

## **NAIC Focus : News, Notes and Commentary**

Date February 6, 2012  
Author Connie Jasper Woodroof  
Email connie.woodroof@stoneriver.com

# A Look at 2012

Happy New Year!! Ok, I am a little late using that salutation, but I didn't want to post a new NAIC Focus during January's accounting closing time. But a new year is here and that usually has a lot of us wondering what topics the regulators will be discussing and possibly implementing changes. Looking into my crystal ball, I predict that the following items will be significant in the new year and beyond. Some of these issues, ok, probably most of these issues, will not only be discussed during the upcoming NAIC March meeting, but will be ongoing topics of discussion throughout the year.

### **Solvency Modernization Initiative (SMI)**

The NAIC's Solvency Modernization Initiative continues to move forward. SMI is a sweeping reform project that covers a variety of topics and has already given the industry new Holding Company and Credit for Reinsurance models as well as a process called ORSA (Own Risk Self Assessment).

Work is progressing on new group capital requirements, including possible revisions to the current RBC formulas. The goal is to have a plan of action completed by December 2012. As part of group capital requirements, implementation plans for ORSA also need to be initiated.

Next on our SMI list is review of corporate governance issues, with a goal of adopting solutions to address perceived gaps in the existing corporate governance requirements by November 2012.

Although Principles-Based Reserving (PBR) for Life products has been in the works for several years, it now falls under the umbrella of SMI. The good news, or maybe not, is that the project is nearing completion. The model law has already been adopted and an industry study on the effects of the transition has been completed. The three things left on the PBR "to do" list are all scheduled for 2012 and include the adoption of the Valuation Manual (VM-20), the statistical agent policy decisions, and the implementation plans. Life companies, are you ready for this?

With the adoption of the new Reinsurance models, several follow-up pieces are needed to complete the new reinsurance puzzle. Work will now focus on the development of the CR-F and CR-S forms applicable to certified reinsurers, development of a process to determine which jurisdictions the states can consider as qualified jurisdictions, and the formation of a new NAIC group to provide advisory support to states for the review of reinsurance collateral reduction applications under the new models. All of this is scheduled for completion in 2012.

## **Investment Valuation**

As the economy continues to try to heal itself, regulators continue to initiate measures that allow them a greater comfort level regarding not only the types of investments insurers are making, but the quality and valuation of those investments as well. After recognizing that they might have overreacted in implementing the modified FE process at the end of 2010, the Valuation of Securities Task Force (VOSTF) suspended modified FE requirements for a few investment types at year-end 2011. Now the decision has been made to continue to decipher modified FE problems and consider implementing additional changes.

However, that is just one specific area of interest. Expect the VOSTF to continue working with the NAIC's Securities Valuation Office (SVO) in an effort to learn more about and monitor new investment vehicles and existing investment vehicles that might be heading for problems, much like the mortgage-backed securities for the past few years.

There are two significant projects occurring as the VOSTF headed into their new year. The Task Force has voted to revamp the NAIC's current designations for bonds and preferred stocks. The result will be more tiers of designations to be used by insurers, which may result in new valuation methods for statement reporting. This, in turn, will also mean that all of the risk-based capital formulas (and AVR for the Life companies) will need to have revised factors for bonds and preferred stocks.

The newest project is aimed at broadening the number of SEC recognized NRSROs (Nationally Recognized Statistical rating Organizations) that become NAIC AROs (Acceptable Rating Organization). Currently, an NRSRO wanting to become an NAIC ARO has to complete an application and go through an approval process. During a January conference call, the VOSTF decided to eliminate the approval process, allowing any SEC NRSRO to become an NAIC ARO if they can meet certain process needs, such as being able to download information into the SVO's database. The SVO staff is currently working on the wording to be used in the SVO's *Purpose and Procedures Manual* to implement the new process.

## **Captives and Special Purpose Entities (SPV)**

A newly formed NAIC subgroup for this issue kicked off their new year with a January conference call. Regulators are concerned with the increased use of captives and SPVs to transfer third party insurance risk. The group has been charged with reviewing established state regulations and determining if those requirements are appropriate. The subgroup plans to submit a survey to the state regulators as well as accept comments from others, with a comment deadline of February 20. Those comments will then be discussed at the upcoming March NAIC meeting in New Orleans. From this process, the group hopes to pinpoint specific topics for discussion and to determine if any current NAIC model regulations/statutes need to be revised. They have set the 2012 August NAIC meeting as the goal for having a "draft proposal" available for discussion. A draft proposal? Guess that means changes are imminent!

## **Federal Insurance Office (FIO)**

| [Because of](#) the Dodd-Frank Wall Street Reform and Consumer Protection Act, the FIO was organized to monitor the insurance industry (along with a few other responsibilities), but does not presently have regulatory powers. One of the first undertakings of the FIO was to solicit comments on how the US insurance regulatory system can be modernized and/or improved. Having received its requested input, the director of the FIO, Michael T. McRaith, the former Illinois Director of Insurance, was expected to release the FIO's report to Congress around the end of January. As one can imagine, the received comments cover quite a wide perspective of insurance regulation that needs/does not need

improvement, is handled / not handled well by state regulation, and whether the federal government should/should not become more/less involved. Often five comment letters all covering the same topics, present five different opinions.

Why should we care? As a former US insurance regulator, McRaith brings a wealth of understanding and knowledge to the FIO. Observers are anxious to see what direction his report to Congress will take. There are many issues that could be focused upon in the report, but the bottom line comes down to whether the FIO will eventually lead to more federal involvement in insurance regulation. Yes, I know this is not a new topic of debate. Now, however, there is an "official" resource to lead Congress, not one or two congressman with an agenda. This same Congress could eventually give the FIO regulatory powers. Once again, the industry is in a wait-and-see mode.

### **Accounting Issues**

It is always difficult to predict what, if any, accounting issue will become the "hot topic" of the year, so I will not even attempt that. There are several issues that are definitely on the agenda of the Statutory Accounting Principles Working Group (SAPWG) for the year. Just prior to the end of 2011, SAPWG re-activated work on pensions and other post-retirement benefits. Since this project has been ongoing for about three years, it is hoped the wrap-up process will happen quickly. Although the official agenda for SAPWG for the March NAIC meeting has not yet been released, it is anticipated these two issues will be listed.

Other items that are anticipated to be addressed during March include items that were exposed for comment during the NAIC November 2011 meeting. Those items are revisions to both SSAP Nos. 27 and 56 regarding embedded credit derivatives; changes to SSAP No. 36 for disclosures pertaining to trouble debt restructuring; additions to SSAP No. 35R to prescribe statutory accounting provisions for the annual fee mandated by the PPACA; and modifications to SSAP No. 62R.

The final agenda is usually posted about 30-days before the March meeting, so I am sure there the list will be longer. After all, SAPWG along with the Emerging Accounting Issues Working Group (EAIWG) has a 2.5 hour time block to fill!

### **Statement Changes**

At this time, very few changes have been adopted by the Blanks Working Group (BWG) for 2012 implementation. However, the NAIC has until the end of June to finalize the 2012 statement and if they follow the path of the last two years, most of the changes will be adopted in June during a conference call. Items to be considered for adoption in June, must be submitted to BWG at least 30 days prior to the March NAIC meeting, so they can be exposed for comment during the March meeting. That 30-day cutoff point has not quite arrived yet, so I have no idea how many items there will be for consideration. As always, we will post a discussion of these decisions after the March meeting, as well as after the June conference call.

In March, the NAIC Focus will be posted after the NAIC meeting, which is scheduled from March 3 – 5. Until then, live long and prosper!

*Although StoneRiver, Inc. takes all reasonable steps to ensure that the information in this document is current and correct, it neither warrants nor guarantees its accuracy.*

*StoneRiver, Inc. does not render legal services or advice. This newsletter is not intended to substitute for legal advice, which can be rendered only by an attorney.*

© 2011 StoneRiver, Inc. All rights reserved. StoneRiver is a trademark of StoneRiver, Inc.  
Information is subject to change. Printed in U.S.A. 08/11

2110 Wiley Blvd SW

Cedar Rapids, IA 52404

800-815-7134

[www.stoneriver.com](http://www.stoneriver.com)

[solutions@stoneriver.com](mailto:solutions@stoneriver.com)