start or how to get to feeling comfortable. Missouri expressed similar concerns, saying that when doing an exam with sophisticated models, they have contracted with outside firms because they aren’t comfortable.

Iowa said one concern was that some of the predictive items are coming from entities that are not insurance regulated. A priority model might be coming from a noninsurance entity. Nevada said of financial models that if they don’t get the data they need to validate the model, they don’t approve the filing. It takes months to peel apart each one, according to Iowa, and once a model is approved, it is only approved for that purpose and not allowed for others.

NAIC consumer representative Birny Birnbaum said the issues being discussed about accelerated underwriting are the same that the casualty actuarial working group is discussing with regard to advanced models for personal lines. Does the regulator have the ability and the capacity to confirm that the models are complete, accurate, and nonbiased? Is the algorithm sound? Does it perpetuate discriminatory past practices or use variables that are a proxy for prohibited variables? The same thing holds for claim settlement and anti-fraud models. These are all questions for regulators and examiners who may be limited in tools, skill sets, and regulatory authority.

One firm’s representative said InsurTechs are building models before there is an actual insurance company to do a filing. They would like an avenue to submit the model to get some suggestions back. That way they can get and incorporate feedback from states before they go to insurers.

Regulators noted that part of the onus falls on the InsurTech companies. If they reached out to their state’s regulators, the regulator would almost always be willing to engage in a dialogue.

A representative of the ACLI humorously said that the organization was delighted to have this be a property-casualty conversation, a comment that was received with lots of laughter. Speaking seriously, the representative said the ACLI was looking at this and spending time with member life insurers. From its perspective, these are still early days, and so far, they did not believe companies were looking to use these tools to discriminate. In his view, a lot of companies are excited about using these tools to bring a broader suite of products to Middle America. The ACLI also believes that while there are a number of strong prior protections in place, stakeholders need to be pro-consumer and let them know if there are adverse underwriting actions taken.

NAIC consumer representative Peter Kochenburger of UConn Law School said he believed big data could be a win for consumers and insurers, and that concerns will continue to exist in the absence of regulatory tools. He said that proxies, while they may not be intentional, would be inevitable with the use of hundreds or thousands of variables. It is important to help consumers understand data use, he added.
Health care update

As defined in its 2018 charge, the mission of the Health Insurance and Managed Care (B) Committee is to consider issues relating to all aspects of health insurance. The charges in support of this mission include providing a means to analyze and discuss the implications and effects of proposed and enacted federal legislation and regulations on states, including the examination of rising health care costs. Analyzing the impact of federal regulation, including the Affordable Care Act (ACA), and identifying opportunities to innovate outside of the federal exchange in order to reduce costs continued to be a focus of the Fall 2018 meeting for the B Committee, its subgroups, and task forces.

The fall meeting in San Francisco focused on the increasing cost of health care premiums, understanding the dynamics that contribute to the continuing increase, and the potential role of state and private insurance providers outside of the federal exchange in managing premiums and out-of-pocket costs for the individual consumer.

Section 1332 of the ACA was recently incorporated by CMS, which allows a state to apply for a “State Relief and Empowerment Waiver” lowering barriers to state innovation strategies, and providing residents with access to quality, affordable health insurance that meets the basic protections of the ACA. This provision to the ACA is intended to stabilize markets and increase choice and affordability, subject to approval by state legislature. However, there continue to be concerns by the states related to short-duration health plans and other nonregulated insurance vehicles included in the Section 1332 strategies that could leave consumers with large out-of-pocket costs.

To provide comprehensive care and better serve residents, states including Nevada and New Mexico are looking to state-run exchanges. The decision to implement alternatives such as state-run exchanges or private insurance alternatives will continue to be a state-by-state decision largely prompted by evolving legislation and the economic environment unique to that state.

It is becoming increasingly important for health plans to remain relevant in this evolving health care landscape, rendering it critical to continually evaluate state insurance offerings while balancing health care costs and quality care.

This summary was prepared by Lynn Friedrichs and Sara Gambino. For your comments and suggestions, please contact the authors at lfriedrichs@deloitte.com and sgambino@deloitte.com.

Photo courtesy of the NAIC
Casualty Actuarial and Statistical Task Force (CASTF) update

Discussion on appointed actuary charges (attestation and three-year experience) and comments received

The CASTF exposed a draft of a single document that addressed both charges, and received five comments, of which two were deemed to be substantive by the committee:

- Comment 1 – Remove a redundancy in the reporting requirements with regard to overlap with other professional actuarial organizations
- Comment 2 – Opinion that it may be difficult for an Appointed Actuary to provide the required documentation within two weeks, depending on the timing of the request

The committee's initial recommendation was to move forward with the draft as is, without changes based on the comments received so far. The document will be reexposed on December 15, 2018, for 60 days. In the meeting, commentary was provided by representatives from the American Academy of Actuaries (AAA) and Society of Actuaries (SOA).

- AAA – The representative noted that the exposure draft does not provide an example of what the attestation should look like. The AAA has an attestation that follows the language of the US Qualification Standards exactly. The AAA representative believed that there should be something that provides some format, even if there's not a formal prescription.
- SOA – The SOA representative commented that the three-year experience should be related to the subject of the opinion, to more closely align with existing US Qualification Standards.

The CASTF noted that the operative language is "relevant to the company's structure and lines of business." The goal of the regulation is to ensure the Appointed Actuary has experience that meets this, but they believe the language should be broad enough not to be restrictive.

Predictive analytics update

Echoing the discussion in the Big Data Working Group, the CASTF discussed the in-flight white paper on the best practices and necessary data items for regulatory review of generalized linear models (GLMs) used for rate-making.

The CASTF noted that the goal is to help shorten the review cycle, which will encourage the use of big data models that should, in theory, improve competition and ultimately benefit consumers. Following the best practices and requesting the appropriate data should reduce the amount of back-and-forth between regulators and companies.

It was noted that states with the least amount of resources tend to take the most “cookie-cutter approach” to requesting information, and companies with the least amount of resources tend to take the most cookie-cutter approach to providing it, such that inclusion of all the information in the list could actually slow down the review cycle.

Life Actuarial Task Force (LATF) update

NPR mortality adjustment

The LATF exposed APF 2018-57, “Adjustments to NPR Mortality,” for comment, with the comment period extending until January 3, 2019. This amendment was proposed because in the current Valuation Manual, the "NPR definition does not allow for any adjustments to mortality when additional conservatism may be warranted. This APF broadly allows for adjustments as appropriate, so long as it does not decrease the NPR for the policy."

The amendment would potentially apply to substandard policies and Simplified Issue policies. The language allows a company to make the following adjustment: “For policies where the anticipated mortality experience materially exceeds the prescribed CSO mortality rates determined in Section 3.C.1a through 3.C.d above, the company shall consider adjusting the CSO mortality rates used in the NPR calculation in a manner commensurate with the anticipated mortality experience for the policy, subject to a cap that ensures mortality rates do not exceed 1000 per 1000.”

Aggregation of mortality experience for PBR

The LATF adopted amendment proposal form APF 2018-17, which provides clarity on approaches to aggregate mortality experience for a group of segments. It also clarifies how the mortality rates should be determined for each individual segment.
The APF also provided clarity on cases where accelerated underwriting may have been used to issue the policy. Specifically, the language in the APF notes that “the adoption by a company of a modified underwriting process that involves a new or significantly altered method of risk assessment, such as accelerated underwriting, is not an incremental change and is thus subject to the requirements in (iii) above regarding retrospective demonstrations . . .”

The APF also provides information regarding the “top-down” and “bottom-up” approaches to mortality assumption development. An example is provided in the APF for the bottom-up approach, and there have been requests to include additional examples on the LATF website.

**YRT reinsurance: premium rate increase treatment**

The LATF exposed APF 2018-58 for comment, ending on January 31, 2019. The APF addresses an issue raised by the American Academy of Actuaries. The issue is with material differences in the approaches for projecting future YRT premium rate increases between ceding and assuming companies for stochastic and deterministic reserve projections, for the calculation of VM-20 reserves.

The final language is closest to option 2 in the AAA report: “an increase in the YRT scale, if necessary, to achieve breakeven starting at the next date at which non-guaranteed premiums may be increased (raise reinsurance premiums such that the present value of future reinsurance premiums equals the present value of future reinsurance benefits).”

The APF would modify language to VM-20 Section 8.C and 8.D.

**Valuation Analysis Working Group’s public 2017 Principle-Based Reserving (PBR) Review Report and its recommendations and referrals to the task force**

Larry Bruning and Pat Allison of the NAIC presented selected findings from the report, which can be found at [https://www.naic.org/documents/cmte_e_valuation_analysis wg_2017_pbr_review_report.pdf](https://www.naic.org/documents/cmte_e_valuation_analysis wg_2017_pbr_review_report.pdf). Key highlights of the report include:

- **Reporting issues** – Many companies had reporting issues, including reserves and face amounts that were reported in the incorrect units. In some cases, these values were reported in dollars (similar to exhibit 5) as opposed to in thousands as required. Additionally, some companies did not fully complete all columns, and reserves in the supplement often did not tie out to exhibit 5.

- **Organization and communication issues** – The report noted that dispersed information made it difficult for reviewers to gain a complete understanding of a given topic. One example was that modeling systems were often spread across different sections (e.g., the asset model was listed only in the asset section, the liability model was listed only in the liability section). Additionally, there was unclear communication with regard to what the actual final assumptions were in many cases.

- **Missing information** – The report noted that information was commonly omitted, including materiality standards, asset type/duration/quality, details on reinsurance agreements, and anticipated experience assumptions, margins, and prudent estimate assumptions.

- **Other methodology, modeling, and assumption issues** – Companies often neglected to provide VM-20 Section 2.G support for simplifications, approximations, and modeling efficiency techniques. Companies also provided limited explanation on unusual patterns of net asset earned rates and slower-than-allowed mortality grading.

The committee provided a number of recommendations to companies that have already implemented or will be implementing PBR, including:

- Leveraging existing documentation, such as Actuarial Opinions and Memoranda
- Using graphs, tables, and spreadsheets where appropriate, to communicate information in a concise manner
- Performing a peer review, completed by an actuary that is qualified in the same practice area, to assess for readability and compliance with the requirements
- Considering ASOP 41 on Actuarial Communications while drafting the documentation

This summary was prepared by Jason Hiquet. For your questions, comments or suggestions, please contact the author at jhiquet@deloitte.com.
Accounting update

This section of the NAIC update focuses on accounting and reporting changes discussed, adopted, and exposed by the Statutory Accounting Principles (E) Working Group, the Accounting Practices and Procedures (E) Task Force, and the Financial Condition (E) Committee during the Fall 2018 meeting. Substantive changes finalized during these meetings have explicit effective dates as documented below. All nonsubstantive changes finalized during these meetings are effective upon adoption unless otherwise noted.

**Statutory Accounting Principles Working Group (SAPWG)**

**Current developments:** The SAPWG adopted the following *substantive* items as final during the meeting:

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<thead>
<tr>
<th>Ref#</th>
<th>Title</th>
<th>Sector</th>
<th>Amendments adopted</th>
<th>F/S impact</th>
<th>Disclosure</th>
<th>Effective date</th>
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<tbody>
<tr>
<td>2018-17</td>
<td>SSAP No. 21—Other admitted assets</td>
<td>P&amp;C Life Health</td>
<td>This item addresses accounting requirements for acquired structured settlement payments rights resulting from a factoring transaction. Revisions adopted provide that period-certain structured settlements that are acquired in accordance with state and federal laws are admitted assets. Period-certain structured settlements that are not acquired in accordance with state and federal laws are nonadmitted. Life-contingent structured settlements are nonadmitted, regardless of whether the right to future payments has been legally transferred. All acquired income streams from structured settlements are required to be reported as another long-term invested asset on Schedule BA, even if nonadmitted.</td>
<td>Y</td>
<td>N</td>
<td>2018</td>
</tr>
<tr>
<td>2017-32</td>
<td>SSAP No. 30R—Unaffiliated common stock</td>
<td>P&amp;C Life Health</td>
<td>Revisions update the common stock definition to include US Securities Exchange Commission registered closed-end funds and unit-investment trusts within the scope of the statement.</td>
<td>Y</td>
<td>N</td>
<td>2019</td>
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Issue Paper 158—Unaffiliated common stock
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| 2017-28 | SSAP No. 62R—Property and casualty reinsurance                         | P&C    | Revisions incorporate US-GAAP guidance from EITF 93-6, Accounting for Multi-Year Retrospectively Rate Contracts by Ceding and Assuming Enterprises and from EITF D-035, FASB Staff Views on Issue No. 93-6. This US-GAAP guidance was previously adopted by reference, with elements included in various sections of SSAP No. 62R. The guidance incorporated is intended to clarify the statutory requirements.  

In addition, comments received from the states of Connecticut and New Jersey were forwarded to the informal Life and Health Reinsurance Drafting Group for consideration during their review of the guidance included in SSAP No. 61R—Life, Deposit-Type and Accident and Health Reinsurance. | N         | N          | 2019 |
| 2016-03 | SSAP No. 10B—Derivatives hedging variable annuity guarantees           | Life   | Adopted a new statement of statutory accounting principle that prescribes accounting and disclosure guidance for derivatives that hedge interest rate risk of variable annuity guarantees.  

Early adoption permitted beginning January 1, 2019, and applied prospectively.  

Insurers that have previously applied a permitted or prescribed accounting practice must work with their domiciliary regulator for an appropriate method of transition, including disclosure of the transition method. | Y         | Y          | 2020 |

**Current developments:** The SAPWG adopted the following *nonsubstantive* items as final during the meeting:

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| 2018-20 | SSAP No. 15—Debt and holding company obligations                     | P&C    | Revisions clarify the accounting treatment for forgiveness of debt obligation as follows:  

- Forgiveness of an insurer’s obligation to its parent or other stockholders is accounted for as contributed surplus as required by SSAP No. 72—Surplus and Quasi-Reorganization (SSAP No. 72).  
- An insurer’s forgiveness of any debt, surplus note, or other obligation of its parent or other stockholders is accounted for as a dividend as required by SSAP No. 72. | N         | N          | 2018 |
<p>| 2018-25 | SSAP No. 22—Leases                                                 | P&amp;C    | Revisions reject ASU 2018-01, Leases – Land Easement Practical Expedient for Transition to Topic 842 for statutory accounting, as Topic 842 (new US-GAAP guidance for leases) is expected to be rejected. | N         | N          | 2018 |</p>
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<th>Disclosure</th>
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</tr>
</thead>
<tbody>
<tr>
<td>2018-19</td>
<td>SSAP No. 43R—Loan-backed and structured securities</td>
<td>P&amp;C Life Health</td>
<td>Revisions remove the modified filing exempt (MFE) process for determining NAIC designations. As noted by the Valuation of Securities (E) Task Force, markets have stabilized. The MFE process was producing unusual results that are counter to the original intent of the process.</td>
<td>N</td>
<td>N</td>
<td>2019</td>
</tr>
<tr>
<td>2018-27</td>
<td>SSAP No. 48—Joint ventures, partnerships, and limited liability companies</td>
<td>P&amp;C Life Health</td>
<td>Revision adds disclosure requirements for joint ventures, partnerships, and limited liability companies whose shares of losses exceed its investment value (carrying value). This disclosure also includes a loss-tracking schedule.</td>
<td>N</td>
<td>Y</td>
<td>2018</td>
</tr>
<tr>
<td>2018-28</td>
<td>SSAP No. 51—Life contracts</td>
<td>Life Health</td>
<td>Revisions add life liquidity disclosures and expand the variable annuity liquidity disclosures to enhance the ability of the NAIC to address its role in macroprudential surveillance of the insurance industry.</td>
<td>N</td>
<td>Y</td>
<td>2019</td>
</tr>
<tr>
<td>2018-23</td>
<td>SSAP No. 68—Business combinations and goodwill</td>
<td>P&amp;C Life Health</td>
<td>Revisions clarify that statutory mergers include scenarios in which the stock of an owned entity is canceled, with the parent entity reporting the assumed assets and liabilities.</td>
<td>N</td>
<td>N</td>
<td>2018</td>
</tr>
<tr>
<td>2018-21</td>
<td>SSAP No. 72—Surplus and quasi-reorganization</td>
<td>P&amp;C Life Health</td>
<td>Revisions clarify that when a reporting entity provides a distribution that is a return of capital, it shall be reported with a charge to gross paid in and contributed surplus.</td>
<td>N</td>
<td>N</td>
<td>2018</td>
</tr>
<tr>
<td>2018-30</td>
<td>SSAP No. 86—Derivatives</td>
<td>P&amp;C Life Health</td>
<td>Revisions adopt certain aspects of ASU 2017-12 — Derivatives and Hedging—Targeted Improvements to Accounting for Hedging Activities related to hedge effectiveness documentation requirements. Early adoption permitted. Reporting entities that are also US-GAAP filers may only early adopt if the ASU was also early adopted.</td>
<td>Y</td>
<td>N</td>
<td>2019</td>
</tr>
<tr>
<td>2018-29</td>
<td>Appendix A—Excerpts of NAIC model laws</td>
<td>Life</td>
<td>Revisions remove the phrase “good and sufficient” from Appendix A-820—Minimum Life and Annuity Reserve Standards to be consistent with the related model law.</td>
<td>N</td>
<td>N</td>
<td>2018</td>
</tr>
</tbody>
</table>
The SAPWG exposed the following items for written comments (due by February 15, 2019) by interested parties:

<table>
<thead>
<tr>
<th>Ref#</th>
<th>Title</th>
<th>Sector</th>
<th>Amendments exposed</th>
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<tbody>
<tr>
<td>2018-18</td>
<td>SSAP No. 2R—Cash, cash equivalents, drafts, and short-term investments</td>
<td>P&amp;C Life Health</td>
<td>The focus of this agenda item is on instruments that combine characteristics of a debt instrument with a derivative component.</td>
<td>Y</td>
<td>N</td>
<td>TBD</td>
</tr>
<tr>
<td></td>
<td>SSAP No. 26R—Bonds</td>
<td>P&amp;C Life Health</td>
<td>Investment products that are structured to resemble debt instruments, where the investor assumes a risk of principal loss based on an underlying component unrelated to the credit risk of the issuer.</td>
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<tr>
<td></td>
<td>SSAP No. 43R—Loan-backed and structured securities</td>
<td>P&amp;C Life Health</td>
<td>Reexposed proposed revisions to identify that structured notes, except for mortgage-referenced securities, for which (1) the contractual principal amount to be paid at maturity or (2) the original investment amount is at risk for other than failure of the borrower to pay the contractual amount due, shall be reported as derivatives within the scope of SSAP No. 86.</td>
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<tr>
<td></td>
<td>SSAP No. 86—Derivatives</td>
<td>P&amp;C Life Health</td>
<td>The proposed revisions note that mortgage-referenced securities will be in scope of SSAP No. 43R.</td>
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<tr>
<td>2018-32</td>
<td>SSAP No. 26R—Bonds</td>
<td>P&amp;C Life Health</td>
<td>Proposed revisions provide guidance for determining the prepayment penalty for called bonds when consideration received is less than par.</td>
<td>TBD</td>
<td>N</td>
<td>TBD</td>
</tr>
<tr>
<td>2018-33</td>
<td>SSAP No. 30R—Unaffiliated common stock</td>
<td>P&amp;C Life Health</td>
<td>Proposed revisions clarify that assets pledged to a Federal Home Loan Bank (FHLB) on behalf of an affiliate shall be nonadmitted pursuant to SSAP No. 4—Assets and Nonadmitted Assets.</td>
<td>N</td>
<td>N</td>
<td>TBD</td>
</tr>
<tr>
<td>2018-34</td>
<td>SSAP No. 30R—Unaffiliated common stock</td>
<td>P&amp;C Life Health</td>
<td>Reexposed proposed revisions to clarify that a mortgage loan acquired through a mortgage loan participation agreement is limited to a single mortgage loan and excludes “bundled” mortgage loans.</td>
<td>TBD</td>
<td>TBD</td>
<td>TBD</td>
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<td>2018-38</td>
<td><strong>SSAP No. 55—Unpaid claims, losses, and loss adjustment expenses</strong></td>
<td>P&amp;C Life Health</td>
<td>Proposed revisions provide guidance clarifying that prepayments to providers of claims and adjusting services shall be recognized as miscellaneous underwriting expenses, with guidance for reclassification as claims adjustment expense or claims expense, as applicable, as claims are paid.</td>
<td>N</td>
<td>N</td>
<td>TBD</td>
</tr>
<tr>
<td>2018-39</td>
<td><strong>SSAP No. 55—Unpaid claims, losses, and loss adjustment expenses</strong></td>
<td>P&amp;C Life Health</td>
<td>Proposed revisions clarify that interest paid on accident and health claims in accordance with prompt pay laws or regulations shall be reported as other claims adjustment expense.</td>
<td>N</td>
<td>N</td>
<td>TBD</td>
</tr>
<tr>
<td>2018-37</td>
<td><strong>SSAP No. 92—Postretirement benefits other than pensions</strong></td>
<td>P&amp;C Life Health</td>
<td>Proposed revisions adopt, with modification, the disclosure amendments reflected in ASU 2018-14, Changes to the Disclosure Requirements for Defined Benefit Plans. Certain disclosures are deleted, while others are added or clarified, which corresponds to the requirements for public entities under the ASU.</td>
<td>N</td>
<td>Y</td>
<td>TBD</td>
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<tr>
<td>2018-35</td>
<td><strong>SSAP No. 95—Nonmonetary transactions</strong></td>
<td>P&amp;C Life Health</td>
<td>Proposed revisions adopt, with modification, ASU 2018-07, Improvements to Nonemployee Share-Based Payment Accounting to eliminate the specific section for nonemployee awards and include guidance for nonemployees with the share-based payment guidance for employees. Proposed revisions to SSAP No. 95 update previously adopted US-GAAP guidance to reflect the revisions from ASU 2018-07.</td>
<td>TBD</td>
<td>TBD</td>
<td>TBD</td>
</tr>
<tr>
<td>2018-26</td>
<td><strong>SSAP No. 97—Subsidiary, controlled, and affiliated entities</strong></td>
<td>P&amp;C Life Health</td>
<td>Reexposed the agenda item with direction for NAIC staff to work with interested parties and research applicable US-GAAP guidance to consider revisions to existing guidance that requires negative subsidiary, controlled, and affiliated (SCA) entity reporting when there is a guarantee or commitment to provide financial support.</td>
<td>TBD</td>
<td>TBD</td>
<td>TBD</td>
</tr>
<tr>
<td>2018-36</td>
<td><strong>SSAP No. 100R—Fair value</strong></td>
<td>P&amp;C Life Health</td>
<td>Proposed revisions adopt, with modification, the disclosure amendments in ASU 2018-13, Changes to the Disclosure Requirements for Fair Value Measurement.</td>
<td>N</td>
<td>Y</td>
<td>TBD</td>
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</tbody>
</table>

- **Proposed revisions provide guidance clarifying that prepayments to providers of claims and adjusting services shall be recognized as miscellaneous underwriting expenses, with guidance for reclassification as claims adjustment expense or claims expense, as applicable, as claims are paid.**

- **Proposed revisions clarify that interest paid on accident and health claims in accordance with prompt pay laws or regulations shall be reported as other claims adjustment expense.**

- **Proposed revisions adopt, with modification, the disclosure amendments reflected in ASU 2018-14, Changes to the Disclosure Requirements for Defined Benefit Plans.**

- **Certain disclosures are deleted, while others are added or clarified, which corresponds to the requirements for public entities under the ASU.**

- **Proposed revisions adopt, with modification, ASU 2018-07, Improvements to Nonemployee Share-Based Payment Accounting to eliminate the specific section for nonemployee awards and include guidance for nonemployees with the share-based payment guidance for employees.**

- **Proposed revisions to SSAP No. 95 update previously adopted US-GAAP guidance to reflect the revisions from ASU 2018-07.**

- **Reexposed the agenda item with direction for NAIC staff to work with interested parties and research applicable US-GAAP guidance to consider revisions to existing guidance that requires negative subsidiary, controlled, and affiliated (SCA) entity reporting when there is a guarantee or commitment to provide financial support.**

- **Proposed revisions adopt, with modification, the disclosure amendments in ASU 2018-13, Changes to the Disclosure Requirements for Fair Value Measurement.**
  - Eliminate information on transfers between level 1 and level 2
  - Eliminate disclosure of policy for determining when transfers between levels occur
  - Calculation of net asset value
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<tr>
<td>2018-41</td>
<td>Appendix D—Nonapplicable GAAP pronouncements</td>
<td>P&amp;C</td>
<td>Revisions reject the following ASUs as not applicable to statutory accounting:</td>
<td>NA</td>
<td>NA</td>
<td>TBD</td>
</tr>
<tr>
<td>2018-42</td>
<td></td>
<td>Life</td>
<td>- ASU 2017-13, Amendments to SEC Paragraphs Pursuant to the Staff Announcement at the July 20, 2017, EITF Meeting and Rescission of Prior SEC Staff Announcements and Observer Comments</td>
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<tr>
<td>2018-43</td>
<td></td>
<td>Health</td>
<td>- ASU 2018-02, Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income</td>
<td></td>
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<tr>
<td>2018-44</td>
<td></td>
<td></td>
<td>- ASU 2018-04, Investments—Debt Securities (Topic 320) and Regulated Operations (Topic 980), Amendments to SEC Paragraphs</td>
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<tr>
<td>2018-45</td>
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<td></td>
<td>- ASU 2018-05, Income Taxes (Topic 740), Amendments to SEC Paragraphs Pursuant to SEC Staff Accounting Bulletin No. 118</td>
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<td></td>
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<td>- ASU 2018-06, Codification Improvements to Topic 942, Financial Services—Depository and Lending</td>
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</table>
The SAPWG also took the following actions, received updates, and provided direction to NAIC staff on the following items:

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<tr>
<td>2018-40</td>
<td>SSAP No. 16R—Electronic data-processing equipment and software</td>
<td>P&amp;C Life Health</td>
<td>Directed NAIC staff to draft proposed revisions to adopt with modification ASU 2018-15, Customer’s Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract, allowing for capitalization and amortization of the implementation costs as nonoperating system software for interim exposure consideration. When subsequent exposure occurs, comments will be requested on whether any of the implementation costs would qualify as operating system software under existing concepts in SSAP No. 16R and if so, whether it would be possible to bifurcate the costs between operating and nonoperating system software.</td>
<td>Y</td>
<td>TBD</td>
<td>TBD</td>
</tr>
<tr>
<td>TBD</td>
<td>Financial Accounting Standards Board (FASB) ASU 2018-12, Targeted improvements to the Accounting for Long-duration contracts</td>
<td>P&amp;C Life Health</td>
<td>NAIC anticipates rejecting ASU 2018-12 for statutory accounting.</td>
<td>NA</td>
<td>NA</td>
<td>TBD</td>
</tr>
<tr>
<td>2016-20</td>
<td>Various SSAPs</td>
<td>P&amp;C Life Health</td>
<td><strong>Substantive</strong> – This item originally exposed a concept paper considering adoption of the US-GAAP guidance included in ASU 2016-13: Credit Losses. • Considers replacing the “incurred loss model” with an “expected credit loss” concept. It should be noted that other statutory elements already consider credit risk (e.g., Risk-Based Capital and the Asset Valuation Reserve). UPDATE: The working group directed additional work and coordination with interested parties prior to further working group discussion. Intent of the concept paper was to consider utilizing an approach similar to the available-for-sale US-GAAP guidance, with the inclusion of a fair value floor.</td>
<td>TBD</td>
<td>TBD</td>
<td>TBD</td>
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This summary was prepared by John Tittle, Lynn Friedrichs, Diane Craanen, and Ed Wilkins. For your comments and suggestions, please contact the authors: johntittle@deloitte.com, jfriedrichs@deloitte.com, d CRAANEN@deloitte.com, or ewilkins@deloitte.com.
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