

Financial Analysis Handbook

Property/Casualty
Life/A&H
Health
Title

2023 Annual
2024 Quarterly

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ISBN: 978-1-64179-204-2

Printed in the United States of America

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Financial Analysis Handbook

Property/Casualty, Life/A&H, Health

2023 Annual/2024 Quarterly Edition

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Printed in the United States of America

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Date: February 8, 2024
To: Users of the NAIC's *Financial Analysis Handbook*
From: NAIC Staff

This edition of the NAIC *Financial Analysis Handbook* is to be used in conjunction with the 2023 Annual and 2024 Quarterly Financial Statements. The following summarizes the most significant changes since the prior edition:

I. Introduction A. Department Organization and Communication

A reference to the optional memorandum of understanding (MOU) and guidance emphasizes the benefits of early communication in a pre-receivership situation.

III.A.4. Risk Assessment (All Statement Types) – Analyst Reference Guide

Additional guidance was drafted under Depth of Review and Level of Documentation to advise the analyst that in certain situations, it may be appropriate to reference documentation located in another area of the analysis as opposed to duplicating the documentation.

III.A.6. Template for Planning Meeting with Financial Examiner

A new agenda topic was added as guidance to assist in clarifying the role and expectations for the department analyst in participating in certain exam activities, monitoring the status of the exam, and communicating new information about the insurer arising during the examination process.

VI.I. Group-Wide Supervision – Group Capital Calculation (Lead State) – Analyst Reference Guide

Based on a recommendation from the Risk Retention Group (E) Task Force, guidance was added for exempting groups from the group capital calculation to include special considerations for Risk Retention Groups (RRGs).

VI.L. Group-Wide Supervision – Supervisory Colleges Guidance

A reference was added to the Receivership & Insolvency (E) Task Force's template for drafting a resolution plan for internationally active insurance groups within the Supervisory College chapter footnote vi.

Procedures for Addressing Climate Risk

The following revisions incorporate climate change risks in response to a referral from the Climate Risk and Resiliency (EX) Task Force.

III.B.1.a., b., and c. Credit Risk Repository – Annual

III.B.3.a., b., and c. Liquidity Risk Repository – Annual

III.B.4.a., b., and c. Market Risk Repository – Annual

Similar procedures and guidance were added for the Credit, Liquidity, and Market risk repositories for all three statement types (Property & Casualty, Life/A&H, and Health) to ensure that the impact of climate change, energy transition risk, and asset devaluation risk is appropriately considered in ongoing financial analysis on the insurer's invested asset portfolio.

III.B.6.a. Pricing/Underwriting Risk Repository – Property & Casualty Annual

Procedures were added only the Property & Casualty to determine whether concerns exist regarding the insurer's exposure to catastrophic events, including the potential for increased physical losses, due to climate change.

III.B.6.d. Pricing/Underwriting Risk Repository – Analyst Reference Guide – Property & Casualty Annual

Guidance was added to assist analysts in identifying and assessing the insurer's current and prospective exposure to catastrophic events, as well as the risk management practices of insurers writing a significant percentage of their business in products and geographic areas that are exposed to severe loss events.

III.B.9.a. Strategic Risk Repository – Property & Casualty Annual

Procedures were developed in this area similar to Pricing/Underwriting Risk to evaluate the adequacy of the insurer's catastrophic reinsurance coverage at various modeled loss levels, including the potential impact on capital and surplus and its RBC position and the insurer's reinsurance strategy.

Transactions and Service Agreements with Affiliates

In response to a referral from the Risk-Focused Surveillance (E) Working Group guidance was developed for reviewing affiliated service agreements, specifically market-based expense allocations in affiliated service agreements.

III.A.5. Risk Assessment (All Statement Types) – IPS Example

Under Analysis Follow Up, an additional follow-up procedure was added to address any potentially significant unresolved concerns with cost sharing or service agreements with affiliates or significant reliance on affiliates to provide services.

III.B.5.a., b., c., and d. Operational Risk Repository (All Statement Types) and Analyst Reference Guide

V.C. Domestic and/or Non-Lead State Analysis – Form D Procedures

V.F. Domestic and/or Non-Lead State Analysis – Analyst Reference Guide

Procedures and guidance were added to address concerns related to the economic substance of a transaction with affiliates and/or related parties.

Guidance was added to determine whether an agreement with affiliates merits review during an onsite examination.

If you have questions regarding the *Financial Analysis Handbook*, contact Ralph Villegas, Life/A&H Financial Analysis Manager at (816) 783-8411, rvillegas@naic.org, or Rodney Good, Property/Casualty Financial Analysis Manager at (816) 786-8430, rgood@naic.org, or Bill Rivers, Health Financial Analysis Program Manager at (816) 783-8142, wrivers@naic.org.

**PROCEDURES OF THE FINANCIAL ANALYSIS SOLVENCY TOOLS (E) WORKING GROUP IN CONNECTION WITH
PROPOSED AMENDMENTS TO THE *FINANCIAL ANALYSIS HANDBOOK***

The following establishes procedures of the Financial Analysis Solvency Tools (E) Working Group (“the Working Group”) for proposed changes, amendments and/or modifications to the NAIC *Financial Analysis Handbook* (“the Handbook”).

1. The Working Group may consider relevant proposals to change the Handbook at any conference call, interim or national meeting (“the meeting”) throughout the year as scheduled by the Working Group.
2. If a proposal for suggested changes, amendments and/or modifications is submitted to, or filed with, NAIC staff support it may be considered at the next regularly scheduled meeting of the Working Group.
3. The Working Group publishes a formal submission form and instructions that can be used to submit proposals and is available on the Group’s webpage. However, proposals may also be submitted in an alternate format provided that they are stated in a concise and complete format. In addition, if another NAIC committee, task force or working group is known to have considered this proposal, that committee, task force or working group should provide any relevant information.
4. Any proposal that would change the Handbook will be effective for analysis conducted in the year following the NAIC Fall National Meeting (i.e. of the preceding year) in which it was adopted (e.g., a change proposed to be effective January 1, 2025 must be adopted no later than the 2024 Fall National Meeting).
5. Upon receipt of a proposal, the Working Group will review the proposal at the next scheduled meeting and determine whether to consider the proposal for public comment. The public comment period shall be thirty days unless extended by the Working Group. The Working Group will consider comments received on each proposal at its next meeting and take action. Proposals under consideration may be deferred by the Working Group until the following scheduled meeting. The Working Group may form an ad hoc group to study the proposal, if needed. The Working Group may also refer proposals to other NAIC committees for technical expertise or review. If a proposal has been referred to another NAIC committee, the proposal will come off the Working Group’s agenda until a response has been received.
6. NAIC staff support will prepare an agenda inclusive of all proposed changes. The agenda and relevant materials shall be sent via e-mail to each member of the Working Group, interested regulators and interested parties and posted to the Working Group’s webpage approximately 5-10 business days prior to the next regularly scheduled meeting during which the proposal would be considered.
7. In rare instances, or where emergency action may be required, suggested changes and amendments can be considered as an exception to the above stated process and timeline based on a two-thirds majority consent of the Working Group members present.
8. NAIC staff support will publish the Handbook on or about February 1 each year. NAIC staff will post to the NAIC Publications Web site any material subsequent corrections to these publications.

**EXAMINATION OVERSIGHT (E) TASK FORCE
FINANCIAL ANALYSIS SOLVENCY TOOLS (E) WORKING GROUP**

**SUBMIT TO
NAIC – KC
By June 1, 2024**

Financial Analysis Handbook Proposed Revision Form

<u>INSTRUCTIONS</u>	<u>FOR NAIC USE ONLY</u>
<ol style="list-style-type: none">1. Complete this form for EACH Handbook proposal. Under "Identification of Item(s) to be Changed," include section & page number, line or item identifier.2. All attachments should be presented in a format wherein new language is underscored and deletions struck through.3. Please consider whether this revision proposal is also addressed elsewhere in the Handbook.4. CAUTION: before completing this form, please read additional instructions on reverse side of this form.	<u>DISPOSITION</u> <div style="display: flex; justify-content: space-between;"><div style="width: 10%;"><input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/></div><div style="width: 85%;"><div>ADOPTED</div><div>REJECTED</div><div>DEFERRED</div><div>OTHER (SPECIFY)</div><div>_____</div></div></div>
DATE: _____ NAME: _____ TITLE: _____ STATE: _____ ADDRESS: _____ TELEPHONE: _____ CONTACT PERSON : _____	<u>NOTES</u>

HANDBOOK SECTION NAME AND NUMBER TO WHICH PROPOSAL APPLIES

IF STATEMENT TYPE SPECIFIC, ALSO IDENTIFY THE TYPE:

☐ Life/A&H ☐ Property & Casualty ☐ Title ☐ Health

IDENTIFICATION OF ITEM(S) TO BE CHANGED

**REASON OR JUSTIFICATION FOR CHANGE **
(STATE, IN SPECIFIC TERMS, THE BENEFIT TO BE DERIVED FROM THIS PROPOSAL)**

Additional Instructions and Information

The Financial Analysis Solvency Tools (E) Working Group meets via conference call throughout the year to consider proposed changes to the NAIC *Financial Analysis Handbook* (Handbook). Suggestions to the Handbook should be submitted by **June 1, 2024**. Send proposals via email to Ralph Villegas, Life/Health Financial Analysis Manager, rvillegas@naic.org, or send to Rodney Good, Property/Casualty Financial Analysis Manager, rgood@naic.org. Original copies may be sent to:

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Kansas City, MO 64106-2197

For questions, call the Financial Analysis & Examination Unit at (816) 842-3600.

Proposed Revisions

- During the Working Group's review, changes proposed via this form will be considered along with an analysis conducted by the NAIC Financial Analysis & Examination Unit of the effectiveness and usefulness of procedures, ratio limits and language.
- The NAIC Financial Analysis & Examination Unit also studies adopted changes to the Annual Statements and provides revision proposals to the Working Group. The NAIC Financial Analysis & Examination Unit automatically makes changes to the Handbook for minor changes, such as for page and line numbers.
- The Handbooks are automated on i-Site+. The Handbook is intended to be a dynamic tool. The Working Group is interested in feedback on both analytical and software features. Please contact the NAIC Help Desk at (816) 842-3600 before submitting a form. Many enhancements have been proposed which could not be implemented. Also, some proposals may relate to existing features that the Help Desk may be able to explain.

**** This section must be completed on all forms.**

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Preface

The NAIC *Financial Analysis Handbook* (Handbook) was developed and released by the Financial Analysis Handbook Working Group (n.k.a. Financial Analysis Solvency Tools Working Group) of the Examination Oversight (E) Task Force in 1997 for Property/Casualty and Life/A&H, and in 2004 for Health. In 2017, the Handbook was revised to incorporate a risk-focused framework approach for financial analysis. This analysis framework identifies and assesses risks based on the nine branded risk classifications to complete and document an overall assessment of the financial solvency condition of the insurer and insurance holding company group.

The Handbook does not include state-specific information or regulations and does not establish guidelines that insurance companies must follow. Parameters or benchmarks utilized are not regulatory requirements to be complied with by insurance companies.

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I.

Introduction

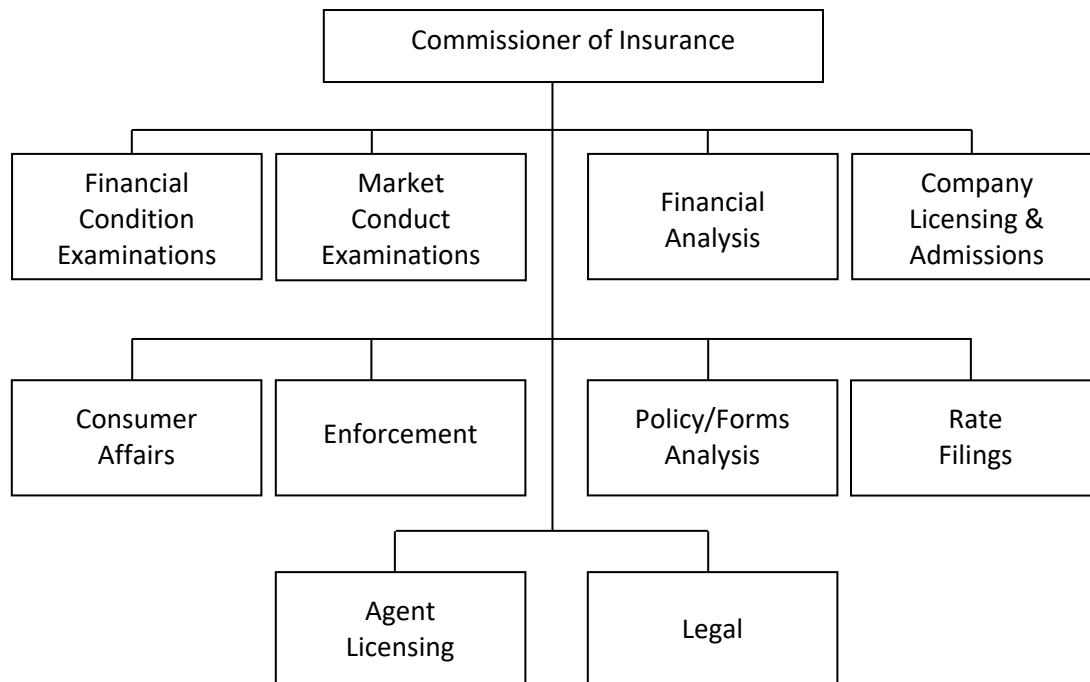
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- B. Interstate Communication and Cooperation
- C. External Information
- D. NAIC Information
- E. SAP vs. GAAP
- F. Prioritization of Work

I. Introduction A. Department Organization and Communication

Organization Chart

The organizational structure of a state insurance department varies by state. There are several basic functions that are performed by all departments. It is important for the analyst to understand the purpose of each function and the information obtained that may assist the analyst in the financial monitoring and solvency surveillance process. Due to the variance in organizational structure, the chart below depicts typical state insurance department functions rather than trying to highlight a typical organizational structure.

Chart of State Insurance Department Functional Units



In many states, more than one of the above functions may be performed or supervised by the same individuals. For example, the financial analysts may also perform financial examinations, and financial examiners may also perform market conduct examinations. Additionally, some state insurance departments rely on the Attorney General's office for legal assistance rather than having separate department counsel.

Risk-Focused Financial Condition Examinations

The insurance code in most states allows the state insurance department to examine insurers as often as the insurance commissioner deems appropriate and requires that each insurer be examined at least once every three to five years (as determined by each state). Risk-focused financial condition examinations performed by the state insurance departments include full-scope periodic examinations and limited-scope or targeted examinations, which focus on the review and evaluation of an insurer's business process and controls (including the quality and reliability of corporate governance) to assist in assessing and monitoring its current financial condition and prospective solvency. Through the risk-focused financial condition examinations, the state insurance department gains knowledge about all aspects of the insurer, including its risk management practices and key business activities, which can be useful information to incorporate into the department's ongoing solvency analysis.

The results of a financial condition examination are documented in an examination report that assesses the financial condition of the insurer and sets forth findings of fact (together with citations of pertinent laws, regulations and rules) with regard to any material adverse findings disclosed by the examination. Examiners complete Exhibit AA – Summary Review Memorandum (SRM), or something similar, at the conclusion of the

I. Introduction A. Department Organization and Communication

exam. The SRM includes discussion of potential ongoing or prospective solvency concerns, corporate governance, examination adjustments, risk mitigation strategy issues, report findings, management letter comments, responses to issues raised by financial analysts, subsequent events, and other residual risks the examiner may want to communicate to state insurance department personnel. The SRM is a useful tool to communicate information and findings to the analyst, chief examiner, and other state insurance regulators. The final section of the SRM, prioritization level and changes to the supervisory plan, provides discussion of the examiner's overall conclusions regarding ongoing monitoring, including specific follow-up recommended to the analyst.

Additionally, key documents should be available to analysts, including examination reports and management letter comments, which may also include corrective actions required to be taken by the insurer and/or recommendations for improvements.

Market Conduct Examinations

The market conduct examination focuses on such areas as sales, advertising, rating, and the handling of claims. Market conduct examinations evaluate an insurer's business practices and its compliance with statutes and regulations relating to dealings with policyholders and claimants. The results of a market conduct examination are documented in an examination report, which summarizes examination findings so that the insurer's performance can be assessed. The report may also recommend a corrective action to deal with significant problem areas. Because financial conditions and market conduct problems are often interrelated, the examinations are frequently conducted simultaneously. Market conduct examinations are conducted by financial condition examiners in many of the states, usually an impact of the size of the state insurance department.

Risk-Focused Financial Analysis

Risk-focused financial analysis provides continuous off-site monitoring of the state's domestic insurers' financial condition, significant internal/external changes relating to all aspects of the insurer, maintains a prioritization system, provides input into the state insurance department's priority of each insurer, works with the examination staff to develop an ongoing Supervisory Plan and updates the Insurer Profile Summary (IPS), providing department management with timely information of significant events relating to the domestic insurers in assessing prospective risks. The analyst should refer to all available information to monitor the insurer's statutory compliance and solvency on a continuous basis in coordination with the periodic on-site field examination process. As part of the analysis process and the review of the examination report and summary review memorandum, the analyst should incorporate into his/her analysis information gained about the corporate governance and risk management processes of the insurer. If desired, regulators can request the IPS, if applicable, for non-domestic insurers from the domestic or lead state.

As a result of concerns identified during the risk-focused financial analysis process, the insurance department may take a variety of actions, including but not limited to contacting the insurer seeking explanations or additional information, obtaining the insurer's business plan, requiring additional interim reporting from the insurer, calling for a targeted or limited-scope financial condition examination, engaging an independent expert to assist in determining whether a problem exists, meeting with the insurer's management, obtaining a corrective plan from the insurer, and/or restricting, suspending, or revoking an insurer's Certificate of Authority.

Financial Analyst Salary Guidelines

The compensation guidelines in this section of the Handbook were developed in recognition of the importance of compensation particularly as it affects an Insurance Department's ability to hire and retain well-qualified employees. The guidelines were developed based on surveys of analyst pay across Insurance Departments, as well as external comparisons to other similar professions, including other financial regulators, internal auditors

I. Introduction A. Department Organization and Communication

and external auditors. In using the information below, the following are brief descriptions of the associated positions listed:

Financial Analyst

Financial analysts are responsible for conducting a risk-focused financial analysis on assigned insurers under the supervision of an analyst supervisor. The financial analyst reviews annual and quarterly insurer financial statements and all related supplemental regulatory filings to assess and monitor the current financial condition and prospective financial solvency of insurance companies.

Senior Financial Analyst

Senior financial analysts are responsible for conducting a risk-focused financial analysis on assigned insurers under the supervision of the supervising analyst. The senior financial analyst reviews annual and quarterly insurer financial statements and all related supplemental regulatory filings to assess and monitor the current financial condition and prospective financial solvency of more complex and higher priority insurance companies. Senior financial analysts may also be asked to provide guidance, support and training to financial analysts.

Supervising and Assistant Chief Analyst

A supervising or assistant chief analyst is responsible for supervising the financial analysts and senior financial analysts conducting a risk-focused financial analysis on assigned insurers. This position provides input on technical matters, acts as a reviewer of the work performed by the financial analysts and senior financial analysts, and ensures that analyst work is an appropriate execution of the risk-focused analysis approach.

Chief Analyst

This position is responsible for overall staff performance and development and should serve as the department's main point of contact for analysis and ongoing monitoring of regulated entities. This position should oversee company assignments and priority ratings. This position should work under the general direction of a commissioner or deputy commissioner and should oversee a consistent risk-focused financial analysis process across the department.

Use of Salary Tables

The salary tables included below generally require certain adjustments before being applied by a state or jurisdiction in setting analyst compensation. Factors to consider in setting analyst compensation include:

- Specific job responsibilities and expectations
- Location or market-based adjustments
- Complexity of industry
- Specialization requirements (e.g., reinsurance/investment/information technology [IT] specialist)
- Travel expectations (including consideration of amount of travel and in consideration of work from home or other similar arrangements)
- Retirement and other benefits (not included in table)

Position	Salary Range	
	Low End	High End
Financial Analyst	\$52,000	\$85,000
Senior Financial Analyst	\$64,500	\$105,000
Supervisor/Assistant Chief Analyst	\$87,000	\$150,000
Chief Analyst	\$100,000	\$170,000

Note: The data above is based on a national average and is not appropriate to be applied to all locations without consideration of market and cost of living variances.

I. Introduction A. Department Organization and Communication

Company Licensing and Admissions

An insurer that wishes to obtain a Certificate of Authority to write business in a state must generally complete an application indicating the line(s) of business it plans to write and submit the application (along with other information, including the most recent Annual Financial Statement, Audited Financial Report, Actuarial Opinion, etc., to support its financial condition of the insurer) to the insurance department for review and evaluation. In addition, insurance departments frequently request information supporting the insurer's experience and expertise in writing the line(s) of business requested, background information regarding the insurer's management and board of directors, a business plan, and a multi-year pro-forma financial projection. After reviewing this information and any other information obtained, the insurance department makes a determination on whether to issue a Certificate of Authority.

The Uniform Certificate of Authority Application, also known as the UCAA or Uniform Application, is a process designed to allow insurers to file copies of the same application for admission to numerous states. The National Treatment and Coordination (E) Working Group currently maintains and updates the UCAA application. Each state that accepts the UCAA is designated as a uniform state. While each uniform state still performs its own independent review of each application, the need to file different applications in different formats has been eliminated for all states that accept the uniform application. The Uniform Application is available to any insurer in good standing with its domiciliary state, regardless of size. Currently, all 50 states and the District of Columbia are uniform.

The UCAA includes three applications. The Primary Application is for use by newly formed companies seeking a Certificate of Authority in their domicile state and by companies wishing to re-domesticate to a uniform state. The Expansion Application is for use by companies in good standing in their state of domicile that wish to expand their business into a uniform state. The Corporate Amendments Application is for use by an existing insurer for requesting amendments to its certificate of authority.

Consumer Affairs

Consumer Affairs is responsible for developing and distributing information regarding insurance products and the insurance industry to consumers. Consumer Affairs is also generally responsible for addressing complaints filed with the insurance department by policyholders and claimants against insurers and agents. Detailed statistics regarding complaints, both in number and type of complaint, and the resolutions may be maintained as a part of this function. Complaints are recorded on the Complaints Database System if filed with the NAIC.

Enforcement

Punitive actions taken against companies, agents, and other licensees found to be in violation of the insurance code are handled by the enforcement function. This function issues orders, and levies fines and other penalties based on the results of investigations performed by other functions within the insurance department. Detailed records are maintained by the department on all regulatory actions taken against companies, agents, and other licensees. In addition, regulatory actions are also recorded in the Regulatory Information Retrieval System (RIRS) database if filed with the NAIC.

Policy/Forms Analysis and Rate Filings

Every state requires an insurer to file policy forms for most lines of business for review and/or approval prior to selling the policies. The primary purpose of this review is to determine statutory compliance regarding policy provisions and benefits.

Information regarding premium rates, including actuarial rate development assumptions, is generally required to be filed with the insurance department for certain lines of business. Some states are "file and use" states, which allow insurers to begin selling policies at the rates filed as soon as the filing is made. In other states, rates

I. Introduction A. Department Organization and Communication

must be approved by the insurance department prior to use by the insurer. Rate filings, including the actuarial assumptions, are reviewed for reasonableness and statutory compliance as a part of this function.

The NAIC's System for Electronic Rate and Form Filing (SERFF) is an electronic platform used by industry for form submittal, document management and state insurance regulatory review that accelerates the pace of market-entry for new and renewing products, while ensuring compliance with consumer protection requirements. The NAIC's Speed to Market (EX) Working Group governs the SERFF product.

Agent/Producer Licensing

Agents must be licensed by the insurance department in order to write business in the state. The agent licensing function administers tests for agents, reviews new and renewal applications from agents, and performs background checks on agents. In addition, many states have continuing education requirements for agents, and agent licensing monitors compliance with these requirements. Detailed records of licensed agents are maintained by agent licensing, including information regarding the insurers for which the agents produce business.

The National Insurance Producer Registry (NIPR) is a nonprofit affiliate of the NAIC. NIPR developed and implemented the Producer Database (PDB) and the NIPR Gateway. The PDB is an electronic database consisting of information relating to insurance agents and brokers (producers). The PDB links participating state regulatory licensing systems into one common repository of producer information. The PDB also includes data from the RIRS to provide a more comprehensive producer profile. The NIPR Gateway is a communication network that links state insurance regulators with the entities they regulate to facilitate the electronic exchange of producer information.

Legal

Legal is generally involved in the review of proposed changes of control of insurers and other holding company transactions and frequently supports the other functions. Legal may also draft statutes and regulations to assist the insurance department in regulating insurers, agents, and other licensees; hold administrative hearings between the commissioner and insurers, agents, and other licensees; and represent the department in judicial and other proceedings.

Intra-Departmental Communication

Communication with other divisions or areas within the state insurance department on a timely basis is an important element of effective solvency surveillance and is essential to the coordination of results of the risk-focused surveillance approach. Upon identifying a problem or concern during the risk-focused financial analysis process, the financial analyst should communicate this information to other divisions within the department. In addition, other divisions within the department should communicate certain information to the financial analyst so that the analyst has all of the relevant information available regarding the insurer being analyzed. (Refer to the example of an IPS in the Analyst Reference Guide for Risk Assessment.)

To assist in the coordination of risk-focused financial condition examination, state insurance regulators use the NAIC's Financial Exam Electronic Tracking System (FEETS). FEETS allows state insurance regulators to call an examination of a multistate insurer, facilitate coordination via various functionality within the program, communicate the completion of an examination, and share the completed version of the state insurance department's examination report. Use of FEETS on iSite+ is required by the NAIC when calling examinations on multistate insurers and is recommended for all examinations.

Communication from the Financial Analyst to Financial Examiners

The analyst may identify concerns as a result of the risk-focused financial analysis process that, when communicated to the financial condition examinations division, may lead to a targeted or limited scope financial condition examination. In addition, since the risk-focused analysis and examinations are interactive processes, the analyst should be familiar with the insurer's current financial condition; including any changes in its operations since the last periodic financial condition examination as well as the insurer's exposure to branded risks, which include prospective risks.

In communicating information to the examiners for examination planning, the analyst should review the examiner's Exhibit B – Examination Planning Questionnaire to note any items already accumulated and provide access to relevant information that has already been obtained by the analyst function and is available at the state insurance department.

Communication between examiners and analysts should occur for examination planning and at the conclusion of the examination. Specifically, regarding exam planning, results of ongoing analysis procedures should be shared with the financial examiners to assist in examination planning through a coordination meeting. An email exchange alone, between analyst and examiner, is not considered sufficient communication in planning an examination. During the preplanning process of each examination, the analyst should communicate areas of concern and specific issues to address during the examination. To assist in communication, the analyst should provide a current copy of the, IPS as well as other supporting analyst work papers and other documentation already on file at the department to communicate current or prospective concerns or observations and suggested procedures.

Regarding exam follow-up the financial analyst should participate in a collaborative follow-up meeting or conference call at the end of the examination to discuss the following:

- Examination results and/or findings
- Insurer's prioritization level
- Ongoing supervisory plan and the completed Summary Review Memorandum
- Re-assessment of branded risks as contained in the IPS

Such information may be shared by providing and discussing the current IPS, as well as other supporting analysis documentation necessary to support the branded risk assessment or other issues noted in the analysis. Statutory violations identified as a part of the analysis should be communicated to the enforcement division for the issuance of appropriate penalties and/or corrective orders against the insurer. Additionally, solvency related concerns, when communicated to the legal division, may result in the restriction, suspension, or revocation of an insurer's Certificate of Authority.

The avoidance of redundancy in the risk-focused analysis and examination is of critical importance for an enhanced and more efficient overall regulatory process that will benefit both regulators and industry. An efficient regulatory process fosters clarity and consistency, which results in a better understanding of how individual insurers operate across the different aspects of the regulatory spectrum, including the areas of financial analysis, financial examination and other solvency-related regulation.

The information that insurers submit to the insurance department which are received and reviewed by the analysts as well as the analysts' final work product should be documented in a clear and consistent format that can be easily understood and utilized by analysts, their supervisors, and financial examination staff. In particular, workpapers supporting and summarizing the analysts' risk-focused analysis, an outline of mapping of what documentation was reviewed and a summary of conclusions reached, i.e., an updated Insurer Profile Summary, should be maintained in a manner that can be easily shared and discussed during the pre-examination planning meeting with the examiner.

I. Introduction A. Department Organization and Communication

Refer to the III.A.4 Analyst Reference Guide for further guidance on communication between analysts and examiners.

Communication from Other Divisions or Areas to the Financial Analyst

In addition to intra-department communication, which originates within the financial analysis division, it is equally important that the department's procedures be designed to ensure relevant information and data received by the other divisions within the department be directed to the financial analysis division. The following are some examples of information or data that may be received by other divisions within the department (including an indication of the functional unit that would likely have received the information or data), which should be directed to the financial analysis division for consideration as a part of the financial analysis process:

1. Information from Risk-Focused Financial Examination:
 - a. If recently completed, the SRM, financial condition examination reports and management letter comments that include significant adjustments to the financial information reported to the department, corrective actions required to be taken by the insurer, and/or recommendations for improvements based on examination results. (See above)
 - b. If an examination is in progress, communication from examination staff should include information on the planning, progress and preliminary findings, based on the phase of the examination Risk-Focused Financial Examination.
 - c. Any relevant information obtained in planning the financial examination stage.
2. Market conduct examination reports containing corrective actions required to be taken by the insurer as a result of violations in sales, advertising, rating, and/or claim practices, which might be an indication of financial problems or lead to the risk of financial losses through class action suits or regulatory fines (market conduct examinations).
3. An increase in the number or type of complaints filed by policyholders, claimants, employees, agents, or third parties that could indicate liquidity or internal control problems (consumer affairs).
4. Corrective orders and other regulatory actions taken against an insurer and fines and penalties levied (enforcement).
5. New policy form filings or expansion into new lines of business, including high-risk and long-tail lines of business, which might imply planned rapid growth to obtain premiums in order to improve liquidity or cover prior losses (policy/forms analysis).
6. Requests for significant premium rate increases, which might be an indication of insufficient rates to cover losses and expenses in the past (rate filings).
7. An increase in the licensing of agents, including managing general agents or third-party administrators, which could indicate planned rapid expansion or relaxed underwriting standards (agent licensing).
8. The use of managing general agents or third-party administrators, which might be an indication that the insurer is not in control of its operations (agent licensing).
9. Information that management personnel of an insurer (including officers, directors, or any other persons who directly or indirectly control the operations of the insurer) fail to possess and demonstrate the competence, fitness, and reputation deemed necessary to serve the insurer in such a position (legal).
10. The unexpected resignation of an insurer's officer(s), director(s), or other key management personnel, which might indicate internal turmoil or dissatisfaction with the insurer's goals or operating practices (legal).

I. Introduction A. Department Organization and Communication

Intra-Department Communication System

Intra-department communication in most state insurance departments is primarily informal due to the size of the department and the location of personnel. The commissioner may hold periodic meetings with the division heads to discuss current developments and concerns in each division. In some states, division heads prepare monthly activity reports highlighting current developments which are circulated to the other divisions within the department. Departments should have a formal structured mechanism to assure appropriate ongoing intra-department communication. Adequate controls should be implemented to assure that recommendations, decisions, actions, and results are effectively communicated and documented. Among the key objectives of a department's intra-department communication system are the following:

1. Key insurance department officials should possess all relevant information to permit decisions to be made on a timely basis.
2. The department should assure that all levels of staff have the appropriate knowledge, information, and feedback to effectively perform the assigned functions.
3. Managers within various functional units or divisions should be responsible for the proper internal communications and documentation of decisions and actions taken under their authority.
4. The department should establish procedures to assure that orders and directives are effectively communicated to the appropriate staff and that the staff observes such orders and directives.

Considerations for Troubled Insurance Companies

In troubled or potentially troubled insurance company situations, proactive and timely communication to the appropriate persons within the department and with non-domiciliary state departments (for multistate companies) is critical. It is also important that the non-domiciliary state communicate with the domestic regulator prior to taking any action against the insurer. In certain circumstances, it may also be appropriate to communicate certain information with other parties (e.g., other regulatory bodies, company management, state guaranty funds, etc.). Establishing a coordinated communication system among the relevant parties will help facilitate the domestic regulator's surveillance of the troubled or potentially troubled insurance company. The *Troubled Insurance Company Handbook* (regulator only) provides additional guidance to assist in enhancing a state's monitoring and surveillance of troubled insurance companies, including communication and coordination of troubled or potentially troubled insurance companies.

At some point, the insurance department may determine that a corrective action plan cannot be implemented or completed successfully. Under these circumstances, the department may determine that the appropriate course of action is to place the troubled company in receivership. The *Troubled Insurance Company Handbook* outlines specific steps the department should take at all times during the development and implementation of a corrective action plan to prepare itself for this eventuality. This includes knowledge and control over the company's assets, determining and reviewing the company's obligations, operational considerations, information gathering, data/IT systems, other jurisdiction/regulatory considerations, etc. In addition to the *Troubled Insurance Company Handbook*, the *Receiver's Handbook for Insurance Company Insolvencies*¹ provides detailed information and guidance regarding pre-receivership considerations. Both handbooks emphasize the benefits of early communication in a pre-receivership situation. The handbooks offer state insurance regulators tools and best practices for communication and coordination with other relevant parties in a pre-receivership situation, including other state insurance departments, federal and international regulatory authorities, guaranty associations, etc. Examples of tools include checklists to assist in the takeover phase of the

¹ The *Receiver's Handbook for Insurance Company Insolvencies* is available on the NAIC website at: <https://content.naic.org/sites/default/files/publication-rec-bu-receivers-handbook-insolvencies.pdf>.

I. Introduction A. Department Organization and Communication

receivership process and an optional memorandum of understanding template for advance communication with guaranty associations in a property/casualty (P/C) liquidation.ⁱⁱ

ⁱⁱ The optional memorandum of understanding template is available on the NAIC website at: https://content.naic.org/sites/default/files/inline-files/2022_PreLiquidation_PC_MOU.docx.

I. Introduction B. Interstate Communication and Cooperation

Coordination of Regulatory Efforts

The operations of an insurance company often are not limited to one jurisdiction. Therefore, state insurance departments need to coordinate its regulatory efforts with those of other state insurance departments where its insurers do business. The *Troubled Insurance Company Handbook* states that opportunities to coordinate efforts should be sought throughout the entire process, from the monitoring and surveillance of insurers through regulatory actions regarding identified troubled insurers. Coordinated activities may take various forms, including:

- Communication of information regarding the troubled company with other departments through established department procedures
- Participation in coordinated examinations
- Lead states coordination in situations involving troubled insurance groups with affiliated insurers
- Assignment of specific regulatory tasks to different insurance departments to achieve efficiency and effectiveness in regulatory efforts and to share personnel resources and expertise
- Establishment of task forces consisting of personnel from various insurance departments to carry out coordinated actions

Additionally, in some cases, coordination on nonfinancial issues may also be necessary. This is quite common when dealing with health entities because regulatory agencies, such as the federal Centers for Medicare & Medicaid Services (CMS), maintain authority in dealing with issues related to Medicare and Medicaid products and certain comprehensive health care issues under the federal Affordable Care Act (ACA).

Accreditation Standards and Guidelines

The NAIC Financial Regulation Standards and Accreditation Program indicates that a state insurance department should generally follow and observe the procedures set forth in the *Troubled Insurance Company Handbook*. The *Troubled Insurance Company Handbook* provides guidance regarding communication with other state insurance departments about domestic insurers identified as troubled. Once the department has identified an insurance company as troubled or potentially troubled, the department should 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.

Regulatory Information

The department should establish and implement procedures to ensure that regulatory actions are reported to the Regulatory Information Retrieval System (RIRS), summary information on consumer complaints is reported to the Complaints Database System (CDS), and that the status of receivership actions is reported to the Global Receivership Information Database (GRID). These databases are discussed in more detail in section I.D. NAIC Information.

Interdepartmental Communication

Effective interdepartmental action requires timely and effective communication among the various state insurance departments. Insurance departments should develop methods of multilateral communication in order to coordinate the prompt sharing of pertinent information regarding troubled insurers that may impact other jurisdictions. Open lines of communication may provide additional information to a department to assist in its surveillance, as well as provide information to other state insurance departments. Such communications should be established to foster cooperation among the various state insurance departments, so that each department

I. Introduction B. Interstate Communication and Cooperation

works toward the satisfactory resolution of all troubled insurer situations, regardless of the insurer's domicile, license, or operating status. Communications to other state insurance departments regarding troubled insurers should be made in an atmosphere of appropriate confidentiality. Knowledge by outsiders of actual or contemplated regulatory activities may cause undue negative consequences to the insurer (e.g., cancellation of policies or unavailability of reinsurance coverage), which may diminish the insurer's ability to receive assistance or to remain solvent.

The *Troubled Insurance Company Handbook* indicates that the effects on policyholders in all jurisdictions that may result from the actions of a department should be considered. Although the department should consider any adverse consequences that could possibly result from making certain information known to other state departments, those possible disadvantages may be outweighed by the advantages gained from sharing information and working with the other state insurance departments.

An insurance department may go beyond routine communications to allow other departments to participate in decision-making activities related to an insurer that operates in more than one jurisdiction. Any such joint action depends on the nature of the decisions to be made and the relative impact on a particular jurisdiction. However, cooperation of this nature can significantly improve communications between departments, and the resulting increased knowledge of the insurer's condition and circumstances can lead to more effective regulatory action.

The NAIC and its various committees, task forces, and working groups may also provide a means for facilitating coordination and communication among the various departments. For example, the NAIC Financial Examiners Coordination (E) Working Group promotes coordination by assisting and advising domiciliary regulators and exam coordination states as to what might be the most appropriate regulatory strategies, methods and actions regarding financial examinations of holding company groups. The Financial Analysis (E) Working Group functions as a peer review by identifying insurance companies of national significance that are or may be financially troubled and determining whether appropriate regulatory action is being taken. The NAIC may also assist in organizing and facilitating other cooperative regulatory efforts, such as the formation of working groups to address specific troubled insurance company situations.

Redomestication and Acquisition—Communication of Regulatory Actions and Analysis

Communication between states in situations where a company has redomesticated or is being acquired by a party that owns other insurers since the last annual analysis is an important step in conducting effective solvency oversight. In addition to the review of the application for redomestication or Form A, the state insurance regulator should engage the domestic state insurance regulator of the former state in the case of redomestication or the lead state or domestic state(s) of other insurers in the new group in the case of Form A in communication to request the Insurer Profile Summary (IPS), supervisory plan and other relevant solvency monitoring information to effectively incorporate insights from the other domestic state's supervisory plan into the current analysis. In these situations, it is imperative that state insurance regulator concerns and supervisory plans be appropriately transitioned to avoid losing regulatory insights accumulated over years of oversight. Communication should include (but not be limited to) such items as:

- IPS and supervisory plan, including analysis detail for significant risks
- History of regulatory actions
- History of communication with the insurer/group
- Assessment of senior management, board of directors and corporate governance
- Findings (i.e., Summary Review Memorandum (SRM), exam report and management letter) from the most recent financial and market conduct examinations, including the status of the resolution to issues identified
- Assessment of Enterprise Risk Management (ERM), including risks from Form F that are provided in the GPS or provided by the lead state

I. Introduction B. Interstate Communication and Cooperation

- Group Profile Summary (GPS) and Supervisory Plan from the holding company analysis, including detail on any significant risks obtained from the lead state Assessment of Own Risk and Solvency Assessment (ORSA) Summary Report, if applicable.

In situations where the company seeking redomestication is considered a priority company (i.e., NAIC 1 or 2) by the current domestic state, the department should communicate the company's intent to redomesticate with all licensed states prior to approval. This type of communication will ensure that all licensed states are informed of the company's plan and encourage an open dialogue between all interested regulators as part of the approval process.

I. Introduction C. External Information

In addition to the NAIC information, there are a number of external sources of information available credit rating agencies, industry analysts and external news sources. The analyst should refer to these sources of information in order to increase his or her knowledge of the insurer's financial position and to corroborate the financial information filed by the insurer with the NAIC and state insurance departments. These sources of information are all available through direct purchase or subscription order from the credit rating agencies and/or industry analysts. Following is a discussion of a few of the major sources of external information available.

Credit Rating Agencies

There are ten credit rating agencies currently registered with the U.S. Securities and Exchange Commission (SEC) as Nationally Recognized Statistical Rating Organizations (NRSROs) under the Credit Rating Agency Reform Act of 2006. Each has its own unique methodology for assigning ratings. The rating agencies also produce other types of financial information that may be helpful to the analyst. The following is a current list of NRSROs and the classes of ratings for which the rating agency is currently registered. Specific details on the rating agency's rating methodology and other types of financial information available can be found on the agency's Website.

Rating Agency	Classes of Ratings
A.M. Best Rating Services, Inc. www.ambest.com	<ul style="list-style-type: none"> • insurance companies • corporate issuers • issuers of asset-backed securities
DBRS, Inc. www.dbrsmorningstar.com	<ul style="list-style-type: none"> • financial institutions • insurance companies • corporate issuers • issuers of asset-backed securities • issuers of government securities
Demotech, Inc. www.demotech.com	<ul style="list-style-type: none"> • insurance companies
Egan-Jones Ratings Company www.egan-jones.com	<ul style="list-style-type: none"> • financial institutions • insurance companies • corporate issuers
Fitch Ratings, Inc. www.fitchratings.com	<ul style="list-style-type: none"> • financial institutions • insurance companies • corporate issuers • issuers of asset-backed securities • issuers of government securities
HR Ratings de Mexico, S.A. de C.V. www.hrratings.com	<ul style="list-style-type: none"> • financial institutions • corporate issuers • issuers of government securities
Japan Credit Rating Agency, Ltd. www.jcr.co.jp	<ul style="list-style-type: none"> • financial institutions • insurance companies • corporate issuers • issuers of government securities
Kroll Bond Rating Agency, Inc. www.krollbondratings.com	<ul style="list-style-type: none"> • financial institutions • insurance companies • corporate issuers • issuers of asset-backed securities • issuers of government securities
Moody's Investors Services, Inc. www.moodys.com	<ul style="list-style-type: none"> • financial institutions • insurance companies • corporate issuers • issuers of asset-backed securities • issuers of government securities
S&P Global Ratings www.standardandpoors.com	<ul style="list-style-type: none"> • financial institutions • insurance companies • corporate issuers • issuers of asset-backed securities • issuers of government securities

Other rating organizations not registered as NRSROs may provide useful information to the analyst in addition to a NRSRO ratings report, or when a rating is not provided by a NRSRO. An example of a non-NRSRO would be Weiss Ratings, LLC.

I. Introduction C. External Information

Industry Analysts

In addition to the rating agencies, many of the investment houses and stock research firms do considerable research on the insurance industry. The following paragraphs briefly describe several sources.

1. **Investment Houses** — The major Wall Street firms dedicate considerable resources toward researching insurance industry issues. In general, much of this research is oriented towards emerging issues facing the industry. Specific insurance company research is also available but is generally limited to companies with publicly traded debt or equity securities.
2. **Ward's Results** — Annually, Ward Financial Group publishes a financial reference series entitled *Ward's Results*, available in separate Life, Health & Annuity and Property/Casualty editions. The books include financial benchmarks for U.S. domiciled insurers, including unique peer group benchmarks. Each company is grouped into peer groups that consider the insurer's asset size, premium volume, geographic mix of business and ownership structure. In addition to peer group benchmarks, the books also include top performing stock company and mutual company benchmarks.

Securities and Exchange Commission Filings

Insurers that offer debt or equity securities to the public must register with the SEC and fulfill various reporting requirements. Where applicable, the various SEC filings provide significant background information about the insurer and can assist the analyst in corroborating the information filed by the insurer with the NAIC or state insurance departments. Most of the filings are available through SEC's Electronic Data Gathering Analysis and Retrieval (EDGAR) system via the SEC's website (www.sec.gov) at no charge, as well as on CD-ROM. While the SEC filing requirements are quite comprehensive, the following summarizes three of the SEC filing forms that may be of particular interest to the analyst.

1. **Form 10-K** is used to fulfill the SEC's annual reporting requirements. The 10-K must be filed with the SEC within 90 days after the company's year-end for a non-accelerated filer. Accelerated filers must file the 10-K 60 or 75 days after their fiscal year-end, depending on whether they are considered a large filer. Information incorporated into the 10-K includes:
 - Item 1 – Business
 - Item 1A – Risk factors
 - Item 1B – Unresolved staff comments
 - Item 2 – Properties
 - Item 3 – Legal proceedings
 - Item 4 – Mine safety disclosures
 - Item 5 – Market for registrant's common equity, related stockholder matters and issuer purchases of equity securities
 - Item 6 – [Reserved]
 - Item 7 – Management's discussion and analysis of financial condition and results of operations
 - Item 7A – Quantitative and qualitative disclosures about market risk
 - Item 8 – Financial statements and supplementary data
 - Item 9 – Changes in and disagreements with accountants on accounting and financial disclosure
 - Item 9A – Controls and procedures

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- Item 9B – Other information
 - Item 9C – Disclosure regarding foreign jurisdictions that prevent inspections
 - Item 10 – Directors, executive officers and corporate governance
 - Item 11 – Executive compensation
 - Item 12 – Security ownership of certain beneficial owners and management and related stockholder matters
 - Item 13 – Certain relationships and related transactions, and director independence
 - Item 14 – Principal accountant fees and services
 - Item 15 – Exhibits and financial statement schedules
 - Item 16 – Form 10-K summary
2. **Form 10-Q** is used to fulfill the SEC's quarterly reporting requirements. The 10-Q must be filed with the SEC within 40 days for an accelerated filer and 45 days for a non-accelerated filer after the end of each of the first three fiscal quarters and must include a condensed income statement, a condensed balance sheet, and an abbreviated statement of cash flow.
3. **Form 8-K** is used to report material events or corporate changes that have not yet been reported. The 8-K is required after any of the following events occur (see SEC website for a complete list):
- Section 1: Registrant's Business and Operations
 - Entry into or Termination of a Material Definitive Agreement
 - Bankruptcy or Receivership
 - Section 2: Financial Information
 - Completion of Acquisition or Disposition of Assets
 - Results of Operations and Financial Condition
 - Material Impairments
 - Section 3: Securities and Trading Markets
 - Notice of Delisting
 - Material Modification to Rights of Security Holders
 - Section 4: Matters Related to Accountants and Financial Statements
 - Changes in Registrant's Certifying Accountant
 - Section 5: Corporate Governance and Management
 - Changes in Control of Registrant
 - Departure of Directors or Certain Officers; Election of Directors; Appointment of Certain Officers; Compensatory Arrangements of Certain Officers
 - Amendments to Articles of Incorporation or Bylaws; Change in Fiscal Year

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Other External Research and News Sources

In addition to the specific sources referenced above, other resources that provide updates about the industry and specific insurers include:

- *BestWeek*
- *Best Review*
- *Bloomberg Financial*
- *Business Insurance*
- *Factiva*
- *Insurance Journal*
- *National Underwriter*
- *The Wall Street Journal*
- Individual company websites

I. Introduction D. NAIC Information

In addition to the external information discussed in the previous chapter, there is a considerable amount of information available from the NAIC to assist the analyst in analyzing insurance companies. Most insurers are required to file Annual and Quarterly Financial Statements with the NAIC. Much of the information available from the NAIC is based on data included in these filings, which is made available on the Financial Data Repository. In addition, other NAIC databases contain information input by the various state insurance departments regarding regulatory actions taken against insurers, regulatory concerns about insurers or individuals, and consumer complaints filed against insurers. Following is a discussion of the more significant information available to the analyst from the NAIC.

Financial Analysis Solvency Tools

Financial Analysis Solvency Tools (FAST) is a collection of analytical tools within the Insurance Regulatory Information System (IRIS) designed to provide state insurance departments with an integrated approach to screening and analyzing the financial condition of insurance companies. In addition, FAST assists state insurance departments in allocating resources to those insurers in greatest need of regulatory attention targeting those specific aspects of an insurer's financial position that could put the insurer at risk of future insolvency.

Scoring System

The Scoring System consists of a series of ratios, calculated annually and quarterly, for which an insurer scores a given number of points based on certain parameters set for each ratio. Certain insurers writing both life and accident and health (A&H) insurance meet the requirements for "hybrid" status. For these hybrid insurers, both life and A&H ratios are available. There are 11 annual ratios and 14 quarterly ratios for life insurers, 11 annual ratios and 18 quarterly ratios for A&H insurers, 16 annual ratios and 13 quarterly ratios for health entities, and 22 annual ratios and 16 quarterly ratios for property/casualty (P/C) insurers. These ratios focus on an insurer's financial position, results of operations, cash flow and liquidity, and leverage. Insurers with the highest scores would generally be considered a higher risk of potential insolvency. The Scoring System is designed so that an analyst can screen insurers on a total score basis or analyze each ratio result separately. Annually, the NAIC Financial Analysis and Examination Unit, under the direction of the Financial Analysis Solvency Tools (E) Working Group, is responsible for ensuring that the Scoring System ratios are current and continue to be relevant to solvency monitoring, and that scoring parameters remain appropriate.

Financial Profile Reports

Financial Profile Reports are generated from data in an insurer's Annual and Quarterly Financial Statements. The Financial Profile Report provides a condensed summary of an insurer's financials on either a quarterly or annual basis also displaying the current period and four prior periods. The Financial Profile Report can assist the analyst in identifying unusual fluctuations, trends, or changes in the mix of an insurer's assets, liabilities, capital and surplus, and operations.

IRIS Ratio Application

The NAIC IRIS ratio application is a tool that assists in identifying those insurers that merit highest priority in the allocation of the state insurance department's resources, thus directing those resources to the best possible use.

The IRIS ratio application uses key financial data from the Annual Financial Statement to calculate ratio results. There are 13 IRIS ratios calculated for P/C insurers and 12 for life insurers. The calculated results for each insurer are compared to the usual range of results for each ratio. Falling outside the usual range is not considered a failing result. For example, an increase in surplus or premiums that is larger than usual is not necessarily a problem. Furthermore, in some years it may not be unusual for financially stable insurers to have several ratios with results outside the usual range.

IRIS ratio results are dependent on the accuracy of the Annual Financial Statement filed by insurers. The ratios cannot identify a misstatement of financial condition or the application of improper accounting practices or

I. Introduction D. NAIC Information

procedures. In fact, the NAIC warns state insurance departments not to rely on IRIS ratios as the only form of financial surveillance of insurers. IRIS ratios should be used in conjunction with the other NAIC solvency tools.

Jumpstart Reports

Jumpstart Reports, which are available through iSite+, were developed by the NAIC to assist examiners in performing financial condition examinations. Numerous reports can be generated pertaining to an insurer's reinsurance program and investment portfolio based on the information included in the NAIC database from the insurer's Annual Financial Statement. Although the Jumpstart Reports were developed to assist examiners in performing financial condition examinations, many of the applications may be of interest to the financial analyst as well. Following is a brief discussion of some of the Jumpstart Reports available that may assist the financial analyst in the analysis process. Additional information can be found on iSite+ under the Welcome/Documentation tab.

1. Assumed/Ceded Reinsurance Reports—Verifies reinsurance ceded for an insurer by comparing reserves and premiums ceded per the reinsurance schedules of the insurer being analyzed with reserves and premiums assumed per the assuming insurers' reinsurance schedules.
2. Company Valuation Exception Report—This report compares the company reported price to the Securities Valuation Office (SVO) unit price, and the low, average, high, and median prices along with the reported designation and values.
3. Investment Committee on Uniform Security Identification Procedures (CUSIP) Exception Report—Matches the insurer's Schedule D with the SVO database and produces an exception report of all securities with CUSIP numbers not listed on the SVO database.
4. Investment Designation Exception Report—Matches the insurer's Schedule D with the SVO database and produces an exception report of all securities with SVO designations different from those listed on the SVO database.
5. Investment Market Value Exception Report—Matches the insurer's Schedule D with the SVO database and produces an exception report of all securities with market values different from those listed on the SVO database.
6. Investment Material Holdings Report—Produces a listing of all securities owned, by issuer, where the market value of all securities of an individual issuer owned by the insurer is greater than a specified percentage of the insurer's prior year admitted assets or capital and surplus.
7. Investment Specified Designation Report—Produces a listing of all securities owned by an insurer whose designations match a specified designation.

Loss Reserves

Loss reserve analysis for a specific line of business can be performed for P/C insurers via iSite+. The following is a brief discussion of some of the loss reserve reports.

1. Data Triangles—Formats Schedule P, Parts 2, 3, and 6 data into a triangle that is traditionally used to analyze loss data.
2. Age-To-Age Development Factors—Creates age-to-age development factors in a triangle format for various projection methods.
3. Loss Ratios—Computes loss ratios based on premium and loss information by line of business in a triangle format.
4. Loss Reserve Projections—Creates a loss projection report by line of business using case reserves or paid numbers using various projection methods.

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Financial Exam Electronic Tracking System (FEETS)

To assist in the coordination of risk-focused financial condition examination, state insurance regulators use the NAIC's Financial Exam Electronic Tracking System (FEETS). FEETS allows state insurance regulators to call an examination of a multistate insurer, facilitate coordination via various functionality within the program, communicate the completion of an examination and share the completed version of the department's examination report. Use of FEETS on iSite+ is required by the NAIC when calling examinations on multistate insurers and is recommended for all examinations.

Regulatory Information Retrieval System

The Regulatory Information Retrieval System (RIRS) is a computerized database that contains information regarding formal administrative and regulatory actions taken against insurers and insurance agents. Information on the RIRS includes the insurer or insurance agent against which formal administrative or regulatory action was taken, the date of the action, the state taking the action, the reason for the action, the disposition, and the amount of monetary penalty levied. The RIRS relies on input from state insurance departments of all final actions taken and is available online to all state insurance departments.

Complaints Database System

The Complaints Database System (CDS) is a computerized database that contains information regarding consumer complaints filed against a firm or individuals in the insurance industry. The CDS provides state insurance departments with the ability to evaluate an insurer's comparative performance in the marketplace. Complaint reports can be generated by coverage, complaint reason, count, or time depending on the criteria selected.

Market Actions Tracking System (MATS)

The Market Action Tracking System (MATS) provides state insurance regulators a way to communicate action schedules and results. Actions include market conduct examinations or other actions on the continuum of regulatory responses. MATS includes functions for calling market regulation actions, reporting and access to full information about the people involved in the market action. MATS can also be used to view or update action information for a specific entity, individual, non-risk bearing entity or company.

Market Analysis Review System (MARS)

The Market Analysis Review System (MARS) is available to specific state regulator users for the purpose of tracking, recording and reviewing Level 1 analysis and Level 2 analysis completed by other state regulators. A Level 1 analysis requires an analyst to analyze specific company information to determine if any market conduct issues are present. The Level 1 analysis is a detailed review of certain information contained in NAIC databases. A Level 2 analysis requires the market analyst to seek input and gather information from sources outside of the NAIC databases and the company's financial and market conduct annual statements. By its very nature, a Level 2 Analysis is much more labor intensive than a Level 1 Analysis.

Global Receivership Information Database

The iSite+ application Global Receivership Information Database (GRID) allows the regulator to review the status of a receivership (e.g., conservatorship, rehabilitation, or liquidation). GRID provides information including contacts, company demographics, post receivership data, creditor class/claim data, legal data, financial data, and reporting data.

Accounting Guidance

Statutory Accounting Principles (SAP) are those accounting principles or practices that are prescribed or permitted by the insurer's domiciliary state insurance department. SAP is prescribed in the insurance statutes, regulations, administrative rules of the various states, and in the NAIC's *Accounting Practices and Procedures Manual* (AP&P Manual), *Annual Statement Instructions*, *Financial Condition Examiners Handbook*, *Purposes and Procedures Manual of the NAIC Investment Analysis Office* (P&P Manual), and subcommittee and task force minutes. In addition, certain accounting practices are explicitly or implicitly permitted by various state insurance departments on an issue-by-issue and/or company-by-company basis.

Financial statements filed with state insurance departments are prepared on a SAP basis. Since the primary concerns of insurance regulators are the protection of the policyholders and the solvency of each insurer, SAP places emphasis on the adequacy of statutory capital and surplus. Adequate capital and surplus provides protection against adverse operating results and also permits an insurer to expand its business. In addition, SAP emphasizes the balance sheet rather than the income statement. Statutory accounting is primarily directed toward the determination of an insurer's financial condition and its ability to satisfy its obligations to policyholders and creditors as of a certain date.

As stated in the preamble to the AP&P Manual, SAP is based on the concepts of conservatism, consistency, and recognition. Each of these concepts is discussed in more detail below.

- **Conservatism**—Financial reporting by insurers requires the use of substantial judgments and estimates by management. Such estimates may vary from the actual amounts for various reasons. To the extent that factors or events result in adverse variation from management's accounting estimates, the ability to meet policyholder obligations may be lessened. In order to provide a margin of protection for policyholders, the concept of conservatism should be followed when developing estimates as well as establishing accounting principles for statutory reporting.

Conservative valuation procedures provide protection to policyholders against adverse fluctuations in financial condition or operating results. Statutory accounting should be reasonably conservative over the span of economic cycles and in recognition of the primary responsibility to regulate for financial solvency. Valuation procedures should, to the extent possible, prevent sharp fluctuations in surplus.

- **Consistency**—The regulators' need for meaningful, comparable financial information to determine an insurer's financial condition requires consistency in the development and application of SAP. Because the marketplace, the economic and business environment, and insurance industry products and practices are constantly changing, regulatory concerns are also changing. An effective statutory accounting model must be responsive to these changes and address emerging accounting issues. Precedent or historically accepted practice alone should not be sufficient justification for continuing to follow a particular accounting principle or practice that may not coincide with the objectives of regulators.
- **Recognition**—The principal focus of solvency measurement is determination of financial condition through analysis of the balance sheet. However, protection of the policyholders can only be maintained through continued monitoring of the financial condition of the insurer. Operating performance is another indicator of an insurer's ability to maintain itself as a going concern. Accordingly, the income statement is a secondary focus of statutory accounting and should not be diminished in importance to the extent contemplated by a liquidation basis of accounting.

The ability to meet policyholder obligations is predicated on the existence of readily marketable assets available when both current and future obligations are due. Assets having economic value other than for fulfilling policyholder obligations, or those assets that may be unavailable due to encumbrances or other third-party interests should not be recognized on the balance sheet but rather should be charged against surplus when acquired or when availability otherwise becomes questionable.

I. Introduction E. SAP vs. GAAP

Liabilities require recognition as they are incurred. Certain statutorily mandated liabilities may also be required to arrive at conservative estimates of liabilities and probable loss contingencies (e.g., interest maintenance reserves, asset valuation reserves, and others).

Revenue should be recognized only as the earnings process of the underlying underwriting or investment business is completed. Accounting treatments that tend to defer expense recognition do not generally represent acceptable SAP treatment.

SAP income reflects the extent that changes have occurred in SAP assets and liabilities for current period transactions, except changes in capital resulting from receipts or distributions to owners. SAP income also excludes certain other direct charges to surplus that are not directly attributable to the earnings process (e.g., changes in nonadmitted assets).

Although the insurers' Annual and Quarterly Financial Statements and Audited Financial Reports filed with the state insurance departments are prepared on a statutory basis, financial analysts also review Holding Company Form B filings and U.S. Securities and Exchange Commission (SEC) filings that may include financial statements prepared based on generally accepted accounting principles (GAAP). Therefore, the analyst must also have a general understanding of GAAP.

Though most non-publicly traded insurers are not required to produce financial statements on a GAAP basis, many do for internal purposes. Therefore, the analyst should consider requesting and analyzing GAAP financial statements in addition to SAP financial statements, if concerns warrant. Comparing financial results based on SAP to those based on GAAP for an insurer can provide meaningful information to the analyst regarding the insurer's financial status.

There are two main conceptual differences between SAP and GAAP.

1. SAP stresses measurement of the ability to pay claims in the future
2. GAAP stresses measurement of emerging earnings of a business from period to period (e.g., matching revenue to expenses)

Appendix D of the *AP&P Manual* is a useful reference in understanding how SAP addresses an issue that has been adopted by GAAP. Additionally, the *NAIC Statutory Accounting Principles Self-Study Program* provides additional guidance on the difference between GAAP and SAP. The following is a discussion of the more significant specific differences between SAP and GAAP for property/casualty, life/A&H insurers, fraternal societies and health entities:

- **Acquisition Costs—Under Statement of Statutory Accounting Principles (SSAP) No. 71—Policy Acquisition Costs and Commissions**, all acquisition costs, such as commissions and other costs incurred in acquiring and renewing business, are expensed as they are incurred. Under GAAP, those acquisition costs that are primarily related to, and vary with, the volume of premium income are capitalized as an asset and are then amortized by periodic charges to earnings over the terms of the related policies.
- **Valuation of Bonds and Redeemable Preferred Stocks—Under SSAP No. 26R—Bonds and SSAP No. 32R—Preferred Stock**, bonds and redeemable preferred stocks are carried at amortized cost or NAIC values in accordance with the NAIC designation of the securities. Under GAAP, bonds and redeemable preferred stocks are carried at amortized cost only if the insurer has the ability and intent to hold the securities to maturity and there are no (other than temporary) declines in fair value, otherwise, they are carried at market.
- **Nonadmitted Assets—Under SSAP No. 4—Assets and Nonadmitted Assets**, assets having economic value, other than those that can be used to fulfill policyholder obligations or other third-party interests, should not be recognized on the balance sheet and are, therefore, considered nonadmitted. SSAP No. 4 defines nonadmitted assets as an asset that is accorded limited or no value in statutory reporting and is one that is either specifically identified as a nonadmitted asset or not specifically identified as an admitted asset within

I. Introduction E. SAP vs. GAAP

the AP&P Manual. *SSAP No. 20—Nonadmitted Assets*, specifically identifies the following as nonadmitted assets: deposits in suspended depositories; bills receivable not for premium and loans unsecured or secured by assets that do not qualify as investments; loans on personal security, cash advances to, or in the hands of, officers or agents and travel advances; all non-bankable checks (e.g., non-sufficient funds); trade names and other intangible assets; automobiles, airplanes, and other vehicles; furniture, fixtures, and equipment; and company's stock as collateral for loan.

- **Deferred Income Taxes—Under SSAP No. 101—Income Taxes**, deferred income tax assets are limited under admissibility test and amounts over the criterion are nonadmitted. Under GAAP, a valuation allowance is used to reduce the asset to what can be realized. Also, under SSAP No. 101, changes in deferred tax assets (DTAs) and deferred tax liabilities (DTLs) are reported as a separate line in the surplus section. Under GAAP, changes in DTAs and DTLs are recognized in earnings.
- **Goodwill—Under SSAP No. 68—Business Combinations and Goodwill**, goodwill represents the difference between the cost of acquiring the entity and the reporting entity's share of the book value of the acquired entity. Under GAAP, goodwill represents the difference between cost of acquiring the entity and the fair value of the assets less liabilities acquired.
- **Surplus Notes—Under SSAP No. 41R—Surplus Notes**, surplus notes meeting certain requirements are considered as surplus. Under GAAP, surplus notes are considered to be debt.

The following discusses the specific differences between SAP and GAAP for property/casualty insurers only:

- **Reinsurance in Unauthorized Companies—Under SSAP No. 62R—Property and Casualty Reinsurance**, reserves are required for the excess of unearned premiums and losses recoverable over funds held on business reinsured with companies not authorized to do business in the insurer's state of domicile. Under GAAP, reinsurance recoverables are allowed regardless of whether the reinsurer is authorized, subject to tests of recoverability.

The following addresses reporting for insurers filing on a basis of accounting that deviates from SAP (e.g., GAAP or other permitted practices):

State regulators use financial analysis tools and risk-based capital (RBC) standards to evaluate the financial condition of insurance companies. The benchmarks for these tools are based on SAP. If an insurer prepares statements utilizing accounting practices that deviate from SAP, consider the impact to the RBC results.

Prioritization Framework

The financial analysis process should be priority-based to ensure that insurers are reviewed promptly and at a level commensurate with the nature of their risks, complexity, and solvency position. To facilitate priority-based analysis, state insurance departments should utilize the following general framework to prioritize or classify insurance companies according to each insurer's relative stability and the perceived need for enhanced analysis:

- **Priority 1 (Troubled)** – The highest priority insurers from a solvency monitoring perspective, based on significant financial solvency risks. Insurers prioritized at this level are considered troubled and subject to comprehensive annual and quarterly analysis procedures, detailed considerations outlined with the *Troubled Insurance Company Handbook*, and a significantly elevated level of ongoing regulatory monitoring and oversight. Upon designating an insurer as a Priority 1, the domestic state should follow required procedures for troubled companies in communicating with other state insurance regulators. Insurers prioritized at this level would also be considered priority insurers for accreditation timeliness purposes and should generally be analyzed ahead of Priority 2, Priority 3, and Priority 4 insurers.
- **Priority 2 (Priority)** – High-priority insurers that are not yet considered troubled but may become so if recent trends or unfavorable metrics are not addressed. High-priority insurers may also include those subject to heightened monitoring for reasons other than financial solvency risks, as determined by the department. Insurers prioritized at this level may be subject to full quarterly analysis procedures and are subject to comprehensive annual analysis and an elevated level of ongoing regulatory monitoring and oversight. Insurers prioritized at this level would also be considered priority insurers for accreditation timeliness purposes and should generally be analyzed ahead of Priority 3 and Priority 4 insurers.
- **Priority 3 (Non-Priority)** – Moderate priority insurers that indicate some need for additional monitoring. Insurers prioritized at this level should be subject to comprehensive annual analysis procedures, should generally be analyzed ahead of Priority 4 insurers, and may be subject to an enhanced level of ongoing regulatory monitoring and oversight.
- **Priority 4 (Non-Priority)** – Low priority insurers that are fundamentally sound, not overly complex and/or nationally significant, and do not currently indicate a need for additional monitoring as no material regulatory concerns have been identified and their solvency risk is viewed as remote. Such insurers demonstrate a track record of stable operations, strong capitalization, and effective corporate governance. In addition, such insurers are not subject to significant business fluctuations or major changes to their core operations and strategies. These insurers should be subject to a basic level of regulatory monitoring and oversight, including annual analysis.

The prioritization framework outlined above is primarily intended for use in communicating the prioritization of insurers on a uniform basis across state insurance departments. Therefore, state insurance regulators should present the prioritization of its insurers in accordance with the NAIC framework above when preparing and sharing information on insurers (i.e., Insurer Profile Summary) with other regulators. However, each state insurance department may adjust, enhance and/or develop an alternate prioritization framework and scale for its own internal purposes, as long as the framework outlined above is used in external communication with other regulators.

An insurer's priority level should be reconsidered as the result of each review performed to determine whether the designation is still appropriate and rationale for changes in priority ratings should be clearly documented within analysis files. However, changes in priority levels should only be made after approval by senior insurance department personnel.

ⁱ The use of the term "nationally significant" is not intended to reference the nationally significant monitoring criteria utilized by the NAIC's Financial Analysis (E) Working Group. Regulators may use judgment in evaluating the significance of an individual insurer to the national insurance market to determine which domestic insurers qualify for low priority treatment.

I. Introduction F. Prioritization of Work

Prioritization Factors

Although prioritization is, to a large extent, subjective, a state insurance department should establish guidelines to assist in the consistent assignment of priority designations to its insurers. These guidelines may consist of both quantitative and qualitative considerations. Factors that may be given consideration in the state insurance department's prioritization system include, but are not limited to, the following:

- Results of the most recently completed risk-focused analysis, including branded risk exposures and assessments (based on analysis of the Annual Financial Statement, Quarterly Financial Statements, supplemental filings, holding company analysis and any other documents reviewed by the analyst)
- Level of capitalization and identification of unfavorable trends
- Negative trends in profitability and/or cash flow from operations
- Insurance Regulatory Information System (IRIS) ratio results
- Annual and Quarterly Scoring System ratio results
- Changes in the insurer's officers or board of directors
- Changes in the insurer's business strategy or operations
- Summary of results of the automated quantitative data and benchmarks in the *Financial Analysis Handbook* risk repositories
- Issues/questions identified by the NAIC Financial Analysis (E) Working Group
- Examination findings and recommendations (financial condition and market conduct)
- Information from other divisions or areas within the insurance department
- Independent organization ratings and reports
- Information obtained from other regulatory agencies (including federal)
- RBC and RBC Trend Test results
- Impact on the public of an insurer's insolvency (policyholders and jurisdictions potentially affected)
- Structure and complexity of the insurer or insurance group
- Current or pending regulatory actions
- Standing of insurer in relation to statutes that impact financial solvency (e.g., hazardous financial condition)

As a general rule financial statements and other materials pertaining to those insurers that are deemed higher in priority should be reviewed before those materials pertaining to lower priority insurers. In addition, the review of higher priority insurers should typically be more in-depth than the review of lower priority insurers.

II. Risk-Focused Financial Analysis Framework

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Overview of Risk-Focused Surveillance Process

The intent of the risk-focused surveillance process is to broaden and enhance the identification of risk inherent in an insurer's operations and use that evaluation in formulating the ongoing surveillance of the insurer. Through their activities, insurers assume a variety of risks, which is the essence of an insurance transaction. The type of risk and its significance vary by activity. Investment activities may involve credit risk, market risk and liquidity risk. In product sales, insurers may assume market risk, pricing/underwriting risk, strategic risk or liquidity risk in varying degrees, depending on the product. Over the years, state insurance regulators have developed numerous tools to address the risks insurers assume. Investment laws limit the market and credit risk insurers can assume. Limitations on net retentions help reduce catastrophe risk. Risk-based capital requirements establish capital levels in recognition of a variety of risks. State insurance regulators have always considered the risk profiles of licensed insurers and the activities that may pose risk to the company in the future. The risk-focused surveillance process uses an organization-wide risk assessment process to enhance evaluation and to better coordinate the activities of financial solvency surveillance through greater consistency within the state insurance department, and with other departments.

A risk-focused surveillance process includes identifying significant risks, assessing and analyzing those risks, documenting the results of the analysis, and developing recommendations for how the analysis can be applied to the ongoing monitoring of the insurer. This increased attention by state insurance regulators to risk assessment and risk management processes used by insurers will be a positive development.

The enhancements included in the risk-focused surveillance process, including examination and analysis, intend to provide the following benefits:

1. Strengthen regulatory understanding of the insurer's corporate governance function by documenting the composition of the insurer's board of directors and the executive management team, as well as the quality of guidance and oversight provided by the board and management.
2. Enhance evaluation of risks through assessment of inherent risks and risk management processes to determine if there are weaknesses of management's ability to identify, assess and manage risk.
3. Improve early identification of emerging risks at individual insurers on a sector-wide basis.
4. Enhance effective use of regulatory resources through increased focus on higher risk areas.
5. Increase regulatory understanding of the insurer's quality of management, the characteristics of the insurer's business and the risks it assumes.
6. Enhance the value of surveillance work and establishment of risk assessment benchmarks performed by insurers and state insurance regulators, who have common interest in ensuring that risks are properly identified and that adequate, effective control systems are established to monitor and control risks.
7. For examinations, better formalize and document the risk assessment process via the use of the risk assessment matrix tool to assist in examination planning and resource assignment.
8. Expand risk assessment to provide a more comprehensive and prospective look at an insurer's risks through identification of the insurer's current and/or prospective high-risk areas.
9. For examinations, coordinate the results of the risk-focused examination process with other financial solvency surveillance functions (i.e., establishing/updating the priority score and supervisory plan).

In full, the risk-focused surveillance process provides effective procedures to monitor and assess the solvency of insurers on a continuing basis. The risk-focused approach consists of a structured methodology designed to establish a forward-looking view of an insurer's risk profile and the quality of its risk management practices. This

II. Risk-Focused Financial Analysis Framework

approach permits a direct and specific focus on the areas of greatest risk to an insurer. Through this approach, state insurance regulators can be more proactive and better positioned to identify and respond to any serious threat to the stability of the insurance company from any current or emerging risks. This regulatory approach will benefit all participants in the insurance marketplace.

ROLE OF THE FINANCIAL ANALYST

In the risk-focused surveillance approach, the financial analyst's role is to provide continuous off-site monitoring of the state's domestic insurers' financial condition, monitor internal/external changes relating to all aspects of the insurer, maintain a prioritization system and provide input into the state insurance department's priority of each insurer, work with the examination staff to develop an ongoing Supervisory Plan as well as update the Insurer Profile Summary (IPS), and provide state insurance department management with timely knowledge of significant events relating to the domestic insurers.

RISK-FOCUSED SURVEILLANCE CYCLE

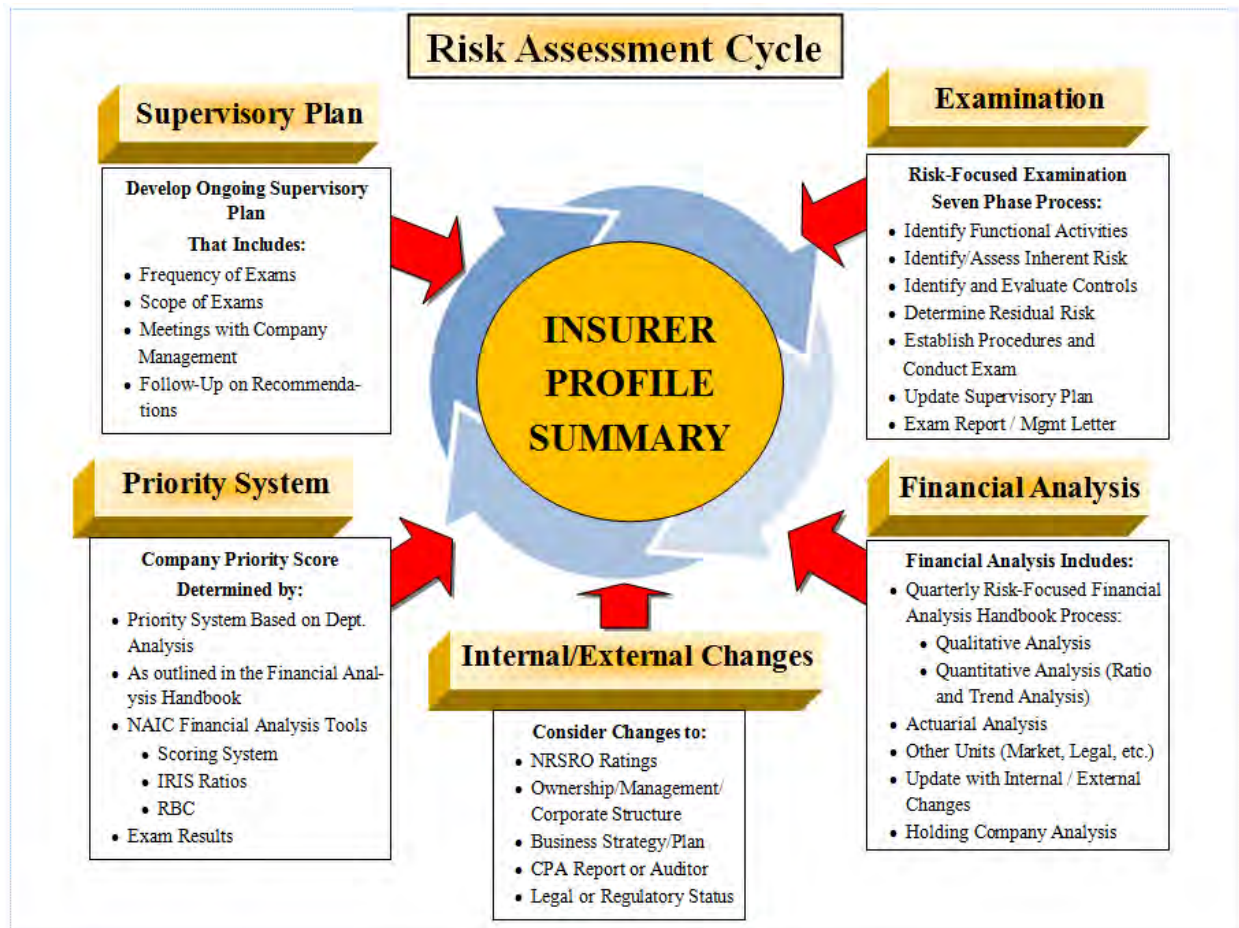
The risk-focused surveillance framework is designed to provide continuous regulatory oversight. The risk-focused approach requires fully coordinated efforts between the financial examination function and the financial analysis function. There should be a continuous exchange of information between the field examination function and the financial analysis function to ensure that all members of the state insurance department are properly informed of solvency issues related to the state's domestic insurers.

The regulatory Risk-Focused Surveillance Cycle involves five functions, most of which are performed under the current financial solvency oversight role. The enhancements coordinate all of these functions in a more integrated manner that should be consistently applied by state insurance regulators. The five functions of the risk assessment process are illustrated within the Risk-Focused Surveillance Cycle.

As illustrated in the Risk-Focused Surveillance Cycle diagram, elements from the five identified functions contribute to the development of an IPS. Each state will maintain an IPS for its domestic companies. State insurance regulators that wish to review an IPS for a non-domestic company will be able to request the IPS from the domestic or lead state. The documentation contained in the IPS is considered proprietary, confidential information that is not intended to be distributed to individuals other than state insurance regulators.

Please note that once the Risk-Focused Surveillance Cycle has begun, any of the inputs to the IPS can be changed at any time to reflect the changing environment of an insurer's operation and financial condition.

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The elements of the risk assessment process are:

- **IPS:** This profile is used to “house” summaries of risk-focused examinations, financial analyses, internal/external changes, priority scores, supervisory plan and other standard information. This profile is intended to be a “living document” and preferably shared with other state insurance regulators who have signed the *NAIC Master Information Sharing and Confidentiality Agreement* verifying that such shared information would remain confidential.
- **Risk-Focused Examinations:** These examinations consist of a seven-phase process that can be used to identify and assess risk, assess the adequacy and effectiveness of strategies/controls used to mitigate risk, and assist in determining the extent and nature of procedures and testing to be used in order to complete the review of that activity. The risk-focused surveillance process can be used to assist examiners in targeting areas of high-risk.
- **Risk-Focused Financial Analysis:** This function consists of a risk-focused analysis processes performed by state insurance regulators as outlined in the *Financial Analysis Handbook* (Handbook). This analysis process identifies and assesses risk based on the nine branded risk classifications to complete and document an overall assessment of the financial condition of the insurer.
- **Internal/External Changes:** Changes in rating agency ratings, ownership/management/corporate structure, financial condition/risk profile, business strategy or plan, external audit reports, and legal or regulatory status should be considered in developing the priority and supervisory plan.
- **Priority System:** The prioritization of the insurer, changes in priority or rationale for changes. See chapter I.F. Prioritization of Work for details.

II. Risk-Focused Financial Analysis Framework

- **Supervisory Plan:** At least once a year, a supervisory plan should be developed or updated by the domestic state for each domestic insurer. The supervisory plan should be concise and outline the type of surveillance planned, the resources dedicated to the oversight, and the consideration and communication and/or coordination with other states.

Overview of the Risk-Focused Financial Analysis Process

Financial analysis is an ongoing process that can be divided into annual cycles, each of which includes the analysis of the Annual Financial Statement, Quarterly Financial Statements and the various supplemental filings, such as the Actuarial Filings, Management's Discussion and Analysis (MD&A), Audited Financial Report and holding company filings. The financial analysis process is designed to assist the analyst in reviewing and analyzing insurers throughout the annual cycle in a logical manner, focusing on areas of concern within the nine branded risk classifications. The end result of this process is a financial analysis of each insurer specifically tailored to the concerns of that insurer as a result of its unique risks.

<u>Procedure Description</u>	<u>Expectation</u>
Risk Assessment Procedures and Insurer Profile Summary (annual and quarterly).	Complete for all domestic insurers.
Non-Lead State Holding Company Analysis (applies only to non-lead state domestic insurance regulators).	Complete for all domestic insurers that are part of an insurance holding company system.
Lead State Holding Company Analysis Documented within the Group Profile Summary (applies only to lead state domestic insurance regulators).	Complete for all insurance holding company system groups.

Annual/Quarterly Risk Assessment Procedures – Domestic Insurer

Annual and Quarterly Financial Statements

An insurer is required to file an Annual Financial Statement with its state of domicile, the NAIC and all jurisdictions in which the insurer is authorized to transact business by March 1 of each year for the 12 months ended December 31 of the previous year. An insurer is required to file Quarterly Financial Statements for the first, second and third quarters with the state of domicile, the NAIC and, in most instances, all states in which the insurer is authorized to do business by May 15, August 15 and November 15, respectively. The Financial Statement information is loaded onto the NAIC database, at which time automated financial analysis solvency tools are calculated and the Handbook's quantitative results are generated. All of this information is available to the state insurance departments via iSite+.

Scope and Depth of Risk-Focused Analysis

The depth of review will depend on the complexity, financial strengths and weaknesses, and known risks of the insurer and the priority designation established by the state insurance department. Other factors—such as the insurer's past regulatory history, accuracy of filing, age of insurer, stability of business plan, knowledge of insurer's operations, and materiality of the regulatory concerns, etc.— may affect the scope and depth of analysis. The flexibility to customize the scope and depth of the analysis is determined at the state insurance department's discretion and should include analyst and supervisor input. Therefore, the state insurance department should tailor the data and procedures used and the level of documentation to sufficiently address the specific risks of the insurer.

The Risk Assessment procedures for annual analysis consists of an overall analysis of the insurer documented in the nine branded risk classifications. Refer to section III.A.4 Risk Assessment – Analyst Reference Guide for further explanation of the risk classifications. The analyst should perform a background analysis, a current

II. Risk-Focused Financial Analysis Framework

period analysis, and a review of data and procedures within the nine branded risk classification repositories. All of these data and procedures provide the basis for the completion of a thorough review of the insurer's financial solvency.

The nine branded risk classification chapters are designed as "repositories" of data, benchmarks and procedures the analyst may select from in order to perform his/her analysis of that risk category. The analyst's review should use data relevant to each specific risk classification and customized for the insurer such that it is sufficient to perform and document his/her analysis and investigation of risks. Analysts are not expected to respond to all procedures, data or benchmark results listed in the Risk Assessment procedures or the nine branded risk repositories. Rather, analysts and supervisors should use their expertise, knowledge of the insurer and professional judgement to tailor the analysis to address specific risks of the insurer and document completion of analysis. Documentation of the risk assessment analysis should be sufficiently robust to explain the risks and reflect the strengths and weaknesses of the insurer.

At the conclusion of the risk assessment, the analyst should develop and document an overall summary and conclusion based on the results of the risk-focused analysis performed, prospective risks of the insurer, follow-up analysis or regulatory actions, any correspondence and the impact of the holding company on the insurer. The analyst should update the IPS (and supervisory plan, if applicable) to document this summary and conclusion. Note that an analyst's documentation of the risk assessment represents the *detail* of the analysis of risks, which may be more in-depth for certain material risks or complex insurers, whereas the IPS represents a *summary* of the risks of the insurer. Refer to section III.A.4 Risk Assessment – Analyst Reference Guide for further explanation on completing the IPS.

Quarterly Non-Troubled Quantitative Review

For first-, second- and third-quarter financial statement analysis, if the results for the non-troubled automated system calculation indicate a full quarterly risk assessment should be completed and if it is not, then the analyst should justify and document the reason(s) why.

Prioritization of Analysis Work

The analyst should ensure that those insurers identified as having significant concerns will be analyzed on a priority basis for future filings. Those insurers with the highest priority should receive the most in-depth review. Refer to section I.F. Prioritization of Work for further guidance.

Supervisor Input and Review

It is important for the analyst's supervisor to be actively involved in the financial analysis performed, including determination of the scope and depth of analysis. It also is important that the review and supervision be performed on a timely basis.

The branded risk repositories offer suggestions for the types of information the analyst may consider requesting. It is important that the analyst's proposed follow-up procedures be discussed with the analyst's supervisor.

Captives and/or Insurers Filing on a U.S. GAAP Basis

These procedures are designed for insurers filing on a U.S. generally accepted accounting principles (GAAP) (or modified GAAP) basis, after the completion of the traditional Risk Assessment Procedures. (See section III.C.1. Special Analysis Procedures – Captives and/or Insurers Filing on a U.S. GAAP Basis Worksheet.) The procedures provide guidance on the review of a GAAP filer on a statutory blank and address the following areas:

- Management assessment
- Balance Sheet assessment
- Operations assessment
- Investment practices

II. Risk-Focused Financial Analysis Framework

- Review of disclosures
- Assessment of results from prioritization and analytical tools

Domestic and/or Non-Lead State Holding Company System Analysis

Procedures for evaluating and considering the impact of an insurance holding company system on individual insurers should be completed for all domestic insurers. For lead states, this consideration is included within the VI.C Insurance Holding Company System Analysis Guidance (Lead State). For non-lead states, this consideration is included in V.A Holding Company Procedures (Non-Lead State). The depth of the holding company analysis of an insurer in a holding company system will depend on the characteristics (e.g., sophistication, complexity and financial strength) of the holding company system, availability of information, and existing potential issues and problems found during review of the holding company filings. Non-lead states should obtain, utilize and rely on holding company analysis work performed by the lead-state, as appropriate, in fulfilling their review responsibilities. Lead state and non-lead state responsibilities are further defined in section VI.C.

The following procedures are also included within section V.A. Note that Form A, Form D, Form E and Extraordinary Dividends/Distributions are transaction-specific and are not part of the regular annual/quarterly analysis process. The review of these transactions may vary as some states may have regulations that differ from these Forms.

- **FORM A**

The Form A review is to be completed for all acquisitions, mergers or changes in control. Form A is filed with the domestic state of each insurer in the group. The analyst should review the transaction and all applicable documents and complete the Form A Procedures, when necessary.

- **FORM D**

The Form D review is to be completed for all prior notices of material transactions. Form D must be filed with the domestic state. The analyst should review the transaction and all applicable documents and complete the Form D Procedures, when necessary.

- **FORM E OR OTHER REQUIRED INFORMATION ON COMPETITIVE IMPACT**

The Form E or other review of competitive impact is to be completed for all pre-acquisition notifications regarding the potential competitive impact of a proposed merger or acquisition by a non-domiciliary insurer doing business in the state or by a domestic insurer. Form E or other required information must be filed with the domestic state. The insurer may also be required to file documents with the Federal Trade Commission (FTC) and the U.S. Department of Justice (DOJ) under the federal Hart-Scott-Rodino (HSR) Act. The analyst should review the transaction and all applicable documents and complete the Form E Procedures, when necessary.

- **EXTRAORDINARY DIVIDENDS/DISTRIBUTIONS**

The extraordinary dividends/distributions review is to be completed for any domestic insurers planning to pay any extraordinary dividend or make any other extraordinary distribution to its shareholders. Such dividends and distributions must receive proper prior regulatory approval. The analyst should review the transaction and all applicable documents and complete V.E Extraordinary Dividends/Distributions Procedures, when necessary.

At the end of section V.A., the analyst is asked to develop and document a conclusion regarding the impact of the holding company system on the domestic insurer and update the IPS accordingly. In addition, the analyst is encouraged to notify the lead state of any material risks or events that the lead state may not be aware of, that should be considered in the evaluation of the overall financial condition of the holding company system.

II. Risk-Focused Financial Analysis Framework

Group-Wide Supervision

The Group-Wide Supervision procedures establish guidance for lead state use in the analysis of insurance company holding systems. This includes a risk-focused approach to group regulation where specific risks that are relevant to insurance holding company structures are addressed.

- **INSURANCE HOLDING COMPANY SYSTEM ANALYSIS DOCUMENTED IN THE GROUP PROFILE SUMMARY (GPS) (LEAD STATE):**
 - Understanding the insurance holding company system (lead state)
 - Addressing lead state analysis considerations
 - Evaluating the overall financial condition of the holding company system by completing a detailed analysis through the group's exposure to each of the nine branded risk classifications
 - Assessing corporate governance and enterprise risk management
 - Documenting material concerns or conditions in the group that affect the lead state's domestic companies
 - Performing additional procedures on key risk areas, as needed
 - Sharing the results of the analysis, through the GPS, with other impacted regulators on a timely basis
- **CORPORATE GOVERNANCE DISCLOSURE PROCEDURES**

The *Corporate Governance Annual Disclosure Model Act* (#305) and *Corporate Governance Annual Disclosure Model Regulation* (#306) require an insurer, or an insurance group, to file a summary of an insurer or insurance group's corporate governance structure, policies and practices with the commissioner by June 1 of each calendar year. The lead state should take primary responsibility for reviewing the CGAD filing, if it is filed on a group basis, and should incorporate any takeaways or concerns into the GPS. Any concerns relevant only to a specific insurance entity in the group should be communicated to the domestic state in a timely manner.
- **OWN RISK AND SOLVENCY ASSESSMENT (ORSA) PROCEDURES**

The *Risk Management and Own Risk and Solvency Assessment Model Act* (#505) requires insurers above a specified premium threshold, and subject to further discretion, to submit a confidential annual ORSA Summary Report.
- **FORM F PROCEDURES**

The Form F is filed with the lead state commissioner of the insurance holding company system for every insurer subject to registration under the *Insurance Holding Company System Regulatory Act* (#440). The Form F review is to be completed by the lead state in conjunction with the review of Form B. The lead state analyst should identify the material risks within the insurance holding company system that could pose enterprise risk to the insurers in the group. Takeaways and concerns from the review should be documented in the GPS. Any concerns relevant only to a specific insurance entity in the group should be communicated to the domestic state in a timely manner.
- **PERIODIC MEETING WITH THE GROUP PROCEDURES**

These procedures are intended to demonstrate the type of potential questions a lead state may want to consider when it conducts a periodic meeting with the group.
- **TARGETED EXAMINATION PROCEDURES**

The targeted examination procedures provide examples of potential risk areas where the lead state may want to perform certain limited examination procedures as part of the continual risk assessment process.

II. Risk-Focused Financial Analysis Framework

LEAD STATE REPORT

The Lead State Report is located in iSite+, within Summary Reports, and is designed to improve communication and coordination between state insurance regulators. It provides a list of all insurance groups and the companies within each group, which can be sorted in various ways. The report also contains current contact information for the state's assigned insurance company analyst and the state's chief analyst, which is maintained by state insurance department staff.



Annual/Quarterly Worksheets, Repositories and Analyst Reference Guides

- A. Risk Assessment (All Statement Types)
 - 1. Risk Assessment Worksheet
 - 2. Analyst Reference Guide
 - a. Insurer Profile Summary Example
 - 3. Template for Planning Meeting with Financial Examiner
- B. Risk Classification Repositories
 - 1. Credit Risk
 - a. Property & Casualty Repository
 - b. Life, Accident & Health Repository
 - c. Health Repository
 - d. Analyst Reference Guide
 - 2. Legal Risk
 - a. Repository (All Statement Types)
 - b. Audited Financial Report Worksheet
 - c. MD&A Worksheet
 - d. Analyst Reference Guide
 - 3. Liquidity Risk
 - a. Property & Casualty Repository
 - b. Life, Accident & Health Repository
 - c. Health Repository
 - d. Analyst Reference Guide
 - 4. Market Risk
 - a. Property & Casualty Repository
 - b. Life, Accident & Health Repository
 - c. Health Repository
 - d. Analyst Reference Guide
 - 5. Operational Risk
 - a. Property & Casualty Repository
 - b. Life, Accident & Health Repository
 - c. Health Repository
 - d. Analyst Reference Guide
 - 6. Pricing & Underwriting Risk
 - a. Property & Casualty Repository
 - b. Life, Accident & Health Repository
 - c. Health Repository
 - d. Analyst Reference Guide
 - 7. Reputational Risk
 - a. Repository (All Statement Types)
 - b. Analyst Reference Guide
 - 8. Reserving Risk
 - a. Property & Casualty Repository
 - i. Statement of Actuarial Opinion Worksheet
 - ii. Analyst Reference Guide



Annual/Quarterly Worksheets, Repositories and Analyst Reference Guides

- b. Life, Accident & Health Repository
 - i. Statement of Actuarial Opinion Worksheet
 - ii. Analyst Reference Guide
 - c. Health Repository
 - i. Statement of Actuarial Opinion Worksheet
 - ii. Analyst Reference Guide
 - 9. Strategic Risk
 - a. Repository (All Statement Types)
 - b. Analyst Reference Guide
- C. Special Analysis Procedures and Worksheets
 - 1. Insurers Filing on a U.S. GAAP Basis Worksheet (P&C)
 - 2. XXX/AXXX Captive Reinsurance Transactions Procedures (Life)
 - 3. Title Insurer Worksheet (Title)

Legend of Abbreviations

Branded Risk Classifications		
Symbol	Risk	Description
CR	Credit	Amounts actually collected or collectible are less than those contractually due or payments are not remitted on a timely basis.
LG	Legal	Non-conformance with laws, rules and regulations, prescribed practices or ethical standards (in any jurisdiction in which the entity operates) will result in a disruption in business and financial loss.
LQ	Liquidity	Inability to meet contractual obligations as they become due because of an inability to liquidate assets and/or obtain adequate funding without incurring unacceptable losses.
MK	Market	Movement in market rates or prices (such as interest rates, foreign exchange rates or equity prices) adversely affect the reported and/or market value of the investments.
OP	Operational	The risk of financial loss resulting from inadequate or failed internal processes, personnel and systems, as well as unforeseen external events.
PR/UW	Pricing/ Underwriting	Pricing and underwriting practices are inadequate to provide for risks assumed.
RP	Reputation	Negative publicity, whether true or not, causes a decline in the customer base, costly litigation and/or revenue reductions.
RV	Reserving	Actual losses and/or other contractual payments reflected in reported reserves or other liabilities will be greater than estimated.
ST	Strategic	Inability to implement appropriate business plan, to make decisions, to allocate resources or to adapt to changes in the business environment will adversely affect competitive position and financial condition.

III.A.1. Risk Assessment (All Statement Types) – Annual Procedures Worksheet

Analyst:	Date:
Supervisor Review:	Date:
Supervisor Comments:	

Overall Risk Assessment Instructions

The insurance department should generally follow the risk-focused financial analysis process outlined in *The Financial Analysis Handbook* to ensure that appropriate analysis procedures are performed on each domestic insurer. The documentation must be prepared in sufficient detail to provide a clear understanding of the work performed and conclusions reached.

Risk Assessment procedures should be completed and tailored to address the specific risks of the insurer based on the complexity, financial strengths and weaknesses, and known risks of the insurer. Analysts should document the detailed results of the review in Section III: Risk Assessment and the summary in the Insurer Profile Summary (IPS) report.

The Risk Assessment procedures are comprised of the following four sections, which collectively represent a full analysis of an insurer: I) Background Analysis; II) Current Period Analysis; III) Risk Assessment; and IV) Update the IPS.

Section I: Background Analysis

1. **Prior Year Analysis and Prioritization:** Review the analysis performed on the insurer for the prior year and prior quarters.
 - a. Review and consider the state's priority designation, prioritization tool results (if applicable) as of the last review and start of the current review and the Preliminary Analysis (if applicable) as of the current review.
 - b. In preparing for current year analysis, review and consider the issues, concerns and prospective risks, noted in previous annual or quarterly analyses work papers, the IPS and supervisory plan, including analysis of the Own Risk and Solvency Assessment (ORSA) Summary Report (if applicable), completed in the prior year that affects the current analysis.
 - c. Consider any follow-up conducted and correspondence with the insurer, along with any conclusions.
2. **Communication:** Review any inter-departmental communication, as well as communication with other state, federal or international insurance regulators and the insurer. Consider in the current analysis any unusual items or prospective risks that indicate further analysis or follow-up is necessary. Document risks identified and assessed in the appropriate branded risk category in Section III: Risk Assessment.
3. **Examination Planning:** If a financial examination is currently being planned, meet with the assigned examiner in-charge (EIC) or examination supervisor to:
 - a. Discuss information on risks and concerns provided in the IPS, as well as additional information on the company's financial condition, operating results since the last examination, and reasons for any unusual trends, abnormal ratios and transactions that are not easily discernible.
 - b. Communicate and provide access to relevant information that has already been obtained by the analyst function and is available to the state insurance department. It may be helpful for the analyst to review the Examiner's Exhibit B questionnaire and note specific items that have already been accumulated and available to the examiner.
4. **Examination Analysis Follow-Up:** Review the Annual Financial Statement, General Interrogatories, Part 1, #3 and determine if a financial examination report was released by the domiciliary state since the last review.

III.A.1. Risk Assessment (All Statement Types) – Annual Procedures Worksheet

Document risks identified and assessed in the appropriate branded risk category in Section III: Risk Assessment.

a. Balance sheet date of the latest financial examination of the insurer	[Data]
b. Balance sheet date of the latest financial examination report available from either the state of domicile or the insurer	[Data]
c. Release date of the latest financial examination report available from either the state of domicile or the insurer, and what state insurance department or departments completed the Financial Examination Report	[Data]
d. Have any financial statement adjustments within the latest financial examination report not been accounted for in a subsequent financial statement filed with the state insurance department?	[Data]
e. Have any of the recommendations within the latest financial examination report not been complied with?	[Data]

If 4.d. or 4.e. is “yes,” or if follow-up was required from the review of the examination report, management letter or summary review memorandum in a previous analysis period, document risks identified and assessed in the appropriate branded risk category of Section III: Risk Assessment.

- f. Implementation of financial examination report recommendations or management letter comments.
- g. Impact of any financial statement adjustments on the insurer’s financial condition.
- h. Findings from the results of the examination represent risks being monitored, procedures performed or yet to be performed and prospective risks.

Section II: Current Period Analysis

The intent of the current period analysis section is for an analyst to perform a review of current results that may identify a change in a risk assessment either with new risks or by updating previously identified risks in Section III: Risk Assessment. Analysts should identify and assess changes in the insurer’s current financial status compared to the prior period, new or continuing trends, and unusual items. The following procedures do not constitute an all-inclusive list to be considered. Analysts should use their knowledge, expertise and professional judgement to complete a thorough analysis of the current period financial results.

5. **Financial Reporting and Data Applications:** Review and assess material changes and trends in the balance sheet, income statement, cash flow, and related financial metrics. Document risks identified and assessed in the appropriate branded risk category of Section III: Risk Assessment.
 - Annual Financial Statement including the Risk-based Capital Report (March 1st and April 1st Filings)ⁱ
 - Actuarial filingsⁱⁱ
 - Financial Ratios and Financial Analysis Solvency Toolsⁱⁱⁱ, such as: the Financial Profile Report, Scoring System, Insurance Regulatory Information System (IRIS), Investment and Reinsurance Jumpstart Reports, Investment Snapshot Reports, market conduct information, and etc.
 - Industry reports, news releases, ratings and information about emerging issues

ⁱ The analyst should review and consider information from these data sources in conducting a risk-focused analysis. The review should be evidenced by sign-off and dating of the information source, procedure step or simplified checklist.

ⁱⁱ See footnote i

ⁱⁱⁱ See footnote i

III.A.1. Risk Assessment (All Statement Types) – Annual Procedures Worksheet

6. **Management Assessment:** Review the Annual Financial Statement, including the Jurat page and General Interrogatories and other available information, to determine compliance with and if any changes have occurred in the following areas. Document risks identified and assessed in the appropriate branded risk category of Section III: Risk Assessment. (e.g., Operational or Strategic)

<i>In the review of the following, note any risks in the Operational or Strategic branded risks within Section III Risk Assessment.</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Properly executed and notarized Jurat page			
b. Change(s) in officers, directors or trustees since the previous Annual Financial Statement filing	= “#” after name	[Data]	[Data]
i. If 6.b. is “yes,” review of the Biographical Affidavit(s) for any new officers, directors or trustees indicated above. Assess any areas of concern that would indicate further review is necessary. (i.e., suitability and other governance-related concerns)			
ii. Assess any follow-up analysis or communication on any previously identified corporate governance issues.			
iii. Assess any significant corporate governance changes and determine whether these changes appear to indicate a shift in management philosophy, or whether management has made any changes in its business culture or business plan.			
c. If the insurer has been a party to a merger or consolidation, note any observations or concerns and ensure Form A or additional filings have been approved. [Annual Financial Statement, General Interrogatories, Part 1, #5.1 and #5.2]	=YES	[Data]	[Data]
d. Identify if any Certificates of Authority, licenses or registrations have been suspended or revoked. [Annual Financial Statement, General Interrogatories, Part 1, #6.1 and #6.2]	=YES	[Data]	[Data]

7. **Compliance Analysis:** Review and assess state-specific compliance or other analysis required by the state insurance department. Document risks identified and assessed in the appropriate branded risk category of Section III: Risk Assessment.
- a. Identify if the insurer is compliant with state statutes and regulations, including those that are new or revised (e.g., hazardous financial condition analysis, investment limitation analysis, etc.).
 - b. Assess if surplus meets the statutory minimum amount required by state law (varies by state and business type).
8. **Supplemental Filings:** Review and assess supplemental filings (other than the March 1 and April 1 financial statement) for compliance and identification of risks. Document risks identified and assessed in the appropriate branded risk category of Section III: Risk Assessment.
- a. Management Discussion & Analysis (MD&A) (April 1)^{iv}
 - b. Audited Financial Statement Report (June 1)^v

^{iv} See footnote i

^v See footnote i

III.A.1. Risk Assessment (All Statement Types) – Annual Procedures Worksheet

- c. For holding company groups, if performing the review of the group as the lead state, or receiving the lead state's group analysis summary, and assessing the impact of the group on the domestic insurer, incorporate risks identified and assessed related to the domestic insurer into Section III: Risk Assessment.
 - d. For ORSA Summary Reports, if required, when receiving and performing the review of the ORSA Summary Report or receiving the lead state's review, incorporate risks identified and assessed that relate to the domestic insurer into Section III: Risk Assessment.
9. **Business Plan and Projections (If Available):** Document risks identified and assessed in the appropriate branded risk category of Section III: Risk Assessment.
- a. Identify and assess any material variances between actual financial results compared to the most recent business plan and financial projections.
 - b. Identify and assess any material changes in the business strategy.

The following procedures related to the insurer's business plan and projections are required for all Risk Retention Groups (RRGs) regardless of accounting treatment (Generally Accepted Accounting Principles [GAAP]/Statutory Accounting Principles [SAP]) or organizational structure (captive/traditional laws):

- c. Review the insurer's business plan (plan of operation) to ensure that it is unchanged from the prior year.
 - d. If changes were made to the plan, ensure that the changes have been approved.
 - e. Review the Annual Financial Statement, General Interrogatories, Part 2, #13.1 to identify the insurer's largest net aggregate risk insured. Measure this exposure as a percent of surplus to ensure that it is in compliance with state guidelines.
 - f. Ensure that the financial projections on file accurately reflect the operations as presently conducted.
 - g. Ensure that the notes relating to the operation of the company agree with the approved plan.
10. **Analyst Notes of Current Period Results (Optional):** Include any analytical notes of material information.

Source	Notes	Risk Category

11. **Information Request:** If based on the above procedures performed and information gathered, the analyst does not have a sufficient understanding of the insurer's operations and strategies, consider requesting information from the insurer to complete the Section III: Risk Assessment. Refer to the Analyst Reference Guide for instructions.

Section III: Risk Assessment

Risk Assessment Instructions

Risk Assessment includes the accumulation of information gathered from the sections above, as well as a review of the data, benchmarks and procedures provided in each of the nine branded risk repositories to develop and document a risk assessment of each relevant material risk of the insurer. Analysts should review and use all data relevant and necessary to focus on specific risks to complete the analysis, which may include select data from the risk repositories and other relevant tools. The depth of review will depend on the complexity, financial strengths and weaknesses, and known risks of the insurer.

Analysts should not rely solely on the risk repositories for identification of all risks (or risk metrics) as the repositories are not analysis checklists and do not represent a complete list of possible risks for every analysis.

III.A.1. Risk Assessment (All Statement Types) – Annual Procedures Worksheet

Analysts should customize their analysis to include risks unique to the insurer and utilize risk metrics (whether quantitative or qualitative) that are best suited for measuring the insurer's exposure to those risks. Note that procedures included in each of the branded risk repositories are "best fit" as some procedures may identify risks that could be categorized in more than one branded risk category. Analysts should use their knowledge of the insurer and analytical skills to exercise discretion in re-categorizing risks as needed to document the details of the analysis and to update the IPS. Analysts are not expected to respond separately to procedures or benchmark results in the risk repositories that fall outside the benchmarks, rather, analysts should use their expertise and knowledge of the insurer to customize the analysis to address those risks deemed material or that require further investigation.

Complete the following to identify, document and explain each of the nine branded risks below. Refer to the Analyst Reference Guide discussion for further guidance. Documentation of the analysis should contain sufficient detail to adequately explain the risks identified, the metrics/benchmarks used to assess the insurer's exposure to the identified risks, and the results of the risk assessment (i.e., the level and trend of the insurer's risk exposure).

1. **Credit Risk Assessment:** Amounts actually collected or collectible are less than those contractually due, or payments are not remitted on a timely basis. Document the analysis of Credit risk.

Detail of Analysis	Assessment	Trend	IPS Y/N
#1 [Risk Component]		↑	
#2		↔	
#3		↓	

2. **Legal Risk Assessment:** Non-conformance with laws, rules, regulations, prescribed practices or ethical standards (in any jurisdiction in which the entity operates) will result in a disruption in business and financial loss. Document the analysis of Legal risk.

Detail of Analysis	Assessment	Trend	IPS Y/N
#1 [Risk Component]		↑	
#2		↔	
#3		↓	

3. **Liquidity Risk Assessment:** Inability to meet contractual obligations as they become due because of an inability to liquidate assets and/or obtain adequate funding without incurring unacceptable losses. Document the analysis of Liquidity risk.

Detail of Analysis	Assessment	Trend	IPS Y/N
#1 [Risk Component]		↑	
#2		↔	
#3		↓	

4. **Market Risk Assessment:** Movement in market rates or prices (such as interest rates, foreign exchange rates or equity prices) adversely affects the reported and/or market value of investments. Document the analysis of Market risk.

III.A.1. Risk Assessment (All Statement Types) – Annual Procedures Worksheet

Detail of Analysis	Assessment	Trend	IPS Y/N
#1 [Risk Component]		↑	
#2		↔	
#3		↓	

5. **Operational Risk Assessment:** The risk of financial loss resulting from inadequate or failed internal processes, personnel and systems, as well as unforeseen external events. Document the analysis of Operational risk.

Detail of Analysis	Assessment	Trend	IPS Y/N
#1 [Risk Component]		↑	
#2		↔	
#3		↓	

6. **Pricing/Underwriting Risk Assessment:** Pricing and underwriting practices are inadequate to provide for risks assumed. Document the analysis of Pricing/Underwriting risk.

Detail of Analysis	Assessment	Trend	IPS Y/N
#1 [Risk Component]		↑	
#2		↔	
#3		↓	

7. **Reputational Risk Assessment:** Negative publicity, whether true or not, causes a decline in the customer base, costly litigation and/or revenue reductions. Document the analysis of Reputational risk.

Detail of Analysis	Assessment	Trend	IPS Y/N
#1 [Risk Component]		↑	
#2		↔	
#3		↓	

8. **Reserving Risk Assessment:** Actual losses or other contractual payments reflected in reported reserves or other liabilities will be greater than estimated. Document the analysis of Reserving risk.

Detail of Analysis	Assessment	Trend	IPS Y/N
#1 [Risk Component]		↑	
#2		↔	
#3		↓	

III.A.1. Risk Assessment (All Statement Types) – Annual Procedures Worksheet

9. **Strategic Risk Assessment:** Inability to implement appropriate business plans, to make decisions, to allocate resources or to adapt to changes in the business environment will adversely affect competitive position and financial condition. Document the analysis of Strategic risk.

Detail of Analysis	Assessment	Trend	IPS Y/N
#1 [Risk Component]		↑	
#2		↔	
#3		↓	

Section IV: Update Insurer Profile Summary (IPS)

Prioritization: Consider any recommendation for a change in the priority designation of the insurer, including justification. Document it by updating the IPS.

PRIOR YEAR PRIORITY DESIGNATION=	[Analyst Input]
CURRENT YEAR PRIORITY DESIGNATION=	[Analyst Input]
	Current Year
i. RBC Ratio	[Data]
ii. RBC Trend Test	[Data]
iii. Scoring System Result	[Data]
iv. IRIS Ratio Result	[Data]
v. Net Income (Loss)	[Data]
vi. Capital and Surplus	[Data]
vii. Hazardous Financial Condition Regulation	[Analyst Input]
viii. [Insert Other State Specific Prioritization Criteria]	[Analyst Input]
Rationale for Change:	

Summary and Conclusion: Develop an overall summary and conclusion based on the completion of the risk-focused analysis performed, and document it by updating the IPS, including the Supervisory Plan, if applicable, for the following:

- Summary of the above risk-focused analysis results by risk classification
- Prospective risks of the insurer in current analysis, as well as to identify future areas for analysis
- Impact of the holding company on the insurer
- Completed or in-progress communication or other follow-up with the insurer, other areas of the Department of Insurance (DOI), financial examiners and other state insurance regulators
- Additional analysis yet to be performed
- Regulatory actions
- Any other factors or information that, in the analyst's judgment, are relevant to evaluating the insurer's overall financial condition

III.A.2. Risk Assessment (All Statement Types) – Quarterly Procedures Worksheet

Analyst:	Date:
Supervisor Review:	Date:
Supervisor Comments:	

Overall Risk Assessment Instructions

The insurance department should generally follow the risk-focused financial analysis process outlined in the Financial Analysis Handbook to ensure that appropriate analysis procedures are performed on each domestic insurer. The documentation must be prepared in sufficient detail to provide a clear understanding of the work performed and conclusions reached.

Risk Assessment procedures should be completed and tailored to address the specific risks of the insurer based on the complexity, financial strengths and weaknesses, and known risks of the insurer. The quarterly procedures include a review that focuses primarily on changes from the prior year that may identify new or changing risks. Analysts should document the detailed results of the review in Section III: Risk Assessment and update the summary in the Insurer Profile Summary (IPS) report.

The Risk Assessment Procedures are comprised of the following four sections, which collectively represent a full analysis of an insurer: I) Background Analysis, II) Current Period Analysis, III) Risk Assessment, and IV) Update the IPS.

Section I: Background Analysis

1. **Prior Year and Prior Quarter Analysis and Prioritization:** Review the analysis performed on the insurer for the prior year and prior quarters.
 - a. Review and consider the state's priority designation, any prioritization tool results (if applicable) as of the last review and start of the current review.
 - b. In preparing for current quarter analysis, review and consider the issues, concerns and prospective risks, noted in previous annual or quarterly analyses work papers, the IPS and supervisory plan, including analysis of the Own Risk and Solvency Assessment (ORSA) Summary Report (if applicable), completed in the prior year that affects the current analysis.
 - c. Consider any follow-up conducted and correspondence with the insurer, along with any conclusions.
2. **Communication:** Review any inter-departmental communication, as well as communication with other state, federal or international insurance regulators and the insurer. Consider in the current analysis any unusual items or prospective risks that indicate further analysis or follow-up is necessary. Document risks in the appropriate branded risk category in Section III: Risk Assessment.
3. **Examination Analysis Follow-Up:** Review the Quarterly Financial Statement, General Interrogatories, Part 1, #6, and determine if a financial examination report was released by the domiciliary state since the last review. Document risks in the appropriate branded risk category in Section III: Risk Assessment.

a. Balance sheet date of the latest financial examination of the insurer	[Data]
b. Balance sheet date of the latest financial examination report available from either the state of domicile or the insurer	[Data]
c. Release date of the latest financial examination report available from either the state of domicile or the insurer, and what state insurance department or departments completed the Financial Examination Report	[Data]
d. Have any financial statement adjustments within the latest financial examination	[Data]

III.A.2. Risk Assessment (All Statement Types) – Quarterly Procedures Worksheet

report not been accounted for in a subsequent financial statement filed with the state insurance department?	
e. Have any of the recommendations within the latest financial examination report not been complied with?	[Data]

If 3.d. or 3.e. is “yes,” or if follow-up was required from the review of the examination report, management letter or summary review memorandum in a previous analysis period, document the following, as applicable, in the appropriate branded risk category of the Section III: Risk Assessment:

- f. Implementation of financial examination report recommendations or management letter comments,
- g. Impact of any financial statement adjustments on the insurer’s financial condition.
- h. Findings from the results of the examination represent risks being monitored, procedures performed or yet to be performed and prospective risks.

Section II: Current Period Analysis

The intent of the current period analysis section is for an analyst to perform a review of current results that may identify a change in a risk assessment either with new risks or by updating previously identified risks in the Section III: Risk Assessment. Analysts should identify and assess changes in the insurer’s current financial status compared to the prior period, new or continuing trends, and unusual items. The following bulleted lists do not constitute an all-inclusive list to be considered. Analysts should use their knowledge, expertise and professional judgement to complete a thorough analysis of the current period financial results.

4. **Financial Reporting and Data Applications:** Review and assess material changes and trends in the balance sheet, income statement, cash flow, and related ratios and financial metrics. Document risks in the appropriate branded risk category of Section III: Risk Assessment.
 - Quarterly Financial Statement including the Risk Based Capital (RBC) Reportⁱ
 - Financial Ratios and Financial Analysis Solvency Toolsⁱⁱ, such as the Financial Profile Report, Scoring System, RBC Forecasting, market conduct information, etc.
 - Industry reports, news releases, ratings and information about emerging issues
5. **Management Assessment:** Review the Quarterly Financial Statement, including the Jurat page and General Interrogatories and other available information, to determine compliance with and if any changes have occurred in the following areas. Incorporate risks identified and assessed into Section III: Risk Assessment (e.g., operational or strategic).

<i>In the review of the following, note any risks in the Operational or Strategic branded risks within Section III Risk Assessment.</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Properly executed and notarized Jurat page			
b. Change(s) in officers, directors, or trustees since the previous Quarterly Financial Statement filing	= “#” after name	[Data]	[Data]
i. If “yes,” from the review of the Biographical Affidavit(s) for any new officers, directors, or trustees indicated above. Assess any			

ⁱ The analyst should review and consider information from these data sources in conducting a risk-focused analysis. The review should be evidenced by sign-off and dating of the information source, procedure step or simplified checklist.

ⁱⁱ See footnote i

III.A.2. Risk Assessment (All Statement Types) – Quarterly Procedures Worksheet

areas of concern that would indicate further review is necessary (i.e., suitability and other governance-related concerns).			
ii. Assess any follow-up analysis or communication on any previously identified corporate governance issues.			
iii. Assess any significant corporate governance changes and determine whether these changes appear to indicate a shift in management philosophy, or whether management has made any changes in its business culture or business plan.			
c. If the insurer has been a party to a merger or consolidation, note any observations or concerns, and ensure Form A or additional filings have been approved. [Quarterly Financial Statement, General Interrogatories, Part 1, #4.1 and #4.2]	=YES	[Data]	[Data]
d. Identify if any Certificates of Authority, licenses or registrations have been suspended or revoked. [Quarterly Financial Statement, General Interrogatories, Part 1, #7.1 and #7.2]	=YES	[Data]	[Data]

6. **Compliance Analysis:** Review and assess state-specific compliance or other analysis required by the state insurance department, and incorporate risks identified into Section III: Risk Assessment.
 - a. Identify if the insurer is compliant with state statutes and regulations, including those that are new or revised (e.g., hazardous financial condition analysis, etc.).
 - b. Assess if surplus meets the statutory minimum amount required by state law (varies by state and business type).
7. **Supplemental Filings:** If received since the last analysis, review and assess supplemental filings for compliance and identification of risks. Incorporate risks identified into Section III: Risk Assessment.
 - a. Management Discussion & Analysis (MD&A) (April 1)ⁱⁱⁱ
 - b. Audited Financial Statement Report (June 1)^{iv}
 - c. For holding company groups, if performing the review of the group as the lead state, or receiving the lead state's group analysis summary, and assessing the impact of the group on the domestic insurer, incorporate risks identified related to the domestic insurer into Section III: Risk Assessment.
 - d. For ORSA Summary Reports, if required, when receiving and performing the review of the ORSA Summary Report or receiving the lead state's review, incorporate risks identified that are related to the domestic insurer into Section III: Risk Assessment.
8. **Business Plan and Projections (If Available):** Incorporate risks identified and assessed into Section III: Risk Assessment.
 - a. Identify and assess any material variances between actual financial results compared to the most recent business plan and financial projections.
 - b. Identify and assess any material changes in the business strategy.

ⁱⁱⁱ See footnote i

^{iv} See footnote i

III.A.2. Risk Assessment (All Statement Types) – Quarterly Procedures Worksheet

9. **Analyst Notes of Current Period Results (Optional):** Include any analytical notes of material information.

Source	Notes	Risk Category

Section III: Risk Assessment

Risk Assessment Instructions

Risk Assessment includes the accumulation of information gathered from the sections above, as well as a review of the data, benchmarks and procedures provided in each of the nine branded risk repositories to develop and document a risk assessment of each relevant material risk of the insurer. Analysts should review and use all data relevant and necessary to focus on specific risks to complete the analysis, which may include select data from the risk repositories and other relevant tools. The depth of review will depend on the complexity, financial strengths and weaknesses, and known risks of the insurer.

Analysts should not rely solely on the risk repositories for identification of all risks (or risk metrics) as the repositories are not analysis checklists and do not represent a complete list of possible risks for every analysis. Analysts should customize their analysis to include risks unique to the insurer and utilize risk metrics (whether quantitative or qualitative) that are best suited for measuring the insurer's exposure to those risks. Note that procedures included in each of the branded risk repositories are "best fit" as some procedures may identify risks that could be categorized in more than one branded risk category. Analysts should use their knowledge of the insurer and analytical skills to exercise discretion in re-categorizing risks as needed to document the details of the analysis and to update the IPS. Analysts are not expected to respond separately to procedures or benchmark results in the risk repositories that fall outside the benchmarks, rather, analysts should use their expertise and knowledge of the insurer to tailor the analysis to address those risks deemed material or that warrant further investigation.

Complete the following to identify, document and explain each of the nine branded risks below. Refer to the Analyst Reference Guide discussion for further guidance. Documentation of the analysis should contain sufficient detail to adequately explain the risks identified, the metrics/benchmarks used to assess the insurer's exposure to the identified risks, and the results of the risk assessment (i.e., the level and trend of the insurer's risk exposure).

Quarterly analysis should reflect material changes in the risks from the previous analysis period, identify any new risks in the current period, and reflect changes in the strengths and weaknesses of the insurer. When quarterly changes are not material, analysts may consider including an overall comment as such.

1. **Credit Risk Assessment:** Amounts actually collected or collectible are less than those contractually due, or payments are not remitted on a timely basis. Document the analysis of Credit risk.

Detail of Analysis	Assessment	Trend	IPS - Y/N
#1		↑	
#2		↔	
#3		↓	

III.A.2. Risk Assessment (All Statement Types) – Quarterly Procedures Worksheet

2. **Legal Risk Assessment:** Non-conformance with laws, rules, regulations, prescribed practices or ethical standards (in any jurisdiction in which the entity operates) will result in a disruption in business and financial loss. Document the analysis of Legal risk.

Detail of Analysis	Assessment	Trend	IPS - Y/N
#1		↑	
#2		↔	
#3		↓	

3. **Liquidity Risk Assessment:** Inability to meet contractual obligations as they become due because of an inability to liquidate assets and/or obtain adequate funding without incurring unacceptable losses. Document the analysis of Liquidity risk.

Detail of Analysis	Assessment	Trend	IPS - Y/N
#1		↑	
#2		↔	
#3		↓	

4. **Market Risk Assessment:** Movement in market rates or prices (such as interest rates, foreign exchange rates or equity prices) adversely affects the reported and/or market value of investments. Document the analysis of Market risk.

Detail of Analysis	Assessment	Trend	IPS - Y/N
#1		↑	
#2		↔	
#3		↓	

5. **Operational Risk Assessment:** The risk of financial loss resulting from inadequate or failed internal processes, personnel and systems, as well as unforeseen external events. Document the analysis of Operational risk.

Detail of Analysis	Assessment	Trend	IPS - Y/N
#1		↑	
#2		↔	
#3		↓	

6. **Pricing/Underwriting Risk Assessment:** Pricing and underwriting practices are inadequate to provide for risks assumed. Document the analysis of Pricing/Underwriting risk.

Detail of Analysis	Assessment	Trend	IPS - Y/N
#1		↑	

III.A.2. Risk Assessment (All Statement Types) – Quarterly Procedures Worksheet

#2		↔	
#3		↓	

7. **Reputation Risk Assessment:** Negative publicity, whether true or not, causes a decline in the customer base, costly litigation and/or revenue reductions. Document the analysis of Reputational risk.

Detail of Analysis	Assessment	Trend	IPS - Y/N
#1		↑	
#2		↔	
#3		↓	

8. **Reserving Risk Assessment:** Actual losses or other contractual payments reflected in reported reserves or other liabilities will be greater than estimated. Document the analysis of Reserving risk.

Detail of Analysis	Assessment	Trend	IPS - Y/N
#1		↑	
#2		↔	
#3		↓	

9. **Strategic Risk Assessment:** Inability to implement appropriate business plans, to make decisions, to allocate resources or to adapt to changes in the business environment will adversely affect competitive position and financial condition. Document the analysis of Strategic risk.

Detail of Analysis	Assessment	Trend	IPS - Y/N
#1		↑	
#2		↔	
#3		↓	

Section IV: Update Insurer Profile Summary (IPS)

Prioritization: Consider any recommendation for a change in the priority designation of the insurer, including justification. Document it by updating the IPS.

PRIOR PERIOD PRIORITY DESIGNATION=	[Analyst Input]
CURRENT PERIOD PRIORITY DESIGNATION=	[Analyst Input]
	Current Quarter
i. Scoring System Result	[Data]
ii. Net Income (Loss)	[Data]
iii. Capital and Surplus	[Data]
iv. Hazardous Financial Condition Regulation	[Analyst Input]

III.A.2. Risk Assessment (All Statement Types) – Quarterly Procedures Worksheet

v. [Insert Other State-Specific Prioritization Criteria]	[Analyst Input]
Rationale for Change:	

Summary and Conclusion: Develop an overall summary and conclusion based on the completion of the risk-focused analysis performed, and document it by updating the IPS, including the Supervisory Plan, if applicable, for the following. **Updates to the IPS may be limited when only material changes exist from the previous analysis.**

1. Summary of the above risk-focused analysis results by risk classification
2. Prospective risks of the insurer in current analysis, as well as to identify future areas for analysis
3. Impact of the holding company on the insurer, if received since the last analysis
4. Completed or in-progress communication or other follow-up with the insurer, other areas of the Department of Insurance (DOI), financial examiners and other state insurance regulators
5. Additional analysis yet to be performed
6. Regulatory actions
7. Any other factors or information that, in the analyst's judgment, are relevant to evaluating the insurer's overall financial condition

III.A.3. Risk Assessment (All Statement Types) – Quarterly Quantitative Assessment of Non-Troubled Insurers

Quantitative Risk Assessment

- A. Non-troubled insurers will receive the following automated review each quarter. Troubled insurers will receive a full risk assessment analysis each quarter.

Each quarter, non-troubled insurers should be assessed based on the results of the following automated system. Based on the results of the automated system, you may need to proceed with a full risk assessment analysis. **Also consider any other information that may not be reflected in the quarterly statement but may be known or noted in the analysis file or Insurer Profile Summary (IPS), which could impact the company on a prospective basis prior to relying solely on an automated review.**

- B. If any of the following criteria is met, the insurer may be assigned a full quarterly risk assessment analysis:
1. The insurer is a troubled insurer
 2. Prior year risk-based capital (RBC) is less than 250% (ST)
 3. Prior year triggered the RBC Trend Test (ST)
 4. Scoring System result greater than or equal to:
 - 450 for property/casualty (P/C) insurers
 - 250 for life insurers
 - 200 for accidental and health (A&H) insurers
 - 325 for health entities
- C. Based on the results of the automated system calculations, a full quarterly risk assessment analysis may be completed if the insurer has the following number of “yes” responses from the automated calculations:
1. Four or more for P/C insurers, title insurers and health entities or
 2. Three or more for life/A&H/fraternal insurers

Special Notes: Any automated results in D where the denominator is 0 return a “yes” response.

A default “no” response will be returned for insurers with no net retention for automated results #8 and #9.

For companies that have not filed a prior year-end or quarterly statement (e.g., either a new start-up insurer or exempt from filing), all responses in section D will default to a “yes.” In this scenario, it is recommended the analyst perform a full quarterly risk assessment analysis.

- D. Automated system calculations:
1. Are unassigned funds negative? (ST)
 2. Has surplus/capital and surplus (based on business type) increased $\geq 12.5\%$ (for first quarter), 25% (for second quarter), or 37.5% (for third quarter)? (ST)
 3. Has surplus/capital and surplus (based on business type) decreased $\geq 5\%$ (for first quarter), 10% (for second quarter), or 15% (for third quarter)? (ST)
 4. Has any individual asset category that is greater than 5% of surplus/capital and surplus (based on business type) changed by more than +/- 10% from the prior year-end? (CR, MK, LQ)
 5. Has any individual liability category that is greater than 5% of surplus/capital and surplus (based on business type) changed by more than +/-10% from the prior year-end? (RV, OP, ST)
 6. Are affiliated investments greater than or equal to 75% of surplus/capital and surplus (based on business type), OR unrealized capital loss more than -15% of prior year-end surplus/capital and surplus

III.A.3. Risk Assessment (All Statement Types) – Quarterly Quantitative Assessment of Non-Troubled Insurers

(based on business type)? (CR, LQ)

7. Does the net loss exceed 20% of surplus/capital and surplus (based on business type)? (OP)
8. For property/casualty insurers, title insurers and health entities, is the combined ratio greater than or equal to 100%? (PR/UW, OP)
9. Has net premiums written changed by more than +/- 5% (for first quarter), +/- 10% (for second quarter), or +/- 15% (for third quarter) from the prior year-to-date? (PR/UW)

Follow-up Analysis

If any of the following supplemental filings, information or analyses are received during the quarter, review and assess any risks, and document material risks in the IPS.

- Management Discussion & Analysis (MD&A)
- Audited Financial Statement Report
- Impact of the group on the domestic insurer from the analysis of the Holding Company Analysis (as completed by or received from the lead state)
- Risks related to the insurer from the analysis of the ORSA Summary Report Analysis (as completed by or received from the lead state)
- Business Plan and Projections
- Communications from the insurer, other departments or other regulators

Recommendation for Further Analysis

Does the automated system indicate a full quarterly risk assessment analysis should be performed?

- If “yes,” complete a full risk assessment analysis, or if a full risk assessment analysis was not completed, justify and document the reason(s) on the Quarterly Procedures for Non-Troubled Insurers.
- If “no,” no further actions are required.

III.A.4. Risk Assessment (All Statement Types) – Analyst Reference Guide

Risk Assessment – Financial Analysis

The objective of Risk Assessment is for financial analysts to perform a sufficient level of analysis on all domestic insurers in order to derive an overall assessment that explains the risks of the insurer (including mitigating factors and prospective risks) and summarizes its strengths and weaknesses. Refer to II. Risk-Focused Financial Analysis Framework for further guidance on the risk-focused surveillance process.

Branded Risk Categories

Analysts should have a firm understanding of the branded risk classifications to support the risk assessment process. These risks are discussed in greater detail in each of the nine branded risk chapters but generally are defined as:

- **Credit (CR)**—Amounts actually collected or collectible are less than those contractually due or payments are not remitted on a timely basis.
- **Legal (LG)**—Non-conformance with laws, rules, regulations, prescribed practices or ethical standards (in any jurisdiction in which the entity operates) will result in a disruption in business and financial loss.
- **Liquidity (LQ)**—Inability to meet contractual obligations as they become due because of an inability to liquidate assets and/or obtain adequate funding without incurring unacceptable losses.
- **Market (MK)**—Movement in market rates or prices (such as interest rates, foreign exchange rates or equity prices) adversely affects the reported and/or market value of investments.
- **Operational (OP)**—The risk of financial loss resulting from inadequate or failed internal processes, personnel and systems, as well as unforeseen external events.
- **Pricing/Underwriting (PR/UW)**—Pricing and underwriting practices are inadequate to provide for risks assumed.
- **Reputational (RP)**—Negative publicity, whether true or not, causes a decline in the customer base, costly litigation and/or revenue reductions.
- **Reserving (RV)**—Actual losses or other contractual payments reflected in reported reserves or other liabilities will be greater than estimated.
- **Strategic (ST)**—Inability to implement appropriate business plans, to make decisions, to allocate resources or to adapt to changes in the business environment will adversely affect competitive position and financial condition.

Corporate Governance

As part of the risk-focused surveillance approach, analysts should work with the examination staff to assess the quality and reliability of corporate governance in order to identify, assess and manage the risk environment facing the insurer. This assessment will assist in identifying current or prospective solvency risk areas. Corporate Governance Disclosures will assist in assessing corporate governance of the insurer or the insurer group. (See section VI.D. Corporate Governance Disclosure Procedures) By understanding the corporate governance structure and assessing the “tone at the top,” analysts will obtain information on the quality of guidance and oversight provided by the board of directors and the effectiveness of management, including the code of conduct established in cooperation with the board. To assist in this assessment, analysts may utilize:

- Board and audit committee minutes
- List of critical management and operating committees, the members and meeting frequencies
- Examination findings related to the insurer’s risk assessment and risk management activities
- Sarbanes-Oxley filings and similar filings through the NAIC Model Audit Rule, as applicable

III.A.4. Risk Assessment (All Statement Types) – Analyst Reference Guide

Prospective Risks

A prospective risk is a residual risk that impacts future operations of an insurer. These anticipated risks arise due to assessments of company management and/or operations or risks associated with future business plans. The analyst's understanding of the above nine branded risk classifications includes an assessment of the level of that risk and the ability of the insurer to appropriately manage the risk during the current period and prospectively. These prospective risks require assessment and identification of how they may evolve related to the insurer's overall risk profile. Understanding how risks that may or may not appear urgent now will potentially impact future operations and how management plans to address those risks is key to prospective risk analysis. All insurers have prospective risks. It is highly unlikely that an insurer would be identified as having no prospective risks. The assessment of these nine branded risk classifications both currently and prospectively should be part of the quantitative and qualitative analysis completed within the Risk Assessment Procedures.

Insurer Profile Summary

An Insurer Profile Summary (IPS) should be developed by the domestic state insurance regulator for each domestic insurer. The IPS should be updated each year through the annual risk-focused analysis process, updated after the conclusion of onsite examination activities at the insurer (full-scope or limited scope) and updated as significant information impacting the insurer is identified throughout the year (e.g., quarterly risk-focused analysis or other interim information received). The IPS is intended to provide a high-level overview of the current and prospective solvency of the insurer as well as the ongoing regulatory plan to ensure effective supervision. A separate Supervisory Plan may also be utilized to outline steps to ensure effective supervision for high-priority or potentially troubled insurers.

The IPS should be concise and should contain information related to each of the five elements of the regulatory Risk-Focused Surveillance Cycle:

- Financial Analysis
- Financial Examination
- Internal/External Changes
- Priority System
- Supervisory Plan

In addition, the IPS should provide an assessment of the insurer's prospective exposure to each of the nine branded risk classifications. This assessment is intended to foster improved communication regarding risk exposures between functions (e.g., financial analysis, financial exam, etc.) and across states.

A template that can be used in developing an IPS, including example company information, is provided below; however, the actual form and content should be determined by each respective state as the only required elements of an IPS are those listed above. In addition, each state should determine how it will allocate its resources to create and maintain the IPS. Regardless of who creates and maintains the document, a current version should be available for review and use by assigned financial analysts and financial examiners as well as individuals from other relevant internal departments with a need to access the information (e.g., licensing, rates and forms, legal) upon request. In addition, the IPS should be made available to other relevant states, upon written request, in accordance with the "Insurer Profile Summary Sharing Best Practices Guide" posted on iSite+.

At the end of this chapter is an example of the template of an IPS. (*The interactive template of the IPS and heat map are located in iSite+ below the Risk Assessment Procedures link*)

III.A.4. Risk Assessment (All Statement Types) – Analyst Reference Guide

Continual Review Process

A continual review process is necessary to address ongoing and emerging issues that arise in the solvency monitoring of insurers. For example, to the extent that an analyst completes the Risk Assessment procedures for an insurer and has concerns with an identified risk, this analysis may result in questions posed to the insurer and additional information being supplied to the analyst. In some cases, the state may choose to perform a more in-depth analysis of the identified risk, or it may consider a targeted examination, if warranted. These are a few of many recommendations that could result from the ongoing analysis of an insurer. Other recommendations include:

- Requesting additional information from the insurer
- Obtaining the insurer's business plan
- Requesting additional interim reporting
- Engaging an independent expert
- Meeting with the insurer's management
- Obtaining a corrective action plan from the insurer

Regardless of the final outcome, the results of ongoing analysis should be documented in the IPS.

Financial Examination Assessment

In performing the procedures related to financial examinations, analysts should review information received from the examination function via the Summary Review Memorandum (SRM) and, to the extent necessary, review other key documents as identified by the examiners (e.g., examination report, management letter, etc.). Following the review of the SRM, analysts should be able to update the Supervisory Plan and IPS as appropriate for additional information obtained through the risk-focused surveillance approach. Communication and/or coordination with other internal departments (or other areas within the state insurance department) is crucial during the consideration of these procedures. (See discussion below.) Analysts should also consider the insurer's corporate governance, which includes the assessment of the risk environment facing the insurer in order to identify current or prospective solvency risks, oversight provided by the board of directors, and the effectiveness of management, including the code of conduct established by the board.

Summary Review Memorandum (SRM)

The SRM is a memorandum prepared by examiners at the conclusion of an examination. The SRM includes discussion of the insurer's governance and risk management practices, and a summary, by branded risk classification, of significant exam findings and/or concerns warranting communication. These findings may include overarching solvency concerns, examination adjustments, other examination findings, management letter comments, subsequent events and other residual risks or concerns the examiner may want to communicate to department personnel. The final sections, prioritization level and changes to the supervisory plan provide discussion of the examiner's overall conclusions regarding ongoing monitoring, including specific follow-up recommended for analysts. After reviewing the SRM, analysts may determine that he or she needs to review further documentation to understand the implications for ongoing solvency monitoring.

Financial Condition Examination Report

The fundamental purposes of a full-scope financial condition examination report are: (1) to assess the financial condition of the company; and (2) to set forth findings of fact (together with citations of pertinent laws, regulations and rules) with regard to any material adverse findings disclosed by the examination. The report on examination should be structured and written to communicate to regulatory official's examination findings of regulatory importance.

III.A.4. Risk Assessment (All Statement Types) – Analyst Reference Guide

Management Letter

Management letter comments are considered to be examination workpapers and can be used to present results and observations noted during the examination. These comments are similar to management letter comments frequently made by CPA firms as a result of an audit. Many insolvencies have been caused by mismanagement. When examiners identify systems, or operational or management problems that exist, management letter comments are an opportunity to alert management and other readers of the financial examination report to problems that, if left uncorrected, could ultimately lead to insolvency.

Management letter comments generally contain the following information:

- A concise statement of the problem found
- The factors that caused or created the problem
- The materiality of the problem and its effect on the financial statements
- The financial condition of the insurer or the insurer's operations
- The examiner's recommendation to the insurer regarding what should be done to correct the problem

Examination Follow-Up Procedures

The effectiveness of the financial examination process is enhanced if effective follow-up procedures have been established by the domiciliary state insurance department. Periodically, after a financial examination report has been issued, inquiries should be made to the insurer to determine the extent to which corrective actions have been taken on reported recommendations and findings. Because the examiners have usually moved on to another examination, many states utilize financial analysts to perform this function. A lack of satisfactory corrective action by the insurer may be cause for further regulatory action.

Risk-Focused Examinations

The concept of risk in the risk-focused examination encompasses not only risk as of the examination date, but also risks that extend or commence during the time in which the examination was conducted, and risks that are anticipated to arise or extend past the point of completion of the examination. Risk reviewed as part of the examination process include other than financial reporting (operating) and financial reporting type risks. The risks determined to be relevant for ongoing solvency monitoring should be identified as prospective risks on the SRM and, therefore, communicated to the financial analyst.

Certain information including examination reports is included in the Financial Exam Electronic Tracking System (FEETS) on iSite+. The NAIC requires the full use of FEETS when calling examinations on multistate insurers and recommends the use of FEETS for all examinations.

Phases of Risk-Focused Examinations

The risk-focused examination anticipates that risk assessment may extend through all seven phases of the examination.

- Phase 1 – Understand the Company and Identify Key Functional Activities to be Reviewed: Researching key business processes and business units.
- Phase 2 – Identify and Assess Inherent Risk in Activities: These risks include those previously identified by the department's financial analyst related to the branded risk categories.
- Phase 3 – Identify and Evaluate Risk Mitigation Strategies/Controls: These strategies/controls include management oversight, policies and procedures, risk measurement, control monitoring, and compliance with laws.
- Phase 4 – Determine Residual Risk: Once this risk is determined, the examiner can determine where to focus resources most effectively.

III.A.4. Risk Assessment (All Statement Types) – Analyst Reference Guide

- Phase 5 – Establish/Conduct Detail Examination Procedures: Upon completion of risk assessment, determine the nature and the extent of detailed examination procedures to be performed.
- Phase 6 – Update Prioritization and Supervisory Plan: Incorporate the material findings of the risk assessment and examination in the determination of the prioritization and supervisory plan.
- Phase 7 – Draft Examination Report and Management Letter: Incorporate into the examination report, management letter, and SRM the results and observations noted during the examination.

Goals of Risk-Focused Examinations

- Evaluate an insurer's business processes and controls, including the quality and reliability of corporate governance to identify, assess and manage the risk environment facing the insurer in order to identify current or prospective solvency risk areas.
- Assess the risks that a company's surplus is materially misstated.

Role of the Analyst in Risk-Focused Examinations

The role of the financial analyst in risk-focused examinations should be to assist in the planning and scope of the examination including: (1) provide information from recent analysis performed that identifies current and prospective risks; and (2) provide information to assist examiners in understanding the company (e.g., structure, management, functional areas and business segments, affiliated agreements, etc.).

Communication Between Analysts and Examiners Before and After Examinations

In preparation for an examination, communication between analysts and examiners should include a thorough discussion of key risks (current and prospective) highlighted in the IPS, as well as the company's financial condition and operating results since the last examination. Analysts should be prepared to explain during this discussion the reasons for any unusual trends, abnormal ratios and transactions that are not easily discernible. This discussion should occur through a meeting (in-person or via conference call), rather than only through e-mail exchanges, which are not deemed sufficient to achieve the expectation of a planning meeting with the examiner. During the course of this discussion, analysts should communicate and provide access to relevant information that has already been obtained by the analyst function and is available to the department. It may be specifically helpful for analysts to review the Exhibit B questionnaire and note specific items that have already been accumulated and available to the examiner. Contained in III.A.6 Exam Planning Agenda is an optional tool highlighting agenda items that may be discussed during a planning meeting with the assigned financial examiner in support of the financial exam planning process. The information provided to examiners is also used as input for scheduling and staffing of examinations. Follow-up meetings/calls to discuss analysis of subsequent filings may also be helpful to the examination process.

During the course of the exam, analysts may also be asked to participate in exam interviews in the planning portion of the exam as this would allow analysts to add their insights during the course of the interview process and gain meaningful information as part of this assignment. Examiners should also provide analysts with regular updates on the exam fieldwork to permit the department analyst to incorporate relevant updates in a timely manner.

As the examiners conduct the financial examinations, they should inform analysts of any significant examination findings. At the conclusion of the on-site examination, the examiners and analysts should work together to determine the company's priority score. The development of the management letter to the company should include contributions from the examiners and should be shared with the analyst. Additionally, analysts may have input into the letter. It is strongly recommended that analysts be responsible for evaluating and following up with the company responses to any examination management letter comments, as after the report of the examination has been issued, the analysts will be the primary regulatory contact with the company until the next examination. Analysts should have a good understanding of any material examination findings that in turn may help analysts to focus on their next review.

III.A.4. Risk Assessment (All Statement Types) – Analyst Reference Guide

At the end of the exam, examiners should provide analysts with an SRM that is organized using the branded risk categories. This SRM should comment on the results of the examination and the resulting implications on each of the branded risk categories. Examiners may use the SRM to suggest changes to the branded risk assessments (e.g., if the analyst assessed credit risk as moderate risk with no trend, the examiner may suggest that the category be assessed as high and/or have an increasing trend based on the results of the examination.). Examiners may suggest additional concerns within each branded risk assessment that analysts should consider when updating the IPS. Lastly, the SRM will contain insights into issues of non-compliance, prioritization and ongoing monitoring, and proposed changes to the supervisory plan.

Risk Assessment Levels and Trends

The financial analysis process assigns each risk component within the branded risk classification an assessment level commensurate with the nature, complexity and severity of the risk of either Minimal, Moderate or Significant. Additionally, analysts also assign a trend level to indicate the direction the risk is moving, either decreasing, static or increasing. Although risk assessment levels and trends are based on the judgement of the analyst and supervisor, they should factor in both quantitative and qualitative elements, as well as both current and prospective considerations. Note that within each of the three assessment levels, there may be appropriate grading of the severity of the risk.

With regard to setting individual risk assessments, the level of concern and trend of a risk is not defined relative to other risks facing the insurer. Risks should be assessed individually on each's factors and circumstances. Analysts should not automatically assess the "top" risks of an insurer as Significant, Moderate, or Increasing, if the factors don't meet the criteria for those assessment levels and trend. An insurer may have none, one, or multiple Significant risks, depending upon individual facts and circumstances. Failing to follow this guidance may result in an inappropriately high-risk assessment for the individual risk component, but also for the branded risk category and the overall assessment of the insurer.

Factors that may be given consideration include, but are not limited to, the following:

- **Significant:** The highest level of severity of risk from a solvency perspective. Risks assessed at this level require an elevated level of ongoing monitoring and/or regulatory actions.
 - A risk that has the potential to result in the future insolvency of the insurer, independently or in combination with other significant risks
 - A risk that impacts the going concern of the insurer or a major line of business of the insurer
 - A risk that represents a trend that if continued may result in a prospective necessity for the insurer to make significant changes in its business strategies or operations
 - A risk that represents a potential for material financial loss (i.e., earnings, surplus, asset value decline, etc.)
 - A risk identified by the insurer as high/critical/significant (i.e., through Own Risk and Solvency Assessment (ORSA) or communication with the insurer)
 - A risk that has rapidly escalated in severity due to known or unforeseen circumstances (e.g., economic impacts that result in significant decline in market value of assets)
 - A material risk for which the insurer has no mitigation strategy
 - A risk of an affiliate that could have a materially adverse impact on the insurer due to interdependencies (e.g., financial losses/strain at a subsidiary for which the insurer is the parental capital support, operational or strategic changes at the holding company that negatively impact or increase the risks of the insurer, financial solvency concerns of the parent, etc.)
 - A risk identified as a high risk during a recent financial condition examination

III.A.4. Risk Assessment (All Statement Types) – Analyst Reference Guide

- A risk related to a business activity that is significant and/or transactions are large in relation to the company's financial strength. Complexity and volatility are higher than normal.
- A risk that is occurring frequently
- A risk/event that results in a material rating agency downgrade
- A risk/event that requires board of director or senior management attention to address the issue
- A risk that impacts shareholder value or reputation currently
- **Moderate:** The medium level of severity of risk from a solvency perspective. Risks assessed at this level require routine ongoing regulatory monitoring and oversight and/or regulatory action.
 - A risk that represents a potential for some financial loss (i.e., earnings, surplus, asset value decline, etc.)
 - A risk identified by the insurer as a moderate risk (i.e., through ORSA or communication with the insurer)
 - A material risk for which the insurer has a mitigation strategy but that does not fully mitigate the risk
 - A moderate risk of an affiliate that could have some negative impact on the insurer due to interdependencies (e.g., financial losses/strain at a subsidiary for which the insurer is the parental capital support, operational or strategic changes at the holding company that negatively impact or increase the risks of the insurer, financial solvency concerns of the parent, etc.)
 - A risk that continues to worsen, though not rapidly, and for which no improvement in the risk is expected
 - The risk poses a prospective threat to financial solvency
 - A risk identified as a moderate risk during a recent financial condition examination
 - A risk related to a business activity that is significant, but transactions are moderate in size in relation to the company's financial strength. Complexity and volatility are easily managed.
 - A risk/event that requires senior or middle management attention to address the issue
 - A risk where the shareholder value or reputation could be impacted prospectively in the short term
- **Minimal:** The lowest level of severity of risk from a solvency perspective. Risks assessed at this level do not currently indicate a need for additional monitoring or regulatory actions.
 - A risk determined to be minimal due to the adequacy of mitigating strategies
 - A risk that does not pose a financial solvency concern
 - A risk with limited materiality
 - A risk that has improved from a moderate assessment but are not yet diminished to the point of being excluded
 - A risk related to a business activity or transactions that is remote or would have an insignificant impact to the company's financial strength
 - A risk/event that is handled by junior management to address the issue
 - A risk that has no impact on shareholder value or reputation

Factors that may be given consideration when assigning a trend include, but are not limited to the following:

- **General Considerations:**
 - Consider trending within quantitative metrics to assist in determining the trend assessment

III.A.4. Risk Assessment (All Statement Types) – Analyst Reference Guide

- Consider qualitative factors such as the insurer's planned business strategies to address the risk
- Consider both historical/current and prospective/planned trends in exposure.
- **Increasing Trend:**
 - The risk has historically increased year-over-year and continues to increase
 - The risk has the potential to increase prospectively if not addressed
 - The risk is expected to increase prospectively as outlined in the company's business plan and projections
 - The risk has escalated rapidly and materially from the prior analysis period but may have been static in the prior years
- **Static Trend:**
 - The risk has historically remained consistent year-over-year with only minor fluctuations
 - The risk is being addressed and no further fluctuation is expected in the near future
 - The company's business plans and projections don't show any significant movement in risk exposure
 - The risk is not likely to change materially in the future
- **Decreasing Trend:**
 - The risk has been on a historically declining trend year-over-year and continues to decrease
 - The risk is being addressed and is expected to decline in the near future
 - The risk is expected to decrease prospectively as outlined in the company's business plan and projections
 - The risk has declined materially from the prior analysis period

Developing an Overall Assessment

Risk assessment, either for an individual risk component or for the overall branded risk classification reflected in the heat map of the IPS, should be based on the ultimate overall assessment of the risk to the insurer, which should take into account any known positive attributes including risk-mitigation strategies and internal controls established by the insurer to ensure management's business objectives are being followed. Risk-mitigation strategies and internal controls are assessed during examinations; however, they may not all be apparent or known to analysts during interim analysis periods. To the extent known either through current analysis, recent examination results or communication with the insurer, analysts should factor risk-mitigation strategies and internal controls into the overall assessment of the risk. Analysts should also consider that changes in risk-mitigation strategies and internal controls may occur between examinations, which will affect the overall risk assessment process. Therefore, the overall assessment reflects the ultimate impact of risks on the insurer after consideration of mitigation strategies and controls.

Examples of risk-mitigation strategies that may be considered positive attributes during the analysis may include (but are not limited to):

- reinsurance programs intended to mitigate underwriting & strategic risks
- derivatives hedging programs intended to mitigate market risks
- strong enterprise management controls over IT systems to mitigate operational risks
- regular auditing and strong oversight of MGAs & TPAs to mitigate underwriting and operational risks
- strong corporate governance and enterprise risk management that mitigate various risk components

III.A.4. Risk Assessment (All Statement Types) – Analyst Reference Guide

- capital maintenance agreements with a financially strong parent holding company that ensure payment of claims and/or maintenance of capital above certain thresholds to mitigate strategic risk

Discussion of Annual Procedures

The Risk Assessment annual procedures are designed to identify and assess potential areas of concern, including prospective risks. The Risk Assessment procedures are comprised of the following four sections, which collectively represent a complete analysis of an insurer: (1) Background Analysis; (2) Current Period Analysis; (3) Risk Assessment; and (4) Update the IPS.

The department should generally follow the risk-focused financial analysis process outlined in this Handbook to ensure that appropriate analysis procedures are performed on each domestic insurer. The documentation must be prepared in sufficient detail to provide a clear understanding of the work performed and conclusions reached.

SECTION I: BACKGROUND ANALYSIS

The background analysis is intended to assist analysts in “pre-analysis” procedures, including identifying current prioritization of the analysis of the insurer, current and prospective risks identified in the prior analysis, and new information provided by other inter-state departments. **The procedures outline a thought process for analysis; however, there is no documentation requirement in this section.**

Any comments or notes on key issues analysts chooses to include in this section to assist in developing the scope of the analysis should be concise and may include links to source documents but should avoid lengthy restatements of narratives from prior period work papers.

PRIOR PERIOD ANALYSIS AND PRIORITIZATION PROCEDURE #1 provides guidance to analysts in determining if any conclusions reached in prior period(s) analysis (annual and/or quarterly) of the insurer should be considered in the work to be completed for the current year. Areas of concern noted in the prior period and/or insurers who were classified as priority companies in the prior period should be reviewed carefully in the current year. Analysts should use their state’s definition/criteria for determining the hazardous financial condition of an insurer. Analysts should review the IPS (including the Supervisory Plan, if applicable), for any concerns or risks that may require additional attention during the current analysis. While analysts may choose to highlight a few material issues that should be carried forward to the current analysis, it is not expected that analysts restate the prior period IPS. Material information and risks in the current period analysis should be documented in Section III: Risk Assessment.

PRELIMINARY ANALYSIS: States have the option to conduct a preliminary analysis of non-priority companies. If a preliminary analysis indicates no immediate concerns, then analysis of non-priority insurers should be completed by analysts and reviewed by supervisors by the end of July. This provides an extension of the non-priority deadline that is normally the end of June. Preliminary analysis performed and relied upon for analysis completion dates should be completed within two weeks from receipt of filing.

- Determination of “no immediate concerns” should be based on sound judgement and knowledge of the insurer.
- The following considerations are recommended to be included in preliminary analysis:
 - Has the minimum capital and surplus requirements been met?
 - Did the insurer report a decline in capital and surplus of greater than 10% from the prior year-end?
 - If yes, was the decline due to an ordinary or approved extraordinary dividend, approved reinsurance or other transaction, or has the cause been previously adequately addressed by the insurer?
 - What is the RBC?
 - Did the RBC trigger the RBC Trend Test?

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- Did the insurer report a net loss?
 - If “yes,” did the insurer trigger Hazardous Financial Condition?
- Did the insurer trigger Hazardous Financial Condition from any other criteria?

COMMUNICATION PROCEDURE #2 alerts analysts to review recent inter-departmental communication, as well as communication with other state insurance departments and the insurer that may not be included in the prior-period risk assessment or IPS. Internal communication may include departments such as examination, licensing and admissions, consumer affairs, rate filings, policy/forms analysis, agents’ licensing, legal, and market conduct. It may be necessary to communicate with other state departments if a multi-state domestic insurer writes a significant amount of business in other states. Additional communication with the insurer throughout the year should be reviewed to identify any items or areas that may require special attention during the analysis process. Refer to the introductory chapters for further discussion on internal and external communication.

EXAMINATION PROCEDURES #3 AND #4 are intended to assist analysts in determining if information from a recent examination is available and analyst follow-ups are outstanding OR if a new examination is in the planning phases or soon to be in a planning phase so that analysts can perform necessary analysis and communication with the examiners to assist in the risk-focused examination process. Information collected from this procedure should be included in the related branded risk assessment of the insurer.

NOTE: If no exam is being planned, then #3 is not applicable. If the findings and follow-up analysis from the most recent exam have been completed and documented in a prior period analysis, with no further follow-up required, then #4 is not applicable.

Procedure #3 assists analysts in participation in the planning of upcoming examination activities and gathering specific information related to the insurer’s most recently completed financial examination. As stated above, communication between the analyst and the examiner in preparation of an examination should include a thorough discussion of key risks and concerns highlighted in the IPS, as well as additional information from the risk assessment on the company’s financial condition and operating results since the last examination.

Procedure #4 assists analysts in assessing results of the latest examination. In following up on completed examinations, analysts should identify any items or areas that indicate further review is necessary. This might include such things as internal control issues, risk management, information technology, or other issues that could impact the insurer’s priority. Analysts should review the SRM and to the extent considered necessary, the Examination Report and management letter comments, which may include risks or progress on issues that the analyst should give attention to while the current analysis is being performed. Analysts should consider the impact of the examination findings on the conclusions reached as a result of the current analysis and the need to perform detailed analysis on identified risks. Effective communication between the analyst and the examination staff is important in developing a good understanding of the insurer’s management and financial position. As an example, the examination staff may have specific information on the reliability of the insurer’s financial reporting.

SECTION II: CURRENT PERIOD ANALYSIS

Comments or notes on key issues analysts chooses to include in this section to assist in developing the scope of the analysis should be concise and may include links to source documents but should avoid lengthy narratives that duplicate the documentation in Section III: Risk Assessment. Large variances noted in the current period review that do not warrant inclusion in Section III or the IPS may be documented in this section. However, avoid lengthy documentation or investigation of small or immaterial variances.

FINANCIAL REPORTING AND DATA APPLICATION PROCEDURE #5: The intent of the current period analysis section of the Risk Assessment procedures is analysts to perform a review of current results that may identify a change from the prior period or a new risk that should either be updated or further analyzed and documented in

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the Section III: Risk Assessment. Analysts should use their knowledge, expertise and professional judgement to complete a thorough analysis of the current period financial results.

Analysts should review and consider information from data sources including the Annual Financial Statement, Actuarial Filings, Financial Ratios and Financial Analysis Solvency Tools, MD&A and the Audited Report in conducting a risk-focused analysis. The review should be evidenced by sign-off and dating of the information source, a procedure step (i.e., within TeamMate TeamStores), a simplified checklist developed by the department, or within Section II #5. Note that signoff of the completed risk assessment would not be considered a signoff of the review of source information.

MANAGEMENT ASSESSMENT PROCEDURES #6A AND #6B assist analysts in determining if changes in the insurer's management or board of directors have occurred. Changes such as these can have a significant impact on the ongoing operations of the insurer and management philosophy. Changes in the board of directors may also indicate changes in the audit committee. When assessing management, analysts should take into consideration not only the changes in management, but also the analyst's and examiner's knowledge about the current management team and any concerns that may exist regarding management. While management changes alone may not indicate a problem, knowledge of these changes may help analysts understand other potential problems. Information and risks identified from this assessment should be documented in the related branded risk classifications in Section III: Risk Assessment.

With regard to corporate governance, there are many aspects that require consideration, such as: adequate competency; independent and adequate involvement of the board of directors; multiple channels of communication; code of conduct between the board and management; sound strategic and financial objectives; support from relevant business planning; reliable risk management processes; sound principles of conduct; reporting of findings to the board; adoption of Sarbanes-Oxley provisions; and board oversight and approval of executive compensation and performance evaluations.

Analysts should review the biographical affidavits for any new officers, directors, or trustees; follow up on any previously identified unusual corporate governance items or areas of concern; and consider whether changes identified will alter management philosophy. Analysts should pay close attention to responses regarding any suspensions, revocations or non-approval of licenses, conflicts of interest, civil actions, or criminal violations and follow up on any areas of concern. In performing such review, analysts should also consider on a regular basis whether officers, directors and trustees are suitable for the positions they hold within an insurer. Suitability includes considering whether the individual has the appropriate background and experience to perform the duties expected of his or her position. Communication with other state insurance departments (and also possibly with international regulators) may be necessary if the officer previously worked for an insurer domiciled in another state.

MANAGEMENT ASSESSMENT PROCEDURE #6C directs analysts to determine whether the insurer was a party to a merger or consolidation, which can have a significant impact on the ongoing operations of the insurer. This procedure also directs analysts to determine if significant changes in the organizational structure or management have taken place. While organizational changes alone may not indicate a problem, knowledge of the change may help analysts understand the insurer's future plans and goals. Additionally, analysts should verify that Form A or additional filings have been approved.

MANAGEMENT ASSESSMENT PROCEDURE #6D requires analysts to review the Annual Financial Statement, General Interrogatories, Part 1, #6.1 and #6.2, to determine whether the insurer had any Certificates of Authority, licenses or registrations (including corporate registration if applicable) suspended or revoked by any governmental entity during the reporting period and investigate the reason(s) for the action(s).

COMPLIANCE ANALYSIS PROCEDURE #7: States generally have specific compliance analysis that is performed (e.g., compliance with hazardous financial condition and investment limitation laws, or compliance with state statutes on minimum capital and surplus standards). The procedure directs analysts to identify if the insurer is in compliance with the state's statutes and regulations that could have an impact on the insurer's financial position or reporting. To the extent that information is available regarding a new or revised statute or regulation,

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analysts should determine if the insurer has failed to comply with the new state statutes and/or regulations that have been enacted during the period. Analysts may choose to include a link to other work papers, but generally it is not expected that compliance also be documented here. Information and risks gathered from these analyses should be considered and documented in the review of related branded risk classifications in Section III: Risk Assessment.

SUPPLEMENTAL FILINGS PROCEDURE #8 requires analysts to review supplemental filings and other state compliance analysis, including a review of filings such as the MD&A, the Audited Financial Statement, Holding Company Analysis and the ORSA Summary Report (if applicable), to determine if any information is provided in these filings that helps identify or explain risks (current and prospective), trends or other information that can be used in the assessment of specific risks within each branded risk classification. If received prior to the completion of the annual analysis, any issues or risks identified and investigated as a result of the review of the filing should be documented in the related branded risk classifications in Section III: Risk Assessment. Risks identified and assessed in filings received after the completion of the annual analysis should be documented in the subsequent quarterly analysis and, if warranted, the IPS.

The review should be evidenced by sign-off and dating of the information source.

BUSINESS PLAN AND PROJECTIONS PROCEDURE #9 directs analysts to review the business plan of the insurer if it is available from recent surveillance activity, such as in follow-up to a previous analysis or examinations, and if a review of the business plan is considered necessary based on the insurer's priority designation and financial condition. If reviewed, analysts should assess if the plan is consistent with current operations and expectations of projected results. For example, consider if the insurer is writing more or less premium or different lines of business outlined in the plan. Consider if the plan is consistent with changes in the markets or geographical areas where business is being written, or new licenses obtained to write business. Analysts should assess significant variances in the business plan through review of the plan and/or through communication with the insurer. If a business plan is not available or current and, based on the analysis performed, the analyst feels it is necessary to request a business plan and recommend further analysis in this area, the analyst should consider requesting a new business plan as part of any analysis follow-up with the insurer. If received prior to the completion of the annual analysis, any issues or risks identified and investigated as a result of the review of the filing should be documented in the related branded risk classifications in Section III: Risk Assessment. Risks identified and assessed in filings received after the completion of the annual analysis should be documented in the subsequent quarterly analysis and, if warranted, the IPS.

REQUESTING BUSINESS PLANS AND PROJECTIONS – The following are examples of scenarios when it may be appropriate to request business plans and multi-year pro-forma financial projections as part of risk-focused analysis and assessment of prospective risks for both legal entities and holding company groups, by the domestic or lead state (in the case of groups). Note this list is not all-inclusive as other situations may occur where requesting a business plan and projections may be appropriate.

- For non-troubled insurers, it may be sufficient to receive updated business plans and projections less frequently than every year.
- For non-troubled insurers that have indications of material changes occurring or expected, for example through communication between the insurer and the state insurance regulator, or reflected in financial results, it may be appropriate to request updated business plans and projections more frequently, such as annually.
- For troubled insurers, it may be appropriate to request updated business plans and projections annually.
- When concerns are noted during risk-focused analysis, holding company analysis and/or when actual results vary materially from previously provided projections, requesting an updated business plan and projections may be an appropriate action along with communication with the insurer/group for explanations of the concerns.

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- As noted below in #11-Information Request, it may be necessary to request a business plan and projections to assess the insurer's strategy, which impacts various risk categories primarily, operational and strategic risks.
- As a result of financial examination findings, monitoring of certain risks may require a request for a business plan and projections.
- If the insurer submits an application for Certificate of Authority to write business in the state, it may be appropriate to request additional information including a business plan and projections.
- For insurers undergoing a merger or acquisition, business plans and projections are generally included in the Form A application and approval process (see V.B. Form A Procedures). Upon completion of the Form A, it may be appropriate to request updated plans and projections after a year or more to determine if any concerns exist regarding the insurer's actual results subsequent to acquisition.

ANALYST NOTES #10 (OPTIONAL): This optional section may be used as a tool for notating any material information from above that, for example, is not specific to assessment of risks in Section III: Risk Assessment; or short notations regarding the analyst's completion of their review. Comments or notes on key issues analysts chooses to include in this section to assist in developing the scope of the analysis should be concise and may include links to source documents. It may also be beneficial to provide a reference to where the issues are addressed within Section III: Risk Assessment. However, to avoid inefficiencies, analysts should avoid the creation of notes that are lengthy narratives that duplicate or replace the documentation in Section III: Risk Assessment. Instead, the detailed discussion of risks and results of analysis should be documented in Section III: Risk Assessment.

INFORMATION REQUEST PROCEDURE #11: In order to effectively enhance risk-focused financial analysis, state insurance regulators may need to gain a greater understanding of the insurer's strategies, risk exposures and business operations. While a general understanding of the insurer can be obtained through a review of regulatory filings and publicly available information, additional information may be needed on certain strategies, risk exposures and business operations before the insurer can be fully understood and evaluated.

State insurance regulators should first review existing sources of information available to the department (e.g., annual and quarterly statement Notes to Financial Statements and General Interrogatories, MD&A, filed business plans, recent examination results, etc.). Additionally, if the insurer is part of a holding company group and the department is not the lead state, if not already provided by the lead state, the non-lead state should contact the lead state to obtain analysis already prepared by the lead state for additional holding company group information (i.e., the Group Profile Summary). For Corporate Governance Annual Disclosure (CGAD) filed don a group basis and the Enterprise Risk Report (Form F), the non-lead states should rely on the information provided in the GPS, or other information provided by the lead state on material risks relevant to the insurance entity. Contacting the lead state first will help eliminate the duplicate requests for holding company group level information.

If it is determined that additional information is still needed, state insurance regulators may choose to conduct in-person meetings with the insurer, hold conference calls, submit written information requests or take other steps necessary to obtain a sufficient understanding of the insurer. If meetings or conference calls are scheduled with the insurer to gather additional information, state insurance regulators should give consideration to the level at which the meetings should be conducted (i.e., legal entity, intermediate holding company, or ultimate controlling parent) and involve the lead state and other affected state insurance regulators in the process as appropriate. If a meeting is conducted at the group level, lead states may also wish to consider topics and questions outlined in V.H. Periodic Meeting with Group.

The following table highlights topics where the information available through regulatory filings may not be sufficient to provide an adequate understanding of the insurer.

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General Topic and Description (The suggested areas of understanding within each general topic below are not meant to be an all-inclusive list.)	Primary Branded Risks
Underwriting Strategy – Understand the insurer’s overall underwriting strategy and goals, including its target market(s), geographic locations, products/lines of business, profitability challenges and distribution channels.	PR/UW, RV
Reinsurance Strategy – Understand the insurer’s overall reinsurance strategy, including its identification and modeling of risk exposure and concentrations, reinsurance program structure (affiliated and non-affiliated), reinsurer selection, and quality.	CR, PR/UW, LQ, ST
Investment Strategy – Understand the insurer’s investment strategy and goals, including its policies and guidelines that specify the type, credit quality and maturity of investments to be held. In addition, understand roles and responsibilities related to investment decision-making, oversight and reporting.	CR, MK, LQ, ST
Legal and Regulatory Issues – Understand significant legal, ethical and regulatory issues affecting the insurer’s current and prospective solvency, including the status or results of ongoing/recent regulatory investigations, pending/upcoming regulatory filings (e.g., rate filings, Form Ds, etc.), material ongoing litigation, and violations of the insurer’s code of ethics.	LG, RP
IT Systems – Understand significant changes made to IT systems since the last examination, including related implementation and transition plans, cybersecurity measures, etc.	OP, LG
Outsourcing of Functions – Understand the significant functions outsourced by the insurer to third parties, including the insurer’s use and oversight of MGAs/TPAs, investment advisers, producers, custodians, and affiliated service providers.	OP, RP, LG
Risk Management (for non-ORSA filers) – Understand the overall risk management practices in place at the insurer, including how material and relevant risks are identified, assessed, monitored, managed, and reported.	ST, OP
Business Plans – Understand the insurer’s overall business plans, including its historical performance against projections, as well as current/future goals and initiatives.	ST, OP
Overall Strengths and Weaknesses – Understand the insurer’s view of its overall strengths and weaknesses, including market position, financial resources, reputation and competition.	ST, OP, RP

Once state insurance regulators have a sufficient understanding of the insurer in relation to all identified areas of importance, as determined by the analyst’s judgment, such an understanding should be updated through the IPS and/or the Risk Assessment Analysis or other analysis documentation to facilitate effective and efficient analysis processes. In years where the insurer is currently undergoing or preparing for a financial condition examination, such an understanding should be maintained, communicated and updated through participation in the examination process. In other years, the steps highlighted above (e.g., meetings with the insurer, conference calls or written information requests) may be necessary to supplement or update the state insurance regulator’s understanding. However, once the initial understanding is obtained, such steps should focus on changes in strategies, risk exposures and business operations in an effort to promote efficiency.

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SECTION III: RISK ASSESSMENT

Risk assessment includes the documentation of information reviewed in Section I and Section II, as well as a review of the data, benchmarks and procedures provided in each of the nine branded risk repositories to develop and document a risk assessment of each relevant material risk of the insurer.

Depth of review and level of documentation:

- The depth of review and level of documentation should be commensurate with the nature, complexity, financial strengths and weaknesses, and known risks of the insurer. New risks and significant changes in exposures will require more investigation than risks that the insurer has routinely been exposed to and that don't change materially year-over-year.
- Other factors, such as the insurer's past regulatory history, accuracy of filing, age of insurer, stability of business plan, and knowledge of the insurer's operations, materiality of the concerns etc., may affect the scope and depth of analysis. The flexibility to customize the scope and depth of the analysis is determined at the state insurance department's discretion, should include analyst and supervisor input and may vary between analyses. Therefore, the state insurance department should tailor the data and procedures used and the level of documentation to sufficiently address the specific risks of the insurer. It is expected that the risk assessment documentation will be at a level that is more detailed than the IPS.
- In certain situations, it may be appropriate to reference documentation located in another area of the analysis file (e.g., Form D review, ORSA review template) as opposed to duplicating the documentation here. However, in such situations, the risk component title should still be presented, along with a conclusion on the current level of concern/trend in Section III, with a cross-reference to supporting documentation provided in other areas of the file. When doing this, the analyst should carefully consider whether the risk exposure has shifted since it was assessed in another area of the file and whether the level of concern/trend conclusion is adequately supported by the cross-referenced work.

Branded Risk Repositories:

- **Analysts should not rely solely on the risk repositories for identification of risks as the repositories do not represent a complete list of possible risks. Analysts should customize their analysis to identify and assess risks unique to the insurer.**
- It is not necessary and may be inefficient and unproductive to include every risk component from the repositories in the analysis if it is not applicable to the insurer.
- The risk repositories are a tool for helping identify and investigate risks; however, there is no documentation requirement within the repositories themselves.
- Analysts are not expected to respond separately to procedures or benchmark results in the risk repositories that fall outside the benchmarks, rather, analysts should use their expertise and knowledge of the insurer to tailor the analysis to address those risks they deem material or that warrant further investigation.
- Analysts may choose to use the repositories as a starting point for analysis; however, alternatively for analysts that have a good understanding of their assigned insurers' risks, the analyst might consider using the repository as a completeness check at the end of their review to ensure they have not overlooked any material issues.
- Note that procedures included in the branded risk repositories are "best fit" as some procedures may identify risks that could be categorized in more than one branded risk category. Analysts should use his or her knowledge of the insurer and critical thinking skills to exercise discretion in re-categorizing risks as needed to document the details of the analysis and to update the IPS.
- Analysis results from the repositories should be documented in Section III: Risk Assessment section of the worksheet.

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For reserving risk: Analysts should also consider the risk repository for review of the Statement of Actuarial Opinion and other related actuarial filings. For property/casualty (P/C) insurers, this includes completion of the Actuarial Opinion Summary procedures. For life/health and fraternal insurers, this includes completion of the procedures for the Regulatory Asset Adequacy Issues Summary (RAAIS).

For Title insurers: Analysts should first utilize the III.C.3 Title Insurer Worksheet to develop the risk assessment, and then reference the applicable risk repositories as needed.

Inclusion in the IPS: The Risk Assessment worksheet provides for consideration of whether the risk warrants inclusion in the IPS, the assessment level (minimal, moderate, or significant) and the trend (static, decreasing or increasing). Not all issues analyzed will warrant inclusion on the IPS due to materiality or other reasons.

Refer to the Analyst Reference Guide branded risk chapters for explanation of the risk category and of the data, benchmarks and procedures provided for each.

SECTION IV: UPDATE INSURER PROFILE SUMMARY

At the conclusion of the analysis, analysts should also assess the priority level based on the results of the current analysis. While summary documentation of the rationale for the insurer's priority may be included in the IPS, detailed documentation of the rationale for a change in priority should be included in the risk assessment worksheet.

At the conclusion of the Risk Assessment procedures, analysts are asked to develop and document an overall summary and conclusion based on the results of the risk-focused analysis performed, prospective risks of the insurer, follow-up analysis or regulatory actions, impact of the holding company on the insurer, and any correspondence. Analysts should update the IPS (and supervisory plan, if applicable). **Note that an analyst's documentation of the Section III: Risk Assessment and other cross-referenced work represents the *detail* of the analysis of risks, which should be more in-depth for certain material risks or complex insurers, whereas the IPS represents a *summary* of the risks of the insurer for purposes of communication to other state insurance regulators and departments.**

Ensure that all nine branded risk classifications are addressed in the IPS, even if documentation is limited to *"Assessment of this risk classification was performed, and no material risks were identified for this risk."* Where no individual risk components were identified within a branded risk classification, it is acceptable to include a statement, such as the above, in the narrative of the branded risk classification and list no risk components in the table, so as to avoid listing items that do not represent a risk to the insurer (i.e., generic or positive attributes). Positive attributes may be included in the narrative or other areas of the IPS as appropriate (e.g., background, strengths and weaknesses).

Because some items, such as the Audited Financial Report and the various holding company filings are not required to be filed until after most of the annual review is completed, analysts will document a conclusion based on the current analysis of the insurer. The Audited Financial Report should be reviewed upon receipt, and if additional concerns are noted, the conclusion or the quarterly conclusion should be revised to reflect the most recent information.

While analysts may consider a cursory review of holding company filings when received to identify any material or urgent solvency concerns, the review of holding company filings is required to be completed by October 31st for analysis conducted by the lead state or by December 31st for analysis conducted by the domestic state.

Discussion of Quarterly Procedures

The Quarterly Risk Assessment Procedures are designed to help analysts perform a general review of the insurer with the quarterly filings. The quarterly procedures are similar to the risk-focused annual procedures. However, the quarterly procedures include a review that focuses primarily on changes from the prior year that may identify new or changing risks and leveraging the existing analysis documentation that is still relevant. Quarterly

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analysis should also include assessment of any risks identified in supplemental filings or correspondence received after the annual analysis has been completed. In updating analysis work on a quarterly basis, analysts should:

- Clearly document those risk assessments or sections of the IPS that have been updated in order to avoid confusion when sharing the most current analysis.
- Avoid performing detailed and time-consuming or duplicative analysis work and documentation from year-end if the insurer's exposure has not significantly changed from the prior year.
- Consider limiting quarterly documentation to only those risk components that are new or that have changed significantly from the prior year. If there are no changes in a risk component from the prior year, analysts may consider simply referring to the prior year analysis and commenting in the narrative that no material changes in the risk component have occurred.
- Given the limited data available in the quarterly filings, not all risks may be assessable on a quarterly basis. Therefore, no additional analysis documentation would be expected for these risks.

At the conclusion of the Quarterly Risk Assessment procedures, analysts are asked to develop and document an overall summary and conclusion based on the results of the risk-focused analysis performed, prospective risks of the insurer, follow-up analysis or regulatory actions, and any correspondence. As with the annual review, the Summary and Conclusion should be reviewed and revised as necessary when subsequent procedures and follow-up with the insurer are completed. Analysts should update the IPS (including the Supervisory Plan, if applicable). Note, however, that updates to the IPS may be limited to material changes from the previous analysis.

Discussion of Quarterly Procedures for Non-Troubled Insurers

The Quarterly Procedures for Non-Troubled Insurers are designed to help analysts perform a quantitative review of the insurer and its operations. Analysts should use their state's guidelines and policy for determining whether an insurer is considered to be a troubled insurer to answer procedure B.1. The non-troubled quarterly procedures include key broad-based questions and questions that focus primarily on changes from the prior year.

Updates/New Information:

- Although not required, analysts may consider updating the risk assessment for non-troubled insurers on a quarterly basis if new information or trends regarding various risk exposures or components are identified.
- If the department receives new information to update the IPS with this information, the quarterly risk assessment may not need to be completed since the IPS will be updated for the quarter.
- Analysts can choose to only update the IPS as needed as the risk assessment would be updated during the next annual review so long as the information does not impact whether the insurer would be considered non-troubled.
- If appropriate, analysts may consider including a brief narrative regarding the information received at the bottom of the non-troubled checklist under "Follow-Up Analysis".

Special note for new or previously exempt filers: For companies that have not filed a prior year-end or quarterly statement (e.g., either a new start-up insurer or exempt from filing), all responses in section D will default to a "yes." In this scenario, it is recommended analysts perform a full risk-focused review.

Discussion of Analysis for Intercompany Pooling Arrangements

Intercompany pooling arrangements involve the establishment of a quota share reinsurance agreement under which pooled business is ceded to a lead entity and then retroceded back to pool participants in accordance

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with stipulated shares (if any). This generally results in pool participants sharing exposure to the various insurance risks ceded into the pool. Because of this structure, financial analysts may be able to gain efficiencies by conducting and documenting the analysis of insurance risks associated with the pooled business on a combined basis and then leveraging the results of that work to complete legal entity analysis. For example, in situations where the majority of the group's writings are ceded into the intercompany pool and there are few unique legal entity risks, analysts may choose to create and maintain a combined risk assessment and/or IPS for all of the legal entities participating in the pool (if domiciled in the same state). In other situations, it may be more appropriate to maintain separate risk assessment worksheets and/or IPSs for each legal entity, but to reference work completed in the pool lead's documentation or include substantially similar information in each legal entity's risk assessment worksheet and IPS.

While insurers participating in intercompany pooling arrangements often share exposure to pooled insurance risks, differences in the overall risk exposure of participants may arise due to a number of factors including, but not limited to, the following:

- Surplus/RBC levels
- Balance sheet composition
- Pool participation percentages
- The timing of pool participation
- Premiums not ceded to the pool
- Reinsurance arrangements outside of the pool (e.g., facultative placement prior to cessions to the pool lead)
- Current or legacy risks (e.g., asbestos exposure) disclosed within the financial statement

Regardless of the method utilized to assess and document the analysis of the pool, the financial analyst should ensure that all significant, unique exposures of each pool participant are separately assessed and addressed within analysis documentation.

If pool participants are domiciled in various states, communication and coordination across states is needed to achieve efficiencies in analysis. For example, the domestic state of the pool lead would generally be expected to indicate to the analysts of the other insurers in the pool if it intends to complete a combined risk assessment and IPS and specifically when both will be provided to the other domestic states for their review. This will enable other states with domestics in the pool to leverage the completed work. To allow sufficient time for this coordination to take place, domestic states that intend to place reliance on the work of the pool lead state will have 30-days from the receipt of completed analysis work from the pool lead to complete the analysis of their legal entity or until the end of the prescribed analysis timeline, if longer. During this 30-day review period, prior to accepting the risk assessment and the IPS from the pool lead as satisfying all legal entity analysis requirements, each domestic state should consider and document the following:

- The extent to which they are satisfied with the quality of work performed by the pool lead state and willing to be judged on that work from an NAIC Accreditation perspective (if relevant);
- The extent to which the work performed by the pool lead addresses all relevant and material solvency risks of the individual legal entity, including common differences in the risk exposure of pool participants noted above; and
- The completion of any supplemental, state specific analysis procedures (compliance or otherwise) that are necessary to finalize the legal entity analysis.

In situations where an insurer cedes business to an intercompany pool but does not participate in retrocession, the analysis of the pooled business should be obtained/reviewed to evaluate reinsurance credit risk. If the pool is troubled or potentially troubled, this may require more in-depth analysis to evaluate the potential impact of claims associated with the insurer's direct writings not being covered by the pool.

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Discussion of Non-Routine Analysis

The Handbook contains procedures that assist an analyst in deriving an overall assessment of the insurer's financial condition; however, situations may exist when it is necessary to perform additional procedures and analysis not contained in the Handbook for one or more insurer.

On occasion, events or situations outside of the normal course of business occur that may have a material impact on the overall financial condition of an insurer. During these occasions, state insurance regulators may need to perform non-routine analysis, which may require additional reporting from a specific insurer or from a group of insurers. A few examples of these occasions may include significant financial events such as material investment defaults, credit market stress, or catastrophic events. Non-routine analysis may also be appropriate and necessary in situations impacting a single insurer, a group, or a small group of insurers. For example, when permitted practices are granted, there may be a need to perform follow-up analysis of the situation requiring the permitted practice (e.g., assessing the reliability of deferred tax assets). The state may conduct this analysis itself or enter into an agreed-upon procedures audit with a CPA firm to assist in the assessment and analysis of the projected future deferred tax assets and the impact to surplus.

The following are a few examples of types of non-routine analysis that may be appropriate in an economic downturn, investment defaults, and changes in the credit markets (Note that some or all of these may also be applicable in other non-market or investment related situations).

- Focused analysis on asset quality where insurers hold higher amounts of riskier assets. Analysts should not only consider exposure to individual default events, but also aggregate exposure. Additional review or explanation from the insurer may be requested when high amounts of other-than-temporary impairments, unrealized losses and/or large variances between book and market value are reported. Analysts should review the value of affiliated investments and assess indirect exposure to economic events that may result in the decline in the affiliated holdings. Analysts may consider other sources of analysis or information to assist in the review of investments. For example, an analyst may consider requesting assistance from the NAIC Capital Markets Bureau.
- Analysts should consider the impact of tightened short-term credit markets on insurers or groups that depend on commercial paper, overnight repos, dollar repos, etc. Another area that could be impacted by changes in credit markets is the insurer's ability to obtain letters of credit (LOCs) provided for XXX (life reserves) or other reinsurance reserves, and the costs of those LOCs for an insurer dependent on LOCs.
- If the insurer engages in securities lending, analysts may consider requesting detailed information about the program to review the types of assets (risk and duration match) within the program, gain an understanding of the structure and terms of the program, and, if material, monitor monthly changes in the program.
- Certain insurance products may be impacted more than others in an economic downturn. Analyst should consider the impact to an insurer that writes a material amount of products that are more likely to be accelerated (e.g., funding agreements, guaranteed interest contract (GICs) or where the liability can be accelerated (e.g., variable annuities, living benefit/death benefit on variable annuities).
- Analysts should consider the level of sensitivity of the insurer to ratings downgrades and the possible impact on the insurer or the group. For example, its ability to market new business or the impact of rating downgrades on any debt covenants. If an insurer is downgraded, analysts may consider monitoring surrenders, new business sales, and any changes in the insurer's business plans.
- Where liquidity is a concern, analysts may also consider requesting interim reporting from the insurer on areas of risk specific to that insurer. For example, surrender activity, high-risk investment exposures, GICs, capital and surplus, available liquidity, available credit facilities and capital losses.
- Where significant concerns exist, the state may consider requesting the insurer to perform stress testing on the possible future impacts of additional equity losses, defaults, or other areas relevant to the situation.

Examples of types of non-routine analysis that may be appropriate in catastrophic events:

III.A.4. Risk Assessment (All Statement Types) – Analyst Reference Guide

- Implement disaster reporting requests to appropriate insurers and monitor claims exposure during future periods following the event
- Identify insurers and reinsurers with material exposure
- Implement appropriate procedures to identify fraudulent activities
- Perform an in-depth analysis of liquidity to ensure timely payment of claims
- Engage legal staff to ensure appropriate claims payment practices

III.A.5. Risk Assessment (All Statement Types) – IPS Example

XX DEPARTMENT OF INSURANCE

INSURER PROFILE SUMMARY

COMPANY NAME

As of 12/31/20XX

Updated as of XX/XX/20XX

BUSINESS SUMMARY

Provide a summary of the business operations and lines of business of the insurer.

ABC is an independently owned property and casualty insurance organization based in state X that specializes primarily in writing private passenger automobile insurance coverage. Through its subsidiaries, DEF Insurance Company, GHI Insurance Company, JKL Underwriters, and MNO Premium Finance Company, the group offers a variety of insurance related services including premium finance and claims processing.

REGULATORY ACTIONS

Discuss any significant actions taken against the company, permitted practices, issues of non-compliance, results from the most recent financial examination, etc.

In 20XX, ABC was required to file a corrective action plan with the department to address its breach of the RBC Company Action Level. Since that time, ABC received a capital infusion from its parent and has raised its RBC to an acceptable level. The company has been granted a permitted practice relating to its SCA investment in JKL Underwriters. The permitted practice allows ABC to admit its investment in JKL (\$2 million at 12/31/XX) without requiring an independent financial statement audit.

FINANCIAL SNAPSHOT (SUMMARY DATA) – OPTIONAL

Assets and Liabilities

Years Ended December 31 (Dollars in millions)

	20XX	20XX
Total Invested Assets	219	253
Other Assets	111	131
TOTAL ASSETS	330	384

LIABILITIES

Insurance reserves	97	95
Other liabilities	169	193
TOTAL LIABILITIES	266	288
Capital and Surplus	64	96
TOTAL LIABILITIES AND C&S	330	384

Operations

	20XX	20XX
Premiums	218	233
Investment income (net of gains/losses)	1	8
Other income	0	0
Total revenues	219	241

LOSSES, BENEFITS AND EXPENSES

Policyholder Benefits	177	157
Expenses	77	80
Total losses, benefits and expenses	254	237
Other	0	2
NET INCOME	(35)	2

Insurer's Group Number

List here

Lead State/Groupwide Supervisor

List here

State Prioritization

List X out of X

RBC Ratio

List % here as calculated in the 5-year history by the Company

Insurer's Financial Strength/Credit Ratings

List here

Contact at Insurer

List name here

List phone here

List e-mail here

Key Personnel

List name here – CEO

List name here – CFO

List name here – CRO

List name here – Other

CPA Firm

List here

Appointed Actuary

List here

Analyst

List here

Date of Last Exam

List here

Examiner In Charge

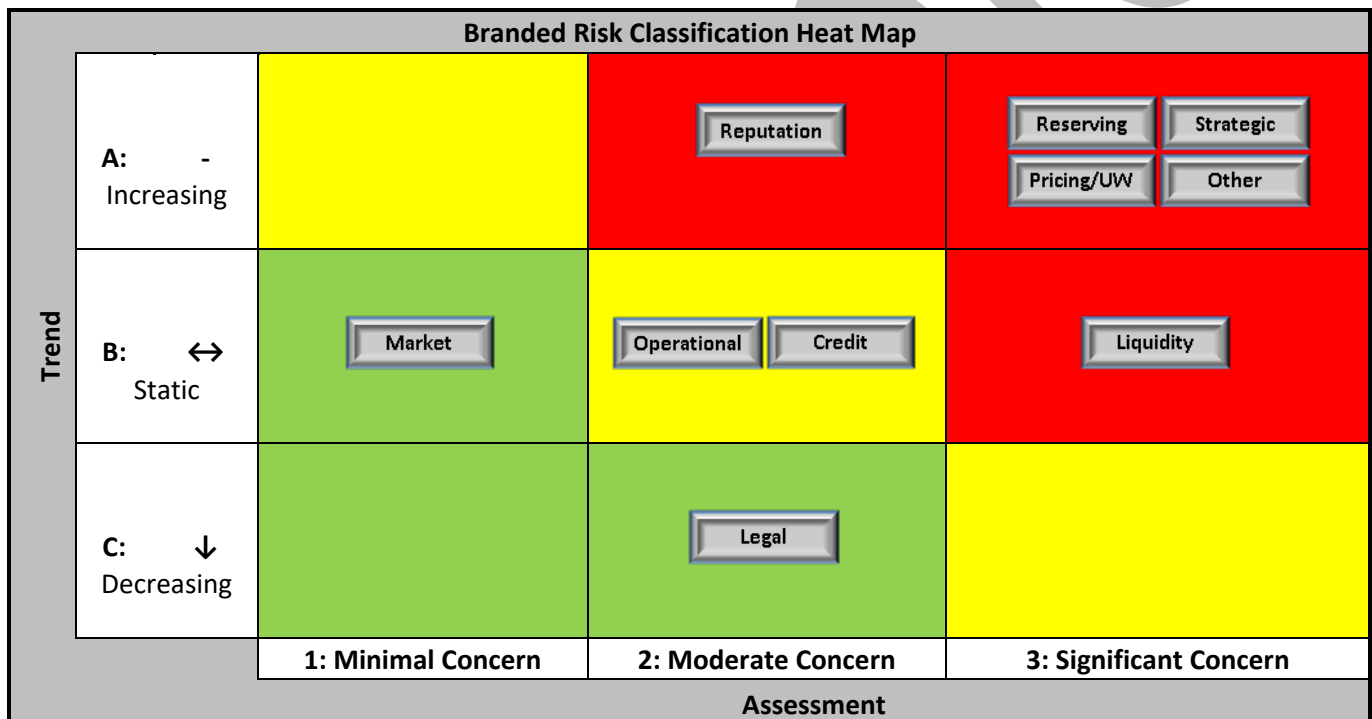
List here

III.A.5. Risk Assessment (All Statement Types) – IPS Example

BRANDED RISK ASSESSMENTS

Summarize your assessment of the branded risk classifications for the insurer based upon both quantitative (e.g., 5-year trending of key ratios) and qualitative information. An assessment of each significant individual risk component (including prospective risks) relevant to the classification should be provided by indicating either “minimal concern,” “moderate concern” or “significant concern” as well as the direction in which the risk is trending. If no significant individual risk components are identified for a branded risk classification, documentation should be provided to support this conclusion. Consider the materiality and/or significance of each individual risk component in aggregating the overall assessment and overall trend for each branded risk classification. Update the Branded Risk Classification Heat Map to illustrate your conclusions.

The following is an interactive map. Click and drag the risk classification to the appropriate section of the risk classification heat map after assessing the trend in each individual category.



III.A.5. Risk Assessment (All Statement Types) – IPS Example

Credit: This risk is considered moderate, driven primarily by a fairly conservative investment mix (96.4% of bonds are NAIC 1 with 28% US government, 14% US states, most of the rest high quality corporates) and limited exposure to equities, offset by a relatively high amount of real estate (\$33 million), growing agent balances (\$99 million) and significant reinsurance recoverables (paid and unpaid) of \$81 million. However, the reinsurance recoverables are diversified across a number of highly rated reinsurers.

Minimal Concern	Moderate Concern	Significant Concern	Trend
Bonds			↑
Reinsurance Recoverable			↑
	Real Estate-Home Office		↔
		Agent Balances and Uncoll Prem	↑
Overall Credit Assessment: Moderate Concern		Overall Trend:	↑

Legal: The Company has a vested interest in the outcome of the case of GEI v. Virtual Imaging which is before the State Supreme Court. This case pertains to a change in statutes, effective January 1, 2008, that affected the manner in which insurers, including the Company, have paid claims. Subsequent to the statutory change, cases have been brought and trial courts have concurred that the statutes and resulting payments are ambiguities in the statutes. These cases are collectively known as the “Fee Schedule” matter. The Company began receiving lawsuits on this matter in May 2010, some of which were closed at high cost. Since that time, the Company has modified its strategy for handling these cases and has received multiple trial victories from juries that ruled no further payments were owed to the plaintiffs. Exam results indicate that the Company’s legal team tracks and monitors outstanding lawsuits and involves experienced external counsel in representing the Company in these matters.

Minimal Concern	Moderate Concern	Significant Concern	Trend
Effectiveness of legal counsel			↔
	Fee Schedule lawsuits		↓
Overall Legal Assessment: Moderate Concern		Overall Trend:	↓

Liquidity: The Company is subject to high liquidity risk due to the lines of business written and the corresponding need to meet short-term obligations. The Company’s high exposure to the volatile PIP market and related losses has reversed the trend of improved liquidity in recent years. Trends in the Company’s five-year liquidity ratio are shown in the following chart, which was indicating improvements before a negative shift in the current year:

	CY	PY	PY1	PY2	PY3
Liquidity Ratio	108.5%	98.3%	101.4%	107.1%	113.0%

Minimal Concern	Moderate Concern	Significant Concern	Trend
		Exposure to PIP Market	↔
		Liquidity Ratio	↔
Overall Liquidity Assessment: Moderate Concern		Overall Trend:	↔

Market: Market risk includes equity risks, changes in credit spreads, and also interest rate risks. Most of these risks are not inherently significant to the Company due to its relatively conservative investment portfolio and relatively short-term policies (typically 6 months or 1 year), which allow the Company to reprice fairly easily to align with shifts in the market. However, as shown during the financial crisis, some of the Company’s products are more sensitive to general economic downturns, which can impact the Company’s performance.

Minimal Concern	Moderate Concern	Significant Concern	Trend
Equity			↔

III.A.5. Risk Assessment (All Statement Types) – IPS Example

Changes in Credit Spreads			↔
	Economic Downturn		↑
Overall Market Assessment: Moderate Concern		Overall Trend:	↔

Operational: The results of the last exam indicated that the Company has a reliable IT environment and effective internal controls in most areas. However, concerns were raised regarding segregation of duty issues relating to the handling of claims and cash disbursements during the last exam. In addition, a recent news report indicated that one of the Company's independent agents has been charged with committing fraudulent activities. Due to the Company's heavy reliance on independent agents to generate business and manage policyholder relations, even though the report might be an isolated incident it represents a moderate concern in this category.

Minimal Concern	Moderate Concern	Significant Concern	Trend
IT Environment			↔
	Segregation of Duties		↔
	Agent Fraud		↑
Overall Operational Assessment: Moderate Concern		Overall Trend:	↔

Pricing/Underwriting: Although the Company is primarily engaged in short-term products (6 months or 1 year), it is subject to highly competitive price pressure and has shown historically weak underwriting results. Underwriting results have shown a negative trend over the past 6 periods as losses incurred continue to rise, a sign that pricing pressures are influencing the bottom line. The Company appears to be utilizing cash flow underwriting as a way to bolster earnings through investment income, which leads to a concern regarding the adequacy/appropriateness of rates used by the Company. In addition, the last financial exam noted a lack of documented underwriting guidelines at the Company, which is in the process of being corrected. However, the lack of documented, detailed underwriting guidelines represents a moderate concern in this area. Overall, this risk category represents a significant ongoing concern for the Company.

Minimal Concern	Moderate Concern	Significant Concern	Trend
	Underwriting Guidelines		↔
		Rate Adequacy	↑
Overall Pricing/Underwriting Assessment: Moderate Concern		Overall Trend:	↑

Reputation: The Company's business is not rating sensitive, but the Company is highly dependent upon business produced by agents. As noted above, a recent concern has been identified regarding potential fraud committed by one of the Company's agents. In addition, the findings of a recent market conduct examination led to numerous violations. These violations related to claims handling issues, such as failure to comply with timely payments and denial of legitimate claims. Although the Company has disputed these findings, gross writings continue to suffer as several agents have stopped writing on behalf of the Company.

Minimal Concern	Moderate Concern	Significant Concern	Trend
	Agent Fraud		↑
	Market Conduct Findings		↑
Overall Reputation Assessment: Moderate Concern		Overall Trend:	↑

Reserving: The Company is subject to high reserving risk, as shown in the following reserve trending of information. The Company historically has been overly optimistic in the forecasting of future liabilities and reserving, where actual reported results have failed to meet projections. The types of business written and geographic regions in which coverage is provided leave the Company vulnerable to high losses and a greater than industry average risk for adverse reserve development.

III.A.5. Risk Assessment (All Statement Types) – IPS Example

		<u>CY</u>	<u>PY</u>	<u>PY1</u>	<u>PY2</u>	<u>PY3</u>
Two Year Develop		53.4%	8.0%	-20.3%	25.7%	100.1%
Loss & LAE/C&S		204.1%	132.3%	168.0%	235.2%	496.9%
Minimal Concern	Moderate Concern			Significant Concern		Trend
				Lines of Business		↔
				Loss Development		↑
Overall Reserving Assessment: Moderate Concern				Overall Trend:		↑

Strategic: The following issues have been identified relating to the Company's strategy:

- As discussed above, the Company has experienced weak underwriting, which has resulted in material losses and material reductions in capital. Underwriting losses have been reported in each of the past five years. Consequently, profitability and capital are considered weak as investment activity has been used to prop up the bottom line, in addition to capital contributions from the Company's parent. The Company has not yet finalized and presented an updated business plan to demonstrate how it will address these strategic issues going forward.
- The Company indicated in its Form F that it was changing its mix of business in states other than State X and Y. This could create a risk as the Company has only been writing in the other states for a few years; therefore, there is limited historical development available for these states. This should be considered in the context of the targeted examination.

Minimal Concern	Moderate Concern	Significant Concern	Trend
	Expansion in new jurisdictions		↑
		Profitability/capital concerns	↑
Overall Strategic Assessment: Significant Concern		Overall Trend:	↑

Other: The following other issues have been identified that don't clearly fit into one of the branded risk classifications highlighted above:

- The company has consistently been out of compliance with one or more laws, regulations or requirements of the Department and other states.

Minimal Concern	Moderate Concern	Significant Concern	Trend
	Incorrect statutory financial statements		↑
		Lack of knowledge or laws	↑
Overall Reserving Assessment: Moderate Concern		Overall Trend:	↑

IMPACT OF HOLDING COMPANY ON INSURER

Summarize the evaluation of the impact of the holding company system on the domestic insurer.

The group is highly dependent upon cash flows from the various entities, including ABC, to make payments on the holding company debt used to help finance past transactions associated with the growth of the group. The Form F provides more specific information on necessary cash flows expected in the near term. Others risk from the non-insurers is not significant. See Domestic and/or Non-Lead State Analysis Holding Company Procedures for further discussion.

EXAMPLE:

The holding company's UCP, has provided capital to the insurer when it has been required. The presence of many agreements involving the insurer and its affiliates indicate that the holding company is highly interconnected with entities being dependent on one another. The insurer provides services to, as well as

III.A.5. Risk Assessment (All Statement Types) – IPS Example

receives services from affiliates. This is accomplished via a Risk Share Agreement which superseded previous agreements the insurers had with the affiliated entities. The insurer provides TPA services for certain members of the group.

Overall, the operations of the holding company are profitable and able to maintain the ability for the holding company to infuse capital into the three insurers when needed. The holding company has requested distributions from the insurer from time to time to help fund capital deficiencies in two affiliates, but there is no concern with the insurer's financial condition or independent ability to provide this support at the present time. In evaluating whether the holding company has the ability to provide necessary financial support to its insurers, it is noted that the holding company has equity of \$X billion as of its most recent audited financial statements and has positive net operating income over the past several years. In addition, the holding company has bond ratings from Moody's of Aa3 and from Standard & Poors of AA. These strong ratings coupled with a strong balance sheet provide evidence that the holding company has the ability to continue to assist the insurer by means of capital infusions should the needs arise.

OVERALL CONCLUSION AND PRIORITY RATING

This section should include an overall conclusion as to the Company's financial condition, discuss strengths that potentially mitigate the risks assessed above, and highlight weaknesses and any concerns with the Company's operations going forward. Include any actions that may have been taken (e.g., significant holding company transactions, prior or planned meetings with management, and referrals to/from other divisions, etc.). Recommend the priority level that should be assigned to the Company and explain the rationale.

EXAMPLE:

Based on the branded risk assessments provided above as well as the Company's poor financial results reported in recent periods, the Company appears to be potentially troubled. The Company has triggered more than five of the department's prioritization criteria and is a multi-state insurer; therefore, the Company has been assigned our highest priority rating of 1, which is unchanged from the prior year. Some of the most significant issues facing the Company include rate adequacy, reserve sufficiency and overall cash flow and liquidity issues. However, these weaknesses are somewhat offset by Company strengths including a conservative investment portfolio, brand recognition and a strong historical reputation. The department has scheduled a meeting with senior management for the 3rd Quarter to discuss the Company's poor financial performance and ongoing business plan. During the meeting, the department plans to share its concerns and inform the Company of steps planned to monitor the company's operations more closely, as described below.

SUPERVISORY PLAN

List any specifically identified items that require further monitoring by the analyst or specific testing by the examiner. In addition, indicate if the Company is or should be subject to any enhanced monitoring, such as monthly reporting, a targeted examination, or a more frequent exam cycle.

EXAMPLE:**Analysis Follow Up**

- Obtain further detail regarding the impact of proposed rate increases and monitor through monthly financial reporting.
- Obtain further detail regarding the insurer's liquidity strategy.
- Assess the reasonableness of the Company's business plan as soon as it is received, given the inability to execute the most recent strategy. Consider attending board meetings to reflect the concern regarding the future viability of the Company.
- Include suggested follow-up procedures to address any potentially significant unresolved concerns with cost sharing or service agreements with affiliates or significant reliance on affiliates to provide services.

III.A.5. Risk Assessment (All Statement Types) – IPS Example

Examination Follow-Up

- During the next regularly scheduled examination, audit the specific risks associated with the Company's agents' balances and uncollected premiums to determine if further concerns exist.
- Follow-up on segregation of duties issues noted in the last examination.
- Perform a targeted examination of the reserves, pricing and claims management. Consider in the reserve study any pricing review, information related to the changing legal environment, as well as the mix of business in states outside of X and Y.

Example

III.A.6. Template for Planning Meeting with Financial Examiner

Overview

This template is intended as an optional tool highlighting items that may be discussed during a planning meeting between the assigned financial analyst and the financial examiner in support of the financial exam process. This meeting should ensure that the examiner both understands the company that will be examined and also receives details on work that has already been performed in supervising the company's operations. An effective exchange of information will promote efficiencies in the financial examination process by allowing the examiner to leverage the knowledge and work performed by the financial analyst. It may also prove useful to supplement this meeting with a discussion of the Exam Planning Questionnaire (Exhibit B) so that the analyst can review during the discussion to highlight or indicate if a document being requested has been obtained and/or reviewed by the insurance department. Although this template focuses on discussions between the assigned financial analyst and the financial examiner, the examiner may also consider incorporating this discussion into a broader planning meeting with members of department management and representatives from other areas of the department. However, if such an approach is taken, it should not reduce or diminish the level of discussion between the analyst and the examiner.

Given the importance of the Insurer Profile Summary (IPS) in communicating the results of the department's financial analyst's review of the company's operations, the planning meeting with the analyst is intended to generally follow the format of the IPS template.

Depending on the significance of operations at the group level, the examiner should consider whether additional agenda items should be added to focus on risks posed and discussed on the Group Profile Summary that are relevant for consideration during the examination.

NOTE: The exhibit was prepared to assist examiners in obtaining a general knowledge of the company through the meeting with the analyst. The examiner leading the discussion should not rely exclusively on these topics and should tailor agenda items based on knowledge of the company and based on knowledge of work that has been performed by the department. In situations where the exam is being led by an independent contractor, the department may consider having the insurance department's designee to lead the discussion of certain agenda items such as the role of the financial analyst in the examination.

Planning Meeting Between the Financial Analyst and Financial Examiner – Agenda Items

1. **Business Summary** – Discuss a summary of the business operations and lines of business of the insurer.
 - a. Discuss whether the department has received a recent business plan from the company and has identified any significant changes in strategy/operations.
 - b. Discuss any recent meetings with the company and their potential impact on the examination.
 - c. Discuss the corporate governance in place at the company and any recent changes or concerns identified.
2. **Regulatory Actions** – Discuss any significant recent steps taken in supervising the company, including, but not limited to:
 - a. Granting of permitted practices
 - b. Identification of issues of non-compliance
 - c. Follow-up on items from the last financial examination
 - d. Review of items filed with the department for approval
3. **Financial Snapshot/Overview of Financial Position** – Discuss the company's recent financial results, including, but not limited to:
 - a. Changes in profitability trends.

III.A.6. Template for Planning Meeting with Financial Examiner

- b. Deterioration in asset quality, liquidity or capital adequacy.
 - c. Changes in investment holdings and strategy.
 - d. Changes in key annual statement balances.
 - e. Changes in reinsurance balances and program structure.
 - f. Significant results noted in financial analysis solvency tools.
4. **Branded Risk Assessments** – Discuss individual branded risk assessments with a focus on moderate and significant areas of concern. For example:
- a. Discuss a summary of detailed analysis work performed to address key issues.
 - b. Discuss the status of any outstanding inquiries or requests for the company.
 - c. Discuss any management representations to the department that should be verified or corroborated during the exam.
 - d. Discuss any recommended exam procedures and/or follow-up on key issues.
5. **Impact of Holding Company on Insurer** – Discuss the impact of the holding company system on the domestic insurer. For example:
- a. Discuss and obtain the Group Profile Summary and non-lead state holding company analysis work as necessary.
 - b. If the lead state, discuss whether the analyst's review of the group's Corporate Governance Annual Disclosure (CGAD), if applicable, Own Risk and Solvency Assessment (ORSA) Summary Report and/or Form F reporting indicate a need for additional follow-up and review during the exam.
 - c. If not the lead state, discuss whether your state's review of the following indicates a need for additional follow-up and review during the exam.
 - i. As applicable, either the insurance entity CGAD, or the lead state's review of the group's CGAD provided in the GPS and other information provided by the lead state
 - ii. The lead state's analysis of the ORSA Summary Report
 - iii. The lead state's analysis of the Form F provided in the GPS or other information provided by the lead state
 - d. Discuss any developments or follow-up items resulting from recent supervisory college sessions.
6. **Overall Conclusion and Priority Rating** – Discuss the analyst's overall conclusion on the company's financial condition, strengths, weaknesses, and priority rating assigned to the company.
7. **Supervisory Plan** – Discuss the analyst's plans for the ongoing supervision of the company, including any specific examination procedures identified.
8. **Access to Work Papers and Company Documents** – Discuss the best way that the analyst's work can be reviewed/obtained. As the number of files that examiners wish to review and obtain increases, they may consider obtaining access to the analyst's workpapers and receiving specific locations (i.e., workpaper references) for all requested documents.
9. **Input from Other Areas of the Department** – Discuss whether the analyst has received recent communications from other areas of the insurance department regarding issues that could affect the financial examination including, but not limited to, units in charge of:
- a. Approving rates and forms filings
 - b. Legal and administrative matters

III.A.6. Template for Planning Meeting with Financial Examiner

- c. Market conduct examinations/filings
10. **General Observations** – Depending on the information already provided, determine whether there are any additional topics relevant for discussion, such as:
- a. If you were going on-site to examine this company, where would you focus your time?
 - b. What are your biggest concerns in terms of things that could go wrong at this company to result in a solvency concern?
 - c. Are you aware of any fraud allegations or concerns at the company? Are there any fraud risk factors that the exam team should be aware of?
11. **Communication/Coordination Throughout Exam** – Discuss the role of the financial analyst in the examination, including the following:
- a. Participation in examination activities (e.g., Meetings with the company, C-Level interviews)
 - b. Ongoing monitoring of exam status and findings; and
 - c. Responsibility to communicate new information about the company (e.g., Form D filings, quarterly analysis results/updated Insurer Profile Summary) to the examination team timely throughout the course of the exam.

III.B.1.a. Credit Risk Repository – P/C Annual

Credit Risk: Amounts actually collected or collectible are less than those contractually due or payments are not remitted on a timely basis.

Note: The repository is not an all-inclusive list of possible procedures. Therefore, risks identified for which no procedure is available should be analyzed by the state insurance department based on the nature and scope of the risk. Also, note that key insurance operations or lines of business, for example, may have related risks addressed in different repositories. Therefore, analysts may need to review other repositories in conjunction with credit risk. For example:

- Investment strategy is also discussed in the Liquidity, Market, and Strategic Risk Repositories.
- Investment asset classes (Bonds, Mortgages, etc.) are also discussed in the Market and/or Liquidity Risk Repositories.
- Reinsurance is also discussed in the Operational and Strategic Risk Repositories.

Analysis Documentation: Results of credit risk analysis should be documented in Section III: Risk Assessment of the insurer.

Investment Portfolio Diversification

1. Determine whether the insurer's investment portfolio appears to be adequately diversified to avoid any undue concentration of investments by type or issue. (*See also Market Risk Repository for diversification of other asset classes*)

<i>"a" through "i": Shown are as a percent of total net admitted assets</i>	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Industrial and miscellaneous bonds (unaffiliated)		>25%	[Data]	[Data]
b. Residential mortgaged-backed securities (RMBS), commercial mortgage-backed securities (CMBS) or other loan-backed and structured securities (LBaSS)	MK*	>20%	[Data]	[Data]
c. Preferred stocks		>10%	[Data]	[Data]
d. Mortgage loans	MK*	>5%	[Data]	[Data]
e. Other invested assets (Schedule BA)	LQ	>5%	[Data]	[Data]
f. Derivative exposure to any single exchange, counterparty, or central clearinghouse	MK	>5%	[Data]	[Data]
g. Aggregate write-ins for invested assets	LQ	>5%	[Data]	[Data]
h. Investments in affiliates	LQ, MK*	>10%	[Data]	[Data]
i. Any one single investment (by issuer) for bonds, preferred stock, mortgages, BA assets (excluding federal issuers and affiliated investments)	MK	>3%	[Data]	[Data]
				<i>Other Risks</i>
j. Review the Percentage Distribution of Total Assets in the Financial Profile Report for significant shifts in the mix of investments owned during the past five years.				MK*
k. Compare the insurer's distribution of cash and invested assets per the Percentage Distribution of Total Assets in the Financial Profile Report and Investment Snapshot Report to industry and peer averages to determine any significant deviations from the industry				MK*

III.B.1.a. Credit Risk Repository – P/C Annual

averages.	
l. Review the Annual Supplemental Investment Risks Interrogatories and assess any unusual items or areas that indicate a non-diversified portfolio.	MK*
m. Perform sector analysis of Schedule D holdings with assistance of the NAIC Capital Markets Bureau if concerns exist that indicate a sector of the market may be experiencing financial distress that could result in credit risk to holders of bonds or stocks in that sector.	MK
n. If concerns exist regarding counterparty credit risk on derivatives, review Annual Financial Statement, Schedule DB – Part D to identify the counterparties and use available information (e.g., rating agency reports) to identify any concerns with the credit quality of the counterparty.	

Exposure to Non-Investment Grade Bonds

2. Determine whether there are concerns due to the level of investment in non-investment grade bonds.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Ratio of non-investment grade bonds and non-investment grade short-term investments to surplus		>10%	[Data]	[Data]
b. Increase in non-investment grade bonds and non-investment grade short-term investments, where such investments are greater than 5% of surplus	LQ	>10%	[Data]	[Data]
c. Compare the insurer's holdings of non-investment grade bonds to the limitations included in the NAIC <i>Investments in Medium and Lower Grade Obligations Model Regulation</i> (#340) [Annual Financial Statement, Schedule D – Part 1A – Section 1]:				
i. Aggregate amount of all bonds owned which have an NAIC rating of 3, 4, 5 or 6 to total net admitted assets	LG	>20%	[Data]	[Data]
ii. Aggregate amount of all bonds owned which have an NAIC rating of 4, 5 or 6 to total net admitted assets	LG	>10%	[Data]	[Data]
iii. Aggregate amount of all bonds owned which have an NAIC rating of 5 or 6 to total net admitted assets	LG	>3%	[Data]	[Data]
iv. Aggregate amount of all bonds owned which have an NAIC rating of 6 as a percent to total net admitted assets	LG	>1%	[Data]	[Data]
				<i>Other Risks</i>
d. If the level of non-investment grade bonds is high, review Annual Financial Statement, Schedule D – Part 1A and Part 1, Jumpstart Reports (e.g., Bond Investment Designation Exception Report) and the Financial Profile Report to assess and understand the composition of non-investment grade bonds:				

III.B.1.a. Credit Risk Repository – P/C Annual

<ul style="list-style-type: none"> Amount and/or percentage of bonds in each class 3, 4, 5 or 6 Concentration by sector or issuer, including affiliates If bonds have been rated by a credit rating provider (CRP) (e.g., Moody's Investors Service, Standard & Poor's, A.M. Best or Fitch Ratings) 	
e. For the more significant non-investment grade bonds, request the current report from a CRP regarding the issuer to determine the issuer's financial position and ability to repay its debt.	

Exposure to Mortgage - and/or Asset-Backed Securities

3. Review Annual Financial Statement, Schedule D – Part 1A – Section 2 to determine whether there are concerns due to the level of investment in RMBS, CMBS and LBaSS.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Ratio of all RMBS, CMBS and LBaSS owned to surplus	LQ	>50%	[Data]	[Data]
b. Increase in all RMBS, CMBS and LBaSS investments from the prior year, where such investments are greater than 15% of surplus	LQ	>20%	[Data]	[Data]
c. Ratio of RMBS to surplus	LQ	>5%	[Data]	[Data]
				<i>Other Risks</i>
d. Review the RMBS, CMBS and LBaSS categories in Annual Financial Statement, Schedule D – Part 1 for bonds with a book/adjusted carrying value significantly in excess of par value, which could result in a loss being realized if bond prepayments occur faster than anticipated.				
e. Review the RMBS, CMBS and LBaSS categories in Annual Financial Statement, Schedule D – Part 1 for bonds with an unusually high effective yield.				
f. Review Annual Financial Statement, Schedule D – Part 1 and the Snapshot Investment Summary Report on iSite+ to assess exposure to agency versus non-agency RMBS, CMBS and LBaSS.				
g. Consider having the RMBS, CMBS and LBaSS modeled by an independent actuary as a part of an independent cash flow analysis.				

Exposure to Mortgage Loans

4. Determine whether there are concerns due to the level or quality of investment in mortgage loans.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Ratio of total mortgage loans to surplus	LQ	>5%	[Data]	[Data]
b. Increase in mortgage loans the prior year, where the ratio of mortgage loans to surplus is greater than 10%	LQ	>15%	[Data]	[Data]
				<i>Other Risks</i>

III.B.1.a. Credit Risk Repository – P/C Annual

c. Using postal codes and property type reported in Annual Financial Statement, Schedule B – Part 1, identify if mortgage loans owned is concentrated in one or a few geographical areas.	
d. Review debt service coverage ratios and adjusted loan-to-values of the individual mortgage loans.	
e. If concerns exist, review Schedule B – Part 1: <ul style="list-style-type: none"> i Determine the amount of each type of mortgage loan owned. ii Compare the book value/recorded investment of each loan to the value of the land and buildings mortgaged to determine whether the mortgage loans are adequately collateralized. iii Review the date of last appraisal or valuation to determine whether updated appraisals should be obtained. iv Determine whether any of the mortgage loans are to an officer, director, parent, subsidiary, or affiliate. 	MK

Exposure to Other Invested Assets (Schedule BA)

5. Determine whether there are concerns due to the level of investment in other invested assets (Schedule BA).

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Ratio of BA assets to surplus	LQ*, MK*	>10%	[Data]	[Data]
b. Increase in BA assets from the prior year, where the ratio of BA assets to surplus is greater than 5%	LQ*, MK*	>10%	[Data]	[Data]
				<i>Other Risks</i>
c. Review Annual Financial Statement, Schedule BA – Part 1 to determine the amount and types of other invested assets owned and identify if the insurer's exposure to certain classes of BA assets are significant (e.g., hedge funds, private equity funds, etc.). <ul style="list-style-type: none"> i. Determine whether concerns exist regarding the insurer's exposure to non-traditional investments (i.e., hedge funds and private equity funds, Lines 25 & 26) as compared to capital and surplus and impact on liquidity. ii. Review the experience of the insurer with respect to investing in alternative investments such as hedge funds and private equity funds. iii. Obtain and review cash flow projections to ensure that the insurer understands the cash flow characteristics of such investments. iv. Inquire of the insurer regarding the liquidity of non-traditional investments to ensure that limitations in this area are understood. v. Perform procedures to test the accuracy of reporting for non-traditional investments. vi. Ensure that senior management and the Board of the insurer have explicitly signed off on non-traditional investments. 	LQ, MK			
d. Review Annual Financial Statement, Schedule BA – Part 1 to determine if a significant amount of BA assets have NAIC ratings of 3, 4, 5, or 6 or have a "Z" designation.				

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Invested Asset Exposure to Climate Change Risk

6. Assess the potential impact of material climate change and/or transition and asset devaluation risk on the insurer's invested asset portfolio.

	<i>Other Risks</i>
a. Review information provided in the insurer's response to the NAIC's Climate Risk and Disclosure Survey (if available) on its exposure to material climate change/energy transition risk and related mitigation activity in this area.	LQ*, MK*
b. Review relevant information provided in the Own Risk and Solvency Assessment (ORSA) Summary Report, and/or U.S. Securities and Exchange Commission (SEC) 10-K or 10-Q filings (if available) that discusses the insurer's exposure to material climate change/energy transition risk and related mitigation activity in this area.	LQ*, MK*
c. Review information provided in the NAIC's U.S. Insurance Industry Climate Affected Investment Analysis to identify potential concentrations in insurer exposure.	LQ*, MK*

Reinsurance Recoverable and Reinsurer Credit Quality

7. Determine whether amounts recoverable (both paid and unpaid losses on claims and reserve credits) or amounts receivable from reinsurers are significant.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Overdue paid losses and LAE reinsurance recoverables (91 days or more) to surplus	LQ	>10%	[Data]	[Data]
b. Total reinsurance recoverables from unauthorized reinsurers to surplus		>25%	[Data]	[Data]
c. Total reinsurance recoverables from alien reinsurers to surplus		>10%	[Data]	[Data]
d. Provision for overdue authorized and reciprocal jurisdiction reinsurance to authorized and reciprocal jurisdiction reinsurance recoverables on paid losses and LAE in dispute		<20%	[Data]	[Data]
e. Non-affiliated reinsurance recoverables on paid losses to surplus		>10%	[Data]	[Data]
f. Non-affiliated reinsurance recoverables on unpaid losses and LAE to surplus		>50%	[Data]	[Data]
g. Provision for unauthorized and certified reinsurance to total reinsurance recoverables from unauthorized and certified reinsurer		>30%	[Data]	[Data]
h. Total amount of funds withheld for payment of losses by ceding companies to surplus		>10%	[Data]	[Data]
i. Is the reporting entity the beneficiary of the LOC that is unrelated to reinsurance where the issuing or confirming bank is not on the SVO Qualified U.S.		=YES		

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Financial Institutions List? If “yes,” list the name of the issuing or confirming bank, the circumstances that can trigger the LOC, and the amount. [Annual Financial Statement, General Interrogatories Part 1, #15.1 and #15.2]				
				<i>Other Risks</i>
j. Review, by individual reinsurer, the amounts shown as security. Identify any unusual trends and determine the need to examine the underlying security in more detail to ensure its validity.				
k. If the insurer holds a material letter of credit (LOC) securing unauthorized and/or certified reinsurance recoverables, identify the amount of the LOC and the issuing bank. Identify any concerns and assess whether the collateral is at an adequate level.	OP			
l. Review the reinsurer’s historical payment patterns of recoverables and comment on findings or concerns.				
m. Verify by direct contact or confirmation that funds withheld for payment are valid and adequately segregated for payment of losses.				

8. Determine whether amounts recoverable from reinsurers are collectable.

<i>Source: Notes to Financial Statements, #23 – Reinsurance.</i>	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Unsecured reinsurance recoverables to surplus		>25%		
b. Total reinsurance recoverables from any unauthorized or certified reinsurer to surplus		>10%	[Data]	[Data]
c. Total reinsurance recoverables from any alien reinsurer to surplus		>5%	[Data]	[Data]
d. Reinsurance recoverables in dispute to surplus		>5%	[Data]	[Data]
e. Maximum amount of return commissions due to reinsurers in the event of cancellation of all ceded reinsurance to surplus		>15%		
f. Uncollectable reinsurance written off during the year to surplus		>5%		

9. If reinsurance is significant based on the review of above procedure, assess the credit quality and financial solvency of the reinsurers the insurer cedes a material amount of business to or has material reinsurance recoverable due from.

	<i>Other Risks</i>
a. Determine the current ratings of the reinsurer from the major rating agencies and investigate significant changes during the past 12 months.	
b. Obtain and review the Audited Financial Report, Annual Financial Statement, Actuarial Opinion and U.S. Securities and Exchange Commission (SEC) Filings (if applicable) of the	

III.B.1.a. Credit Risk Repository – P/C Annual

reinsurer for additional insight regarding collectability and credit quality of the reinsurers.	
c. Review information about the reinsurer that is available from industry analysts and benchmark capital adequacy with top performers and peer groups.	
d. Contact the domiciliary state to determine whether any regulatory actions are pending against the reinsurer. Also review iSite+ data on the reinsurer (i.e., financial statements, Regulatory Information Retrieval System [RIRS] and Global Receivership Information Database [GRID]).	
e. Review Annual Financial Statement, Schedule F to determine whether adequate levels of collateral (LOCs, trust funds etc.) are being maintained for unauthorized reinsurance and to secure outstanding losses	
f. Review results of reinsurance Jumpstart Reports to determine if material differences exist between amounts reported on reinsurance schedules of the insurer compared to the ceding insurers. i. If significant differences are noted, further investigate if the amounts appear to be due to timing and/or consider asking the insurer for aging of amounts payable/receivable.	

10. Determine whether pyramiding may be occurring that could cause significant collectability risk to the insurer.

	Other Risks
a. For the five largest individual unauthorized reinsurers and the five largest individual certified reinsurers listed in the Annual Financial Statement, Schedule F – Part 3 consider the need to obtain the reinsurer's Annual Financial Statement and determine the extent to which the reinsurer has engaged in retrocession agreements. If considered necessary, was it determined that any of these unauthorized and/or certified reinsurers have ceded reserves greater than 50% of total gross reserves?	
b. If there are any concerns that pyramiding exists, consider reviewing the Annual Financial Statement of the more significant reinsurers to evaluate the extent in which the reinsurers cede business to other reinsurers. If necessary, proceed with this process as long as concerns regarding pyramiding continue to exist. Throughout this process, be alert to declines in the overall quality level of reinsurers throughout the chain of reinsurance. If significant collectability concerns surface as a result of these procedures, perform the appropriate procedures to evaluate collectability.	

Affiliated Receivable or Payable

11. Review the balance sheet asset receivable from parent, subsidiaries and affiliates, as well as the liability payable to parent, subsidiaries and affiliates to determine whether there are concerns with the level of affiliated receivables/payables.

	Other Risks	Benchmark	Result	Outside Benchmark
a. Affiliated receivable or payable to surplus	LQ, OP*	>10%	[Data]	[Data]
				Other Risks

III.B.1.a. Credit Risk Repository – P/C Annual

b. If there are concerns regarding collectability of affiliated receivables, review Annual Financial Statement, Schedule Y – Part 2, Notes to the Financial Statements, Management’s Discussion and Analysis (MD&A) and other available information (e.g., Form D filings) for more information about the nature and timing of the receivable. (Review the Operations Risk Repository for more procedures on affiliated transactions.)	LQ, OP
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Exposure to High Deductible Policies

12. Assess credit risk from high-deductible policies.

	Other Risks
a. Review Annual Financial Statement, Notes to Financial Statements, Note #31 for exposure to high-deductible policies. i. Determine the materiality of any reserve credit that has been recorded and is recoverable. ii. Determine the materiality, aging and collateral held on any deductible recoverables and unpaid balances.	

Uncollected Premium and Agents’ Balances

13. Review and assess uncollected premiums and agents’ balances for potential collectability issues.

	Other Risks	Benchmark	Result	Outside Benchmark
a. Ratio of uncollected premiums and agents’ balances to surplus [IRIS ratio #10]	LQ	>40%	[Data]	[Data]
b. Change in uncollected premiums and agents’ balances from the prior year		>25% or <-25%	[Data]	[Data]
c. Ratio of uncollected premiums to net premium income	LQ	>5%	[Data]	[Data]
d. Ratio of non-admitted uncollected premiums to total uncollected premiums	LQ	>10%	[Data]	[Data]
e. Net agents’ balances and premium balances charged off and recovered to total uncollected agents’ balances and premium balances		>5%	[Data]	[Data]
				Other Risks
f. Review amounts non-admitted and compare to prior years.				
g. With respect to agents’ balances, verify the creditworthiness of the agent.				

Related Party Exposure in the Investment Portfolio

#14. Assess related party exposure in the investment portfolio.

	Other Risks
<p>a. Review the Annual Financial Statement investment schedules, as disclosed in the column “Investments Involving Related Parties” and utilizing iSite+ tools, determine if the insurer has material related party exposures in its investment portfolio.</p> <p>This disclosure is included in:</p> <ul style="list-style-type: none"> • Schedule B • Schedule BA • Schedule D • Schedule DA • Schedule DB • Schedule DL • Schedule E, Part 2 <p>Consider exposure by asset class and in aggregate, and by the role of the related party in the investment as designed by the “Investments Involving Related Parties” disclosure.</p>	LQ, MK
<p>b. If concerns exist regarding a material related party exposure in the investment portfolio, assess the credit quality of those investments involving related parties by reviewing designations, assessing historical default experience, etc.</p>	LQ, MK

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<p>c. If concerns exist regarding a material related party exposure in investment management or advisory services, consider the following:</p> <ol style="list-style-type: none"> i. Review the procedures in the “Additional Procedures” section below regarding Third Party Investment Advisors and consider their application to related party advisors in that role. ii. In addition to the additional analysis procedures regarding third party investment advisors, consider the following: <ol style="list-style-type: none"> 1. Review the insurer’s investment policy guidelines and determine whether the related party investments follow the guidelines and are in compliance with regulatory requirements. 2. Review whether the fee structure for asset management is fair, reasonable, and appropriately recognized as investment expenses. 3. If the related party asset manager also originates/securitizes investments held by the insurer, consider requesting additional information from the insurer to determine the following: <ol style="list-style-type: none"> a. Whether the asset manager has adequate experience and knowledge in originating and managing the types of investments; b. Whether the asset manager follows appropriate underwriting practices and applicable regulatory requirements in originating investments; and c. Whether the fee structures embedded in securities (if applicable) are fair, reasonable, and appropriately account for potential duplication of fees or conflicts of interest. 	<p>OP</p>
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Additional Analysis and Follow-up Procedures

Request and Assess the Insurer’s Investment Policies and Strategies:

If concerns exist regarding the level of credit exposure, request and review the insurer’s investment strategy to determine if it is appropriately structured to support its ongoing business plan. Review the guidelines outlined in the plan for:

- Quality of issues invested in and diversification standards pertaining to issuer, industry, duration, liquidity, , geographic location, and issues/sectors exposed to material climate change, transition, and asset devaluation risks.
- Expected rate of returns on investments (projected investment income) compared to actual results.
- Planned increases in investment types, sectors, markets, etc.
- Appropriateness of the investment plan for the liability structure of the insurer. (This may require a review of asset adequacy analysis for asset liability matching [ALM] and discussion with the insurer’s management to better understand their plan.)
- Upon review of the investment plan, compare the plan to actual results. Does the insurer and its investment manager(s) appear to be adhering to the investment policies and guidelines in the investment plan?

III.B.1.a. Credit Risk Repository – P/C Annual

Examination Findings:

Review the most recent examination report and Summary Review Memorandum (SRM) for any findings regarding credit risks associated with:

- Investment concentration
- Exposure to riskier asset classes
- Climate change, transition, and asset devaluation.
- Asset Liability Matching.
- Adherence to investment policies and strategies.
- Investment Management, and use of and monitoring of external investment managers.
- Proper classification (i.e., authorized, unauthorized, reciprocal jurisdiction, certified) and calculation of reinsurance collateral and provision.

If outstanding issues are identified, perform follow-up procedures as necessary to address concerns.

NAIC Capital Market's Bureau Analytical Assistance:

Consider requesting the following analytical reviews:

- Review of the insurer's investment portfolio
- Review of Investment Management Agreements

Third Party Investment Advisers:

Assess and determine if any concerns exist regarding third party investment advisers and associated contractual arrangements.

- Review Annual Financial Statement, General Interrogatories, Part 1, #29.05. Does the insurer utilize third party investment advisers, broker/dealer or individuals acting on behalf of the insurer with access to their investment accounts?

If "yes," consider the following procedures:

- Review the results of the most recent financial examination work papers, follow-up and prospective risk information and the summary review memorandum provided by the examiners. Did the examination identify any issues with regard to investment advisers and associated contractual arrangements that require follow-up analysis or communication with the insurer? If "yes," document the follow-up work performed.
- Compare Annual Financial Statement, General Interrogatories, Part 1, #29.05 for the current year to the prior year to determine if there have been any changes in advisors. If "yes,"
 - Consider obtaining an explanation for the change from the insurer.
 - Consider obtaining a copy of the new investment advisor agreement and review it for appropriate provisions.
- Using the information reported in Annual Financial Statement, General Interrogatories, Part 1, #29.05, obtain and review SEC Form ADV (if available), to determine if the investment advisor is in good standing with the SEC. If not in good standing, contact the insurer to request an explanation.
- If agreements with third party investment advisers are affiliated, have the appropriate Form D – Prior Notice of Transactions been filed and approved by the department? Were any concerns noted or follow-up monitoring recommended?
- Request information from the insurer regarding the background and expertise in structured securities of its

III.B.1.a. Credit Risk Repository – P/C Annual

investment advisors (in-house and/or contractual) and its analytical system capabilities. Determine whether the advisors and systems are adequate to allow the insurer to continuously monitor its structured securities investments.

- If the insurer uses an external asset manager, consider if investments on the Annual Financial Statement, Schedule BA are invested in funds that are affiliated with the asset manager or are managed by that asset manager. Consider the following issues:
 - If any conflicts of interest exist
 - If the investment is appropriate for the insurer's portfolio and arm's-length
 - If the insurer is paying double fees

Inquire of the Insurer:

If concerns exist, consider requesting information from the insurer regarding:

General Investment Inquiries:

- If management has adequately reviewed the investment portfolio and understands the yields, underlying collateral, cash flows and investment volatility.
- Any additional concentration by collateral type
- Management's process for valuing securities to assist analysts in assessing if the securities are valued appropriately.
- Management's intended use of certain riskier investments and purpose within the insurer's portfolio.
- Credit risk associated with sector concentration.
- If management has an appropriate level of knowledge and expertise with the type of securities being purchased/held.
- If the insurer has controls implemented to mitigate the risks associated with this investment type.
- Sources of liquidity, such as LOCs.

Investment Diversification:

- Planned asset mix and diversification strategies.
- How the insurer manages counterparty credit risk, including diversification risk of counterparties

Mortgages:

- Increases by adjustment in book value/recorded investment during the year.

BA Assets:

- Request information necessary to determine the fair value of collateral to the amount loaned to ensure the loan is adequately collateralized.
- Information to support significant increases by adjustment in book/adjusted carrying value during the year.
- Current Audited Financial Statements and other documents (partnership agreements, etc.) necessary to support the value of the insurer's investment in partnerships and joint ventures.
- Information necessary to support the value of significant other invested assets other than partnerships and joint ventures.
- Current details on cash flows and returns for the different types of investments, especially hedge funds and private equity funds.

III.B.1.a. Credit Risk Repository – P/C Annual

Non-Investment Grade Bonds:

- Significant exposures
- Policies and strategy for investing in non-investment grade bonds.

RMBS, CMBS and LBaSS:

- Percentage distribution and amounts of each type of RMBS, CMBS and LBaSS held; planned amortization class (PAC), support bonds, interest only (IO) tranches, and principle only (PO) tranches to evaluate the level of prepayment risk in the portfolio.
- Projected prepayment speeds on its RMBS portfolio and compare with historical prepayments, as well as the prepayment assumption at the time of purchase

Asset Liability Matching:

- If concerns are identified regarding overall liquidity of the asset portfolio, request a copy of the insurer's asset/liability matching policy and/or liquidity stress testing/scenario analysis

Reinsurance:

- Request a copy of the insurer's A.M. Best Supplemental Ratings Questionnaire, and review the reinsurance section for unusual items.
- If concerns exist regarding the credit quality and financial solvency of an unauthorized reinsurer, request a copy of the reinsurance agreement(s), and confirm amounts included on Annual Financial Statement, Schedule F – Part 3
- Aging of reinsurance amounts payable/receivable.

Uncollected Premium and Agents' Balances:

- Explanation for the significant balance
- Listing of balances of subscribers, which individually account for 10% or more of the premiums uncollected and compare to a similar list from prior years.
- Amounts of any uncollectable balances that have been written off in the current period. Compare the write-offs to those of the prior reporting period, if any.
- Written procedures for monitoring and collecting uncollected premiums, including amounts already written off.
- If the insurer has factored or sold its uncollected premium balances to a third party, note whether the receivables were discounted in the transaction.
- Concerns over uncollected agents' balances warrants further investigation to ensure that adequate controls are in place and that trust accounts are properly managed. An increase or trend of material non-admitted agents' balances or write-offs may be a sign of mismanagement or misappropriation of premium trust accounts by the agency. If there are concerns in this area, consider the following:
 - Request additional data/information from the insurer to identify the source(s) of the balances and the reason(s) for the non-admitted or charged-off amounts.
 - Request the insurer to provide a summary of the controls in place over agencies and ensure proper management and oversight of trust accounts.
 - Request monthly reports from the insurer.
- Discuss concerns with the exam team, including whether a targeted exam is necessary.

III.B.1.a. Credit Risk Repository – P/C Annual

Own Risk and Solvency Assessment (ORSA) Summary Report:

If the insurer is required to file ORSA or part of a group that is required to file ORSA:

- Did the ORSA Summary Report analysis conducted by the lead state indicate any credit risks that require further monitoring or follow-up?
- Did the ORSA Summary Report analysis conducted by the lead state indicate any mitigating strategies for existing or prospective credit risks?

Holding Company Analysis:

- Did the Holding Company analysis conducted by the lead state indicate any credit risks impacting the insurer that require further monitoring or follow-up?
- Did the Holding Company analysis conducted by the lead state indicate any mitigating strategies for existing or prospective credit risks impacting the insurer?

Example Prospective Risk Considerations

<i>Risk Components for IPS</i>		<i>Explanation of Risk Components</i>
1	Significant concentration by [asset class, sector, issuer, etc.]	High exposure in any one asset class, industry sector or issuer could result in material credit losses if asset class, industry sector or issuer experience an economic decline.
2	Borrower default risk for [mortgage loans, RMBS, CMBS or LBaSS securities, etc.]	Lower credit quality of the borrowers (i.e., prime versus subprime) may result in higher risk of default, leading to credit losses in the event of a housing and/or commercial real estate market downturn.
3	Prepayment variability in RMBS	Prepayment variability in RMBS could result in actual cash flows and investment yields to be materially different from expectations.
4	Volatility of non-investment grade bonds	The market volatility of below investment-grade bonds makes the price at which bonds are held an important consideration.
5	Foreign security default	Material exposure to foreign investments could result in credit losses if those investments are impacted by negative changes in geopolitical or foreign economic environments.
6	Impairment of [bonds, etc.]	Risk of further deterioration in credit quality may result in other-than-temporary impairments impacting income and surplus.
7	Bondholder default	Investment grade bonds that have declined to a non-investment grade status may not recover lost value.
8	Structured notes cash flow volatility risk	Impact of the volatility of structured notes and the underlying asset on which its cash flows are based.
9	Structured notes collateral concentration risk	Material investment in structured notes that may have collateral type concentration may result in concentration risk (lack of diversity) to the insurer's portfolio.
10	Structured notes default	Structured notes may be subordinated in the overall transaction representing exposure to non-payment in event of default.
11	Second lien mortgage loan risk	High exposure to second lien loans may result in increase in risk of non-payment in the event of default as first lien loans are paid first from the value of the property.
12	Mortgage loan collateral inadequate	Out-of-date appraisals may result in inaccurate valuation, resulting in the underlying collateral asset not being adequate.

III.B.1.a. Credit Risk Repository – P/C Annual

13	High risk mortgage loan valuation	The investments in high-risk mortgage loans are incorrectly valued.
14	Complexity of BA assets	BA assets often have complex investment strategies and unpredictable cash flows.
15	Adequacy of collateral of BA asset	Volatility of underlying assets (e.g., certain hedge funds and private equity funds) may result in underlying asset not adequate.
16	Economic impact on portfolio of [BA assets, derivatives, etc.]	Portfolio volatility driven by economic changes.
17	Hedge effectiveness of derivatives portfolio	Derivatives strategy may not meet hedge effectiveness for mitigating risk.
18	Investment strategy contemplate higher [credit, market, liquidity...] risk	The insurer's investment strategy may not be structured to support its ongoing business plan, which could indicate the strategy enjoys higher credit, market and liquidity risks than are appropriate for the liabilities of the insurer and may lead to financial concerns in the future.
19	Investment results actual to projected variance	The insurer's actual investment portfolio and/or portfolio performance may vary significantly from projections if the insurer is not adhering to the strategy in place (i.e., higher actual credit, market or liquidity risk compared to the plan).
20	Collectability of receivables for [insert name of receivable]	Payments of [insert name of the receivable] may be delayed or not be paid when due, resulting in cash flow mismatch.
21	Credit quality of [reinsurer, agents, professional employer organization (PEO), affiliate, etc.]	Credit quality and poor financial strength of a [reinsurer, agents, etc.] may result in future collectability risk, which may result in ongoing credit risk and future liquidity issues.
22	Exposure to climate change, transition, and asset devaluation risk	The insurer's investment portfolio is subject to prospective devaluation of the assets/changes in the asset return associated with its holdings of climate-affected assets.

III.B.1.a. Credit Risk Repository – P/C Quarterly

Credit Risk: Amounts actually collected or collectible are less than those contractually due or payments are not remitted on a timely basis.

Note: The repository is not an all-inclusive list of possible procedures. Therefore, risks identified for which no procedure is available should be analyzed by the state insurance department based on the nature and scope of the risk. Also, note that key insurance operations or lines of business, for example, may have related risks addressed in different repositories. Therefore, analysts may need to review other repositories in conjunction with credit risk. For example:

- Investment asset classes (Bonds, Mortgages, etc.) also are discussed in the Market and/or Liquidity Risk Repositories.
- Reinsurance is also discussed in the Operational and Strategic Risk Repositories.

Analysis Documentation: Results of credit risk analysis should be documented in Section III: Risk Assessment of the insurer.

Investment Portfolio Diversification

- 1. Determine whether the insurer's investment portfolio appears to be adequately diversified to avoid any undue concentration of investments by type or issue.**

<i>"a" through "f": Shown are as a percent of total net admitted assets</i>	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Preferred stocks		>10%	[Data]	[Data]
b. Non-Investment Grade Bonds		>3.5%	[Data]	[Data]
c. Mortgage loans	MK*	>5%	[Data]	[Data]
d. Other invested assets (Schedule BA)	LQ*	>5%	[Data]	[Data]
e. Aggregate write-ins for invested assets	LQ	>5%	[Data]	[Data]
f. Investments in affiliates	LQ, MK*	>10%	[Data]	[Data]
g. Is the total book/adjusted carrying value net of collateral for derivative investments open as of current statement date greater than 10% of surplus? [Quarterly Financial Statement, Schedule DB – Part D – Section 1]		>10%	[Data]	[Data]
i. If "yes," list the book/adjusted carrying value net of collateral			[Data]	
				<i>Other Risks</i>
h. Review the Financial Profile Report for significant shifts in the mix of investments owned during the past five years.				MK*

Changes in Asset Exposures

- 2. Determine whether there are concerns due to the change in certain asset classes from the prior year-end.**

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>

III.B.1.a. Credit Risk Repository – P/C Quarterly

a. Increase in non-investment grade bonds and non-investment grade short-term investments from the prior year-end, where such investments are greater than 5% of surplus	LQ	>10%	[Data]	[Data]
b. Increase in mortgage loans from the prior year-end, where the ratio of total mortgage loans to surplus is greater than 10%	LQ, MK*	>15%	[Data]	[Data]
c. Increase in BA assets from the prior year-end, where the ratio of BA assets to surplus is greater than 5%	LQ*, MK*	>10%	[Data]	[Data]
d. Increase in aggregate write-ins from the prior year-end, where the ratio of aggregate write-ins to surplus is greater than 10%	LQ	>20%	[Data]	[Data]
e. Increase in affiliated investments from the prior year-end, where the ratio of affiliated investments to surplus is greater than 10%	MK*, LQ	>20%	[Data]	[Data]
				<i>Other Risks</i>
f. If the level of non-investment grade bonds is high (i.e., greater than 5% of surplus), review Quarterly Financial Statement, Schedule D – Part 1B, and the Financial Profile Report to assess and understand the composition of non-investment grade bonds: <ul style="list-style-type: none"> • Amount and/or percentage of bonds in each class 3, 4, 5 or 6 • Concentration by sector or issuer, including affiliates • If bonds have been rated by a credit rating provider (CRP) 				

Reinsurance Recoverable and Reinsurer Credit Quality

3. Determine whether amounts recoverable (both paid and unpaid losses on claims and reserve credits) or amounts receivable from reinsurers are significant and collectable.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Reinsurance amounts recoverable on paid losses to surplus	LQ	>20%	[Data]	[Data]
b. Change in reinsurance recoverables, where recoverables are greater than 20% of surplus	LQ	>10% or <-10% from the prior quarter OR >35% or <-35% from the prior year-end	[Data]	[Data]
c. Provision for reinsurance to surplus		>10%	[Data]	[Data]

III.B.1.a. Credit Risk Repository – P/C Quarterly

d. Change in the Provision for reinsurance, where the provision is greater than 5% of surplus		>10% or <-10% from the prior quarter OR >20% or <-20% from the prior year-end	[Data]	[Data]
e. Were any new reinsurers added since the prior quarter? [Quarterly Financial Statement, Schedule F]	ST*	YES if count >0	[Data]	[Data]
f. Were there any agreements to release reinsurers from liability during the quarter? [Quarterly Financial Statement, General Interrogatories, Part 2, #2]	OP, ST*	=YES		[Data]
g. Were there any cancellations of primary reinsurance contracts during the quarter? [Quarterly Financial Statement, General Interrogatories, Part 2, #3.1 and #3.2]	OP, ST*	=YES		[Data]
h. Did the insurer experience any material transactions requiring the filing of Disclosure of Material Transactions with the state of domicile as required by the Model Act? [Quarterly Financial Statement, General Interrogatories, Part 1, #1.1]	LG*, ST*	=YES		[Data]
i. If “yes,” did the insurer fail to make the appropriate filing of a Disclosure of Material Transactions with the state of domicile? [Quarterly Financial Statement, General Interrogatories, Part 1, #1.2]	LG*, ST*	=YES		[Data]

Affiliated Receivable or Payable

4. Review the balance sheet asset receivable from parent, subsidiaries and affiliates, as well as the liability payable to parent, subsidiaries and affiliates to determine whether there are concerns with the level of affiliated receivables/payables.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Affiliated receivable or payable to surplus	LQ, OP	>10%	[Data]	[Data]
b. Change in affiliated receivable or payable, where the receivable/payable is greater than 10% of surplus	LQ, OP	>25% or <-25% from the prior year-end	[Data]	[Data]
c. Change in federal and foreign income tax recoverables, where recoverables are greater than 5% of surplus	LQ, OP	>10% or <-10% from the prior	[Data]	[Data]

III.B.1.a. Credit Risk Repository – P/C Quarterly

		quarter OR >20% or <- 20% from the prior year-end		
				<i>Other Risks</i>
d. Are there any indications that significant or unusual transactions involve an affiliate or other related party?				
e. If there are concerns regarding collectability of affiliated receivables, review the Annual Financial Statement, Notes to the Financial Statements and other available information (e.g., Form D filings) for more information about the nature and timing of the receivable. (Review the Operations Risk Repository for more procedures on affiliated transactions.)				LQ, OP

Uncollected Premium and Agents' Balances

5. Review and assess uncollected premiums and agents' balances for potential collectability issues.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Ratio of uncollected premiums and agents' balances to surplus	LQ	>40%	[Data]	[Data]
b. Change in uncollected premiums and agents' balances from the prior year-end	LQ	>25% or <-25%	[Data]	[Data]
c. Change in non-admitted uncollected premiums from the prior year-end	LQ	>25% or <-25%	[Data]	[Data]

III.B.1.b. Credit Risk Repository – Life/A&H/Fraternal Annual

Credit Risk: Amounts actually collected or collectible are less than those contractually due or payments are not remitted on a timely basis.

Note: The repository is not an all-inclusive list of possible procedures. Therefore, risks identified for which no procedure is available should be analyzed by the state insurance department based on the nature and scope of the risk. Also, note that key insurance operations or lines of business, for example, may have related risks addressed in different repositories. Therefore, the analyst may need to review other repositories in conjunction with credit risk. For example:

- Investment strategy is also discussed in the Liquidity, Market, and Strategic Risk Repository.
- Investment asset classes (Bonds, Mortgages, etc.) also are discussed in Market and/or Liquidity Risk Repositories.
- Reinsurance also is discussed in the Operations and Strategic Risk Repositories.

Analysis Documentation: Results of credit risk analysis should be documented in Section III: Risk Assessment of the insurer.

Investment Portfolio Diversification

1. Determine whether the insurer's investment portfolio appears to be adequately diversified to avoid any undue concentration of investments by type or issue.

<i>"a" through "j": Shown are as a percent of total net admitted assets (excluding separate accounts)</i>	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Industrial and miscellaneous bonds (unaffiliated).		>50%	[Data]	[Data]
b. Residential mortgaged-backed securities (RMBS), commercial mortgage-backed securities (CMBS) or other loan-backed and structured securities (LBaSS).	MK*	>20%	[Data]	[Data]
c. Preferred stocks.		>5%	[Data]	[Data]
d. Mortgage loans.	MK*	>20%	[Data]	[Data]
e. Other invested assets (Schedule BA).	LQ	>5%	[Data]	[Data]
f. Derivative exposure to any single Exchange, Counterparty or Central Clearinghouse.	MK	>5%	[Data]	[Data]
g. Collateral Loans.		>5%	[Data]	[Data]
h. Aggregate write-ins for invested assets.	LQ	>5%	[Data]	[Data]
i. Investments in affiliates.	LQ, MK*	>10%	[Data]	[Data]
j. Any one single investment (by issuer) in bonds, preferred stock, mortgages or BA assets (excluding federal issuers and affiliated investments).		>3%	[Data]	[Data]
				<i>Other Risks</i>
k. Review the Percentage Distribution of Total Assets in the Annual Financial Profile Report for significant shifts in the mix of investments owned during the past five years.	MK*			
l. Compare the insurer's distribution of cash and invested assets per the Percentage Distribution of Total Assets in the Annual Financial Profile Report and Investment Snapshot Report to industry and peer averages to determine any significant deviations from the industry averages.	MK*			

III.B.1.b. Credit Risk Repository – Life/A&H/Fraternal Annual

m. Review the Annual Supplemental Investment Risks Interrogatories and assess any unusual items or areas that indicate a non-diversified portfolio.	MK*
n. Perform sector analysis of Schedule D holdings with assistance of the NAIC Capital Markets Bureau if concerns exist that indicate a sector of the market may be experiencing financial distress that could result in credit risk to holders of bonds or stocks in that sector.	MK
o. If concerns exist regarding counterparty credit risk on derivatives, review Annual Financial Statement, Schedule DB, Part D to identify the counterparties and use available information (e.g., rating agency reports) to identify any concerns with the credit quality of the counterparty.	

Exposure to Non-Investment Grade Bonds

2. Determine whether there are concerns due to the level of investment in non-investment grade bonds.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Ratio of non-investment grade bonds and non-investment grade short-term investments to capital and surplus.		>25%	[Data]	[Data]
b. Ratio of non-investment grade bonds (excluding short-term investments) to capital and surplus.		>15%	[Data]	[Data]
c. Increase in non-investment grade bonds and non-investment grade short-term investments where such investments currently exceed 3.5% of invested assets.		>15%	[Data]	[Data]
d. Compare the insurer's holdings of non-investment grade bonds to the limitations included in the NAIC <i>Investments in Medium and Lower Grade Obligations Model Regulation</i> (#340) [Annual Financial Statement, Schedule D – Part 1A – Section 1]				
i. Aggregate amount of all bonds owned which have an NAIC rating of 3, 4, 5, or 6 as a percent of total net admitted assets (excluding separate accounts).	LG	>20%	[Data]	[Data]
ii. Aggregate amount of all bonds owned which have an NAIC rating of 4, 5 or 6 as a percent of total net admitted assets (excluding separate accounts).	LG	>10%	[Data]	[Data]
iii. Aggregate amount of all bonds owned which have an NAIC rating of 5 or 6 as a percent of total net admitted assets (excluding separate accounts).	LG	>3%	[Data]	[Data]
iv. Aggregate amount of all bonds owned which have an NAIC rating of 6 as a percent of total net admitted assets (excluding separate accounts).	LG	>1%	[Data]	[Data]
				<i>Other Risks</i>
e. If level of non-investment grade bonds is high, review Annual Financial Statement, Schedule D Part 1A and Part 1, Jumpstart Reports (e.g., Bond Investment Designation Exception				

III.B.1.b. Credit Risk Repository – Life/A&H/Fraternal Annual

Report) and the Financial Profile Report to assess and understand the composition of non-investment grade bonds:	
<ul style="list-style-type: none"> Amount and/or percentage of bonds in each class 3, 4, 5 or 6. Concentration by sector or issuer, including affiliates. If bonds have been rated by a credit rating provider (CRP) (e.g., Moody's Investors Service, Standard & Poor's, A.M. Best or Fitch Ratings). 	
f. For the more significant non-investment grade bonds, request the current report from a CRP regarding the issuer to determine the issuer's financial position and ability to repay its debt.	

Exposure to Mortgage and/or Asset-Backed Securities

3. Review Annual Financial Statement, Schedule D – Part 1A – Section 2 to determine whether there are concerns due to the level of investment in RMBS, CMBS and LBaSS.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Ratio of all RMBS, CMBS and LBaSS owned to capital and surplus plus AVR.	LQ	>200%	[Data]	[Data]
b. Increase in all RMBS, CMBS and LBaSS investments from the prior year where such investments currently exceed 15% of cash and invested assets.	LQ	>20%	[Data]	[Data]
c. Ratio of RMBS to cash and invested assets.	LQ	>5%	[Data]	[Data]
				<i>Other Risks</i>
d. Review the RMBS, CMBS and LBaSS categories in Annual Financial Statement, Schedule D – Part 1 for bonds with a book/adjusted carrying value significantly in excess of par value, which could result in a loss being realized if bond prepayments occur faster than anticipated.				
e. Review the RMBS, CMBS and LBaSS categories in Annual Financial Statement, Schedule D – Part 1 for bonds with an unusually high effective yield.				
f. Review the calculation of the insurer's C-3 Interest Rate Risk Component of its Risk-Based Capital formula.				
g. Review the Statement Actuarial Opinion for any comments regarding modeling of the RMBS portfolio in the cash flow testing that was performed by the insurer.				
h. Review Annual Financial Statement, Schedule D, Part 1, and the Snapshot Investment Summary Report on iSite+ to assess exposure to agency versus non-agency RMBS, CMBS and LBaSS.				
i. Consider having the RMBS, CMBS and LBaSS modeled by an independent actuary as a part of an independent cash flow analysis.				

Exposure to Mortgage Loans

4. Determine whether there are concerns due to the level or quality of investment in mortgage loans.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>

III.B.1.b. Credit Risk Repository – Life/A&H/Fraternal Annual

a. Ratio of total mortgage loans to capital and surplus plus asset valuation reserve (AVR).	LQ	>125%	[Data]	[Data]
b. Increase in mortgage loans from the prior year, where the ratio of total mortgage loans to cash and invested assets exceeds 10%.	LQ	>15%	[Data]	[Data]
c. Ratio of problem mortgage loans to capital and surplus plus AVR.	LQ	>15%	[Data]	[Data]
d. Amount of any “Other than first liens” included in total admitted mortgage loans. [Annual Financial Statement, Assets (page 2)]		>0	[Data]	[Data]
e. Ratio of commercial mortgages to total mortgages.		>50%	[Data]	[Data]
				<i>Other Risks</i>
f. Utilizing postal codes and property type reported in Schedule B – Part 1, identify if mortgage loans owned is concentrated in one or a few geographical areas.				
g. Review debt service coverage ratios and adjusted loan-to-values of the individual mortgage loans.				
h. If concerns exist, review Schedule B – Part 1:	MK			
i. Determine the amount of each type of mortgage loan owned.				
ii. Compare the book value/recorded investment of each loan to the value of the land and buildings mortgaged to determine whether the mortgage loans are adequately collateralized.				
iii. Review the date of last appraisal or valuation to determine whether updated appraisals should be obtained.				
iv. Determine whether any of the mortgage loans are to an officer, director, parent, subsidiary, or affiliate.				

Exposure to Other (Schedule BA) Assets

5. Determine whether there are concerns due to the level of investment in other (Schedule BA) invested assets.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Ratio of Schedule BA assets to capital and surplus plus AVR.	LQ*, MK*	>10%	[Data]	[Data]
b. Increase in Schedule BA Assets from the prior year, where the ratio of investments in Schedule BA assets to cash and invested assets is greater than 3.5%.	LQ*, MK*	>10%	[Data]	[Data]
				<i>Other Risks</i>
c. Review Annual Financial Statement, Schedule BA – Other Invested Assets Owned, to determine the amount and types of other invested assets owned and identify if the insurer’s exposure to certain classes of BA assets are significant (e.g., hedge funds, private equity funds, etc.).	LQ, MK			

III.B.1.b. Credit Risk Repository – Life/A&H/Fraternal Annual

<ul style="list-style-type: none"> i. Determine whether concerns exist regarding the insurer’s exposure to non-traditional investments, (i.e., hedge funds and private equity funds) as compared to capital and surplus and impact on liquidity. ii. Review the experience of the insurer with respect to investing in alternative investments such as hedge funds and private equity funds. iii. Obtain and review cash flow projections to ensure that the insurer understands the cash flow characteristics of such investments. iv. Inquire of the insurer regarding the liquidity of non-traditional investments to ensure that limitations in this area are understood. v. Perform procedures to test the accuracy of reporting for non-traditional investments. vi. Ensure that senior management and the Board of the insurer have explicitly signed off on non-traditional investments. 	
d. Review Schedule BA to determine if a significant amount of BA assets have NAIC ratings of 3, 4, 5 or 6 or have a “Z” designation.	

Invested Asset Exposure to Climate Change Risk

6. Assess the potential impact of material climate change and/or transition and asset devaluation risk on the insurer’s invested asset portfolio.

	<i>Other Risks</i>
a. Review information provided in the insurer’s response to the NAIC’s Climate Risk and Disclosure Survey (if available) on its exposure to material climate change/energy transition risk and related mitigation activity in this area.	LQ*, MK*
b. Review relevant information provided in the Own Risk and Solvency Assessment (ORSA) Summary Report, and/or U.S. Securities and Exchange Commission (SEC) 10K or 10Q filings (if available) that discusses the insurer’s exposure to material climate change/energy transition risk and related mitigation activity in this area.	LQ*, MK*
c. Review information provided in the NAIC’s U.S. Insurance Industry Climate Affected Investment Analysis to identify potential concentrations in insurer exposure.	LQ*, MK*

Quality of Assets Supporting Collateral Loans

7. Determine whether there are concerns due to the quality of assets supporting collateral loans.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Ratio of collateral loans to capital and surplus plus AVR.	LQ*	>20%	[Data]	[Data]
				<i>Other Risks</i>
b. Review Annual Financial Statement, Schedule BA – Other Invested Assets Owned and Schedule DA – Short-term Investments, and perform the following for each such loan:	LQ*, MK			
i. Determine whether the collateral for the loan is an acceptable asset.				

III.B.1.b. Credit Risk Repository – Life/A&H/Fraternal Annual

ii. Determine whether the collateral loan is to an officer, director, parent, subsidiary or affiliate.	
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Reinsurance Recoverable and Reinsurer Credit Quality

8. Determine whether amounts recoverable (both paid and unpaid losses on claims and reserve credits) or amounts receivable from reinsurers are significant and collectable.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Reinsurance amounts recoverable on paid and unpaid losses on claims as a percent of capital and surplus.	LQ	>10%	[Data]	[Data]
b. Reserve credits (Life, A&H, and Annuities) as a percent of capital and surplus.		>25%	[Data]	[Data]
c. Other amounts receivable under reinsurance contracts as a percent of capital and surplus.		>10%	[Data]	[Data]
d. Total amount of funds withheld for payment of losses by ceding companies as a percentage of capital and surplus.		>10%	[Data]	[Data]
				<i>Other Risks</i>
e. Review Annual Financial Statement, Schedule S – Part 3 – Section 1 and Schedule S – Part 3 – Section 2. Are any unusual items noted regarding the types of reinsurance and their relative significance, or the specific reinsurers involved?	OP			
f. If concerns exist, review the reinsurer's history of payments of recoverables and determine compliance with the NAIC <i>Life and Health Reinsurance Agreements Model Regulation</i> (#791) regarding quarterly settlements of payments due from reinsurers.	OP			
g. Determine if and assess any significant write-offs of reinsurance collectables that have occurred during the period.	OP			
h. Verify by direct contact or confirmation that funds withheld for payment are valid and adequately segregated for payment of losses.				

9. If reinsurance is significant based on review of the above procedure, assess the credit quality and financial solvency of the reinsurers the insurer cedes a material amount of business to or has material reinsurance recoverable due from.

	<i>Other Risks</i>
a. Determine the current ratings of the reinsurer from the major rating agencies and investigate significant changes during the past 12 months.	
b. Obtain and review the Audited Financial Report, Annual Financial Statement, Actuarial Opinion and U.S. Securities and Exchange (SEC) Filings (if applicable) of the reinsurer for additional insight regarding collectability and credit quality of the reinsurer.	
c. Review information about the reinsurer available from industry analysts and benchmark capital adequacy with top performers and peer groups.	

III.B.1.b. Credit Risk Repository – Life/A&H/Fraternal Annual

d. Contact the domiciliary state to determine whether any regulatory actions are pending against the reinsurer. Also, review iSite+ data on the reinsurer (i.e., financial statements, Regulatory Information Retrieval System [RIRS] and Global Receivership Information Database [GRID]).	
e. Determine whether the reinsurance transactions involved going “in and out” of treaties in such a manner that, in substance, the transactions are for financial reinsurance purposes.	
f. Review Schedule S – Part 4 to determine if adequate levels of collateral (letters of credit [LOCs], etc.) are maintained for unauthorized reinsurance.	
g. Review results of reinsurance Jumpstart Reports to determine if material differences exist between amounts reported on reinsurance schedules of the insurer compared to the ceding insurers. i. If significant differences are noted, further investigate if the amounts appear to be due to timing and/or consider asking the insurer for aging of amounts payable/receivable.	

10. Determine whether the insurer’s accounting treatment for reinsurance is proper and in *accordance with the Annual Statement Instructions*.

				Other Risks
a. Briefly scan the individual reinsurers listed in Annual Financial Statement, Schedule S – Part 3 – Section 1 - Reinsurance Ceded Life and Annuities and Schedule S – Part 3 – Section 2 - Reinsurance Ceded Accident and Health. Do any of the reinsurers classified as authorized appear to be improperly classified as such?				
	Other Risks	Benchmark	Result	Outside Benchmark
b. Is the liability for reinsurance in unauthorized companies to the sum of reserve credits taken, paid and unpaid losses, and other debits greater than 25%? [Annual Financial Statement, Schedule S – Part 4]		>25%	[Data]	[Data]
c. Review Annual Financial Statement, General Interrogatories, Part 1, #15.1 and 15.2. i. Is the reporting entity the beneficiary of a LOC that is unrelated to reinsurance where the issuing or confirming bank is not on the SVO Qualified U.S. Financial Institutions List? ii. If “yes,” list the name of the issuing or confirming bank, the circumstances that can trigger the LOC and the amount.		=YES		[Data]
				Other Risks
d. Review Annual Financial Statement, Schedule S – Part 4. Determine if there are any concerns about the appropriateness of reinsurance credits taken.				
e. Note any concerns in the Statement of Actuarial Opinion regarding the insurer failing to properly establish a reserve relating to reinsurance assumed from another reinsurer for accident and health.				

III.B.1.b. Credit Risk Repository – Life/A&H/Fraternal Annual

f. Briefly scan the Annual Financial Statement pages relating to Assets; Liabilities, Surplus and Other Funds; and Summary of Operations. Are any unusual items noted relating to write-ins or significant changes or inconsistencies from prior years regarding reinsurance activities?	
g. Generate Examination Jumpstart analysis to determine whether ceding company credits are appropriately “mirrored” by the reinsurer, after considering the impact of normal timing delays.	CR
h. If the insurer holds a material LOC securing unauthorized reinsurance recoverables, identify the amount of the LOC and the issuing bank. If “yes”, then provide the rating of the bank and summarize any concerns.	

Affiliated Receivable or Payable

- 11. Review the balance sheet asset receivable from parent, subsidiaries and affiliates, as well as the liability payable to parent, subsidiaries and affiliates to determine whether there are concerns with the level of affiliated receivables/payables.**

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Affiliate receivable or payable to capital and surplus?	LQ, OP*	>10%	[Data]	[Data]
				<i>Other Risks</i>
b. If there are concerns regarding collectability of affiliated receivables, review the Annual Financial Statement, Schedule Y – Part 2, Notes to the Financial Statements, Management’s Discussion and Analysis (MD&A) and other available information (e.g., Form D filings) for more information about the nature and timing of the receivable. (Review the Operations Risk Repository for more procedures on affiliated transactions.)				LQ, OP

Related Party Exposure in the Investment Portfolio

- 12. Assess related party exposure in the investment portfolio.**

	<i>Other Risks</i>
<p>a. Review the Annual Financial Statement investment schedules, as disclosed in the column “Investments Involving Related Parties” and utilizing iSite+ tools, determine if the insurer has material related party exposures in its investment portfolio.</p> <p>This disclosure is included in:</p> <ul style="list-style-type: none"> • Schedule B • Schedule BA • Schedule D • Schedule DA • Schedule DB • Schedule DL • Schedule E, Part 2 <p>Consider exposure by asset class and in aggregate, and by the role of the related party in the investment as designed by the “Investments Involving Related Parties” disclosure.</p>	LQ, MK

III.B.1.b. Credit Risk Repository – Life/A&H/Fraternal Annual

b. If concerns exist regarding a material related party exposure in the investment portfolio, assess the credit quality of those investments involving related parties by reviewing designations, assessing historical default experience, etc.	LQ, MK
<p>c. If concerns exist regarding a material related party exposure in investment management or advisory services, consider the following:</p> <ol style="list-style-type: none"> i. Review the procedures in the “Additional Procedures” section below regarding Third Party Investment Advisors and consider their application to related party advisors in that role. ii. In addition to the additional analysis procedures regarding third party investment advisors, consider the following: <ol style="list-style-type: none"> 1. Review the insurer’s investment policy guidelines and determine whether the related party investments follow the guidelines and are in compliance with regulatory requirements. 2. Review whether the fee structure for asset management is fair, reasonable, and appropriately recognized as investment expenses. 3. If the related party asset manager also originates/securitizes investments held by the insurer, consider requesting additional information from the insurer to determine the following: <ol style="list-style-type: none"> a. Whether the asset manager has adequate experience and knowledge in originating and managing the types of investments; b. Whether the asset manager follows appropriate underwriting practices and applicable regulatory requirements in originating investments; and c. Whether the fee structures embedded in securities (if applicable) are fair, reasonable, and appropriately account for potential duplication of fees or conflicts of interest. 	OP

Additional Analysis and Follow-up Procedures

Request and Assess the Insurer’s Investment Policies and Strategies

If concerns exist regarding the level of credit exposure, request and review the insurer’s investment strategy to determine if it is appropriately structured to support its ongoing business plan. Review the guidelines outlined in the plan for:

- Quality of issues invested in and diversification standards pertaining to issuer, industry, duration, liquidity, geographic location, and issues/sectors exposed to material climate change, transition, and asset devaluation risks.
- Expected rate of returns on investments (projected investment income) compared to actual results.
- Planned increases in investment types, sectors, markets, etc.
- Appropriateness of the investment plan for the liability structure of the insurer. (This may require a review of asset adequacy analysis for asset liability matching (ALM) and discussion with the insurer’s management to better understand their plan.)

Upon review of the investment plan, compare the plan to actual results. Does the insurer and its investment manager(s) appear to be adhering to the investment policies and guidelines in the investment plan?

III.B.1.b. Credit Risk Repository – Life/A&H/Fraternal Annual

Examination Findings: Review the most recent examination report and Summary Review Memorandum (SRM) for any findings regarding credit risks associated with:

- Investment concentration
- Exposure to riskier asset classes
- Climate change, transition, and asset devaluation
- Asset liability matching
- Adherence to investment policies and strategies
- Investment management and use of and monitoring of external investment managers

Proper classification (i.e., authorized, unauthorized, certified) and calculation of reinsurance collateral and provision.

NAIC Capital Market's Bureau Analytical Assistance:

Consider requesting the following analytical reviews:

- Review of the insurer's investment portfolio.
- Review of Investment Management Agreements.

Third-Party Investment Advisers:

Assess and determine if any concerns exist regarding third party investment advisers and associated contractual arrangements.

- Review Annual Financial Statement, General Interrogatories, Part 1, #29.05. Does the insurer utilize third party investment advisors, broker/dealer or individuals acting on behalf of the insurer with access to their investment accounts?

If "yes", consider the following procedures:

- Review the results of the most recent financial examination work papers, follow-up and prospective risk information and the summary review memorandum provided by the examiners. Did the examination identify any issues with regard to investment advisers and associated contractual arrangements that require follow-up analysis or communication with the insurer? If "yes", document the follow-up work performed.
- Compare Annual Financial Statement, General Interrogatories, Part 1, #29.05 for the current year to the prior year to determine if there have been any changes in advisors. If yes,
 - Consider obtaining an explanation for the change from the insurer.
 - Consider obtaining a copy of the new investment advisor agreement and review it for appropriate provisions.
- Using the information reported in Annual Financial Statement, General Interrogatories, Part 1, #29.05, obtain and review SEC Form ADV (if available), to determine if the investment advisor is in good standing with the SEC. If not in good standing, contact the insurer to request an explanation.
- If agreements with third party investment advisers are affiliated, have the appropriate Form D – Prior Notice of Transactions been filed and approved by the department? Were any concerns noted or follow-up monitoring recommended?
- Request information from the insurer regarding the background and expertise in structured securities of its investment advisors (in-house and/or contractual) and its analytical system capabilities. Determine

III.B.1.b. Credit Risk Repository – Life/A&H/Fraternal Annual

whether the advisors and systems are adequate to allow the insurer to continuously monitor its structured securities investments.

- If the insurer uses an external asset manager, consider if investments on Schedule BA are invested in funds that are affiliated with the asset manager or are managed by that asset manager. Consider the following issues:
 - If any conflicts of interest exist.
 - If the investment is appropriate for the insurer's portfolio and is arm's-length.
 - If the insurer is paying double fees.

Inquire of the Insurer:

If concerns exist, consider requesting information from the insurer regarding:

General Investment Inquiries:

- If management has adequately reviewed the investment portfolio and understands the yields, underlying collateral, cash flows and investment volatility.
- Any additional concentration by collateral type.
- Management's process for valuing securities so as to assist the analyst in assessing if the securities are valued appropriately.
- Management's intended use of certain riskier investments and purpose within the insurer's portfolio.
- Credit risk associated with sector concentration.
- If management has an appropriate level of knowledge and expertise with the type of securities being purchased/held.
- If the insurer has controls implemented to mitigate the risks associated with this investment type.
- Sources of liquidity, such as LOCs.

Investment Diversification:

- Planned asset mix and diversification strategies.
- How the insurer manages counterparty credit risk, including diversification risk of counterparties.

Mortgages:

- Increases by adjustment in book value/recorded investment during the year.

BA Assets:

- Request information necessary to determine the fair value of collateral to the amount loaned to ensure the loan is adequately collateralized.
- Information to support significant increases by adjustment in book/adjusted carrying value (BACV) during the year.
- Current Audited Financial Statements and other documents (partnership agreements, etc.) necessary to support the value of the insurer's investment in partnerships and joint ventures.
- Information necessary to support the value of significant other invested assets other than partnerships and joint ventures.
- Current details on cash flows and returns for the different types of investments, especially hedge funds and private equity funds.

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Non-Investment Grade Bonds:

- Significant exposures.
- Policies and strategy for investing in non-investment grade bonds. Determine if the insurer is adhering to those policies.

RMBS, CMBS and LBaSS:

- Percentage distribution and amounts of each type of RMBS, CMBS and LBaSS held; planned amortization class (PAC), support bonds, interest-only (IO) tranches, and principle-only (PO) tranches to evaluate the level of prepayment risk in the portfolio.
- Projected prepayment speeds on its RMBS portfolio and compare with historical prepayments, as well as the prepayment assumption at the time of purchase.

Reinsurance:

- Request a copy of the insurer's A.M. Best Supplemental Ratings Questionnaire and review the reinsurance section for unusual items.
- If concerns exist regarding the credit quality and financial solvency of an unauthorized reinsurer, request a copy of the reinsurance agreement(s), and confirm amounts included on Annual Financial Statement, Schedule S – Part 4 - Reinsurance Ceded to Unauthorized Companies.
- Aging of reinsurance amounts payable/receivable.

Own Risk and Solvency Assessment (ORSA) Summary Report:

If the insurer is required to file ORSA or part of a group that is required to file ORSA,

- Did the ORSA Summary Report analysis conducted by the lead state indicate any credit risks that require further monitoring or follow-up?
- Did the ORSA Summary Report Analysis conducted by the lead state indicate any mitigating strategies for existing or prospective credit risks?

Holding Company Analysis:

- Did the Holding Company Analysis conducted by the lead state indicate any credit risks affecting the insurer that require further monitoring or follow-up?
- Did the Holding Company Analysis conducted by the lead state indicate any mitigating strategies for existing or prospective credit risks affecting the insurer?

Asset Liability Matching (ALM):

- Did the review of the Statement of Actuarial Opinion or other actuarial filings indicate any concerns regarding the adequacy of ALM and the sufficiency of assets to meet the business obligations of the insurer?
- If concerns are identified regarding overall liquidity of the asset portfolio, request a copy of the insurer's asset/liability matching policy and/or liquidity stress testing/scenario analysis.

Example Prospective Risk Considerations

Risk Component for IPS		Explanation of Risk Component
1	Significant concentration by [asset class, sector, issuer, etc.].	High exposure in any one asset class, industry sector or issuer could result in material credit losses if asset class, industry sector or issuer experiences an economic decline.

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2	Borrower default risk for [mortgage loans, RMBS, CMBS or LBaSS securities, etc.].	Lower credit quality of the borrowers (i.e., prime versus subprime) may result in higher risk of default, leading to credit losses in the event of a housing and/or commercial real estate market downturn.
3	Prepayment variability in RMBS.	Prepayment variability in RMBS could result in actual cash flows and investment yields to be materially different from expectations.
4	Volatility of non-investment grade bonds.	The market volatility of below investment grade bonds makes the price at which bonds are held an important consideration.
5	Foreign security default.	Material exposure to foreign investments could result in credit losses if those investments are impacted by negative changes in geopolitical or foreign economic environments.
6	Impairment of [bonds, etc.].	Risk of further deterioration in credit quality may result in other-than-temporary impairments impacting income and surplus.
7	Bondholder default.	Investment grade bonds that have declined to a non-investment grade status may not recover lost value.
8	Structured notes cash flow volatility risk.	Impact of the volatility of structured notes and the underlying asset on which its cash flows are based.
9	Structured notes collateral concentration risk.	Material investment in structured notes that may have collateral type concentration may result in concentration risk (lack of diversity) to the insurer's portfolio.
10	Structured notes default.	Structured notes may be subordinated in the overall transaction representing exposure to non-payment in event of default.
11	Second lien mortgage loan risk.	High exposure to second lien loans may result in increase in risk of non-payment in the event of default as first lien loans are paid first from the value of the property.
12	Mortgage loan collateral inadequate.	Out-of-date appraisals may result in inaccurate valuation, resulting in the underlying collateral asset not being adequate.
13	High-risk mortgage loan valuation.	The investments in high-risk mortgage loans are incorrectly valued.
14	Complexity of BA assets.	BA assets often have complex investment strategies and unpredictable cash flows.
15	Adequacy of collateral of BA asset.	Volatility of underlying assets (e.g., certain hedge funds and private equity funds) may result in underlying assets not adequate.
16	Economic impact on portfolio of [BA assets, derivatives, etc.].	Portfolio volatility driven by economic changes.
17	Hedge effectiveness of derivatives portfolio.	Derivatives strategy may not meet hedge effectiveness for mitigating risk.
18	Investment strategy contemplate higher [credit, market, liquidity...] risk.	The insurer's investment strategy may not be structured to support its ongoing business plan, which could indicate the strategy enjoys higher credit, market and liquidity risks than are appropriate for the liabilities of the insurer and may lead to financial concerns in the future.

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19	Investment results actual to projected variance.	The insurer's actual investment portfolio and/or portfolio performance may vary significantly from projections if the insurer is not adhering to the strategy in place (i.e., higher actual credit, market or liquidity risk compared to the plan).
20	Collectability of receivables for [insert name of receivable].	Payments of [insert name of receivable] may be delayed or not be paid when due, resulting in cash flow mismatch.
21	Credit quality of [reinsurer, agents, affiliate, etc.].	Credit quality and poor financial strength of a [reinsurer, agent, etc.] may result in future collectability risk, which may result in ongoing credit risk and future liquidity issues.
22	Exposure to climate change, transition, and asset devaluation risk	The insurer's investment portfolio is subject to prospective devaluation of the assets/changes in the asset return associated with its holdings of climate-affected assets.

III.B.1.b. Credit Risk Repository – Life/A&H/Fraternal Quarterly

Credit Risk: Amounts actually collected or collectible are less than those contractually due or payments are not remitted on a timely basis.

Note: The repository is not an all-inclusive list of possible procedures. Therefore, risks identified for which no procedure is available should be analyzed by the state insurance department based on the nature and scope of the risk. Also, note that key insurance operations or lines of business, for example, may have related risks addressed in different repositories. Therefore, the analyst may need to review other repositories in conjunction with credit risk. For example:

- Investment asset classes (Bonds, Mortgages, etc.) also are discussed in Market and/or Liquidity Risk Repositories.
- Reinsurance also is discussed in the Operational and Strategic Risk Repositories.

Analysis Documentation: Results of credit risk analysis should be documented in Section III: Risk Assessment of the insurer.

Investment Portfolio Diversification

1. Determine whether the insurer's investment portfolio appears to be adequately diversified to avoid any undue concentration of investments by type or issue.

<i>"a" through "i": Shown are as a percent of total net admitted assets (excluding separate accounts)</i>	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Preferred stocks.		>5%	[Data]	[Data]
b. Non-Investment Grade Bonds.		>3.5%	[Data]	[Data]
c. Mortgage loans.	MK*	>20%	[Data]	[Data]
d. Other invested assets (Schedule BA).	LQ*	>5%	[Data]	[Data]
e. Aggregate write-ins for invested assets.	LQ	>5%	[Data]	[Data]
f. Investments in affiliates.	LQ, MK*	>10%	[Data]	[Data]
g. Is the total book/adjusted carrying value net of collateral greater than 10 percent of capital and surplus plus AVR? [Quarterly Financial Statement, Schedule DB, Part D, Section 1]		>10%	[Data]	[Data]
i. If "yes," list the book/adjusted carrying value net of collateral.			[Data]	
				<i>Other Risks</i>
h. Review the Percentage Distribution of Total Assets in the Quarterly Financial Profile Report for significant shifts in the mix of investments owned during the past five quarters.	MK			
i. Review General Interrogatories, Part 2 to identify any material amounts of mortgage loans with interest overdue or in the process of foreclosure.				

Changes in Asset Exposures

2. Determine whether there are concerns due to the change in certain asset classes from the prior year-end.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>

III.B.1.b. Credit Risk Repository – Life/A&H/Fraternal Quarterly

a. Increase in non-investment grade bonds and non-investment grade short-term investments from the prior year-end, where such investments are currently greater than 3.5% of cash and invested assets.	LQ	>15%	[Data]	[Data]
b. Increase in mortgage loans from prior year-end, where the ratio of total mortgage loans to cash and invested assets is greater than 10%.	LQ, MK*	>15%	[Data]	[Data]
c. Increase in BA assets from prior year-end, where the ratio of BA assets to cash and invested assets is greater than 3.5%.	LQ*, MK	>10%	[Data]	[Data]
d. Increase in aggregate write-ins from prior year-end, where the ratio of aggregate write-ins to cash and invested assets is greater than 3.5%.	LQ	>20%	[Data]	[Data]
e. Increase in affiliated investments from the prior year-end, where the ratio affiliated investments to cash and invested assets is greater than 3.5%.	LQ, MK*	>20%	[Data]	[Data]
f. Review Schedule DB – Part D – Section 1. If the ratio of potential exposure on counterparty exposure for derivative instruments to capital and surplus plus AVR exceeds 3.5%, have such investments increased more than 10% over the prior year-end?	MK	>10%	[Data]	[Data]
				<i>Other Risks</i>
g. If the level of non-investment grade bonds is high (i.e., greater than 3.5% of cash and invested assets), review Quarterly Financial, Schedule D – Part 1B and the Quarterly Financial Profile Report to assess and understand the composition of non-investment grade bonds: <ul style="list-style-type: none"> • Amount and/or percentage of bonds in each class 3, 4, 5 or 6. • Concentration by sector or issuer, including affiliates. • If bonds have been rated by a credit rating provider (CRP). 				

Reinsurance Recoverable or Payable

3. Determine whether amounts recoverable (both paid and unpaid losses on claims and reserve credits) or amounts receivable from reinsurers are significant and collectable.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Reinsurance amounts recoverable on paid and unpaid losses on claims to capital and surplus.	LQ	>10%	[Data]	[Data]
b. Change in reinsurance recoverables/receivables from prior year-end.		>25%	[Data]	[Data]
c. Review Quarterly Financial Statement, Schedule S – Reinsurance Ceded. Were any new reinsurers added since the prior quarter?	OP, ST*	Yes if count >0	[Data]	[Data]

III.B.1.b. Credit Risk Repository – Life/A&H/Fraternal Quarterly

d. Determine whether the liability for reinsurance in unauthorized and certified companies is significant.		>0	[Data]	[Data]
i. Liability for reinsurance in unauthorized and certified companies.				
ii. Change in liability, reinsurance in unauthorized and certified companies.		>10% or <-10% from the prior quarter OR >20% or <-20% from the prior year-end	[Data]	[Data]
iii. Change in liability for reinsurance in unauthorized and certified companies (per the Summary of Operations, capital and surplus line item).		>10% or <-10% from the prior quarter OR >20% or <-20% from the prior year-end	[Data]	[Data]
e. Did the insurer experience any material transactions requiring the filing of Disclosure of Material transactions with the state of domicile as required by the Model Act? [Quarterly Financial Statement, General Interrogatories, Part, #1.1]	LG*, ST*	=YES		
i. If “yes,” did the insurer fail to make the appropriate filing of Disclosure of Materiality Transactions with the state of domicile? [Quarterly Financial Statement, General Interrogatories, Part 1, #1.2]	LG*, ST*	=YES		
				<i>Other Risks</i>
f. If “yes” and concerns exist, consider the following procedures:				
i. Determine the current ratings of the new reinsurer from the major rating agencies and investigate significant changes during the past 12 months.				
ii. Obtain and review the Annual Audited Financial Report, Financial Statements, Annual Actuarial Opinion and U.S. Securities and Exchange Commission (SEC) Filings (if applicable) of the reinsurer for additional insight regarding collectability and credit quality of the reinsurer.				
iii. Review information about the reinsurer available from industry analysts and benchmark capital adequacy with top performers and peer groups.				
iv. Contact the domiciliary state to determine whether any regulatory actions are pending against the reinsurer. Also, review iSite+ data on the reinsurer (i.e., financial statements,				

III.B.1.b. Credit Risk Repository – Life/A&H/Fraternal Quarterly

Regulatory Information Retrieval System [RIRS] and Global Receivership Information Database [GRID]).	
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Affiliated Receivable or Payable

4. Review the balance sheet asset receivable from parent, subsidiaries and affiliates, as well as the liability payable to parent, subsidiaries and affiliates to determine whether there are concerns with the level of affiliated receivables/payables.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Affiliated receivable or payable to capital and surplus.	LQ, OP	>10%	[Data]	[Data]
b. Change in affiliated receivable or payable, where it is greater than 10% of capital and surplus	LQ, OP	>25% or <-25% from the prior year-end	[Data]	[Data]
c. Change in federal and foreign income tax recoverables where recoverables are greater than 3% of total assets (excluding separate accounts).	LQ, OP	>10% or <-10% from the prior quarter OR >20% or <-20% from the prior year-end	[Data]	[Data]
				<i>Other Risks</i>
d. Are there any indications that significant or unusual transactions involve an affiliate or other related party?				
e. If there are concerns regarding collectability of affiliated receivables, review Notes to the Financial Statements and other available information (e.g., Form D filings) for more information about the nature and timing of the receivable. <i>(Review the Operational Risk Repository for more procedures on affiliated transactions.)</i>	LQ, OP			

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Credit Risk: Amounts actually collected or collectible are less than those contractually due or payments are not remitted on a timely basis.

Note: The repository is not an all-inclusive list of possible procedures. Therefore, risks identified for which no procedure is available should be analyzed by the state insurance department based on the nature and scope of the risk. Also, note that key insurance operations or lines of business, for example, may have related risks addressed in different repositories. Therefore, analysts may need to review other repositories in conjunction with credit risk. For example:

- Investment strategy is also discussed in the Liquidity, Market, and Strategic Risk Repositories.
- Investment asset classes (Bonds, Mortgages, etc.) are also discussed in the Market and/or Liquidity Risk Repositories.
- Reinsurance is also discussed in the Operational and Strategic Risk Repositories.

Analysis Documentation: Results of credit risk analysis should be documented in Section III: Risk Assessment of the insurer.

Investment Portfolio Diversification

1. Determine whether the insurer's investment portfolio appears to be adequately diversified to avoid any undue concentration of investments by type or issue.

<i>"a" through "i": Shown are as a percent of total net admitted assets (excluding separate accounts)</i>	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Industrial and miscellaneous bonds (unaffiliated)		>25%	[Data]	[Data]
b. Residential mortgaged-backed securities (RMBS), commercial mortgage-backed securities (CMBS) or other loan-backed and structured securities (LBaSS)	MK*	>20%	[Data]	[Data]
c. Preferred stocks		>3%	[Data]	[Data]
d. Mortgage loans	MK*	>5%	[Data]	[Data]
e. Other invested assets (Schedule BA)	LQ	>5%	[Data]	[Data]
f. Derivative exposure to any single exchange, counterparty or central clearinghouse	MK	>5%	[Data]	[Data]
g. Aggregate write-ins for invested assets	LQ	>5%	[Data]	[Data]
h. Investments in affiliates	LQ, MK*	>5%	[Data]	[Data]
i. Any one single investment (by issuer) in bonds, preferred stock, mortgages or BA assets (excluding federal issuers and affiliated investments)	MK	>3%	[Data]	[Data]
				<i>Other Risks</i>
j. Review the % Distribution of Total Assets section of the Annual Financial Profile Report for significant shifts in the mix of investments owned during the past five years.	MK*			
k. Compare the insurer's distribution of cash and invested assets per the % Distribution of Total Assets section of the Annual Financial Profile Report and Investment Snapshot Report to industry and peer averages to determine any significant deviations from the industry averages.	MK*			
l. Review the Annual Supplemental Investment Risks Interrogatories and assess any unusual	MK*			

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items or areas that would indicate a non-diversified portfolio.	
m. Perform a sector analysis of Schedule D holdings with assistance of the NAIC Capital Markets Bureau if concerns exist that indicate a sector of the market may be experiencing financial distress that could result in credit risk to holders of bonds or stocks in that sector.	MK
n. If concerns exist regarding counterparty credit risk on derivatives, review Annual Financial Statement, Schedule DB – Part D – Section 1 to identify the counterparties and use available information (e.g., rating agency reports) to identify any concerns with the credit quality of the counterparty.	

Exposure to Non-Investment Grade Bonds

2. Determine whether there are concerns due to the level of investment in non-investment grade bonds.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Ratio of non-investment grade bonds and non-investment grade short-term investments to capital and surplus		>15%	[Data]	[Data]
b. Ratio of non-investment grade bonds (excluding short-term investments) to capital and surplus		>15%	[Data]	[Data]
c. Increase in non-investment grade bonds and non-investment grade short-term investments where such investments are currently greater than 3.5% of invested assets		>15%	[Data]	[Data]
d. Compare the insurer's holdings of non-investment grade bonds to the limitations included in the NAIC <i>Investments in Medium Grade and Lower Grade Obligations Model Regulation</i> (#340) [Annual Financial Statement, Schedule D – Part 1A – Section 1]:				
i. Aggregate amount of all bonds owned which have an NAIC rating of 3, 4, 5, or 6 to total net admitted assets (excluding separate accounts)	LG	>20%	[Data]	[Data]
ii. Aggregate amount of all bonds owned which have an NAIC rating of 4, 5 or 6 to total net admitted assets (excluding separate accounts)	LG	>10%	[Data]	[Data]
iii. Aggregate amount of all bonds owned which have an NAIC rating of 5 or 6 to total net admitted assets (excluding separate accounts)	LG	>3%	[Data]	[Data]
iv. Aggregate amount of all bonds owned which have an NAIC rating of 6 as a percent of total net admitted assets (excluding separate accounts)	LG	>1%	[Data]	[Data]
				<i>Other Risks</i>
e. If the level of non-investment grade bonds is high, review Annual Financial Statement, Schedule D – Part 1A and Part 1, Jumpstart Reports (e.g., Bond Investment Designation Exception Report) and the Financial Profile Report to assess and understand the				

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composition of non-investment grade bonds: <ul style="list-style-type: none"> • Amount and/or percentage of bonds in each class 3, 4, 5 or 6. • Concentration by sector or issuer, including affiliates. • If bonds have been rated by a credit rating provider (CRP) (e.g., Moody's Investors Service, Standard & Poor's, A.M. Best or Fitch Ratings). 	
f. For the more significant non-investment grade bonds, request the current report from a CRP regarding the issuer to determine the issuer's financial position and ability to repay its debt.	

Exposure to Mortgage and/or Asset-Backed Securities**3. Review Annual Financial Statement, Schedule D – Part 1A – Section 2 to determine whether there are concerns due to the level of investment in RMBS, CMBS and LBaSS.**

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Ratio of all RMBS, CMBS and LBaSS owned to capital and surplus	LQ	>25%	[Data]	[Data]
b. Increase in all RMBS, CMBS and LBaSS investments from the prior year where such investments are currently greater than 15% of capital and surplus	LQ	>20%	[Data]	[Data]
c. Ratio of RMBS to capital and surplus	LQ	>5%	[Data]	[Data]
				<i>Other Risks</i>
d. Review the RMBS, CMBS and LBaSS categories in Annual Financial Statement, Schedule D – Part 1 for bonds with a book/adjusted carrying value significantly in excess of par value, which could result in a loss being realized if bond prepayments occur faster than anticipated.				
e. Review the RMBS, CMBS and LBaSS categories in Annual Financial Statement, Schedule D – Part 1 for bonds with an unusually high effective yield.				
f. Review Annual Financial Statement, Schedule D – Part 1 and the Snapshot Investment Summary Report on iSite+ to assess exposure to agency versus non-agency RMBS, CMBS and LBaSS.				
g. Consider having the RMBS, CMBS and LBaSS modeled by an independent actuary as a part of an independent cash flow analysis.				

Exposure to Mortgage Loans**4. Determine whether there are concerns due to the level or quality of investment in mortgage loans.**

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Ratio of total mortgage loans to capital and surplus	LQ	>5%	[Data]	[Data]
b. Increase in mortgage loans from the prior year, where the ratio of mortgage loans to capital and	LQ	>15%	[Data]	[Data]

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surplus is greater than 10%				
				Other Risks
c. Using postal codes and property type reported in the Annual Financial Statement, Schedule B – Part 1 to identify if mortgage loans owned is concentrated in one or a few geographical areas.				
d. Review debt service coverage ratios and adjusted loan-to-values of the individual mortgage loans.				
e. If concerns exist, review Annual Financial Statement, Schedule B – Part 1: i. Determine the amount of each type of mortgage loan owned. ii. Compare the book value/recorded investment of each loan to the value of the land and buildings mortgaged to determine whether the mortgage loans are adequately collateralized. iii. Review the date of the last appraisal or valuation to determine whether updated appraisals should be obtained. iv. Determine whether any of the mortgage loans are to an officer, director, parent, subsidiary, or affiliate.				MK

Exposure to Other (Schedule BA) Assets

5. Determine whether there are concerns due to the level of investment in other (Schedule BA) invested assets.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Ratio of Schedule BA assets to capital and surplus	LQ*, MK*	>10%	[Data]	[Data]
b. Increase in Schedule BA assets from the prior year where the ratio of Schedule BA assets to capital and surplus is greater than 5%	LQ*, MK*	>10%	[Data]	[Data]
				<i>Other Risks</i>
c. Review Annual Financial Statement, Schedule BA – Part 1 to determine the amount and types of other invested assets owned and identify if the insurer’s exposure to certain classes of BA assets are significant (e.g., hedge funds, private equity funds, etc.).				LQ, MK
i. Determine whether concerns exist regarding the insurer’s exposure to non-traditional investments (i.e., hedge funds and private equity funds, lines 25 & 26), as compared to capital and surplus and impact on liquidity.				
ii. Review the experience of the insurer with respect to investing in alternative investments such as hedge funds and private equity funds.				
iii. Obtain and review cash flow projections to ensure that the insurer understands the cash flow characteristics of such investments.				
iv. Inquire of the insurer regarding the liquidity of non-traditional investments to ensure that limitations in this area are understood.				
v. Perform procedures to test the accuracy of reporting for non-traditional investments.				

III.B.1.c. Credit Risk Repository – Health Annual

vi. Ensure that senior management and the Board of the insurer have explicitly signed off on non-traditional investments.	
d. Review Schedule BA to determine if a significant amount of BA assets have NAIC ratings of 3, 4, 5 or 6 or have a “Z” designation.	

Invested Asset Exposure to Climate Change Risk

6. Assess the potential impact of material climate change and/or transition and asset devaluation risk on the insurer’s invested asset portfolio.

	<i>Other Risks</i>
a. Review information provided in the insurer’s response to the NAIC’s Climate Risk and Disclosure Survey (if available) on its exposure to material climate change/energy transition risk and related mitigation activity in this area.	LQ*, MK*
b. Review relevant information provided in the Own Risk and Solvency Assessment (ORSA) Summary Report, and/or U.S. Securities and Exchange Commission (SEC) 10-K or 10-Q filings (if available) that discusses the insurer’s exposure to material climate change/energy transition risk and related mitigation activity in this area.	LQ*, MK*
c. Review information provided in the NAIC’s U.S. Insurance Industry Climate Affected Investment Analysis to identify potential concentrations in insurer exposure.	LQ*, MK*

Reinsurance Recoverable and Reinsurer Credit Quality

7. Determine whether amounts recoverable from reinsurers are significant and collectible.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Amounts recoverable from reinsurers to capital and surplus	LQ	>10%	[Data]	[Data]
b. Ceded premiums written to gross premiums written	ST*	>10%	[Data]	[Data]
c. Ceded reserve credits to capital and surplus		>10%	[Data]	[Data]
d. Is the reporting entity the beneficiary of the LOC that is unrelated to reinsurance where the issuing or confirming bank is not on the SVO Qualified U.S. Financial Institutions List? If “yes,” list the name of the issuing or confirming bank, the circumstances that can trigger the LOC, and the amount. [Annual Financial Statement, General Interrogatories, Part 1, #15.1 and #15.2]		=YES		
				<i>Other Risks</i>
e. Review the Annual Financial Statement, Schedule S – Part 3 – Section 2. Are any unusual items noted regarding the types of reinsurance and their relative significance, or the specific reinsurers involved?				
f. Review the Annual Financial Statement, Notes to Financial Statements, Note #23. Did the insurer report any items that cause concern regarding reinsurance balances?				

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g. Review the results of the Actuarial Opinion analysis. Were any concerns noted regarding the collectability of reinsurance recoverables?	
h. Review the reinsurer's historical payment patterns of recoverables and comment on any findings or concerns.	
i. Determine if and assess any significant write-offs of reinsurance collectables that have occurred during the period.	OP

8. If reinsurance is significant based on review of the above procedure, assess the credit quality and financial solvency of the reinsurers the insurer cedes a material amount of business to or has material reinsurance recoverable due from.

	<i>Other Risks</i>
a. Determine the current ratings of the reinsurer from the major rating agencies and investigate significant changes during the past 12 months.	
b. Obtain and review the Audited Financial Report, Annual Financial Statement, Actuarial Opinion and U.S. Securities and Exchange Commission (SEC) Filings (if applicable) of the reinsurer for additional insight regarding collectability and credit quality of the reinsurer.	
c. Review information about the reinsurer available from industry analysts and benchmark capital adequacy with top performers and peer groups.	
d. Contact the domiciliary state to determine whether any regulatory actions are pending against the reinsurer. Also, review of iSite+ data on the reinsurer (i.e., financial statements, Regulatory Information Retrieval System [RIRS] and Global Receivership Information Database [GRID]).	
e. Determine whether adequate levels of collateral (e.g., letters of credit, etc.) are being maintained to secure outstanding losses.	
f. Determine whether the reinsurance transactions involved going "in and out" of treaties in such a manner that, in substance, the transactions are for financial reinsurance purposes.	
g. Review results of reinsurance Jumpstart Reports to determine if material differences exist between amounts reported on reinsurance schedules of the insurer compared to the ceding insurers. i. If significant differences are noted, further investigate if the amounts appear to be due to timing, and/or consider asking the insurer for aging of amounts payable/receivable.	
h. Review the individual authorized reinsurers listed in Schedule S – Part 3 – Section 2. Are any of the reinsurers generally known to enter into significant retrocession agreements?	
i. If there are concerns that pyramiding exists, consider obtaining the annual financial statement of selected, large reinsurers and determine the extent to which the reinsurer cedes business to other reinsurers. Pay attention to declines in the overall quality level of reinsurers.	
j. If the insurer holds a material letter of credit (LOC) securing unauthorized reinsurance recoverables, identify the amount of the LOC and the issuing bank. If "yes," then provide the American Bankers Association rating of the bank and summarize any concerns.	

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Uninsured Plan Receivable**9. Review and assess the volume and collectability of amounts receivable relating to uninsured accident and health plans.**

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Compare the ratio of ASO/ASC claim payments to total hospital and medical expenses plus ASO/ASC claim payments [Annual Financial Statement, Notes to Financial Statements, Note #18, Part A and Part B]		>10%	[Data]	[Data]
b. Compare the ratio of reimbursements from uninsured plans to total expenses plus reimbursements from uninsured plans [Annual Financial Statement, Underwriting and Investment Exhibit – Part 3]		>25%	[Data]	[Data]
c. Ratio of receivables relating to uninsured plans to capital and surplus	LQ	>5%	[Data]	[Data]
d. Change in uninsured receivable relating to uninsured accident and health plans		>20% or <-20%	[Data]	[Data]
e. Non-admitted uninsured receivables relating to uninsured accident and health plans		>0	[Data]	[Data]
				<i>Other Risks</i>
f. Do concerns exist regarding the profitability of uninsured accident and health plans and the uninsured portion of partially insured plans for which the insurer serves as an Administrative Services Only (ASO) or an Administrative Services Contract (ASC) plan administrator? [Annual Financial Statement, Notes to Financial Statements, Note #18]	LQ			
g. Has the insurer reported ASO and/or ASC amounts in its Risk-Based Capital (RBC) filing (worksheet XR021) and not reported receivables or assets related to uninsured accident and health plans on its Annual Financial Statement or vice versa?				
h. Evaluate the adequacy of funds held for the plans' claims and expenses.				
i. Evaluate the financial condition of the uninsured plans.	LQ			
j. Does the analyst believe that the asset receivables relating to uninsured accident and health plans on page 2 of the Annual or Quarterly Financial Statement have been netted against the liability on page 3 for amounts held under uninsured accident and health plans? One indication that these amounts have been netted would be if there was an uninsured receivable relating to uninsured accident and health plans (Page 2, Column 3, Line 17) without a liability for amounts held under uninsured accident and health plans (Page 3, Column 3, Line 22) or vice versa.				
k. Have disclosures been made in the Notes to Financial Statements regarding the possible uncollectability of amounts receivable under uninsured plans?				

III.B.1.c. Credit Risk Repository – Health Annual

Uncollected Premium and Agents' Balances

10. Review and assess uncollected premiums and agents' balances for potential collectability issues.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Ratio of uncollected premiums and agents' balances to capital and surplus	LQ	>20%	[Data]	[Data]
b. Change in uncollected premiums and agents' balances from the prior year		>25% or <-25%	[Data]	[Data]
c. Ratio of uncollected premiums to net premium income	LQ	>5%	[Data]	[Data]
d. Amount due from any one group or subscriber as percent of the uncollected premiums	LQ	>=10%	[Data]	[Data]
e. Ratio of non-admitted uncollected premiums to total uncollected premiums	LQ	>10%	[Data]	[Data]
f. Review the net agents' balances and premium balances charged off and recovered compared to current year total uncollected agents' balances and premium balances		>5%	[Data]	[Data]
				<i>Other Risks</i>
g. Review amounts non-admitted and compare to prior years.				
h. With respect to agents' balances, verify the creditworthiness of the agent.				

Health Care Receivables

11. Review and assess health care receivables for potential collectability issues.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Ratio of health care receivables to capital and surplus	LQ	>5%	[Data]	[Data]
b. Amount due from any one debtor equal or exceed 10% of gross health care receivable		>10%	[Data]	[Data]
c. Change in health care receivables increased from the prior year	LQ	>20% or <-20%	[Data]	[Data]
d. Ratio of non-admitted health care receivables to admitted health care receivables	LQ	>10%	[Data]	[Data]
				<i>Other Risks</i>
e. Review amounts non-admitted and compare to prior years.				
f. Review capitation and other agreements with providers and hospitals and the level of receivables from these parties.				

III.B.1.c. Credit Risk Repository – Health Annual

Affiliated Receivable or Payable

12. Review the balance sheet asset receivable from parent, subsidiaries and affiliates, as well as the liability payable to parent, subsidiaries and affiliates to determine whether there are concerns with the level of affiliated receivables/payables.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Affiliated receivable or payable to capital and surplus	LQ, OP*	>10%	[Data]	[Data]
				<i>Other Risks</i>
b. If there are concerns regarding collectability of affiliated receivables, review the Annual Financial Statement, Schedule Y – Part 2, Notes to Financial Statements, Management’s Discussion and Analysis (MD&A), and other available information (e.g., Form D filings) for more information about the nature and timing of the receivable. <i>(Review the Operations Risk Repository for more procedures on affiliated transactions.)</i>				LQ, OP

Related Party Exposure in the Investment Portfolio

#13. Assess related party exposure in the investment portfolio.

	<i>Other Risks</i>
<p>a. Review the Annual Financial Statement investment schedules, as disclosed in the column “Investments Involving Related Parties” and utilizing iSite+ tools, determine if the insurer has material related party exposures in its investment portfolio.</p> <p>This disclosure is included in:</p> <ul style="list-style-type: none"> • Schedule B • Schedule BA • Schedule D • Schedule DA • Schedule DB • Schedule DL • Schedule E, Part 2 <p>Consider exposure by asset class and in aggregate, and by the role of the related party in the investment as designed by the “Investments Involving Related Parties” disclosure.</p>	LQ, MK
b. If concerns exist regarding a material related party exposure in the investment portfolio, assess the credit quality of those investments involving related parties by reviewing designations, assessing historical default experience, etc.	LQ, MK

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<p>c. If concerns exist regarding a material related party exposure in investment management or advisory services, consider the following:</p> <ol style="list-style-type: none"> i. Review the procedures in the “Additional Procedures” section below regarding Third Party Investment Advisors and consider their application to related party advisors in that role. ii. In addition to the additional analysis procedures regarding third party investment advisors, consider the following: <ol style="list-style-type: none"> 1. Review the insurer’s investment policy guidelines and determine whether the related party investments follow the guidelines and are in compliance with regulatory requirements. 2. Review whether the fee structure for asset management is fair, reasonable, and appropriately recognized as investment expenses. 3. If the related party asset manager also originates/securitizes investments held by the insurer, consider requesting additional information from the insurer to determine the following: <ol style="list-style-type: none"> a. Whether the asset manager has adequate experience and knowledge in originating and managing the types of investments; b. Whether the asset manager follows appropriate underwriting practices and applicable regulatory requirements in originating investments; and c. Whether the fee structures embedded in securities (if applicable) are fair, reasonable, and appropriately account for potential duplication of fees or conflicts of interest. 	<p>OP</p>
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Additional Analysis and Follow-up Procedures

Request and Assess the Insurer’s Investment Policies and Strategies:

If concerns exist regarding the level of credit exposure, request and review the insurer’s investment strategy to determine if it is appropriately structured to support its ongoing business plan. Review the guidelines outlined in the plan for:

- Quality of issues invested in and diversification standards pertaining to issuer, industry, duration, liquidity, and geographic location and issues/sectors exposed to material climate change, transition, and asset devaluation risks.
- Expected rate of returns on investments (projected investment income) compared to actual results.
- Planned increases in investment types, sectors, markets, etc.
- Appropriateness of the investment plan for the liability structure of the insurer. (This may require a review of asset adequacy analysis for asset liability matching (ALM) and discussion with the insurer’s management to better understand their plan.)

Upon review of the investment plan, compare the plan to actual results. Does the insurer and its investment manager(s) appear to be adhering to the investment policies and guidelines in the investment plan?

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Examination Findings:

Review the most recent examination report and Summary Review Memorandum (SRM) for any findings regarding credit risks associated with:

- Investment concentration.
- Exposure to riskier asset classes.
- Climate change, transition, and asset devaluation.
- Asset liability matching.
- Adherence to investment policies and strategies.
- Investment management and use of and monitoring of external investment managers.
- Proper classification (i.e., authorized, unauthorized, certified) and calculation of reinsurance collateral and provision.

If outstanding issues are identified, perform follow-up procedures as necessary to address concerns.

NAIC Capital Market's Bureau Analytical Assistance:

Consider requesting the following analytical reviews:

- Review of the insurer's investment portfolio.
- Review of Investment Management Agreements.

Third Party Investment Advisers:

Assess and determine if any concerns exist regarding third party investment advisers and associated contractual arrangements.

- Review Annual Financial Statement, General Interrogatories, Part 1, #29.05. Does the insurer utilize third party investment advisors, broker/dealer or individuals acting on behalf of the insurer with access to their investment accounts?

If "yes," consider the following procedures:

- Review the results of the most recent financial examination work papers, follow-up and prospective risk information and the summary review memorandum provided by the examiners. Did the examination identify any issues with regard to investment advisers and associated contractual arrangements that require follow-up analysis or communication with the insurer? If "yes," document the follow-up work performed.
- Compare Annual Financial Statement, General Interrogatories, Part 1, #29.05 for the current year to the prior year to determine if there have been any changes in advisors. If "yes,"
 - Consider obtaining an explanation for the change from the insurer.
 - Consider obtaining a copy of the new investment advisor agreement and review it for appropriate provisions.
- Using the information reported in Annual Financial Statement, General Interrogatories, Part 1, #29.05, obtain and review SEC Form ADV (if available), to determine if the investment advisor is in good standing with the SEC. If not in good standing, contact the insurer to request an explanation.
- If agreements with third party investment advisers are affiliated, have the appropriate Form D – Prior Notice of Transactions been filed and approved by the department? Were any concerns noted or follow-up monitoring recommended?
- Request information from the insurer regarding the background and expertise in structured securities of its investment advisors (in-house and/or contractual) and its analytical system capabilities. Determine

III.B.1.c. Credit Risk Repository – Health Annual

whether the advisors and systems are adequate to allow the insurer to continuously monitor its structured securities investments.

- If the insurer uses an external asset manager, consider if investments on Schedule BA are invested in funds that are affiliated with the asset manager or are managed by that asset manager. Consider the following issues:
 - If any conflicts of interest exist.
 - If the investment is appropriate for the insurer's portfolio and is arm's-length.
 - If the insurer is paying double fees.

Inquire of the Insurer:

If concerns exist, consider requesting information from the insurer regarding:

General Investment Inquiries:

- If management has adequately reviewed the investment portfolio and understands the yields, underlying collateral, cash flows and investment volatility.
- Any additional concentration by collateral type.
- Management's process for valuing securities so as to assist analysts in assessing if the securities are valued appropriately.
- Management's intended use of certain riskier investments and purpose within the insurer's portfolio.
- Credit risk associated with sector concentration.
- If management has an appropriate level of knowledge and expertise with the type of securities being purchased/held.
- If the insurer has controls implemented to mitigate the risks associated with this investment type.
- Sources of liquidity, such as LOCs.

Investment Diversification:

- Planned asset mix and diversification strategies.
- How the insurer manages counterparty credit risk, including diversification risk of counterparties.

Mortgages:

- Increases by adjustment in book value/recorded investment during the year.

BA Assets:

- Request information necessary to determine the fair value of collateral to the amount loaned to ensure the loan is adequately collateralized.
- Information to support significant increases by adjustment in book/adjusted carrying value during the year.
- Current Audited Financial Statements and other documents (partnership agreements, etc.) necessary to support the value of the insurer's investment in partnerships and joint ventures.
- Information necessary to support the value of significant other invested assets other than partnerships and joint ventures and limited liability companies.
- Current details on cash flows and returns for the different types of investments, especially hedge funds and private equity funds.

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Non-Investment Grade Bonds:

- Significant exposures.
- Policies and strategy for investing in non-investment grade bonds.

RMBS, CMBS and LBaSS:

- Percentage distribution and amounts of each type of RMBS, CMBS and LBaSS held; planned amortization class (PAC), support bonds, interest only (IO) tranches, and principle only (PO) tranches to evaluate the level of prepayment risk in the portfolio.
- Projected prepayment speeds on its RMBS portfolio and compare with historical prepayments, as well as the prepayment assumption at the time of purchase.

Reinsurance:

- Request a copy of the insurer's A.M. Best Supplemental Ratings Questionnaire and review the reinsurance section for unusual items.
- If concerns exist regarding the credit quality and financial solvency of an unauthorized reinsurer, request a copy of the reinsurance agreement(s), and confirm amounts included on Annual Financial Statement, Schedule S – Part 4.
- Aging of reinsurance amounts payable/receivable.

Uncollected Premium and Agents' Balances:

- Explanation for the significant balance.
- Listing of balances of subscribers, which individually account for 10% or more of the premiums uncollected and compare to a similar list from prior years.
- Amounts of any uncollectable balances that have been written off in the current period. Compare the write-offs to those of the prior reporting period, if any.
- Written procedures for monitoring and collecting uncollected premiums, including amounts already written off.
- If the insurer has factored or sold its uncollected premium balances to a third party, note whether the receivables were discounted in the transaction.
- If concerns over uncollected agents' balances warrant further investigation ensure that adequate controls are in place and that trust accounts are properly managed. An increase or trend of material non-admitted agents' balances or write-offs may be a sign of mismanagement or misappropriation of premium trust accounts by the agency. If there are concerns in this area, consider the following:
 - Request additional data/information from the insurer to identify the source(s) of the balances and the reason(s) for the non-admitted or charged-off amounts.
 - Request the insurer to provide a summary of the controls in place over agencies and ensure proper management and oversight of trust accounts.
 - Request monthly reports from the insurer.
- Discuss concerns with the exam team, including whether a targeted exam is necessary.

Uninsured Plans:

- Listing of plans administered by the insurer.
- Aging schedule of receivables related to uninsured plans.
- Amounts of any uncollectable receivables under uninsured plans that have been written off in the current period. Compare the write-offs to those of the prior reporting period, if any.

III.B.1.c. Credit Risk Repository – Health Annual

- Request a copy of the I.D. card used by members covered under ASO and ASC arrangements to determine potential exposure to financial risk and compliance penalties.

Health Care Receivables:

- Explanation for the significant balance.
- Listing of balances of debtors, which individually account for 10% or more of the balance of health care receivables and compare to a similar list from prior years.
- Amounts of any uncollectable balances that have been written off in the current period. Compare the write-offs to those of the prior reporting period, if any.
- Written procedures for monitoring and collecting uncollected premiums, including amounts already written off.
- Inquire whether the insurer has factored or sold its health care receivables to a third party. Note whether the receivables were discounted in the transaction.

Own Risk and Solvency Assessment (ORSA) Summary Report:

If the insurer is required to file ORSA or part of a group that is required to file ORSA:

- Did the ORSA Summary Report analysis conducted by the lead state indicate any credit risks that require further monitoring or follow-up?
- Did the ORSA Summary Report analysis conducted by the lead state indicate any mitigating strategies for existing or prospective credit risks?

Holding Company Analysis:

- Did the Holding Company analysis conducted by the lead state indicate any credit risks impacting the insurer that require further monitoring or follow-up?
- Did the Holding Company analysis conducted by the lead state indicate any mitigating strategies for existing or prospective credit risks impacting the insurer?

Actuarial Filings, Including Asset Liability Matching (ALM):

- Did the review of the Statement of Actuarial Opinion or other actuarial filings indicate any concerns regarding the adequacy of asset/liability matching and the sufficiency of assets to meet the business obligations of the insurer?
- If concerns are identified regarding overall liquidity of the asset portfolio, request a copy of the insurer's asset/liability matching policy and/or liquidity stress testing/scenario analysis.

Example Prospective Risk Considerations

Risk Components for IPS		Explanation of Risk Components
1	Significant concentration by [asset class, sector, issuer, etc.]	High exposure in any one asset class, industry sector or issuer could result in material credit losses if asset class, industry sector or issuer experiences an economic decline.
2	Borrower default risk for [mortgage loans, RMBS, CMBS or LBaSS securities, etc.]	Lower credit quality of the borrowers (i.e., prime versus subprime) may result in higher risk of default, leading to credit losses in the event of a housing and/or commercial real estate market downturn.
3	Prepayment variability in RMBS	Prepayment variability in RMBS could result in actual cash flows and investment yields to be materially different from expectations.

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4	Volatility of non-investment grade bonds	The market volatility of below investment-grade bonds makes the price at which bonds are held an important consideration.
5	Foreign security default	Material exposure to foreign investments could result in credit losses if those investments are impacted by negative changes in geopolitical or foreign economic environments.
6	Impairment of [bonds, etc.]	Risk of further deterioration in credit quality may result in other-than-temporary impairments impacting income and surplus.
7	Bondholder default	Investment-grade bonds that have declined to a non-investment grade status may not recover lost value.
8	Structured notes cash flow volatility risk	Impact of the volatility of structured notes and the underlying asset on which its cash flows are based.
9	Structured notes collateral concentration risk	Material investment in structured notes that may have collateral type concentration may result in concentration risk (lack of diversity) to the insurer's portfolio.
10	Structured notes default	Structured notes may be subordinated in the overall transaction representing exposure to non-payment in event of default.
11	Second lien mortgage loan risk	High exposure to second lien loans may result in an increase in risk of non-payment in the event of default as first lien loans are paid first from the value of the property.
12	Mortgage loan collateral inadequate	Out-of-date appraisals may result in inaccurate valuation, resulting in the underlying collateral asset not being adequate.
13	High risk mortgage loan valuation	The investments in high-risk mortgage loans are incorrectly valued.
14	Complexity of BA assets	BA assets often have complex investment strategies and unpredictable cash flows.
15	Adequacy of collateral of BA asset	Volatility of underlying assets (e.g., certain hedge funds and private equity funds) may result in underlying asset not adequate.
16	Economic impact on portfolio of [BA assets, derivatives, etc.]	Portfolio volatility driven by economic changes.
17	Hedge effectiveness of derivatives portfolio	Derivatives strategy may not meet hedge effectiveness for mitigating risk.
18	Investment strategy contemplate higher [credit, market, liquidity...] risk	The insurer's investment strategy may not be structured to support its ongoing business plan, which could indicate the strategy enjoys higher credit, market and liquidity risks than are appropriate for the liabilities of the insurer and may lead to financial concerns in the future.
19	Investment results actual to projected variance	The insurer's actual investment portfolio and/or portfolio performance may vary significantly from projections if the insurer is not adhering to the strategy in place (i.e., higher actual credit, market or liquidity risk compared to the plan).
20	Collectability of receivables for [insert name of receivable]	Payments of [insert name of receivable] may be delayed or not be paid when due, resulting in cash flow mismatch.
21	Credit quality of [reinsurer, agents, affiliate, etc.]	Credit quality and poor financial strength of a [reinsurer, agent, etc.] may result in future collectability risk, which may result in ongoing credit risk and future liquidity issues.

III.B.1.c. Credit Risk Repository – Health Annual

22	Exposure to climate change, transition, and asset devaluation risk	The insurer's investment portfolio is subject to prospective devaluation of the assets/changes in the asset return associated with its holdings of climate-affected assets.
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III.B.1.c. Credit Risk Repository – Health Quarterly

Credit Risk: Amounts actually collected or collectible are less than those contractually due or payments are not remitted on a timely basis.

Note: The repository is not an all-inclusive list of possible procedures. Therefore, risks identified for which no procedure is available should be analyzed by the state insurance department based on the nature and scope of the risk. Also, note that key insurance operations or lines of business, for example, may have related risks addressed in different repositories. Therefore, analysts may need to review other repositories in conjunction with credit risk. For example:

- Investment asset classes (Bonds, Mortgages, etc.) are also discussed in the Market and/or Liquidity Risk Repositories.
- Reinsurance is also discussed in the Operational and Strategic Risk Repositories.

Analysis Documentation: Results of credit risk analysis should be documented in Section III: Risk Assessment of the insurer.

Investment Portfolio Diversification

- Determine whether the insurer's investment portfolio appears to be adequately diversified to avoid any undue concentration of investments by type or issue.

<i>"a" through "h": Shown are as a percent of total net admitted assets (excluding separate accounts)</i>	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Preferred stocks		>3%	[Data]	[Data]
b. Non-investment grade bonds		>3.5%	[Data]	[Data]
c. Mortgage loans	MK*	>5%	[Data]	[Data]
d. Other invested assets (Schedule BA)	LQ*	>3%	[Data]	[Data]
e. Aggregate write-ins for invested assets	LQ	>3%	[Data]	[Data]
f. Investments in affiliates	LQ, MK*	>5%	[Data]	[Data]
g. Is the total book/adjusted carrying value net of collateral for derivative investments open as of current statement date greater than 10% of capital and surplus? [Quarterly Financial Statement, Schedule DB – Part D – Section 1]		>10%	[Data]	[Data]
i. If "yes," list the book/adjusted carrying value net of collateral			[Data]	
				<i>Other Risks</i>
h. Review the Percentage Distribution of Total Assets in the Quarterly Financial Profile Report for significant shifts in the mix of investments owned during the past five years.				MK

Changes in Asset Exposures

- Determine whether there are concerns due to the change in certain asset classes from the prior year-end.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>

III.B.1.c. Credit Risk Repository – Health Quarterly

a. Increase in non-investment grade bonds and non-investment grade short-term investments from prior year-end, where such investments are currently greater than 3.5% of capital and surplus	LQ	>15%	[Data]	[Data]
b. Increase in mortgage loans from prior year-end, where the ratio of total mortgage loans to capital and surplus is greater than 5%	LQ, MK*	>15%	[Data]	[Data]
c. Increase in BA assets from prior year-end, where the ratio of BA assets to capital and surplus is greater than 5%	LQ*, MK*	>10%	[Data]	[Data]
d. Increase in aggregate write-ins from prior year-end, where the ratio of aggregate write-ins to capital and surplus is greater than 2%	LQ	>20%	[Data]	[Data]
e. Increase in affiliated investments from prior year-end, where the ratio affiliated investments to capital and surplus is greater than 10%	LQ, MK*	>20%	[Data]	[Data]
				<i>Other Risks</i>
f. If level of non-investment grade bonds is high (i.e., greater than 3.5% of capital and surplus), review Schedule D – Part 1B and the Quarterly Financial Profile Report to assess and understand the composition of non-investment grade bonds: <ul style="list-style-type: none"> • Amount and/or percentage of bonds in each class 3, 4, 5 or 6. • Concentration by sector or issuer, including affiliates. • If bonds have been rated by a credit rating provider (CRP). 				

Reinsurance Recoverable or Payable

3. Determine whether amounts recoverable (both paid and unpaid losses on claims and reserve credits) or amounts receivable from reinsurers are significant and collectable.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Reinsurance amounts recoverable to capital and surplus	LQ	>10%	[Data]	[Data]
b. Change in reinsurance recoverables where recoverables are greater than 10% of capital and surplus		>10% or <-10% from the prior quarter OR >35% or <-35% from the prior year-end	[Data]	[Data]
c. Were any new reinsurers added since the prior quarter? [Quarterly Financial Statement, Schedule S]	ST*	YES if count >0	[Data]	[Data]

III.B.1.c. Credit Risk Repository – Health Quarterly

d. Did the insurer experience any material transactions requiring the filing of Disclosure of Material Transactions with the state of domicile, as required by the Model Act? [Quarterly Financial Statement, General Interrogatories, Part 1, #1.1]	LG*, ST*	=YES		
i. If “yes,” did the insurer fail to make the appropriate filing of a Disclosure of Material Transactions with the state of domicile? [Quarterly Financial Statement, General Interrogatories, Part 1, #1.2]	LG*, ST*	=YES		
				<i>Other Risks</i>
e. If the answer to 3.c. is “yes,” and concerns exist, consider the following procedures:				
i. Determine the current ratings of the new reinsurer from the major rating agencies, and investigate significant changes during the past 12 months.				
ii. Obtain and review the Annual Audited Financial Report, Financial Statements, Annual Actuarial Opinion and U.S. Securities and Exchange Commission (SEC) Filings (if applicable) of the reinsurer for additional insight regarding collectability and credit quality of the reinsurer.				
iii. Review information about the reinsurer available from industry analysts and benchmark capital adequacy with top performers and peer groups.				
iv. Contact the domiciliary state to determine whether any regulatory actions are pending against the reinsurer. Also, review iSite+ data on the reinsurer (i.e., financial statements, Regulatory Information Retrieval System [RIRS] and Global Receivership Information Database [GRID]).				

Affiliated Receivable or Payable

- 4. Review the balance sheet asset receivable from parent, subsidiaries and affiliates, as well as the liability payable to parent, subsidiaries and affiliates to determine whether there are concerns with the level of affiliated receivables/payables.**

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Affiliated receivable or payable to capital and surplus	LQ, OP	>10%	[Data]	[Data]
b. Change in affiliated receivable or payable, where it is greater than 10% of capital and surplus	LQ, OP	>25% or <-25% from the prior year-end	[Data]	[Data]
c. Change in federal and foreign income tax recoverables, where recoverables are greater than 3% of total assets (excluding separate accounts)	LQ, OP	>10% or <-10% from the prior quarter OR >20% or <-20% from	[Data]	[Data]

III.B.1.c. Credit Risk Repository – Health Quarterly

		the prior year-end		
				<i>Other Risks</i>
d. Are there any indications that significant or unusual transactions involve an affiliate or other related party?				
e. If there are concerns regarding collectability of affiliated receivables, review Notes to the Financial Statements and other available information (e.g., Form D filings) for more information about the nature and timing of the receivable. (Review the Operational Risk Repository for more procedures on affiliated transactions.)				LQ, OP

Receivables for Uninsured Plans, Uncollected Premium and Agents' Balances, Health Care

5. Review and assess amounts receivable relating to uninsured accident and health plans.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Change in receivables relating to uninsured plans from prior year-end	LQ	>10% or <-10%	[Data]	[Data]
b. Ratio of uncollected premiums and agents' balances to capital and surplus	LQ	>20%	[Data]	[Data]
c. Change in uncollected premiums and agents' balances from the prior year-end	LQ	>25% or <-25%	[Data]	[Data]
d. Change in non-admitted uncollected premiums from prior year-end	LQ	>25% or <-25%	[Data]	[Data]
e. Ratio of health care receivables to capital and surplus	LQ	>5%	[Data]	[Data]
f. Change in health care receivables from the prior year-end	LQ	>20% or <-20%	[Data]	[Data]
g. Change in non-admitted health care receivables	LQ	>25% or <-25%	[Data]	[Data]

Credit Risk Assessment

Credit Risk: Amounts actually collected or collectible are less than those contractually due or payments are not remitted on a timely basis.

The objective of Credit Risk Assessment analysis is focused primarily on exposure to credit risk of investments and reinsurance receivables. The following discussion of procedures provides suggested data, benchmarks and procedures analysts can consider in their review. In analyzing credit risk, analysts may analyze specific types of investments and receivables held by insurers. Analysts' risk-focused assessment of credit risk should take into consideration the following areas (but not be limited to):

- Concentrations of investments (i.e., diversification)
- Materiality of high-risk or low-quality investments
- Extensive use of reinsurance
- Credit quality of reinsurers
- Collectability of reinsurance receivables
- Collectability of other receivables
- Credit quality of affiliates
- Quality of collateral
- Strategies for mitigating credit risk (i.e., counterparty risk with derivatives and off-balance sheet transactions)
- Uncollected premium and agents' balances

Overview of Investments

Refer to IV.A. Supplemental Analysis Guidance – Financial Analysis and Reporting Considerations for general information and a primer on derivatives.

Discussion of Annual Procedures

Using the Repository

The credit risk repository is a list of possible quantitative and qualitative procedures, including specific data elements, benchmarks and procedures from which analysts may select to use in their review of credit risk. Analysts are not expected to respond to all procedures, data or benchmark results listed in the repository. Rather, analysts and supervisors should use their expertise, knowledge of the insurer and professional judgement to tailor the analysis to address the specific risks of the insurer and document completion of the analysis. The repository is not an all-inclusive list of possible procedures. Therefore, risks identified for which no procedure is available should be analyzed by the state insurance department based on the nature and scope of the risk.

In using procedures in the repository, analysts should review the results in conjunction with the Supervisory Plan and Insurer Profile Summary and the prior period analysis. Communication and/or coordination with other internal departments are a critical step in the overall Risk Assessment process and are a crucial consideration in the review of certain procedures in the repository.

Analysts should also consider the insurer's corporate governance which includes the assessment of the risk environment facing the insurer in order to identify current or prospective solvency risks, oversight provided by the board of directors and the effectiveness of management, including the code of conduct established by the board.

III.B.1.d. Credit Risk Repository – Analyst Reference Guide

The placement of the following data and procedures in the credit risk repository is based on “best fit.” Analysts should use their professional judgement in categorizing risks when documenting results of the analysis. Key insurance operations or lines of business, for example, may have related risks addressed in different repositories. Therefore, analysts may need to review other repositories in conjunction with credit risk.

ANALYSIS DOCUMENTATION: Results of credit risk analysis should be documented in Section III: Risk Assessment of the insurer. Documentation of the risk assessment analysis should be sufficiently robust to explain the risks and reflect the strengths and weaknesses of the insurer. Analysts are not expected to respond to procedures, data or benchmark results directly in the repository document.

Quantitative and Qualitative Data and Procedures

Investment Portfolio Diversification

<i>Property/Casualty #</i>	<i>Life/A&H/Fraternal #</i>	<i>Health #</i>
1	1	1

The procedure assists analysts in determining whether the insurer’s investment portfolio appears to be adequately diversified to avoid an undue concentration of investments by asset type, duration or issuer. The ratios of the various types of investments to total net admitted assets (excluding separate accounts) are a measure of the diversity of the insurer’s investment portfolio by type of investment. The results of these ratios may also provide some indication of the insurer’s liquidity. Ratios are included for most types of investments except for government and agency bonds and cash and short-term investments, which are generally very liquid and have low credit risk. In addition, the ratio of the investment in any one issuer to total net admitted assets (excluding separate accounts) is a measure of the diversity of the insurer’s investment portfolio by issuer.

ADDITIONAL REVIEW CONSIDERATIONS

- Review the Percentage Distribution of Assets in the Financial Profile Report for significant shifts in the mix of investments owned during the past five years. Analysts should compare the insurer’s distribution of invested assets to industry averages to determine significant deviations from the industry averages. The comparison should focus on an appropriate peer group based on insurer type and asset size.
- Review of the Annual Supplemental Investment Risks Interrogatories to determine whether the insurer’s investment portfolio is adequately diversified with the appropriate level of liquidity to meet cash flow requirements.
- Review the Legal Risk Repository to determine whether the insurer’s investment portfolio is in compliance with the investment limitations and diversification requirements per the state’s insurance laws.

Exposure to Non-Investment Grade Bonds

<i>Property/Casualty #</i>	<i>Life/A&H/Fraternal #</i>	<i>Health #</i>
2	2	2

The procedure assists analysts in determining whether concerns exist due to the level of investment in non-investment grade bonds. Bonds which have NAIC designations of 3, 4, 5 or 6 are considered non-investment grade bonds and represent a significantly higher credit or default risk to the insurer than do investments in investment-grade bonds. In addition, the prices of non-investment grade bonds are frequently more volatile than the prices of investment grade bonds. Analysts should distinguish between the different non-investment grade classes as the risks are materially different. Analysts should also pay attention to issuers that the rating agencies have on negative watch. Given the potential volatility in prices and that the main concern is risk of loss to capital, an important consideration is the price at which non-investment grade bonds are held. The NAIC has adopted the

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Investments in Medium and Lower Grade Obligations Model Regulation (#340). Model #340 establishes limitations on the concentration of non-investment grade bonds because of concerns that changes in economic conditions and other market variables could adversely affect insurers having a high concentration of these types of bonds.

ADDITIONAL REVIEW CONSIDERATIONS

- Review Annual Financial Statement, Schedule D – Part 1A – Section 1 and compare the insurer’s holdings of non-investment grade bonds to the limitations included in Model #340 by NAIC designation.
- For the more significant non-investment grade bonds, consider requesting from the insurer audited financial statements and a rating agency report for the issuer of the bonds to assess the issuer’s current financial position and ability to repay its debt.

Exposure to Mortgage - and/or Asset-Backed Securities

<i>Property/Casualty #</i>	<i>Life/A&H/Fraternal #</i>	<i>Health #</i>
3	3	3

The procedure assists analysts in determining whether concerns exist due to the level of investments in residential mortgage-backed securities (RMBS), commercial mortgage-backed securities (CMBS) and loan-backed and structured securities (LBaSS). Of the structured securities, RMBS can be among the most complex and volatile. RMBS convert a pool of mortgage loans into a series of securities that have expected maturities which vary significantly from the underlying pool as a result of slicing the pool into numerous tranches with different repayment characteristics. RMBS are often issued or backed by the U.S. government, and when they are, they carry very little credit risk. As a result, agency-backed RMBS have been designated category 1.

However, the credit rating does not consider the prepayment or interest rate risk inherent in the RMBS investment. If the underlying mortgage loans are repaid by the borrowers faster or slower than anticipated, the RMBS repayment streams will be affected and the expected durations will either contract or extend. Thus, the cash flows on these investments are much more unpredictable than those for more traditional bonds and the cash flows can be either more or less variable than for mortgage pass-through certificates. If the RMBS prepayments are significantly faster than anticipated, and the insurer had paid a large premium for the RMBS when it was acquired, the insurer could experience a significant loss on the investment even though the par value was received. In addition, cash flows on RMBS are harder to match with corresponding payments on policy liabilities which leads to the risk that prepayments may not be able to be reinvested in investments earning comparable yields in order to support the liability payment streams. When interest rates rise, prepayment will likely slow, meaning that investors will be unable to take advantage of the higher rates, and when interest rates decline, prepayments will rise, forcing investors to reinvest at the lower rates. This will affect the value of bonds in the secondary market.

ADDITIONAL REVIEW CONSIDERATIONS

- Review the RMBS, CMBS and LBaSS securities categories in Annual Financial Statement, Schedule D – Part 1 for bonds with a book/adjusted carrying value (BACV) significantly in excess of par value, which could result in a loss being realized if bond prepayments occur faster than anticipated. Analysts should also consider reviewing a listing of the effective yield on each of the insurer’s RMBS, CMBS and LBaSS securities. The effective yield on most debt securities is generally linked to its credit risk and duration. However, significant prepayment risk can also increase the effective yield.
- There are many different types of RMBS, each of which have different characteristics and inherent risks. Therefore, consider requesting information from the insurer regarding the amount of each type held (e.g., planned amortization class (PAC), support bonds, interest only (IO), and principal only (PO)) to help evaluate the riskiness of the portfolio. IO bonds are particularly volatile.
- Consider requesting information from the insurer regarding estimated prepayment speeds on its RMBS. Several standardized forms of calculating the rate of prepayments of a mortgage security exist in the market.

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Historically, the constant prepayment rate (CPR) and the standard prepayment model of the Bond Market Association (PSA curve) are simple methods used to measure prepayments. Numerous other methods have evolved. Analysts should consider further analysis in those instances that prepayment risk appears high.

- **FOR LIFE INSURERS:** Consider a review of the insurer's life risk-based capital (RBC) formula or its Statement of Actuarial Opinion. The life RBC formula includes a C-3 Interest Rate Risk Component that charges insurer's for securities that have not been cash flow tested. The insurer is charged 0.5 times the excess of the statement value over the value of the security if all of the collateral was immediately repaid. Alternatively, or in addition to this procedure, the Statement of Actuarial Opinion should be reviewed for comments regarding the modeling of the RMBS portfolio in the cash flow testing performed. Analysts might also consider having the RMBS modeled by an independent actuary as a part of an independent cash flow analysis.
- The rationale behind requesting information on these types of investments outlined in the repository is to provide analysts with some insight regarding the level of prepayment risk the insurer holds in its RMBS portfolio and the measurement and monitoring tools the insurer uses to manage this risk. Parts f and g ask the insurer to break down its RMBS portfolio by general definitional classes, each of which has its own relative level of prepayment and cash flow volatility risk. Individual insurers may use different measures and monitoring techniques. If an insurance company cannot supply this data with reasonable ease, analysts may want to look more closely at the management and monitoring systems in place for the RMBS portfolio.

Exposure to Mortgage Loans

<i>Property/Casualty #</i>	<i>Life/A&H/Fraternal #</i>	<i>Health #</i>
4	4	4

The procedure assists analysts in determining whether concerns exist due to the level or quality of investment in mortgage loans. Most states restrict mortgage loan investments to first liens on property, with some states allowing second liens in instances where the insurer also owns the first lien. Second liens are more risky because, in the event of default, the holder of the first lien would be repaid out of any proceeds from the sale of the underlying property prior to the holder of the second lien.

For mortgage loans with interest overdue or in process of foreclosure, analysts should consider reviewing the year of last appraisal of the underlying land and buildings to determine whether updated appraisals should be required. For both real estate and mortgage loans, analysts should utilize postal code and property type information along with the city and state location information in Schedules A and B to identify geographic concentrations and to identify differences in volatility based on the property type and geographic location.

ADDITIONAL REVIEW CONSIDERATIONS FOR LIFE INSURERS

- Review Annual Financial Statement, Schedule B – Part 1 to determine the amount of each type of mortgage loan owned. Commercial mortgages have historically been riskier investments than farm mortgages and residential mortgages.
- Compare the BACV of each loan to the value of the land and buildings mortgaged. Analysts should determine whether the mortgage loans are adequately collateralized and whether any of the mortgage loans are to officers, directors, or other affiliates of the insurer. Important considerations in this analysis are the adjusted loan-to-value and debt service coverage ratio for each property, which are used in the determination of the mortgage's CM category and are detailed in the RBC worksheet.

Exposure to Other Invested Assets (Schedule BA)

<i>Property/Casualty #</i>	<i>Life/A&H/Fraternal #</i>	<i>Health #</i>
5	5	5

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The procedure assists analysts in determining whether concerns exist due to the level of investment in other invested assets (Schedule BA). The types of investments included in Annual Financial Statement, Schedule BA include collateral loans, joint ventures and partnerships, oil and gas production and mineral rights. Joint ventures and partnerships typically involve real estate. These types of assets also tend to be fairly illiquid and may contain significant credit risk.

ADDITIONAL REVIEW CONSIDERATIONS

Review Schedule BA to determine the amount and types of other invested assets owned and to determine whether they are properly categorized as other invested assets. Significant categories within Schedule BA are hedge funds and private equity funds. These and other investments in Schedule BA are characterized by complex strategies, lack of transparency for expected yields and cash flows, as well as high management fees.

Exposure to Other Invested Assets (Schedule BA) – Value of Collateral Loans

<i>Property/Casualty #</i>	<i>Life/A&H/Fraternal #</i>	<i>Health #</i>
N/A	7	N/A

The procedure assists analysts in determining whether concerns exist due to the level of investment in collateral loans. Analysts should review Annual Financial Statement, Schedule BA and Schedule DA. In most states, collateral loans are required to be secured or collateralized by assets which have a value in excess of the amount of the loan and which are considered admitted assets for an insurer.

ADDITIONAL REVIEW CONSIDERATIONS

Compare the fair value of the collateral to the amount loaned to determine whether the loan is adequately collateralized. In those instances where the underlying collateral is comprised of securities, analysts might consider verifying the rate used to obtain the fair value of the securities by referencing the *Purposes and Procedures Manual of the NAIC Investment Analysis Office* (P&P Manual).

Invested Asset Exposure to Climate Change Risk

<i>Property/Casualty #</i>	<i>Life/A&H/Fraternal #</i>	<i>Health #</i>
6	6	6

The procedure assists analysts in identifying and assessing the potential exposure of the insurer's investment portfolio to the impact of material climate change and/or energy transition risks. Transition risks refer to stresses on certain investment holdings arising from the shifts in policy, consumer and business sentiment, or technologies associated with the changes necessary to limit climate change. A few examples of investment holdings and sectors generally subject to greater levels of transition risk include, oil/gas, transportation, heavy manufacturing, and agriculture. In assessing an insurer's exposure to these risks, the analyst is encouraged to review information disclosed by the insurer in its responses to the NAIC's Climate Risk Disclosure Survey, U.S. Securities and Exchange Commission (SEC) filings, and/or the Own Risk and Solvency Assessment (ORSA) Summary Report filings. In addition, the analyst is encouraged to review the results of basic scenario analysis conducted by the NAIC using insurers' Annual Statement filings (U.S. Insurance Industry Climate Affected Investment Analysis) to identify potential concentrations in exposure.

ADDITIONAL REVIEW CONSIDERATIONS

- Review the insurer's investment policies and strategies to assess whether material climate change, transition and asset devaluation risk considerations have been appropriately implemented into the company's investment processes.
- Review the most recent examination report and summary review memorandum (SRM) for any findings regarding climate change/energy transition risks.

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- If concerns exist, consider requesting information from the insurer regarding how the insurer manages its exposure to material climate change/energy transition risk, including how it identifies and estimates current and prospective exposures and the limits (if any) in place to avoid concentrations.

Reinsurance Recoverable and Reinsurer Credit Quality

<i>Property/Casualty #</i>	<i>Life/A&H/Fraternal #</i>	<i>Health #</i>
7, 8, 9, 10	8, 9, 10	6, 7

The procedure assists analysts in determining whether reinsurance recoverables and receivables are significant and if so, whether the amounts involved are collectable. Under a reinsurance contract, the primary insurer transfers or “cedes” to another insurer (the “reinsurer”) all or part of the financial risk of loss for claims incurred under insurance policies sold to the policyholder. Reinsurance does not modify in any way the obligation of the primary insurer to pay policyholder claims. Only after loss claims have been paid can the primary company seek reimbursement from a reinsurer for its share of paid losses. As a result, evaluating the collectability of the recoverables and receivables, as well as the overall credit-worthiness of the reinsurers, is a key concern. Evaluating the collectability of reinsurance recoverables and receivables requires an understanding of the specific facts and circumstances relating to each reinsurer. However, this evaluation is frequently oriented towards the type of reinsurer from whom the reinsurance was obtained.

Reinsurance is generally obtained from one of the following categories of insurers:

- Professional Reinsurers – The main business of professional reinsurers is assuming reinsurance from non-affiliated insurers. In general, the large and well-capitalized professional reinsurers will not pose a serious collectability concern.
- Reinsurance Departments of Primary Insurers – Many insurers assume reinsurance from non-affiliates, but also write significant business on a direct basis. These types of insurers may pose a larger collectability concern than professional reinsurers since the specialized reinsurance expertise may not be as strong.
- Alien Insurers – Reinsurers domiciled in another country may pose a significant collectability concern.

The fundamental issue involved with evaluating collectability is an assessment of the financial stability of the underlying reinsurers, and, if applicable, specific retrocessionaires involved throughout the chain of reinsurance. To evaluate the collectability of reinsurance recoverables, analysts should consider the need to collect as much financial information as possible about the reinsurers, including various regulatory and governmental filings, rating agency reports, and financial analyses available from industry analysts.

A final recoverability issue may involve the treatment of disputed amounts. Occasionally, a reinsurer will question whether an individual claim is covered under a reinsurance contract or may even attempt to nullify an entire treaty. A ceding insurer, depending on the individual facts, may or may not choose to continue to take credit for such disputed balances. The ceding insurer may not take credit for reinsurance recoverables in dispute with an affiliate.

FOR PROPERTY/CASUALTY (P/C) INSURERS: Another important accounting issue relates to the provision for reinsurance. Under statutory accounting practices, the insurer must establish a liability by a formula that considers:

- The amount of overdue reinsurance recoverable on paid losses due from authorized insurers and reciprocal jurisdictions, certified reinsurers or unauthorized reinsurers;
- Any collateral deficiency with respect to the amount of reinsurance recoverable on paid and unpaid losses due from certified reinsurers or unauthorized reinsurers.

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Affiliated Receivable or Payable

<i>Property/Casualty #</i>	<i>Life/A&H/Fraternal #</i>	<i>Health #</i>
10	11	11

The procedure directs analysts to consider if any affiliated transactions have exposed the insurer to significant collectability risk. For example, if the insurer is included in a consolidated federal income tax return and a significant asset for Federal Income Tax Recoverable is recorded on the financial statements of the insurer, analysts should closely review the financial statements of the parent to determine the parent's ability to repay the receivable. Structured settlements acquired from an affiliated life insurance company may also represent a collectability risk to the insurer. When the amounts of structured settlements are significant, analysts should review and understand the financial statements of the life insurance affiliate.

Other Receivables

<i>Property/Casualty #</i>	<i>Life/A&H/Fraternal #</i>	<i>Health #</i>
11, 12	N/A	8, 9, 10

The procedures assist analysts in reviewing receivable assets of an insurer that may have limited collectability.

Uncollected Premiums and Agents' Balances

The asset for uncollected premiums and agents' balances in the course of collection includes amounts receivable that have been billed, but have not yet been collected.

Agencies and brokers receive premium payments from insureds in a fiduciary capacity. Most states have laws that require the agent or producer to maintain trust accounts for the premiums they collect, which must be kept separate from their business operating funds. The premiums, net of commissions, are then remitted to the insurer or general agents from the accounts, leaving an audit trail.

Although agents are used by health entities, they are generally used more extensively with P/C insurers or even life insurers. Agents' balances are admitted to the extent that the assets conform to the requirements of *SSAP No. 6—Uncollected Premium Balances, Bills Receivable for Premiums, and Amounts due from Agents and Brokers*, which also requires that premiums owed by agents should be reported net of commissions and are non-admitted under a 90-day rule. Remaining amounts that are determined to be uncollectable must be written off. Generally, if a contract with an agent permits offsetting, amounts payable to an agent may be offset against a receivable from that agent. Agents' balances carry credit risk and can have a material impact on the net income and capital and surplus of an insurer if the balances are significant. Significant or growing balances can also lead to liquidity problems if the insurer is unable to convert the receivables into cash to be used to pay claims.

Irrespective of the type of business written, inadequate systems and controls over the collection process can lead to uncollectable premiums. Uncollected premium balances on non-government business that are over 90 days due are non-admitted under *SSAP No. 6*. On all business, an evaluation of any remaining asset balance is required to determine any impairment. Amounts deemed uncollectable are required to be written off against income in the period the determination is made. These accounting requirements are designed to limit the total impact that collectability issues can have on an insurer at a given point in time.

Despite the efforts to mitigate the impact of uncollected premiums and agents' balances, write-offs and non-admitted unpaid premium assets can still have a material impact on the net income and capital and surplus of an insurer. These issues can lead to liquidity problems if the insurer is unable to convert the receivable into cash to be used to pay claims. Analysts should monitor the level of this asset as well as the change in the balance to help identify potential collection problems that can ultimately lead to significant decreases in surplus.

A material amount of uncollected agents' balances warrants further investigation to ensure that adequate controls are in place and that trust accounts are properly managed. An increase or trend of material non-admitted

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balances or write-offs may be a sign of mismanagement or misappropriation of trust accounts by the agency and should be investigated. Although this could occur at any agency, the risk is greater at affiliated agencies for the following reasons:

- The same owner controls both sides of the transaction
- There is a lack of internal controls in relation to management overrides
- Affiliated agency balances are often more material to small or medium-sized insurers
- Affiliated agencies may not be subject to the same level of oversight as unaffiliated agencies
- In the event of financial stress to the insurer or the agency, there may be an inherent conflict of interest

If the analyst has concerns about the timely collection of agents' balances, the additional procedures related to premium trust accounts in the repository should be considered.

FOR HEALTH INSURERS: The collectability of amounts reported for uncollected premiums may also be impacted as a result of retroactive additions and deletions that are made subsequent to the date the group was invoiced. There may be a delay (sometimes several months) between the time that a large group adds a new covered employee or deletes an employee that is no longer covered and notice of the change is sent to the health entity. This length of the delay increases since the invoicing of the monthly premium is frequently in advance of the effective date of the coverage. This delay can result in the health entity reporting part of a monthly billing as more than 90 days overdue and ultimately collecting less than what was billed. SSAP No. 6 states that if an installment premium is over 90 days due, the amount over ninety days due plus all future installments that have been recorded on that policy shall be non-admitted. However, for group accident and health contracts, a non-admitted *de minimus* over ninety-day balance would not cause future installments (i.e., monthly billed premiums on group accident & health) that have been recorded on that policy to also be non-admitted. The *de minimus* over 90-day balance itself would be non-admitted and the entire current balance would be subject to a collectability analysis.

The balance for uncollected premium may also result from amounts due from the Centers for Medicare and Medicaid Services or other government plans. Although coverage periods on this type of business are usually the same as comprehensive group business, the payment cycle can be much different due to the longer settlement periods experienced under government contracts. However, collectability of balances associated with government plans is usually not an issue. Because of this, the 90-day rule that is applied to other receivables is not applicable to receivables from these types of government plans.

Uninsured Plan Receivable (for Health Insurers)

SSAP No. 47—*Uninsured Plans* defines uninsured accident and health plans, including HMO administered plans, as plans for which a health entity, as an administrator, performs administrative services such as claims processing for an at risk third party. Accordingly, the administrator does not issue an insurance policy. Two of the more common types of uninsured accident and health plans include an Administrative Services Only (ASO) plan or an Administrative Services Contract (ASC) plan.

Under uninsured plans, there is no underwriting risk to the health entity. The plan bears all of the-utilization risk, and there is no possibility of loss or liability to the administrator caused by claims incurred related to the plan. Although there is no underwriting risk on these types of plans, credit risk can still be an issue. Under these types of agreements, it is common for a receivable to be established for services performed by the health entity, and/or amounts due to the health entity for claims paid by the health entity on behalf of the uninsured plan. The credit risk varies on these types of plans because under an ASC plan, the health entity pays the claims directly from its own bank account, and would seek reimbursement at a later date. In contrast, under an ASO plan, the claims are paid from a bank account owned and funded directly by the uninsured plan sponsor, or are paid by the health entity but only after receiving funds to cover the amount paid. Combination plans may also be administered which contain elements of both an uninsured and an insured plan. If the funds held for disbursement under the uninsured plans are inadequate to meet disbursement needs, the insurer may advance funds to cover such disbursements.

As a result of such advances, the receivable should be recorded as an asset. Liabilities can also result from administering this type of business. This type of liability would result from funds of the uninsured plans being held

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by the health entity for making plan disbursements. Generally, the asset for the receivable and the liability for funds held should not be netted unless individual receivables and payments meet the requirements of *SSAP No. 64—Offsetting and Netting of Assets and Liabilities*.

Expense risk can also result from uninsured plans. This risk results primarily from the health entity incurring more expenses to administer the business than reimbursed from the uninsured plan. Analysts should use the information in Annual Financial Statement, Notes to Financial Statements, Note #18 — Uninsured Plans, to better assess the business risk to which the health entity is exposed under its uninsured plans. Refer to Section IV.B. Supplemental Analysis Guidance – Notes to Financial Statements, for guidance on reviewing Note #18.

Health Care Receivables (for Health Insurers)

Health care receivables can include pharmaceutical rebate receivables, claim overpayment receivables, loans and advances to providers, capitation arrangement receivables, risk-sharing receivables and government insured plan receivables. Similar to other assets in general, each of the above types of health care receivables is individually unique and can carry its own risks to the health entity. Some of them carry a higher degree of risk because of the use of estimates in establishing them. Others carry a low level of risk because the accounting requirements only allow the receivable to be established in certain circumstances. However, ultimately each of the health care receivables can present the same kind of financial risks as uncollected premiums. Like uncollected premiums, the collectability of health care receivables should be monitored by the health entity, as it could become a source of future problems if write-offs of uncollectable receivables become material.

Exposure to High-Deductible Policies (for P/C Insurers)

Large deductible programs for workers' compensation insurance marketplace create added risk. They can be complex arrangements and depend on the employer's fulfillment of its obligation to reimburse all claims within the deductible. If the employer is unable to fulfill that obligation, the financial consequences to the employer could be catastrophic, and the employer's inability to pay could have a cascading impact on the financial health of the insurer. In order to manage this risk successfully, insurers and state insurance regulators must have a clear understanding of the nature and size of the insurer's exposure. Additionally, they must ensure that there are adequate measures in place to limit and mitigate the risk of the employer's failure to pay and ensure injured workers will receive benefits in compliance with state law. For further information and guidance on high-deductible workers' compensation insurance, refer to the *2016 Workers' Compensation Large Deductible Study*.

The procedures assist analysts in gaining some basic understanding of the materiality of any reserve credit that has been recorded and is recoverable, as well as the materiality, aging and collateral held on any deductible recoverables and unpaid balances.

Investments Involving Related Parties

<i>Property/Casualty #</i>	<i>Life/A&H/Fraternal #</i>	<i>Health #</i>
13	12	12

This procedure assists analysts in determining related party exposure in the investment portfolio and assessing any related credit risk.

Related parties are entities that have common interests as a result of ownership, control, affiliation or by contract as defined in *SSAP No. 25—Affiliates and Other Related Parties* (SSAP No. 25). Refer to the *Insurance Holding Company System Model Act* (Model #440) and SSAP No. 25 for a broader definition of "affiliate," "related party" and "control".

Related party transactions are subject to abuse because reporting entities may be induced to enter transactions that may not reflect economic realities or may not be fair and reasonable to the reporting entity or its policyholders. As such, related party transactions require specialized accounting rules and increased regulatory scrutiny.

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The analyst should utilize the tools available in iSite+ to identify if the insurer has a material exposure to investments involving related parties, either on an asset category basis or in aggregate, and by the related party designation noted below. If a material exposure exists, further assessment of the [credit, market, liquidity] risk may be warranted. For example, what is the NAIC designation of investments involving related parties? Analysts may also consider the extent to which related parties are involved in securitizing or originating business for the insurer, and what differences may exist in how investments involving related parties are valued. If the role of the related party is that of a third-party advisor, factors to consider may include for example, the expertise of the related party advisor, any potential conflicts of interest, and if related parties are originating investments only for the insurer or also to the public, the latter being subject to SEC requirements. The analyst may consider utilizing suggested procedures in the “Additional Procedures” section of the repository on third-party advisors, if applicable.

Within the Annual Financial Statement investment Schedules B, BA, D, DA, DB, DL, and E (Part 2), all investments involving related parties must include disclosure to ensure full transparency. This disclosure is in the column “Investments Involving Related Parties”. It designates investments by the following roles:

1. Direct loan or direct investment (excluding securitizations) in a related party, for which the related party represents a direct credit exposure.
2. Securitization or similar investment vehicles such as mutual funds, limited partnerships and limited liability companies involving a relationship with a related party as sponsor, originator, manager, servicer, or other similar influential role and for which 50% or more of the underlying collateral represents investments in or direct credit exposure to related parties.
3. Securitization or similar investment vehicles such as mutual funds, limited partnerships and limited liability companies involving a relationship with a related party as sponsor, originator, manager, servicer or other similar influential role and for which less than 50% (including 0%) of the underlying collateral represents investments in or direct credit exposure to related parties.
4. Securitization or similar investment vehicles such as mutual funds, limited partnerships and limited liability companies in which the structure reflects an in-substance related party transaction but does not involve a relationship with a related party as sponsor, originator, manager, servicer or other similar influential role.
5. The investment is identified as related party, but the role of the related party represents a different arrangement than the options provided in choices 1-4.
6. The investment does not involve a related party.

Additional Analysis and Follow-Up Procedures

INVESTMENT STRATEGY directs analysts to consider requesting and reviewing a copy of the insurer’s formal adopted investment plan. This should be evaluated to determine if the plan appears to result in investments that are appropriate for the insurer, based on the types of business written and its liquidity and cash flow needs and to determine whether the insurer appears to be adhering to its plan. For example, the insurer’s plan for investing in non-investment grade bonds should be reviewed for guidelines for the quality of issues invested in and diversification standards pertaining to issuer, industry, duration, liquidity, and geographic location.

EXAMINATION FINDINGS direct analysts to consider a review of the recent examination report, summary review memorandum and communication with the examination staff to identify if any credit risk issues were discovered during the examination.

NAIC CAPITAL MARKETS BUREAU ANALYTICAL ASSISTANCE directs analysts to consider requesting the NAIC’s Capital Markets Bureau (CMB) to assist with investment portfolio or investment management agreement analysis. The CMB has different levels of analysis that can be arranged to assist the state.

THIRD-PARTY INVESTMENT ADVISORS assist analysts in determining whether concerns exist regarding the use of third-party investment advisers. As investments and investment strategies grow in complexity, insurers may

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consider the use of unaffiliated third-party investment advisers to manage their investment strategy. Investment advisers may operate independently or as part of an investment company. Investment advisers and companies are subject to regulation by the U.S. Securities and Exchange Commission (SEC) and/or by the states in which they operate, generally based on the size of their business. In certain situations, insurers may use a broker-dealer for investment advice. Broker-dealers are subject to regulation by the Financial Industry Regulatory Authority (FINRA). Regardless, most broker dealers and investment advisers will register with the SEC and annually update a Form ADV–Uniform Application for Investment Adviser Registration and Report Form by Exempt Reporting Advisers, which provides extensive information about the nature of the organization’s operations. To locate these forms, analysts can go to <https://adviserinfo.sec.gov> and perform a search based on the company name.

Key information provided on a Form ADV includes:

- a. Regulatory agencies and states in which the adviser/broker is registered
- b. Information about the advisory business including size of operations and types of customers (Item 5)
- c. Information about whether the company provides custodial services (Item 9)
- d. Information about disciplinary action and/or criminal records (Item 11)
- e. A report of the independent public accountant verifying compliance if the investment advisor also acts as a custodian

It is important to note that the information provided on Form ADV is self-reported and is subject to limited regulatory oversight. However, the information may be valuable to analysts in assessing the suitability and capability of investment advisers providing advisory services to insurers.

Analysts should consider any significant risks identified in the most recent risk-focused examination and whether any follow-up procedures were recommended by the examiner. The examiner may have performed steps to determine the following: whether the investment adviser is suitable for the role (including whether he/she is registered and in good standing with the SEC and/or state securities regulators); whether the investment advisory agreements contain appropriate provisions; whether the adviser is acting in accordance with the agreement; and whether management/board oversight of the investment adviser is sufficient for the relationships in place.

Analysts should determine if changes have occurred in the insurer’s use of investment advisers that may prospectively impact the insurer’s investment strategy and overall management of the investment portfolio. If changes have occurred analysts may consider asking the insurer for an explanation for the change in investment advisers and obtain a copy of the new adviser agreement to gain an understanding of the provisions including the advisor’s authority, specific reference to compliance with the insurer’s investment strategy and/or policy statements, as well as state investment laws; conflicts of interest; fiduciary responsibilities; fees; and the insurer’s review of the adviser’s performance. (Refer to the *Financial Condition Examiners Handbook* for further guidance.)

Analysts can determine if the investment advisor is in good standing with the SEC. The SEC does not officially use the term “good standing”; however, for this analysis, the term is used to mean a firm that is registered as an investment adviser with the SEC and does not report disciplinary actions or criminal records in Item 11 of the Form ADV.

If the insurer uses an external asset manager and if investments on Schedule BA assets are invested in funds that are affiliated with the asset manager or are managed by that asset manager, analysts should consider several possible issues that may result from this scenario. A possible concern may exist when the asset manager is also managing other funds in addition to managing assets for the insurer and then invests the insurer’s assets in those other funds that the asset manager manages. While those funds may be good investments, both in general and for the insurer, there are a few issues that may need to be considered. First is the potential for a conflict of interest if the asset manager is using the insurer’s available funds to provide seed money or fund the manager’s other funds. Second is if any concerns exist regarding the appropriateness of the fund for the insurer’s investment portfolio and if the transactions would be considered on an arm’s-length basis. Third is the understanding that the

III.B.1.d. Credit Risk Repository – Analyst Reference Guide

insurer may be paying double fees as the insurer would pay the asset manager a fee for the investment and then also pay a fee within the fund investment.

INQUIRE OF THE INSURER directs analysts to consider requesting additional information from the insurer if credit risk concerns exist in a specific area. The list provided are examples of types of information or explanations to be obtained that may assist in the analysis of credit risk for specific topics where concerns have been identified.

OWN RISK AND SOLVENCY ASSESSMENT (ORSA) directs analysts to obtain and review the latest ORSA Summary Report for the insurer or insurance group (if available) to assist in identifying, assessing and addressing risks faced by the insurer.

HOLDING COMPANY ANALYSIS directs analysts to obtain and review the holding company analysis work completed by the lead state to assist in identifying, assessing and addressing risks that could impact the insurer.

Example Prospective Risk Considerations

The table provides analysts with example risk components for use in the Risk Assessment and Insurer Profile Summary branded risk analysis section and a general description of the risk component. Note that the risks listed are only examples and do not represent a complete list of all risks available for the credit risk category.

Discussion of Quarterly Procedures

The Quarterly Credit Risk Repository procedures are designed to identify the following:

1. Whether the insurer's investment portfolio appears to be adequately diversified to avoid an undue concentration of investments by type or issue
2. Whether the insurer has a significant portion of its assets invested, or has significantly increased its holdings since the prior year-end, in certain types of investments that tend to be riskier
3. Exposure to and/or changes in risk related to reinsurance recoverables
4. Exposure to and/or changes in risks related to affiliated receivables
5. Exposure to and/or changes in risks related to uncollected premium and agents' balances and receivables relating to uninsured plans and health care

For additional guidance on individual procedure steps, please see the corresponding annual procedures discussed above.

III.B.2.a. Legal Risk Repository – Annual (All Statement Types)

Legal Risk: Non-conformance with laws, rules, regulations, prescribed practices or ethical standards in any jurisdiction in which the entity operates will result in a disruption in business and financial loss.

Note: The repository is not an all-inclusive list of possible procedures. Therefore, risks identified for which no procedure is available should be analyzed by the state insurance department based on the nature and scope of the risk. Also, note that key insurance operations or lines of business, for example, may have related risks addressed in different repositories. Therefore, the analyst may need to review other repositories in conjunction with legal risk. For example, market conduct is also addressed as a reputational risk.

Analysis Documentation: Results of legal risk analysis should be documented in Section III: Risk Assessment of the insurer.

Market Conduct

1. Determine if concerns exist regarding market conduct, including complaints, market conduct actions, communication with market conduct staff, etc. If concerns exist, communicate risks/issues to the state insurance department's Market Conduct Unit to investigate further.

	Other Risks	Benchmark	Result	Outside Benchmark
a. Review any market conduct information available from the NAIC market analysis tools and databases (MAP, MARS, MATS, RIRS, & MCAS). Note any unusual items or negative trends that translate into financial risks or indicate further review is needed.	RP*			
i. Count of Regulatory Actions: <ul style="list-style-type: none"> Current Year Prior Year Second Prior Year 			[Data]	
ii. Aggregate of Regulatory Fines: <ul style="list-style-type: none"> Current Year Prior Year Second Prior Year 			[Data]	
iii. Market Conduct Examination Called or Concluded: <ul style="list-style-type: none"> Current Year Prior Year Second Prior Year 		=YES	[Data]	[Data]
b. Average number of days of unpaid claims (<i>Health</i>)	LQ*, RP	>30 days	[Data]	[Data]
				Other Risks
c. Review any market conduct information, including information available from the state's market analysis department (such as the Market Analysis Chief or the Collaborative Action Designee). Note any unusual items that translate into financial risks or indicate further review is needed.				RP*
d. Review any inter-departmental communication, as well as communication with other state, federal or international insurance regulators and the insurer. Note any unusual items or prospective risks that indicate further analysis or follow-up is necessary.				RP*

III.B.2.a. Legal Risk Repository – Annual (All Statement Types)

e. If market conduct information is unusual and indicates potential financial risks, perform the following procedures:	RP*
<ul style="list-style-type: none"> i. Describe and document the findings of the most recent market conduct examination and analysis and communication with the insurance department's market conduct staff. ii. Describe any current or future actions of the insurance department, other state insurance departments or other regulatory bodies against the insurer related to market conduct violations. iii. Describe the actual or projected financial impact of any settlements, fines, or remediation to operations and surplus. 	
f. If concern is noted in 1.b., review the Financial Profile Report to identify changes in the average number of days of unpaid claims in past years for unusual fluctuations or negative trends between years.	
g. If concern is noted in 1.b. or 1.f., determine if the insurer has met state statutes and regulations regarding timely payment of claims.	

Litigation, Legal and Government Expenses

2. Determine if concerns exist regarding expenses for litigation, legal or government.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Investigate any individual payments for legal expenses that represent 25% or more of total legal payments made during the year [Annual Financial Statement, General Interrogatories, Part 1, #41.1 and #41.2]		=YES	[Data]	[Data]
b. Legal expenses of investigation and settlement of policy claims to total legal expenses (Life only) [Annual Financial Statement, Exhibit 2, Line 4.5]		>=75%	[Data]	[Data]
c. Investigate any individual payments for government expenditures in connection with matters before legislative bodies, officers or government departments that represent 25% or more of total legal payments made during the year [Annual Financial Statement, General Interrogatories, Part 1, #42.1 and #42.2]		=YES	[Data]	[Data]
				<i>Other Risks</i>
d. Compare legal expenses with industry averages (Note: Industry aggregate totals are available in the NAIC publication <i>Statistical Compilation of Annual Statement Information</i> .)				
e. Review Annual Financial Statement, Schedule P – Part 1 for Defense and Cost Containment Expenses, Notes to Financial Statements Note #23 for Reinsurance Recoverable in Dispute and Note #14G for Contingencies. Were any legal concerns identified based on this review?				
f. Were any legal concerns identified during the review of the Annual Financial Statement including the Notes to Financial Statements, Audited Financial Report, or Examination findings and follow-up monitoring?				

III.B.2.a. Legal Risk Repository – Annual (All Statement Types)

g. Upon review of the Notes to Financial Statements, was the insurer a party to any significant litigation not in the normal course of business? If so, review and understand a description of the litigation and any contingent liabilities for accrued legal expenses.	
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Fraud

3. Assess if any material fraudulent activity has been identified and evaluate the financial impact of such activity.

	<i>Other Risks</i>
a. Were any fraud concerns disclosed during the review of the Annual Financial Statement, including the Notes to Financial Statements, Audited Financial Statement, and Examination findings (i.e., Exhibit G)?	
b. Contact the state insurance department's Fraud Unit (if applicable). Has the state insurance department concluded any fraud investigations involving the insurer? If so, identify the following: <ul style="list-style-type: none"> • Nature and scope of the investigation and its findings • Regulatory and/or corrective actions required of the insurer • Insurer's plan to address the fraudulent activity • Financial impact of the investigation and corrective actions 	
c. Do any news and media reports, information from the insurer or other information available to the analyst indicate the insurer is under investigation by any regulatory body other than the state insurance department? If so, identify the nature and scope of the investigation and impact on the insurer to determine if further information should be requested from the other regulatory body.	RP
d. Review Regulatory Actions (Regulatory Information Retrieval System—RIRS) on iSite+. Were any regulatory actions taken by other states identified as fraud? If so, and if not communicated to the state insurance department, contact the reporting state insurance department to obtain information regarding the regulatory action.	
e. Contact other regulatory agencies that have regulatory authority over the business of the insurer (e.g., federal agencies where the insurer is engaged in government contracts). Have any regulatory authorities concluded any fraud investigations involving the insurer? If so, request the following information: <ul style="list-style-type: none"> • Nature and scope of the investigation and its findings • Regulatory and/or corrective actions required of the insurer • Insurer's plan to address fraudulent activity • Financial impact of the investigation and corrective actions 	RP
f. Review the GPS and any other information provided by the lead state for any legal risks of the group or the insurance entity (e.g., from the Form F - Enterprise Risk Report) . Were any investigations, regulatory activities or litigations that may impact the insurer or holding company reported?	
g. If the above analysis indicates concerns related to current or prior fraud, inquire of the insurer regarding its internal processes and controls for preventing fraud.	

III.B.2.a. Legal Risk Repository – Annual (All Statement Types)

Compliance with Code of Ethics Standards

4. Assess the insurer's compliance with code of ethics standards.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Identify if senior officers are subject to code of ethics standards [Annual Financial Statement, General Interrogatories, Part 1, #14.1 and #14.11]		=NO	[Data]	[Data]
b. Identify if the code of ethics has been amended [Annual Financial Statement, General Interrogatories, Part 1, #14.2 and #14.21]		=YES	[Data]	[Data]
c. Identify if the code of ethics has been waived [Annual Financial Statement, General Interrogatories, Part 1, #14.3 and #14.31]		=YES	[Data]	[Data]
				<i>Other Risks</i>
d. Determine if the responses provided in 4.a, 4.b, or 4.c identify any concerns with the insurer's compliance with code of ethics.				
e. Corporate Governance Annual Disclosure (CGAD): i. If filed on an insurance entity basis, does the information provided in the CGAD filing on ethics policies identify any concerns with the insurer's ethics standards or conflict with information reported in Annual Financial Statement, General Interrogatories, Part 1, #14? ii. If filed on a group basis, does the information provided in the GPS or provided by the lead state identify any concerns with the insurer's ethics standards or conflict with information reported in the Annual Financial Statement, General Interrogatories, Part 1, #14?				

Compliance with State Laws and Reporting

5. Assess the insurer's compliance with NAIC reporting practices, internal policy, laws, regulations and prescribed practices.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Identify if any certificates of authority, licenses or registrations have been suspended or revoked [Annual Financial Statement, General Interrogatories, Part 1, #6.1 and #6.2]		=YES	[Data]	[Data]
				<i>Other Risks</i>
b. Identify if the insurer is compliant with state statutes and regulations, including those that are new or revised (e.g., hazardous financial condition analysis, investment limitation analysis, etc.).				
c. Assess whether surplus meets the statutory minimum amount required by state law (varies by state and business type).				
d. Review the Annual Financial Statement, Notes to Financial Statements, Note #1 and the				

III.B.2.a. Legal Risk Repository – Annual (All Statement Types)

iSite+ Validation Exceptions tool. Has the insurer reported significant corrections of errors, validation errors, or other accounting and reporting changes that indicate possible concerns regarding the accuracy of the financial reporting?	
e. Is the insurer in compliance with permitted or prescribed practices as reported in Note #1?	
f. If the insurer failed to comply with the state’s statutes and regulations enacted during the period, identify the following: <ul style="list-style-type: none"> • Nature of the non-compliance • Impact to the insurer’s financial position and reporting • Outcome of any department communication with the insurer regarding the non-compliance issues • Resolution of any non-compliance issues or resolution plans of the insurer 	
g. If the insurer had any certificates of authority, licenses, or registrations (including corporate registration, if applicable) suspended or revoked by any governmental entity during the reporting period, identify the following: <ul style="list-style-type: none"> • Nature of the suspension or revocation • Reason(s) stated for the revocation or suspension • Outcome of any department communication with the insurer and/or with the other regulatory authority who issued the revocation or suspension • Resolution of any non-compliance issues or resolution plans of the insurer 	
h. If the insurer has been issued any consent orders or agreements by other regulators/jurisdiction, identify or perform the following: <ul style="list-style-type: none"> • Request a copy of the consent order or agreement from the other regulator/jurisdiction • Reason(s) stated for the consent order or agreement • Outcome of any department communication with the insurer and/or with the other regulatory authority • Resolution of any non-compliance issues or plans of the insurer 	

6. Assess the insurer’s compliance with the state’s investment laws.

	<i>Other Risks</i>
a. Using your state’s investment compliance checklist, determine whether the insurer’s investment portfolio is in compliance with the investment limitations and diversification requirements per the state’s insurance laws.	
b. Reporting its investments (including the related income and expenses) in accordance with NAIC practices, internal policy, Statutory Accounting Principles and the filing requirements set forth in the Purposes and Procedures Manual of the NAIC SVO.	
c. Are affiliated investments in violation of state statutes? If “yes,” gain an understanding of the primary business activity of the affiliate and why such an investment does not comply with regulatory requirements.	
d. If analysis of investment compliance indicates concerns or a pattern of non-compliance:	

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<ul style="list-style-type: none"> Review the most recent examination file for investment compliance Inquire of the insurer about its internal processes and controls for compliance with state investment laws 	
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7. Assess the insurer's compliance with affiliated management and service agreements.

	Other Risks
<p>a. Were management and service agreements between affiliates either submitted and/or approved in conformity with regulatory requirements? [Annual Financial Statement, Schedule Y – Part 2, Notes to Financial Statements, State's records of Form D Filings, etc.]</p> <p>i. Verify that the transactions recorded in the Annual Financial Statement reflect the transactions as approved.</p>	
<p>b. Was the amount of the shareholder dividend at a level that required prior regulatory approval or notification? If the response is "yes," did the insurer obtain proper prior regulatory approvals?</p>	

8. Assess the insurer's compliance with transactions involving other jurisdictions.

	Other Risks
<p>a. Did the insurer redomesticate to your state?</p> <p>i. If "yes," has the insurer failed to comply with any regulatory requirements or stipulations placed on the insurer that were expected to be met subsequent to approval of the redomestication?</p> <p>ii. Identify any legal implications that represent risk to the insurer due to the redomestication.</p>	
<p>b. Did the insurer engage in transaction(s) to redomesticate a subsidiary offshore?</p> <p>i. If "yes," has the insurer failed to comply with any regulatory requirements or stipulations placed on the insurer that were expected to be met subsequent to approval of the redomestication?</p> <p>ii. Identify any legal implications that represent risk to the insurer due to the redomestication.</p>	
<p>c. Did the insurer engage in any transactions to acquire a subsidiary domiciled in a non-U.S. jurisdiction?</p> <p>i. If "yes," has the insurer failed to comply with any regulatory requirements or stipulations expected to be met subsequent to the acquisition?</p> <p>ii. Identify any legal implications that represent risk to the insurer due to the acquisition.</p>	

Compliance with the Federal Affordable Care Act

9. Identify and assess compliance with the federal Affordable Care Act (ACA), Medical Loss Ratio (MLR), MLR Rebate calculations and other ACA requirements. If the insurer is not subject to the ACA, it is recommended to skip procedures #9 and #10.

III.B.2.a. Legal Risk Repository – Annual (All Statement Types)

				Other Risks
a.	Did the insurer file the Supplemental Health Care Exhibit (SHCE) and the SHCE Expense Allocation Report filed in accordance with the Annual Statement Instructions?			
b.	Review the Notes to the Financial Statement (primarily Note #24), the SHCE – Part 1, and the final rebate reporting to the U.S. Department of Health and Human Services (HHS). If the amount of MLR rebate liability reported is material (greater than 5% of capital and surplus), determine whether there are concerns regarding the insurer's liability for rebates.			ST*
c.	Compare the MLR rebate liability, as provided in the SHCE, and the actual rebate calculation in the HHS Medical Loss Ratio Reporting Form. Were any material differences identified? If so, consider requesting an explanation of the differences from the insurer.			
d.	During the review of the health care business pursuant to the federal Public Health Service Act and all applicable filings, did the analyst note any unusual items or areas of concern, not previously noted, that indicate further review is necessary?			
e.	If concerns exist, contact the federal Centers for Medicare & Medicaid Services (CMS) to request information about: <ul style="list-style-type: none"> • CMS sanctions or supervision by the CMS. • MLR audits. 			

10. Determine whether there are concerns regarding the components of the insurer's Preliminary Medical Loss Ratio (MLR).

	Other Risks	Benchmark	Result	Outside Benchmark
a. Review the Preliminary MLR from the SHCE by line of business (either the national Preliminary MLR or the state-level MLR) (or the thresholds applicable under state law) for individuals or small group employers with a ratio less than 80% or large group employers with a ratio less than 85%. For Medicare plans, is the preliminary MLR less than 85%? [See Reference Guide Discussion of these procedures for guidance on an aggregate vs. by state review of Preliminary MLR.]	PR/UW	<80% OR <85%	[Data]	[Data]
• Individual Comprehensive		<80%	[Data]	[Data]
• Small Group Employer Comprehensive		<80%	[Data]	[Data]
• Large Group Employer Comprehensive		<85%	[Data]	[Data]
• Individual Mini-Med		<80%	[Data]	[Data]
• Small Group Employer Mini-Med		<80%	[Data]	[Data]
• Large Group Employer Mini-Med		<85%	[Data]	[Data]
• Small Group Expatriate Plans		<80%	[Data]	[Data]
• Large Group Expatriate Plans		<85%	[Data]	[Data]
• Student Health Plans		<80%	[Data]	[Data]

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b. Review the change in Preliminary MLR for an increase or decrease of more than 5 percentage points from the prior year by line of business (either the national Preliminary MLR or the state-level MLR).	PR/UW			
• Individual Comprehensive		>5 pts or <-5 pts	[Data]	[Data]
• Small Group Employer Comprehensive		>5 pts or <-5 pts	[Data]	[Data]
• Large Group Employer Comprehensive		>5 pts or <-5 pts	[Data]	[Data]
• Individual Mini-Med		>5 pts or <-5 pts	[Data]	[Data]
• Small Group Employer Mini-Med		>5 pts or <-5 pts	[Data]	[Data]
• Large Group Employer Mini-Med		>5 pts or <-5 pts	[Data]	[Data]
• Small Group Expatriate Plans		>5 pts or <-5 pts	[Data]	[Data]
• Large Group Expatriate Plans		>5 pts or <-5 pts	[Data]	[Data]
• Student Health Plans		>5 pts or <-5 pts	[Data]	[Data]
c. In the analyst's review of the components of the Preliminary MLR, review and assess any material differences between the unadjusted and adjusted amounts for premium and claims. Compare Health Premium Earned (Line 1.1) to Adjusted Premium Earned (Line 1.8) by line of business.	PR/UW			
• Individual Comprehensive			[Data]	
• Small Group Employer Comprehensive			[Data]	
• Large Group Employer Comprehensive			[Data]	
• Individual Mini-Med			[Data]	
• Small Group Employer Mini-Med			[Data]	
• Large Group Employer Mini-Med			[Data]	
• Small Group Expatriate Plans			[Data]	
• Large Group Expatriate Plans			[Data]	
• Student Health Plans			[Data]	
d. In the analyst's review of the components of the Preliminary MLR, review and assess any material differences between the unadjusted and adjusted amounts for premium and claims. Compare Incurred Claims excluding prescription drugs (Line 2.1) to Total Incurred Claims (Line 5.0) by line of business.	PR/UW			

III.B.2.a. Legal Risk Repository – Annual (All Statement Types)

• Individual Comprehensive			[Data]	
• Small Group Employer Comprehensive			[Data]	
• Large Group Employer Comprehensive			[Data]	
• Individual Mini-Med			[Data]	
• Small Group Employer Mini-Med			[Data]	
• Large Group Employer Mini-Med			[Data]	
• Small Group Expatriate Plans			[Data]	
• Large Group Expatriate Plans			[Data]	
• Student Health Plans			[Data]	
				<i>Other Risks</i>
e. Did the analyst note any components that appear unusual, or that increased or decreased materially from the prior year that would indicate further review is warranted? If so, request additional information from the insurer.				PR/UW
f. Review the SHCE – Part 3 and the Expense Allocation Report including the expense allocation methodology to determine whether quality improvement (QI) expenses are appropriate and properly accounted for.				
g. During the review of the health care business pursuant to the Public Health Service Act and all applicable filings, did the analyst note any unusual items or areas of concern, not previously noted, that indicate further review is warranted?				PR/UW
h. If there are concerns, contact the CMS to request information on: <ul style="list-style-type: none"> • CMS sanctions and remediation • CMS supervision and any regulatory concerns of CMS • MLR audits 				

Legal Compliance with Federal Regulatory Agencies

11. Identify and assess compliance with other federal regulatory agencies.

	<i>Other Risks</i>
a. Is the insurer subject to regulation by a federal regulatory agency? [Annual Financial Statement, General Interrogatories, Part 1, #8]	
b. If “yes,” consider contacting the applicable federal regulatory agency to request any information about the results of that agency’s oversight, including any issues identified, federal compliance violations, fraud investigations and regulatory actions.	

III.B.2.a. Legal Risk Repository – Annual (All Statement Types)

Management’s Discussion and Analysis Report**12. Assess the insurer’s compliance with the Management’s Discussion and Analysis (MD&A) Report requirements and identify any legal risks through review of the report.**

	<i>Other Risks</i>
a. Utilizing the Handbook’s MD&A Report Work Paper or other state-specific procedures, was the MD&A filed in accordance with the Annual Financial Statement Instructions to include the required content?	
b. Were any compliance issues or legal risks noted based on review of the MD&A?	

Audited Financial Report**13. Assess the insurer’s compliance with the Audited Financial Report requirements and identify any legal risks through review of the Audited Financial Report. (June 1st Filing Date)**

	<i>Other Risks</i>
a. <i>Part I – Audited Financial Report:</i> Using the Handbook’s Audited Financial Report Work Paper or other state-specific procedures, were any compliance issues or legal risks noted based on review of: <ul style="list-style-type: none"> • Compliance with Audited Financial Report requirements • Review of the Report and identification of risks <ul style="list-style-type: none"> ○ Type of Opinion ○ Differences Identified in the Opinion • Certified Public Accountant’s (CPA) Letter of Qualifications (if applicable) • Changes in the CPA (if applicable) 	
b. If material risks are noted, what corrective actions are planned to resolve the issues?	
c. <i>Part II – Management’s Report on Internal Controls over Financial Reporting:</i> Using the Handbook’s Audited Financial Report Work Paper or other state-specific procedures, were any compliance issues or legal risks noted based on review of Management’s Report on Internal Controls over Financial Reporting?	
d. If material weaknesses in internal controls are reported, what corrective actions are planned to resolve the issues?	

Audit Committee

Every insurer is required to have designated an Audit Committee, a percentage of whose members should be independent from the insurer depending upon premium volumes.

14. Assess compliance with audit committee requirements.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Did the insurer fail to establish an Audit Committee in compliance with the domiciliary state insurance laws? If “yes,” review information for an explanation. [Annual Financial Statement, General Interrogatories, Part 1, #10.5 and #10.6]		=YES	[Data]	[Data]

III.B.2.a. Legal Risk Repository – Annual (All Statement Types)

b. Has the insurer been granted any exemptions under Sections 7H, or 18A of the NAIC <i>Annual Financial Reporting Model Regulation</i> ? If “yes,” review information about the exemption. [Annual Financial Statement, General Interrogatories, Part 1, #10.1, #10.2, #10.3 and #10.4]		=YES	[Data]	[Data]
				<i>Other Risks</i>
c. Does the Audit Committee membership meet independence requirements of the domiciliary state insurance laws?				
d. Corporate Governance Annual Disclosure (CGAD):				
i. If filed on an insurance entity basis, does the information provided in the CGAD on auditor independence identify any concerns or conflict with information reported in the Annual Financial Statement, General Interrogatories, Part 1, #10?				
ii. If filed on a group basis, does the information provided in the GPS or provided by the lead state identify any auditor independence concerns or conflict with information reported in the Annual Financial Statement General Interrogatories, Part 1, #10?				

Additional Analysis and Follow-Up Procedures

Examination Findings:

Review the most recent examination report and the Summary Review Memorandum (SRM) for any findings regarding legal risks. If outstanding issues are identified, perform follow-up procedures as necessary to address concerns.

Inquire of the Insurer:

If concerns exist, consider requesting information from the insurer regarding:

Policies and Strategies for Compliance with State, Federal and International Laws and Regulations:

- Information on how the legal/compliance function ensures compliance with relevant laws and regulations

News, Press Releases and Industry Reports:

- The financial impact of any legal issues on the insurer and/or group’s operations and surplus
- Disclosures of financial impact to the public and agent distribution force
- The insurer’s efforts to mitigate any impact of the risk. For ORSA filers, this may be identified in the ORSA Summary Report for certain risks.
- Policies and procedures in place to mitigate adverse publicity
- Revised business plan

Legal Risk Assessment by Management:

- How the insurer assesses its legal risk and reports it to senior management
- The involvement of legal counsel in changes to existing products and development of new products
- The degree to which compliance programs are utilized to control, monitor and report legal risk

Litigation:

- Negative financial impact on the insurer and/or group should the litigation not be ruled in favor of the insurer

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- Negative reputational impact to the insurer and/or group
- Negative impact to shareholders and/or policyholders

Audited Financial Report:

- Letter of Representation
- Schedule of all recorded and unrecorded audit adjustments
- Internal control related presentation materials including Management’s Comment Letter
- Any other audit work papers deemed appropriate or necessary (i.e., Statement of Auditing Standards (SAS) 99 Fraud and Legal Representations Letters)

Report on Internal Controls:

- If weaknesses are noted and no corrective action plan is proposed, contact the insurer and request detailed information regarding the insurer’s remediation and corrective action plan to resolve the weaknesses.

Own Risk and Solvency Assessment (ORSA) Summary Report:

If the insurer is required to file ORSA or part of a group that is required to file ORSA:

- Did the ORSA Summary Report analysis conducted by the lead state indicate any legal risks that require further monitoring or follow-up?
- Did the ORSA Summary Report analysis conducted by the lead state indicate any mitigating strategies for existing or prospective legal risks?

Holding Company Analysis:

- Did the Holding Company analysis conducted by the lead state indicate any legal risks impacting the insurer that require further monitoring or follow-up?
- Did the Holding Company analysis conducted by the lead state indicate any mitigating strategies for existing or prospective legal risks impacting the insurer?

Example Prospective Risk Considerations

Risk Components for IPS		Explanation of Risk Components
1	Market conduct examination/material findings	If a market conduct exam is being conducted or recently concluded, the reasons for calling the exam or the findings from the exam are material issues the insurer will need to correct.
2	Impact of ongoing market conduct remediation	If a recently concluded market conduct examination resulted in regulatory requirement to perform remediation (E.g., reprocessing denied claims) the financial impact may be material to the insurer.
3	Claims payment timeliness issues	The insurer is in violation of claims payment timeliness requirements under state law.
4	Material pending litigation	The insurer has reported material litigation pending, the impact of which is uncertain.
5	High legal expenses due to ...	The insurer has reported high legal, litigation or government expenses that are material to overall operating expenses.
6	Compliance violation for ...	The insurer is in violation of compliance with any state laws, regulations, filing requirements or other requirements of the state

III.B.2.a. Legal Risk Repository – Annual (All Statement Types)

		insurance department. The analyst should specify the violation and the impact.
7	Violation of federal [or other jurisdiction] laws and requirements for ...	The insurer is in violation of compliance with any federal, international or other states' laws.
8	Regulatory findings/actions taken by [specify the other regulatory authority]	Material findings or actions have been taken against the insurer by another regulatory authority, such as federal agencies (CMS, U.S. Securities and Exchange Commission [SEC], etc.).
9	Material fraud investigation results in ...	State's fraud investigation results in material findings against the insurer, its management or board of directors.
10	[None exist or concerns over] ethical standards required of senior management	Concerns exist if the senior management is not required to comply with ethical standards or if senior management is found not to be in compliance with those standards.
11	Audit report is [type other than unmodified]	The type of audit report was modified (qualified, adverse or disclaimer) for reasons stated in the report or includes an emphasis of matter paragraph that raises potential concerns (i.e., going concern issue).
12	Audit report [material differences or material audit adjustments]	The audit report identified material differences to the filed Annual Financial Statement and/or resulted in material audit adjustments that will be made to the current or next financial filing.
13	Material internal control weaknesses [and impact of corrective action plan]	Material weaknesses in internal controls are noted in the Management's Report of Internal Controls Over Financial Reporting. This also may include the financial impact of any corrective actions the insurer is undertaking to correct the weakness.
14	Failure to comply with audit committee requirements	If the insurer failed to establish an audit committee in compliance with state laws.

III.B.2.a. Legal Risk Repository – Quarterly (All Statement Types)

Legal Risk: Non-conformance with laws, rules, regulations, prescribed practices or ethical standards in any jurisdiction in which the entity operates will result in a disruption in business and financial loss.

Note: The repository is not an all-inclusive list of possible procedures. Therefore, risks identified for which no procedure is available should be analyzed by the state insurance department based on the nature and scope of the risk. Also, note that key insurance operations or lines of business, for example, may have related risks addressed in different repositories. Therefore, the analyst may need to review other repositories in conjunction with legal risk. For example, market conduct is also addressed as a reputation risk.

Analysis Documentation: Results of legal risk analysis should be documented in Section III: Risk Assessment of the insurer.

Market Conduct

- Determine if concerns exist regarding Market Conduct, including complaints, market conduct actions, communication with market conduct staff, etc. If concerns exist, communicate risks/issues to the state insurance department's Market Conduct Unit to investigate further.**

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Review any market conduct information available from the NAIC market analysis tools and databases (MAP, MARS, MATS, RIRS, & MCAS). Note any unusual items or negative trends that translate into financial risks or indicate further review is needed.	RP*			
i. Count of Regulatory Actions <ul style="list-style-type: none"> Current Year-to-Date Prior Year-to-Date Second Prior Year-to-Date 			[Data]	
ii. Aggregate of Regulatory Fines <ul style="list-style-type: none"> Current Year-to-Date Prior Year-to-Date Second Prior Year-to-Date 			[Data]	
iii. Market Conduct Examination Called or Concluded <ul style="list-style-type: none"> Current Year Prior Year Second Prior Year 		=YES	[Data]	[Data]
				<i>Other Risks</i>
b. Review any market conduct information, including information available from the state's market analysis department (such as the Market Analysis Chief or the Collaborative Action Designee). Note any unusual items that translate into financial risks or indicate further review is needed.				RP*
c. Review any inter-departmental communication, as well as communication with other state, federal or international insurance regulators and the insurer. Note any unusual items or prospective risks that indicate further analysis or follow-up is necessary.				RP*

III.B.2.a. Legal Risk Repository – Quarterly (All Statement Types)

d. If market conduct information is unusual and indicates potential financial risks, perform the following procedures: <ul style="list-style-type: none"> i. Describe and document the findings of the most recent market conduct examination and analysis and communication with the insurance department's market conduct staff. ii. Describe any current or future actions of the insurance department, other state insurance departments or other regulatory bodies against the insurer related to market conduct violations. iii. Describe the actual or projected financial impact of any settlements, fines, or remediation to operations and surplus. 	RP*
e. Determine if the insurer has met state statutes and regulations regarding timely payment of claims.	

Litigation, Legal and Government Expenses**2. Determine if concerns exist regarding expenses for litigation, legal or government.**

	<i>Other Risks</i>
a. Were any legal concerns identified during the review of the Quarterly Financial Statement including the Notes to Financial Statements, or Examination findings and follow-up monitoring?	
b. Upon review of the Notes to Financial Statements, was the insurer a party to any significant litigation not in the normal course of business? If so, review and understand a description of the litigation and any contingent liabilities for accrued legal expenses.	

Fraud**3. Assess if any material fraudulent activity has been identified and evaluate the financial impact of such activity.**

	<i>Other Risks</i>
a. Were any fraud concerns disclosed during the review of the Quarterly Financial Statement, including the Notes to Financial Statements, Examination findings (i.e., Exhibit G – Consideration of Fraud)?	
b. Contact the state insurance department's Fraud Unit (if applicable). Has the state insurance department concluded any fraud investigations involving the insurer? If so, identify the following: <ul style="list-style-type: none"> • Nature and scope of the investigation and its findings • Regulatory and/or corrective actions required of the insurer • Insurer's plan to address the fraudulent activity • Financial impact of the investigation and corrective actions 	
c. Do any news and media reports, information from the insurer or other information available to the analyst indicate the insurer is under investigation by a regulatory body other than the state insurance department? If so, identify the nature and scope of the	

III.B.2.a. Legal Risk Repository – Quarterly (All Statement Types)

investigation and impact on the insurer to determine if further information should be requested from the other regulatory body.	
d. Review Regulatory Actions (Regulatory Information Retrieval System—RIRS) on iSite+. Were any regulatory actions taken by other states identified as fraud? If so, and if not communicated to the state insurance department, contact the reporting state insurance department to obtain information regarding the regulatory action.	
e. Contact other regulatory agencies that have regulatory authority over business of the insurer (e.g., federal agencies where the insurer is engaged in government contracts). Have any regulatory authorities concluded any fraud investigations involving the insurer? If so, request the following information: <ul style="list-style-type: none"> • Nature and scope of the investigation and its findings • Regulatory and/or corrective actions required of the insurer • Insurer’s plan to address fraudulent activity • Financial impact of the investigation and corrective actions 	RP*
f. If the above analysis indicates concerns related to current or prior fraud, inquire of the insurer regarding its internal processes and controls for preventing fraud.	

Compliance with Code of Ethics Standards

4. Assess the insurer’s compliance with code of ethics standards.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Identify if senior officers are subject to code of ethics standards. [Quarterly Financial Statement, General Interrogatories, Part 1, #9.1]		=NO	[Data]	[Data]
b. Identify if the code of ethics has been amended. [Quarterly Financial Statement, General Interrogatories, Part 1, #9.2]		=YES	[Data]	[Data]
c. Identify if the code of ethics has been waived. [Quarterly Financial Statement, General Interrogatories, Part 1, #9.3]		=YES	[Data]	[Data]
				<i>Other Risks</i>
d. Determine if the responses provided in 4.a, 4.b, or 4.c identify any concerns with the insurer’s compliance with the code of ethics.				
e. Corporate Governance Annual Disclosure (CGAD): <ul style="list-style-type: none"> i. If filed on an insurance entity basis, does the information provided in the CGAD filing on ethics policies identify any concerns with the insurer’s ethics standards or conflict with information reported in General Interrogatory #9? ii. If filed on a group basis, does the information provided in the GPS or provided by the lead state indent any concerns with the insurer’s ethics standards or conflict with information reported in the Annual Financial Statement, General Interrogatories, #9? 				

III.B.2.a. Legal Risk Repository – Quarterly (All Statement Types)

Compliance with State Laws and Reporting

5. Assess the insurer's compliance with NAIC reporting practices, internal policy, laws, regulations and prescribed practices.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Identify if any certificates of authority, licenses or registrations have been suspended or revoked. [Quarterly Financial Statement, General Interrogatories, Part 1, #7.1 and #7.2]		=YES	[Data]	[Data]
				<i>Other Risks</i>
b. Identify if the insurer is compliant with state statutes and regulations, including those that are new or revised. (e.g., hazardous financial condition analysis, investment limitation analysis, etc.)				
c. Assess whether surplus meets the statutory minimum amount required by state law (varies by state and business type).				
d. Review the Quarterly Financial Statement, Notes to Financial Statements, Note #1 and the iSite+ Validation tool. Has the insurer reported significant corrections of errors, validation errors, or other accounting and reporting changes that indicate possible concerns regarding the accuracy of the financial reporting?				
e. Is the insurer in compliance with permitted or prescribed practices? [Quarterly Financial Statement, Notes to Financial Statements, Note #1]				
f. If the insurer failed to comply with the state's statutes and regulations enacted during the period, identify the following: <ul style="list-style-type: none"> • Nature of the non-compliance • Impact to the insurer's financial position and reporting • Outcome of any department communication with the insurer regarding the non-compliance issues • Resolution of any non-compliance issues or resolution plans of the insurer 				
g. If the insurer had any certificates of authority, licenses, or registrations (including corporate registration, if applicable) suspended or revoked by any governmental entity during the reporting period, identify the following: <ul style="list-style-type: none"> • Nature of the suspension or revocation • Reason(s) stated for the revocation or suspension • Outcome of any department communication with the insurer and/or with the other regulatory authority who issued the revocation or suspension • Resolution of any non-compliance issues or resolution plans of the insurer 				
h. If the insurer been issued any consent orders or agreements by other regulators/jurisdiction, identify or perform the following: <ul style="list-style-type: none"> • Request a copy of the consent order or agreement from the other regulator/jurisdiction 				

III.B.2.a. Legal Risk Repository – Quarterly (All Statement Types)

<ul style="list-style-type: none"> Reason(s) stated for the consent order or agreement Outcome of any department communication with the insurer and/or with the other regulatory authority Resolution of any non-compliance issues or resolution plans of the insurer 	
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6. Assess the insurer's compliance with the state's investment laws.

	<i>Other Risks</i>
a. Using your state's investment compliance checklist, determine whether the insurer's investment portfolio is in compliance with the investment limitations and diversification requirements per the state's insurance laws.	
b. Reporting its investments (including the related income and expenses) in accordance with NAIC practices, internal policy, Statutory Accounting Principles and the filing requirements set forth in the Purposes and Procedures Manual of the NAIC SVO.	
c. Are affiliated investments in violation of state statutes? If "yes," gain an understanding of the primary business activity of the affiliate and why such an investment does not comply with regulatory requirements.	
d. If analysis of investment compliance indicates concerns or pattern of non-compliance: <ul style="list-style-type: none"> Review the most recent examination file for investment compliance Inquire of the insurer about its internal processes and controls for compliance with state investment laws 	

7. Assess the insurer's compliance with affiliated management and service agreements.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Did the insurer experience any material transactions requiring the filing of Disclosure of Material Transactions with the state of domicile as required by the Model Act? [Quarterly Financial Statement, General Interrogatories, Part 1, #1.1]	CR*, ST*	=YES		[Data]
i. If "yes," did the insurer fail to make the appropriate filing of a Disclosure of Material Transactions with the state of domicile? [Quarterly Financial Statement, General Interrogatories, Part 1, #1.2]	CR*, ST*	=YES		[Data]
				<i>Other Risks</i>
b. Were management and service agreements between affiliates either submitted and/or approved in conformity with regulatory requirements? [Quarterly Financial Statement, Notes to Financial Statement, states' records of Form D Filings, etc.]				
c. Was the amount of the shareholder dividend at a level that required prior regulatory approval or notification? If the response is "yes," did the insurer obtain proper prior regulatory approvals?				

III.B.2.a. Legal Risk Repository – Quarterly (All Statement Types)

8. Assess the insurer's compliance with transactions involving other jurisdictions.

	<i>Other Risks</i>
<p>a. Did the insurer redomesticate to your state?</p> <p>i. If “yes,” has the insurer failed to comply with any regulatory requirements or stipulations placed on the insurer that were expected to be met subsequent to approval of the redomestication?</p> <p>ii. Identify any legal implications that represent risk to the insurer due to the redomestication.</p>	
<p>b. Did the insurer engage in transaction(s) to redomesticate a subsidiary offshore?</p> <p>i. If “yes,” has the insurer failed to comply with any regulatory requirements or stipulations placed on the insurer that were expected to be met subsequent to approval of the redomestication?</p> <p>ii. Identify any legal implications that represent risk to the insurer due to the redomestication.</p>	
<p>c. Did the insurer engage in any transactions to acquire a subsidiary domiciled in a non-U.S. jurisdiction?</p> <p>i. If “yes,” has the insurer failed to comply with any regulatory requirements or stipulations expected to be met subsequent to the acquisition?</p> <p>ii. Identify any legal implications that represent risk to the insurer due to the acquisition.</p>	

Legal Compliance with Federal Regulatory Agencies

9. Identify and assess compliance with other federal regulatory agencies.

	<i>Other Risks</i>
<p>a. Review Quarterly Financial Statement, General Interrogatories, Part 1, #8. Is the insurer subject to regulation by a federal regulatory agency?</p>	
<p>b. If “yes,” consider contacting the applicable federal regulatory agency to request any information about the results of that agency's oversight, including any issues identified, federal compliance violations, fraud investigations and regulatory actions.</p>	

III.B.2.b. Annual Audited Financial Report Worksheet

Note: The worksheet is intended to provide procedures for reviewing the Audited Financial Report for compliance and assessment of risks. The worksheet provides for the results of the review to be documented by the analyst. Analysts should document overall results of the risks identified in Section III: Risk Assessment of the insurer within the relevant risk category.

Note that overall Audit Report compliance and legal risks are included in the Legal Risk Repository.

Part 1 – Audited Financial Report

1. Assess compliance with Audited Financial Report requirements. Were the financial statements included in the Audited Financial Report:

	Comments
a. Based on statutory accounting practices?	
b. Specific to the insurer rather than on a consolidated or combined basis?	
c. If prepared on a consolidated or combined basis: <ul style="list-style-type: none"> i. Was this basis approved by the domiciliary commissioner upon application by the insurer due to a pooling or a 100% reinsurance agreement with affiliates? ii. Was a consolidating or combining worksheet included with the financial statements that: <ul style="list-style-type: none"> • Shows amounts separately for each insurer (non-insurance operations may be shown on a combined or individual basis)? • Provides explanations for consolidating and eliminating entries? • Includes a reconciliation of any differences between the amounts shown for an individual insurer and the amounts per the insurer's Annual Financial Statement? 	

2. Assess the details of the Audited Financial Report and identify risks.

	Comments
a. What type of opinion was issued by the certified public accountant (CPA)? <ul style="list-style-type: none"> • Unmodified • Modified • Qualified • Adverse • Disclaimer of opinion 	
b. If the opinion was modified, which type of opinion was issued and what was the reason for the deviation?	
c. Were any differences noted between information included in the Audited Financial Report and the insurer's Annual Financial Statement? <ul style="list-style-type: none"> • Total Assets • Net Income • Surplus 	

III.B.2.b. Annual Audited Financial Report Worksheet

If “yes,” review the reconciliation of differences and identify the reasons for the difference, consider the impact of the audit adjustments made by the independent CPA on the conclusions reached as a result of the analysis, and consider the need to perform additional analysis.	
<p>d. If further concerns exist, consider additional procedures that may include, but not limited to, requesting and reviewing the following:</p> <ul style="list-style-type: none"> • Letter of Representation • A schedule of all recorded and unrecorded audit adjustments • Internal control related presentation materials including Management’s Comment Letter • Any other audit work papers deemed appropriate or necessary (i.e., Statement on Auditing Standards (SAS) 99 Fraud and Legal Representation Letters) 	

CPA Letter of Qualifications

A review of the CPA’s Letter of Qualifications should be completed whenever there has been a change in the independent CPA from the prior year and may be completed annually whether there has been a change in the independent CPA.

3. Confirm that the CPA’s Letter of Qualifications includes the following:

	Comments
a. A statement that the CPA is independent with respect to the insurer and conforms to the standards of the profession.	
b. Information regarding the background and experience, including the experience in audits of insurers, of the staff assigned to the audit, and whether each is a CPA.	
c. A statement that the CPA understands that the domiciliary commissioner will be relying on the Audited Financial Report, and the CPA’s opinion thereon, in the monitoring and regulation of the financial position of the insurer.	
d. A statement that the CPA is properly licensed by an appropriate state licensing authority.	
<p>e. A statement that the auditor is in compliance with the following qualifications, which are specified in the NAIC <i>Annual Financial Reporting Model Regulation</i> (#205) for the Audited Financial Reports:</p> <ul style="list-style-type: none"> i. The CPA is in good standing with the American Institute of Certified Public Accountants and with all states in which the CPA is licensed to practice or, for a Canadian or British insurer, is a chartered accountant. ii. The CPA conforms to the standards of the profession. iii. The partner or other person responsible for rendering the Audited Financial Report has not acted in that capacity for more than five consecutive years and, following any such period of service, that 	

III.B.2.b. Annual Audited Financial Report Worksheet

<p>person shall be disqualified from serving in that or a similar position for the same insurer for a period of five years.</p> <p>iv. The domiciliary commissioner has not ruled that the CPA is unqualified for purposes of expressing an opinion on the financial statements included in the Audited Financial Report and by providing prohibited non-audit services to the insurer.</p> <p>v. The domiciliary commissioner has not ruled that the CPA is unqualified if a member of the board, president, chief executive officer, controller, chief financial officer, chief accounting officer, or any other person serving in an equivalent position for that insurer, was employed by the independent CPA and participated in the audit of that insurer during the one-year period preceding the date that the most current statutory opinion is due.</p>	
<p>f. A statement that the CPA agrees to:</p> <p>i. Make available for review by the domiciliary state insurance department examiners, at any reasonable place designated by the domiciliary commissioner, all work papers prepared in the conduct of the audit and any communications between the CPA and the insurer related to the audit.</p> <p>ii. Retain the audit work papers and communications until the domiciliary state insurance department has filed an examination report covering the period of the audit but no longer than seven years from the date of the audit report.</p> <p>iii. Allow copies of pertinent audit work papers to be made and retained by the domiciliary state insurance department examiners.</p>	
<p>g. Were any deviations identified between the statements in the CPA's Letter of Qualifications and the required statements per Model #205 for insurers as summarized above?</p>	

Change in CPA

4. Identify any concerns if a change in CPA has occurred.

	<i>Comments</i>
<p>a. Was the CPA who issued the opinion on the insurer's financial statements the same CPA who issued the opinion on the insurer's financial statements in the prior year?</p>	
<p>b. If the CPA who issued the opinion on the insurer's financial statements this year is different from the CPA in the prior year:</p> <p>i. Was the domiciliary state insurance department notified of the change?</p> <p>ii. Has a letter from the new CPA been filed with the domiciliary state insurance department that affirms: (1) the CPA is aware of the provisions of the Insurance Code and the rules and regulations of the domiciliary state insurance department that relate to accounting and financial matters; and (2) the CPA will express an opinion on the</p>	

III.B.2.b. Annual Audited Financial Report Worksheet

<p>financial statements of the insurer in terms of the insurers conformity to the statutory accounting practices prescribed or otherwise permitted by that department, specifying such exceptions as the CPA may believe appropriate?</p> <p>iii. Did the insurer file a letter with the domiciliary state insurance department stating whether, in the 24 months preceding the change in CPAs, there were any disagreements with the former CPA regarding accounting principles or practices, financial statement disclosure, or auditing scope or procedure which, if not resolved to the satisfaction of the former CPA, would have caused the CPA to make reference to the subject matter of the disagreement in connection with the CPA's opinion?</p> <p>iv. With regard to the letter referred to in procedure #4.b.iii., did the insurer also file a letter from the former CPA stating whether the CPA agrees with the statements regarding disagreements in the insurer's letter?</p>	
c. Were any disagreements noted in the letters from either the insurer or the former CPA?	

Part II – Report on Internal Controls

5. Identify if any concerns exist regarding Management's Report on Internal Controls.

Per the NAIC's *Annual Financial Reporting Model Regulation*, the Management's Report of Internal Control Over Financial Reporting (Section 16) and Communication of Internal Control Related Matters Noted in an Audit (Section 11) are both required by August 1 each year (or 60 days after the Audited Financial Report). The following procedures are applicable to these two filings.

	Comments
a. Review the Communication of Internal Control Related Matters Noted in an Audit and comment on any weaknesses noted and the improvements made or proposed by the insurer to correct those weaknesses.	
b. Review Management's Report of Internal Control Over Financial Reporting and note any unremediated material weaknesses disclosed in the report.	
<p>c. If internal control weaknesses are noted in either the Management's Report of Internal Control Over Financial Reporting or the Communication of Internal Control Related Matters Noted in an Audit, consider the following additional procedures:</p> <p>i. Assess the internal control weaknesses impact on key processes (e.g., the accuracy of financial reporting, reserve valuation, claims processing, or investment practices, etc.).</p> <p>ii. Assess the source of internal control weaknesses and determine if attributed to issues within the insurance entity or the insurance holding company system (i.e., parent, subsidiary or affiliate). If at the holding company system level, contact the lead state to discuss if applicable holding company analysis procedures should be performed</p>	

III.B.2.b. Annual Audited Financial Report Worksheet

<p>by the lead state.</p> <p>iii. If the internal control weaknesses relate to market conduct or rate review practices, communicate with the department's market conduct staff to assess any financial or reputational risk that may result.</p>	
<p>d. If weaknesses were noted and no corrective action plan proposed, contact the insurer and request detailed information regarding the insurer's remediation and corrective action plan to resolve the weaknesses.</p>	
<p>e. Review the Communication of Internal Control Related Matters Noted in an Audit for information provided on the name of the current lead audit partner and the year at which he or she began serving in that capacity, as outlined in the Model Audit Rule Implementation Guide. Consider the following additional procedures to verify compliance with requirements outlined in the CPA Letter of Qualifications section above:</p> <p>i. Utilize the information provided on the partner's name to verify compliance with auditor qualification requirements (i.e., in good standing).</p> <p>ii. Utilize the information provided on the year at which the lead audit partner began serving in that capacity to verify compliance with partner rotation requirements.</p>	

III.B.2.c. Annual Management's Discussion & Analysis Report Worksheet

Note: The worksheet is intended to provide procedures for reviewing the Management's Discussion and Analysis (MD&A) report for compliance and assessment of risks. The worksheet provides for the results of the review to be documented by the analyst. Analysts should document overall results of the risks identified in Section III: Risk Assessment of the insurer within the relevant risk category.

Note that overall MD&A compliance and legal risks are included in the Legal Risk Repository.

Compliance**1. Assess compliance with MD&A Report requirements. Did the MD&A filed in accordance with the Annual Financial Statement Instructions include the following content?**

Analysts should refer to the Annual Statement Instructions for detailed explanation of specific content expectations. Below is an abbreviated list.

	<i>Comments</i>
a. Overall material historical and prospective disclosure to assess financial condition, including a short and long-tailed analysis of the business of the insurer	
b. Results of operations	
c. Prospective information	
d. Material changes	
e. Liquidity, asset/liability matching and capital resources	
f. Loss reserves	
g. Off-balance sheet arrangements	
h. Participation in high-yield financings, highly-leveraged transactions, or non-investment grade loans and investments	
i. Preliminary merger and acquisition negotiation	

Assessment of Management's Discussion and Analysis**2. In review of the MD&A, were any previously unknown and undocumented risks, concerns or unusual items noted in the information reported?**

	<i>Comments</i>
a. Changes in business	
b. Material events	
c. Results of operations	
d. Prospective information	
e. The insurer's explanation of material changes in line items	
f. Liquidity, asset/liability matching and capital resources	
g. Items that affect the volatility of loss reserves (P/C only)	
h. Off-balance sheet arrangements	

III.B.2.c. Annual Management's Discussion & Analysis Report Worksheet

i. Participation in high-yield financings, highly-leveraged transactions, or non-investment grade loans and investments	
j. Discussion on preliminary merger/acquisition negotiations	
k. Any other items reported in the MD&A	

Legal Risk Assessment

Legal Risk: Non-conformance with laws, rules, regulations, prescribed practices or ethical standards in any jurisdiction in which the entity operates will result in a disruption in business and financial loss.

The objective of Legal Risk Assessment analysis is to focus on risks emerging from company activities that might not be in accordance with legal and regulatory requirements. Given the wide range of legal and regulatory requirements that insurers are exposed to, including various jurisdictions and agencies, legal risks can emerge from many different areas. As such, the analyst will need to have a good understanding of the insurer and its operations in order to identify the applicable legal and regulatory requirements that could have a significant impact on the insurer's financial position and prospective solvency.

The Current Period Analysis section of the Risk Assessment Worksheet includes a procedure step related to Compliance Analysis, which may assist in identifying various risks addressed in this repository. In addition, some of the detailed procedures included in this repository may be useful in completing the Compliance Analysis procedure. However, if significant compliance issues are identified that represent a risk to the insurer's financial position or prospective solvency, analysis of such risks should be discussed and documented under Legal Risk in the Risk Assessment section of the worksheet (Section III).

The following discussion provides suggested data, benchmarks and procedures the analyst can consider in his/her review. In analyzing legal risk, the analyst may analyze a wide range of risk exposures related to the insurer's compliance with laws and regulations. An analyst's risk-focused assessment of legal risk should take into consideration the following areas (but not be limited to):

- Market conduct activities and violations
- Expenses and potential liabilities associated with ongoing litigation
- Fraudulent activities
- Compliance with code of ethics
- Compliance with state laws and reporting requirements
- Compliance with federal Affordable Care Act (ACA) provisions (health business only)
- Compliance with federal agency requirements
- Compliance with audit requirements, including those pertaining to the audit committee

Discussion of Annual Procedures

Using the Repository

The legal risk repository is a list of possible quantitative and qualitative procedures, including specific data elements, benchmarks and procedures from which the analyst may select to use in his/her review of legal risk. Analysts are not expected to respond to all procedures, data or benchmark results listed in the repository. Rather, analysts and supervisors should use their expertise, knowledge of the insurer and professional judgement to tailor the analysis to address the specific risks of the insurer and document completion of the analysis. The repository is not an all-inclusive list of possible procedures. Therefore, risks identified for which no procedure is available should be analyzed by the state insurance department based on the nature and scope of the risk.

In using procedures in the repository, the analyst should review the results in conjunction with the Supervisory Plan, Insurer Profile Summary and the prior period analysis. Communication and/or coordination with other

III.B.2.d. Legal Risk Repository – Analyst Reference Guide

internal departments are a critical step in the overall risk assessment process and are a crucial consideration in the review of certain procedures in the repository.

The analyst should also consider the insurer's corporate governance which includes the assessment of the risk environment facing the insurer in order to identify current or prospective solvency risks, oversight provided by the board of directors and the effectiveness of management, including the code of conduct established by the board.

The placement of the following data and procedures in the legal risk repository is based on "best fit." Analysts should use their professional judgement in categorizing risks when documenting results of the analysis. Key insurance operations or lines of business, for example, may have related risks addressed in different repositories. Therefore, the analyst may need to review other repositories in conjunction with legal risk.

ANALYSIS DOCUMENTATION: Results of legal risk analysis should be documented in Section III: Risk Assessment of the insurer. Documentation of the Risk Assessment analysis should be sufficiently robust to explain the risks and reflect the strengths and weaknesses of the insurer. Analysts are not expected to respond to procedures, data or benchmark results directly in the repository document.

Quantitative and Qualitative Data and Procedures

Market Conduct

PROCEDURE #1 directs the analyst to identify and assess legal risks emerging from market conduct practices of the insurer that could have an impact on financial position and prospective solvency. In so doing, the analyst is encouraged to review any communication from the state's market analysis unit, including the results of market conduct exams as well as information drawn from the review of market analysis tools available on iSite+, such as the Market Analysis Profile (MAP), Examination Tracking System (ETS), Market Analysis Review System (MARS), Regulatory Information Retrieval System (RIRS), Special Activities Database (SAD), Market Initiative Tracking System (MITS), Market Conduct Annual Statement (MCAS) and the Complaints database. Quantitative results from some of these tools are presented within the repository to simplify the review process, including counts of regulatory actions, aggregates of regulatory fines and references to market conduct examinations that have taken place over the last couple of years. Analysts should review any market conduct issues identified by market analysis staff (such as the Market Analysis Chief or the Collaborative Action Designee) or iSite+ tools and consider the financial implications those issues may have on the insurer. For example, large fines levied by states, suspensions or revocations of licenses, market conduct exam settlements (whether financial or other), or other regulatory actions taken based on market conduct violations may have a material impact on the financial solvency of the insurer.

Litigation, Legal and Government Expenses

PROCEDURE #2 directs the analyst to identify and evaluate risks related to expenses paid for litigation, other legal issues and/or government lobbying. This procedure includes quantitative metrics identifying individual legal expense payments of significance, situations where investigation and settlement of policy claims make up the bulk of legal expenses and unusual payments for government lobbying. While these metrics might identify a need for further investigation in this area, the analyst should take other steps to identify and assess litigation and other legal risks as outlined in the procedure. Comparing legal expenses to prior years and industry averages might identify an upward trend that should be investigated. In addition, a detailed review of the financial statements, and notes to the financial statements in particular, may disclose information on significant legal cases the company is involved in. If significant cases are identified, additional follow-up and correspondence with the company may be necessary to assess their potential impact on prospective solvency.

III.B.2.d. Legal Risk Repository – Analyst Reference Guide**Fraud**

PROCEDURE #3 directs the analyst to identify and evaluate the impact of any fraudulent activity on the financial position and prospective solvency of the company. The procedure encourages the analyst to review financial statements, review news reports, correspond with other insurance department units (e.g., Fraud, Market Conduct, etc.), review regulatory actions (through RIRS) and contact other state insurance regulators with authority over the businesses of the insurer to identify any instances of fraud or ongoing investigations. If fraud, allegations of fraud or ongoing investigations are identified, the analyst is encouraged to document his/her understanding and assessment of the ongoing issues and to contact the company regarding its plans to address the situation.

Compliance with Code of Ethics Standards

PROCEDURE #4 directs the analyst to identify and evaluate risks related to the insurer's compliance with code of ethics standards. This procedure references information provided in the General Interrogatories of the Annual Statement related to the code of ethics. The analyst is encouraged to use this information, as well as information provided in the Corporate Governance Annual Disclosure (CGAD) (if filed on an insurance entity basis), to identify and assess risks in this area. If the CGAD is filed on a group basis, rely on the information provided in the GPS for group risks or provided by the lead state if risks apply to the insurance entity. If concerns regarding an insurer's failure to implement or abide by a code of ethics are identified, the analyst should correspond with the company to address these concerns and/or identify other compensating controls in place.

Compliance with State Laws and Reporting

PROCEDURE #5 directs the analyst to assess the insurer's compliance with NAIC reporting practices, internal policy, laws, regulations and prescribed practices. This procedure references information provided in the General Interrogatories of the Annual Statement related to whether any certificates of authority, licenses or registrations of the insurer have been suspended or revoked. This assists the analyst in determining whether there are any legal or regulatory impediments that could affect the insurer's operations or result in a significant legal liability. In addition, qualitative procedures are suggested to assist the analyst in identifying issues of noncompliance with other regulatory requirements, including the specific procedures described below.

PROCEDURE #5D asks the analyst to identify through Notes to the Financial Statement, the iSite+ Validation Exceptions tool and through any corrections of reporting errors potential issues with the reliability of financial reporting that may require follow-up discussions with the insurer. Potential missing data, data that does not conform with standards, or any crosscheck errors could materially impact the outcome of an analysis and corrective measures may need be taken by the insurer prior to proceeding with an analysis.

PROCEDURE #5F offers follow-up analysis and actions the analyst may consider if the insurer is in violation of any state statutes or regulations. It is critical that the analyst determine the extent of the non-compliance and document the issue, resolution, communication by the insurer, and the outcome. The analyst should complete a detailed written explanation of the violation to ensure proper documentation should non-compliance issues recur.

PROCEDURES #5G AND #5H offer follow-up analysis and actions the analyst may consider if the insurer has had a certificate of authority, license, or registration suspended or revoked by any government entity during the period or if the insurer has been issued a consent order or agreement. If the action was taken by another state or regulatory body, the analyst should contact that regulator for details regarding the action.

PROCEDURE #6 directs the analyst to assess the insurer's compliance with state investment laws. The analyst should consider determining whether the insurer's investment portfolio is in compliance with the investment limitations and diversification requirements per the state's insurance laws. In addition, the analyst may review affiliated investments for compliance with state law and review the results of the most recent examination regarding investment compliance.

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PROCEDURE #7 directs the analyst to consider a review affiliated management and service agreements for compliance with state requirements. As material affiliated transactions are generally subject to regulatory review and approval (including extraordinary dividends), the analyst should evaluate the company's compliance with regulatory requirements in this area. The steps listed here are intended to assist the analyst in identifying potential agreements or transactions to check for compliance.

PROCEDURE #8 directs the analyst to assess the insurer's compliance with transactions involving other jurisdictions. Transactions that may be affected by compliance requirements include redomestication, as well as mergers and acquisitions. The steps listed here are intended to assist the analyst in identifying potential transactions to check for compliance.

Compliance with the Federal Affordable Care Act

PROCEDURE #9 directs the analyst to identify and assess compliance with requirements embedded within the federal Affordable Care Act (ACA). This procedure references information provided in the Annual Statement related to whether the insurer filed the Supplemental Health Care Exhibit (SHCE) and reported premium revenues subject to the ACA. If the insurer filed the SHCE, the analyst should consider performing procedures outlined in #9 and #10. Procedures listed under #9 include consideration of whether the SHCE was filed in accordance with Annual Statement Instructions, whether medical loss ratio (MLR) rebate liabilities are material and/or consistent with what is reported to the U.S. Department of Health and Human Services (HHS), and whether the insurer is subject to sanctions, oversight or audit by the federal Centers for Medicare & Medicaid Services (CMS). For purposes of reviewing the SHCE, the analyst should refer to the Annual Financial Statement Instructions for details on reporting requirements for health entities in run-off or that only have assumed and no direct business, and health entities that have no business that would be reported in the columns for Comprehensive Health Care, Mini-Med Plans, Expatriate Plans, and Medicare Advantage Part C and Medicare Part D Stand-Alone Plans. If the health entity's SHCE was reviewed or is under review by examination staff, the analyst should contact the examiner-in-charge (EIC) to inquire about any material examination findings.

PROCEDURE #10 is only applicable to insurers that write insurance premiums subject to the ACA and directs the analyst to determine whether there are concerns regarding components of the insurer's preliminary MLR calculations. The ACA requires health entities to submit data on the proportion of premium revenues spent on clinical services and quality improvement, also known as the MLR. The ACA requires health entities to spend at least 80% of premium for individual and small group policies or 85% of premium for large group policies on medical care, with review provisions imposing tighter limits on health insurance rate increases. When reviewing the results of the preliminary MLR, by state, by line of business, the analyst should be aware that individual states can and may require a higher MLR pursuant to state law. If the health entity fails to meet these standards, the health entity will be required to provide a rebate to policyholders. The purpose of the SHCE is to assist state and federal regulators in identifying and defining elements that make up the MLR as described in Section 2718(b) of the Public Health Service Act (PHSA) and for purposes of submitting a report to the HHS Secretary required by Section 2718(a) of the PHSA. During the review of the Preliminary MLR, the analyst should also consider how the individual state's Preliminary MLR compares to the grand total (refer to the Financial Profile Report).

Beginning in 2014, a similar MLR requirement applies to Medicare Advantage Plans and Medicare Part D Stand-Alone Plans. The health entity must spend at least 85% of premium (with certain adjustments) on clinical services and quality improvement, or rebate premium to the HHS.

In some cases, it may be more useful to use the Preliminary MLR that is calculated by totaling the data from all SCHEs submitted by a company to the states where it has business. This national Preliminary MLR will reduce the impact of potential issues with statistical credibility of claims experience and allocation of various expenses over states and lines of business.

For lines of business in a given state with exposures of less than 1,000 life-years looking at a 5-year trend is of very limited usefulness since in such cases, claims experience is not considered credible and is subject to greater

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variability. More than 1,000 life years, the experience is considered credible, but still subject to large variations until exposures are well above 1,000 life years.

The MLR is not calculated in the traditional sense where medical expenses are simply divided by premiums. Premiums are adjusted for certain taxes and expenses. The numerator in the calculation will include health improvement expenses and fraud and abuse detection and recovery expenses in addition to medical expenses. The expenses for fraud and abuse detection and recovery are limited by the amount actually recovered.

The MLR calculated on the SHCE is a preliminary calculation and will not be used in determining rebates. Health entities will report information concerning rebate calculations directly to the HHS. The numbers that will be utilized for rebate purposes include revisions for claim reserve run-off subsequent to year end, statistical credibility concerns and other defined adjustments.

The analyst should review completeness or consistency validation exceptions on iSite+ that may indicate if the SHCE has not been prepared and submitted for each jurisdiction in which the company has written direct comprehensive major medical business in accordance with the *Annual Statement Instructions*.

The aggregation of data reported on the SHCE is by state, by market (individual, small group, large group) and by licensed entity. In other words, each health insurance issuer needs to meet the minimum loss ratio targets in each state, and market.

The NAIC iSite+ Financial Profile Report for the SHCE should be reviewed and significant fluctuations investigated. For example, how does the percentage change from the prior year in incurred claims (Line 2.1) compare to total incurred claims (line 5.0)?

In addition, the analyst should ensure that the Supplemental filing was made providing a description of the methods utilized to allocate “Improving Healthcare Quality Expenses” to each state and to each line and column on the SHCE Part 3. When reviewing this Supplemental filing the analyst should consider whether the detailed descriptions of the Quality Improvement expenses were included and whether such descriptions conform to the definitions provided in the *Annual Statement Instructions*.

Note that the preliminary MLR included in this SHCE (for any given state) is not the MLR that is used in calculating the federal mandated rebates. The MLR used in the rebate calculation (i.e., the ACA MLR) will differ for two reasons. First the ACA MLR will reflect the development of claims and claims reserves between December 31 of the Statement Year and March 31 of the following year. The second and far more important reason is that the ACA MLR includes a credibility adjustment that is based on the number of covered lives and certain benefit provisions of the coverages provided. The adjustment takes the form of an addition of percentage points to the calculated MLR. The ACA MLR is then used to determine if a rebate is due and to calculate the amount of the rebate. If the ACA MLR is greater than the relevant MLR standard no rebate is due. If the ACA MLR is less than the relevant MLR standard the rebate is calculated by multiplying the difference between the ACA MLR and the standard MLR by earned premium. Except for very large blocks of business (75,000 lives or more), the ACA MLR will always be larger than the Preliminary MLR. Conversely, for very small blocks of business (under 1,000 lives) the ACA MLR is not calculated since no rebate is due.

Despite the differences, the validity and reasonableness of the ACA MLR calculation, and therefore of the rebate calculation can be assessed using the data from the SHCE. The following elements from the SHCE and the rebate calculation can be used for such an assessment. For the following items there should be little or no difference between the amounts in the SHCE and the rebate calculation:

- Earned premium
- Federal and state taxes and licensing or regulatory fees
- Expenses to improve health care quality

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For other items there are expected to be differences between the SHCE and the rebate calculation due to the difference in the time of reporting between the two:

- Paid claims, unpaid claim reserve, and incurred claims
- Experience rating refunds and reserves for experience rating refunds
- Change in contract reserves
- Incurred medical pool incentives and bonuses
- Net healthcare receivables

For the Contingent Benefit Reserve, the expected relationship between the SHCE and the rebate calculation is unknown as yet.

After completing analysis in this area, if specific concerns are identified regarding MLR compliance, the analyst is encouraged to contact the CMS to request information on CMS sanctions and remediation, as well as CMS supervision and regulatory concerns (including MLR audits).

Legal Compliance with Federal Regulatory Agencies

PROCEDURE #11 directs the analyst to identify and assess compliance with other federal regulatory agencies. This procedure references information provided in the General Interrogatories of the Annual Statement related to whether the insurer is subject to regulation by a federal regulatory agency. In addition to the HHS and the CMS oversight of health insurance, insurers may be subject to regulation by the Federal Reserve, U.S. Securities and Exchange Commission (SEC), U.S. Department of the Treasury and other federal regulatory bodies depending upon the nature, scope and extent of the insurer's or insurance group's activities. If the insurer is subject to federal regulation, the analyst is encouraged to contact the applicable federal agency (as appropriate) to inquire about the insurer and assess any issues raised.

Management's Discussion and Analysis Report

PROCEDURE #12 directs the analyst to assess the insurer's compliance with the Management's Discussion and Analysis (MD&A) report requirements and to identify any legal risks noted in the report. To assist the analyst in conducting the review, an optional MD&A review workpaper is included in the Handbook at III.B.2.c. The MD&A workpaper breaks down analysis of the MD&A into two distinct steps: 1) Compliance Analysis; and 2) Assessment. For purposes of simplifying the review of the MD&A, guidance for consideration in performing both of these steps has been included within this reference guide.

In considering compliance, the analyst should determine whether the MD&A addresses the two-year period covered in the insurer's Annual Financial Statement and discusses any material changes. In addition, the analyst should determine whether the insurer prepared the MD&A on a non-consolidated basis, which is required unless one of the following conditions were met: 1) the insurer is part of a consolidated group of insurers that utilizes a pooling arrangement or a 100% reinsurance agreement that affects the solvency and integrity of the insurer's reserves, and the insurer ceded substantially all of its direct and assumed business to the pool (an insurer is deemed to have ceded substantially all of its direct and assumed business to a pool if it has less than \$1 million total direct plus assumed written premiums during a calendar year that is not subject to a pooling arrangement, and the net income of the business not subject to the pooling arrangement represents less than 5% of the company's capital and surplus); or 2) the insurer's state of domicile permits audited consolidated financial statements.

Additional compliance requirements apply to the overall completeness of the MD&A, including elements as described below:

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- Overall material historical and prospective disclosure – Insurers should supply information necessary to assess the insurer’s financial condition, including a short and long-tailed analysis of the business of the insurer.
- Results of operations – Insurers should provide a description of any unusual or infrequent events or transactions or any significant economic changes that materially affected the amount of reported net income or other gains/losses in surplus. Insurers should also describe any known trends or uncertainties that have had or are reasonably probable to have a material favorable or unfavorable impact on premiums, net income, or other gains/losses in surplus. If the insurer knows of events that will cause a material change in the relationship between expenses and premium, the change in the relationship shall be disclosed. To the extent that the Annual Financial Statement discloses material increases in premium, reporting entities should provide a narrative discussion of the extent to which such increases are attributable to increases in prices, increases in the volume or amount of existing products being sold, or the introduction of new products.
- Prospective information – Insurers are encouraged to supply forward-looking information. The MD&A may include discussions of known trends or any known demands, commitments, events, or uncertainties that will result in or that are reasonably likely to result in the reporting entity’s liquidity improving or deteriorating in any material way. Further, descriptions of known material trends in the insurer’s capital resources and expected changes in the mix and cost of such resources should be included. Disclosure of known trends or uncertainties that the insurer reasonably expects will have a material impact on premium, net income, or other gains/losses in surplus is also encouraged.
- Material changes – Insurers are required to provide adequate disclosure of the reasons for material year-to-year changes in line items, or discussion and quantification of the contribution of two or more factors to such material changes. An analysis of changes in line items is required:
 - where material
 - where the changes diverge from modifications in related line items of the Annual Financial Statement
 - where identification and quantification of the extent of contribution of each of two or more factors is necessary to an understanding of a material change
 - where there are material increases or decreases in net premium.
- Liquidity, asset/liability matching and capital resources – Insurers are required to discuss both short-term and long-term liquidity and capital resources. Short-term liquidity shall include a discussion of the nature and extent of restrictions on the ability of subsidiaries to transfer funds to the reporting entity in the form of cash dividends, loans, or advances, and the impact, if any, such restrictions may have on the ability of the reporting entity to meet its cash obligations. The discussion of long-term liquidity and long-term capital resources must address material expenditures, significant balloon payments or other payments due on long-term obligations, and other demands or commitments, including any off-balance sheet items, to be incurred beyond the next 12 months, as well as the proposed sources of funding required to satisfy such obligations. Also, identify and separately describe internal and external sources of liquidity, and briefly discuss any material unused sources of liquid assets. Insurers should describe any known material trends, favorable or unfavorable, in its capital resources, and indicate any expected material changes in the mix and relative cost of such resources.
- Loss reserves – The MD&A should include a discussion of those items that affect the insurer’s volatility of loss reserves, including a description of those risks that contribute to the volatility.
- Off-balance sheet arrangements – Insurers should consider the need to provide disclosures concerning transactions, arrangements, and other relationships with entities or other persons that are reasonably likely to materially impact liquidity or the availability of or requirements for capital resources. Material sources of

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liquidity and financing, including off-balance sheet arrangements and transactions with limited purpose entities, should be discussed.

- Participation high-risk transactions and investments – The insurer should disclose and discuss participation in high-yield financing, highly leveraged transactions, or non-investment grade loans and investments, if such participation or involvement has had or is reasonably likely to have a material effect on financial condition or results of operations. For each such participation or involvement or grouping thereof, there shall be identification consistent with the Annual Financial Statement schedules or detail, description of the risks added to the reporting entity, associated fees recognized or deferred, amount (if any) of loss recognized, the insurer’s judgment whether there has been material negative effects on the insurer’s financial condition, and the insurer’s judgment whether there will be a material negative effect on the financial condition in subsequent reporting periods.
- Preliminary merger/acquisition negotiation – The insurer should disclose and discuss its involvement in any merger/acquisition negotiations, to the extent they are likely to have a material effect on financial condition or operations.

In reviewing the items disclosed in the MD&A filing, the analyst should assess their potential impact on the insurer’s financial condition and prospective solvency by placing and discussing risk information within the appropriate branded risk classification.

Audited Financial Report

PROCEDURE #13 directs the analyst to assess the insurer’s compliance with Audited Financial Report requirements and to identify any legal risks noted in the report. To assist the analyst in conducting the review, an optional Audited Financial Report review workpaper is included in the Handbook at III.B.2.b. This workpaper highlights both compliance and assessment considerations, as discussed below:

- Audited financial report compliance – The financial statements are required to be prepared in conformity with statutory accounting practices prescribed or otherwise permitted by the domiciliary state insurance department. In addition, the financial statements should be prepared on a stand-alone basis, unless the insurer has made written application to the domiciliary commissioner to file audited consolidated or combined financial statements if the insurer is a part of a group of insurance companies that utilizes a pooling or 100% reinsurance agreement. If the insurer is filing financial statements on a consolidated or combined basis, the analyst should determine whether the domiciliary commissioner approved the insurer’s application to file on a consolidated or combined basis, and whether a consolidating or combining worksheet has been included with the financial statements. This worksheet should show amounts for each insurer separately, including explanations for consolidating and eliminating entries, and reconciliations for any differences between the amounts shown for an individual insurer and the amounts per the insurer’s Annual Financial Statement.
- Audited financial report detailed assessment – In addition to reviewing for compliance, the analyst should review information provided in the financial statements to assist in risk identification and detailed assessment. One key step in this area is to determine the type of audit opinion that was issued by the independent certified public accountant (CPA). The opinion may be an unmodified or a modified opinion; however, there are three types of modified opinions: qualified, adverse and disclaimer of opinion.
 - Unmodified Opinion – The auditor should express an unmodified opinion when the auditor concludes that the financial statements are presented fairly, in all material respects, in accordance with the applicable financial reporting framework.
 - Modified Opinion – The auditor should modify the opinion in the auditor’s report, if the auditor concludes that, based on the audit evidence obtained, the financial statements as a whole are materially misstated or is unable to obtain sufficient appropriate audit evidence to conclude that the financial

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statements as a whole are free from material misstatement. There are three types of modified opinions: qualified, adverse and disclaimer of opinion, as explained below:

- The auditor should express a qualified opinion when:
 1. The auditor, having obtained sufficient appropriate audit evidence, concludes that misstatements, individually or in the aggregate, are material but not pervasive to the financial statements; or
 2. The auditor is unable to obtain sufficient appropriate audit evidence on which to base the opinion, but the auditor concludes that the possible effects on the financial statements of undetected misstatements, if any, could be material but not pervasive.
- The auditor should express an adverse opinion when the auditor, having obtained sufficient appropriate audit evidence, concludes that misstatements, individually or in the aggregate, are both material and pervasive to the financial statements.
- The auditor should disclaim an opinion when the auditor is unable to obtain sufficient appropriate audit evidence on which to base the opinion, and the auditor concludes that the possible effects on the financial statements of undetected misstatements, if any, could be both material and pervasive.

If a modified opinion is issued, the analyst should document the reasons for the modification and assess the impact of the modification on the insurer's financial position and prospective solvency.

In addition to reviewing and assessing the opinion, the analyst should also determine whether total assets, net income, and surplus per the Audited Financial Report agree with the amounts per the insurer's Annual Financial Statement. If differences exist, the independent CPA is required to include in the Notes to Financial Statements a reconciliation of the differences between the Audited Financial Report and the Annual Financial Statement along with a written description of the nature of these differences. If differences are identified, the analyst should document these differences and the reasons for the differences based on a review of the independent CPA's reconciliation in the Notes to Financial Statements. The analyst should also consider the impact of the audit adjustments made by the independent CPA on the conclusions reached as a result of the analysis of the Annual Financial Statement and consider the need to perform additional analysis (i.e., complete additional procedures for items impacted by the audit adjustments) on the Annual Financial Statement information.

If further concerns exist, the analyst should consider performing one or more of the following procedures:

- Obtain and review a copy of the signed management representation letter, which acknowledges that management is responsible for the presentation of the financial statements and has considered all uncorrected misstatements and concluded that any uncorrected misstatements are immaterial. The analyst should review the entire management representation letter to determine if there are representations that would impact the insurer's solvency.
- Obtain and review all recorded and unrecorded audit adjustments along with supporting documentation regarding the adjustments or explanations from the external auditor. The analyst may use the information regarding audit adjustments to identify risk or internal control weaknesses to determine what the impact of significant audit adjustments might be on the insurer's solvency.
- Obtain and review the internal control-related matters presentation materials, including the Management Letter, prepared by the external auditor for the audit committee's review. Note the external auditor is required to provide written communication to the audit committee of all significant deficiencies or material weaknesses known. The comments from the external auditors may be used as guidance as to areas that may require additional investigation and the analyst's view of this documentation.

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- Obtain and review any other audit work papers deemed appropriate or necessary (e.g., Statement on Auditing Standards (SAS) No. 99 Consideration of Fraud in a Financial Statement Audit). This documentation should impact the analysts' consideration of risk inherent within the entity and impact the overall risk assessment and analysis procedures completed by the analyst. Further, obtain copies of all legal letters and determine the status of all pending litigation and the impact that potential settlements might have on the insurer's solvency.
- CPA Letter of Qualifications – The analyst should perform procedures in this area whenever there has been a change in the independent CPA from the prior year, although it may be completed annually whether or not there has been a change in independent CPA. The analyst should determine if the independent CPA furnished to the insurer, in connection with and for inclusion in the filing of the Audited Financial Report, a Letter of Qualifications which includes all of the statements listed in the procedure. If any of the statements are missing from the letter, the analyst should contact the CPA firm to discuss and address. In addition, the analyst should determine whether the CPA retained for review by the domiciliary state insurance department all audit work papers prepared during the audit, unadjusted journal entries, letter of representation, management's letter and any communications between the CPA and the insurer related to the audit.
- Change in CPA – The insurer is required to notify the domiciliary state insurance department within five business days when the insurer's independent CPA is dismissed or resigns. The insurer is also required to furnish a separate letter within 10 business days of the previous notification stating whether, in the 24 months preceding such event, there were any disagreements with the former independent CPA on any matter of accounting principles or practices, financial statement disclosure, or auditing scope or procedure, and which disagreements, if not resolved to the satisfaction of the former independent CPA, would have caused the CPA to make reference to the disagreement in connection with the opinion. In addition, the insurer is further required to furnish a letter from the former independent CPA stating whether the independent CPA agrees with the statements contained in the insurer's letter and, if not, stating the reasons for which he or she does not agree. The analyst should determine whether the CPA who issued an opinion on the insurer's financial statements in the current period is the same CPA who issued the opinion in the prior year. If not, the analyst should determine whether all required reports were filed with the state insurance department as outlined above and assess the impact of the change in CPA on the insurer.
- Reports on internal controls – In addition to the Audited Financial Report, insurers are required to furnish the domiciliary state insurance department with a written Management's Report of Internal Control Over Financial Reporting by the independent CPA describing material weaknesses in the insurer's internal control structure as noted by the independent CPA during the audit, if applicable. Such a report is required regardless whether material weaknesses have been identified. In those instances where material weaknesses are noted, the insurer is also required to provide a description of remedial actions taken or proposed to correct the material weaknesses if such actions are not described in the CPA's report. Effective for audits as of 12/31/21 and thereafter, the NAIC's Model Audit Rule Implementation Guide requests that the name of the current lead audit partner and the year at which he or she began serving in that capacity be included in the internal control report, so it can be provided to regulators but kept confidential. Such information may be useful in verifying compliance with audit partner qualification and rotation requirements.

Management of insurance companies with more than \$500 million in direct and assumed premiums are also required to file with the state insurance department an assessment of internal control over financial reporting. This report states whether or not management is confident the internal controls are effective in providing accurate statutory financial statements. If material weaknesses are identified or management cannot attest to effective internal controls over financial reporting, the analyst should consider performing additional procedures as highlighted in the worksheet.

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Audit Committee

PROCEDURE #14 directs the analyst to assess compliance with audit committee requirements. As mandated by the *Annual Financial Reporting Model Regulation*, every insurer required to file an audited financial report is also required to have an audit committee that is directly responsible for the appointment, oversight and compensation of the auditor. Insurers with less than \$500 million in direct and assumed premium may apply for a waiver from this requirement based on hardship. Based on various premium thresholds, a certain percentage of the audit committee members must be independent from the insurer. However, if domiciliary law requires board participation by otherwise non-independent members, such law shall prevail and such members may participate in the audit committee. This procedure references information provided in the General Interrogatories of the Annual Statement related to whether the insurer has established an audit committee in accordance with state insurance laws and requires the insurer to report if it has been granted any exemptions in this area. In assessing compliance with these requirements, the analyst is encouraged to compare other information received on the corporate governance practices of the insurer, including the CGAD (if filed on an insurance entity basis), to information provided in the interrogatories. Note, if the CGAD is filed on a group basis, the analyst should rely on the information provided in the GPS or provided by the lead state if material risks are only relevant to specific insurance entities.

Additional Analysis and Follow-Up Procedures

EXAMINATION FINDINGS direct the analyst to consider a review of the recent examination report, summary review memorandum and communication with the examination staff to identify if any legal risk issues were discovered during the examination.

INQUIRE OF THE INSURER directs the analyst to consider requesting additional information from the insurer if legal risk concerns exist in a specific area. The list provided are examples of types of information or explanations to be obtained that may assist in the analysis of legal risk for specific topics where concerns have been identified.

OWN RISK AND SOLVENCY ASSESSMENT (ORSA) directs the analyst to obtain and review the latest ORSA Summary Report for the insurer or insurance group (if available) to assist in identifying, assessing and addressing legal risks faced by the insurer.

HOLDING COMPANY ANALYSIS directs the analyst to obtain and review the holding company analysis work completed by the lead state to assist in identifying, assessing and addressing risks that could impact the insurer.

Example Prospective Risk Considerations

The table provides the analyst with example risk components for use in the Risk Assessment and Insurer Profile Summary branded risk analysis section and a general discription of the risk component. Note that the risks listed are only examples and do not represent a complete list of all risks available for the legal risk category.

Discussion of Quarterly Procedures

The Quarterly Legal Risk Repository procedures are designed to identify the following:

- 1) Concerns with market conduct, including complaints, market conduct actions, communication with market staff, etc.
- 2) Concerns with litigation, legal, or government expenses
- 3) Material fraudulent activity and the financial impact to the insurer
- 4) Concerns with the insurer's compliance with code of ethics standards
- 5) Compliance concerns with NAIC reporting practices, internal policy, laws, regulations and prescribed practices

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- 6) Concerns with the insurer's compliance with the state's investment laws
- 7) Compliance concerns with affiliated management and service agreements
- 8) Concerns with the insurer's compliance with transactions involving other jurisdictions
- 9) Whether the insurer is subject to regulation by other Federal regulatory agencies

For additional guidance on individual procedure steps, please see the corresponding annual procedures discussed above.

III.B.3.a. Liquidity Risk Repository – P/C Annual

Liquidity Risk: Inability to meet contractual obligations as they become due because of an inability to liquidate assets and/or obtain adequate funding without incurring unacceptable losses.

Note: The repository is not an all-inclusive list of possible procedures. Therefore, risks identified for which no procedure is available should be analyzed by the state insurance department based on the nature and scope of the risk. Also, note that key insurance operations or lines of business, for example, may have related risks addressed in different repositories. Therefore, analysts may need to review other repositories in conjunction with liquidity. For example:

- Investment strategy also is discussed in the Credit, Market and Strategic Risk Repositories.
- Investment assets classes (Bonds, Mortgages, etc.) also are discussed in the Credit and/or Market Risk Repositories.

Analysis Documentation: Results of liquidity risk analysis should be documented in Section III: Risk Assessment of the insurer.

Liquidity of Investment Portfolio and Overall Liquidity

1. Determine if there are any concerns regarding the liquidity of the insurer's asset portfolio and overall liquidity.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Adjusted liabilities to liquid assets ratio [IRIS ratio #9]		>100%	[Data]	[Data]
b. Change in liquid assets	CR	>50% or <-15%	[Data]	[Data]
c. Ratio of restricted assets to total cash and invested assets [Annual Financial Statement, Notes to Financial Statements, Note #5-L]	OP	>10%	[Data]	[Data]
				<i>Other Risks</i>
d. Review the five-year trend for the liquidity ratio within the Financial Profile Report and document any unusual fluctuations.				
e. Compare the insurer's adjusted liabilities to liquid assets ratio with industry and peer group averages in order to identify significant deviations.				
f. Review the Annual Supplemental Investment Risks Interrogatories. Note any unusual items or areas that would indicate inadequate liquidity.				
g. Request and review the insurer's most recent investment plan. Determine if the investment plan is adequate to meet the liquidity needs of the insurer's liability structure.				
h. If there are concerns regarding liquidity or cash flows, consider having a cash flow analysis performed by an actuary.				
i. If restricted assets are material, gain an understanding and assess the types of investments and products that may require collateral to be posted (e.g., derivatives, guaranteed investment contracts [GICs], Federal Home Loan Bank [FHLB], etc.).				
j. If concerns are identified regarding overall liquidity of the asset portfolio, identify and assess other sources of liquidity available to the insurer. (Or, request information from the				

III.B.3.a. Liquidity Risk Repository – P/C Annual

insurer if necessary. See Additional Analysis and Follow-Up Procedures below.)	
k. Assess the impact of market conditions through consideration of industry and economic events (i.e., news, industry analytics). Is the analyst aware of any market conditions that may threaten the liquidity of insurers' investment portfolios (e.g., market dislocation or other events that could affect liquidity of assets classes such as structured securities, structured notes, Schedule BA assets, non-investment grade bonds)?	

2. Assess the value and maturity of bond portfolio impact on liquidity.

	Other Risks
a. Review the Annual Financial Statement, Schedule D – Part 1A – Section 2: <ul style="list-style-type: none"> Identify any material fluctuations/trends over years Compared to a review of the insurer's most recent investment plan, determine if the bond maturity schedule adequately matches future liabilities 	
b. Review the Annual Financial Statement, Schedule D – Part 1 and determine the extent to which the fair value of bonds varies from the statement value. Assess the impact of such variance on the insurer's overall liquidity.	
c. Review the Annual Financial Statement, including Notes to Financial Statements – Note #5, to assess if there are liquidity concerns due to a material exposure to highly structured bonds, including RMBS, loan-backed and structured securities (LBaSS) and structured notes.	

3. Determine whether there are concerns due to the level of investment in private-placement bonds.

	Other Risks	Benchmark	Result	Outside Benchmark
a. Ratio of private-placement bonds owned to surplus		>5%	[Data]	[Data]
b. Increase in private placement bonds from the prior year, where the ratio of investments in private-placement bonds to invested assets is greater than 5%		>15%	[Data]	[Data]
				Other Risks
c. Review Annual Financial Statement, Schedule D – Part 1A – Section 1 and Schedule D – Part 1A – Section 2 to determine the following: <ul style="list-style-type: none"> The total amount of privately-placed bonds owned The types of issues with privately-placed bonds The NAIC designations of the privately-placed bonds The maturity distribution of the privately-placed bonds The amount of total privately-placed bonds that are freely tradable under SEC Rule 144 or qualified for resale under SEC Rule 144A 				
d. For the more significant privately-placed bonds, if rated by a chief revenue officer (CRO) review the issuer's rating or request the Securities Valuation Office's (SVO) assessment of the designation to evaluate the issuer's financial position and ability to repay its debt.				

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4. Determine whether there are concerns due to the level of investment in other invested assets (Schedule BA).

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Ratio of BA assets to surplus	CR*, MK*	>10%	[Data]	[Data]
b. Increase in BA assets from the prior year, where the ratio of BA assets to surplus is greater than 5%	CR*, MK*	>10%	[Data]	[Data]
				<i>Other Risks</i>
c. Upon review of Annual Financial Statement – Schedule BA, is the insurer invested in any assets, such as hedge funds or private equity funds, that may include restrictions on an investor's ability to liquidate the assets, which may include commitments for additional funding, which is common in private equity funds, or which may have the potential to be required to post additional collateral, similar to the variation margin for derivatives?	CR, MK, ST			

Securities Lending

5. Determine whether concerns exist regarding securities lending transactions.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Does the reporting entity engage in securities lending transactions?	OP	>0	[Data]	[Data]
i. Percentage of total securities lending collateral reinvested to total assets			[Data]	
ii. Aggregate total collateral received			[Data]	
				<i>Other Risks</i>
b. Review the Annual Financial Statement investment schedules, General Interrogatories and Notes to Financial Statements to gain an understanding of the scope of the securities lending program and restricted assets, and to understand how the cash collateral is reinvested [Schedule DL].				

Affiliated Investments

6. Determine whether investments in affiliates are significant.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Total of all investments in affiliates to surplus [Annual Financial Statement, Five-Year Historical Data]	CR, MK*	>20%	[Data]	[Data]
b. Change in total of all investments in affiliates from the prior year-end	CR, MK*	>20% or <-20%	[Data]	[Data]
c. Change in any category of affiliated investments from the prior year-end	CR, MK*	>10% or <-10%	[Data]	[Data]

III.B.3.a. Liquidity Risk Repository – P/C Annual

	<i>Other Risks</i>
d. Review the results of the Holding Company Analysis completed by the lead state to determine if any concerns exist regarding affiliated entities.	CR
e. Review Annual Financial Statement, Notes to Financial Statements, Note #10 and Note #14 to identify if the insurer is subject to any guarantees or other commitments to parent, subsidiaries, or affiliates (PSA). If the guarantee or commitment is material to the insurer, assess the nature of the agreement and the financial strength of the PSA.	CR

Special Deposits**7. Review the Annual Financial Statement, Schedule E – Part 3 and determine if any concerns exist.**

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Book/adjusted carrying value of total special deposits to total net admitted assets		>10%	[Data]	[Data]
b. Book/adjusted carrying value of all other special deposits (not for the benefit of all policyholders) to total special deposits		>50%	[Data]	[Data]
c. Difference between the book/adjusted carrying value of total special deposits to the fair value of total special deposits		>5%	[Data]	[Data]
				<i>Other Risks</i>
d. Review the listing of special deposits held by the insurer not for the benefit of all policyholders and there is overall liquidity risk regarding the insurer, consider: <ul style="list-style-type: none"> The number of states in which the insurer has these types of deposits. The greater the number, the more difficult it could be for the domiciliary state to call on these deposits in a rehabilitation. The amount of concentration in any one particular state. 				
e. Contact the domiciliary state or perform research to determine if any of the states have restrictions on the ability of those deposits to be called by the domiciliary state during a rehabilitation.				

Cash Flow from Operations**8. Review cash flow from operations and determine if any concerns exist.**

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Ratio of net cash from operations to surplus		< -5%	[Data]	[Data]
				<i>Other Risks</i>
b. Review the cash flow from operations to determine the underlying cause of the negative cash flow.				
c. Review the trend in net cash from operations for the past five years and note any unusual				

III.B.3.a. Liquidity Risk Repository – P/C Annual

fluctuations or negative trends between years.	
d. Describe any material commitments for capital expenditures as of the end of the reporting period indicating the purpose, anticipated source of funds, changes between equity and debt, and any off-balance sheet financing agreements.	
e. Compare cash flow from operations with the industry and peer group (Peer Financial Report) in order to identify significant deviations.	

Related Party Exposure in the Investment Portfolio

9. Assess related party exposure in the investment portfolio.

	Other Risks
<p>a. Review the Annual Financial Statement investment schedules, as disclosed in the column “Investments Involving Related Parties” and utilizing iSite+ tools, determine if the insurer has material related party exposures in its investment portfolio.</p> <p>This disclosure is included in:</p> <ul style="list-style-type: none"> • Schedule B • Schedule BA • Schedule D • Schedule DA • Schedule DB • Schedule DL • Schedule E, Part 2 <p>Consider exposure by asset class and in aggregate, and by the role of the related party in the investment as designed by the “Investments Involving Related Parties” disclosure.</p>	LQ, MK
b. If concerns exist regarding a material related party exposure in the investment portfolio, assess the credit quality of those investments involving related parties by reviewing designations, assessing historical default experience, etc.	LQ, MK

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<p>c. If concerns exist regarding a material related party exposure in investment management or advisory services, consider the following:</p> <ul style="list-style-type: none"> i. Review the procedures in the “Additional Procedures” section below regarding Third Party Investment Advisors and consider their application to related party advisors in that role. ii. In addition to the additional analysis procedures regarding third party investment advisors, consider the following: <ul style="list-style-type: none"> 1. Review the insurer’s investment policy guidelines and determine whether the related party investments follow the guidelines and are in compliance with regulatory requirements. 2. Review whether the fee structure for asset management is fair, reasonable, and appropriately recognized as investment expenses. 3. If the related party asset manager also originates/securitizes investments held by the insurer, consider requesting additional information from the insurer to determine the following: <ul style="list-style-type: none"> a. Whether the asset manager has adequate experience and knowledge in originating and managing the types of investments; b. Whether the asset manager follows appropriate underwriting practices and applicable regulatory requirements in originating investments; and c. Whether the fee structures embedded in securities (if applicable) are fair, reasonable, and appropriately account for potential duplication of fees or conflicts of interest. 	OP
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Invested Asset Exposure to Climate Change Risk

10. Assess the potential impact of material climate change and/or transition and asset devaluation risk on the insurer’s invested asset portfolio.

	<i>Other Risks</i>
a. Review information provided in the insurer’s response to the NAIC’s Climate Risk and Disclosure Survey (if available) on its exposure to material climate change/energy transition risk and related mitigation activity in this area.	CR*, MK*
b. Review relevant information provided in the Own Risk and Solvency Assessment (ORSA) Summary Report, and/or U.S. Securities and Exchange Commission (SEC) 10-K or 10-Q filings (if available) that discusses the insurer’s exposure to material climate change/energy transition risk and related mitigation activity in this area.	CR*, MK*
c. Review information provided in the NAIC’s U.S. Insurance Industry Climate Affected Investment Analysis to identify potential concentrations in insurer exposure.	CR*, MK*

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Additional Analysis and Follow-up Procedures

Request and Assess the Insurer's Investment Policies and Strategies:

If concerns exist regarding the level of liquidity risk, request and review the insurer's investment strategy to determine if it is appropriately structured to support its ongoing business plan and cash flow needs. Review the guidelines outlined in the plan for:

- Quality of issues invested in and diversification standards pertaining to issuer, industry, duration, liquidity, geographic location, and issues/sectors exposed to material climate change, transition, and asset devaluation risks.
- Expected rate of returns on investments (projected investment income) compared to actual results.
- Planned increases in investment types, sectors, markets, etc.
- Appropriateness of the investment plan for the liability structure of the insurer (This may require a review of asset adequacy analysis for asset liability matching and discussion with the insurer's management to better understand its plan.)

Upon review of the investment plan, compare the plan to actual results. Does the insurer and its investment manager(s) appear to be adhering to the investment policies and guidelines in the investment plan?

Examination Findings:

Review the most recent examination report and Summary Review Memorandum (SRM) for any findings regarding liquidity risks associated with:

- Asset liability matching (ALM) and cash flow stress testing
- Investment returns
- Climate change, transition, and asset devaluation
- Effective management of the insurer's liquidity position
- Other-than-temporary impairment OTTI
- Investment valuation issues
- Adherence to investment policies and strategies
- Investment management, and use of and monitoring of external investment managers
- Determine if liquidity concerns identified during the last exam have been addressed.

If outstanding issues are identified, perform follow-up procedures as necessary to address concerns.

NAIC Capital Market's Bureau Analytical Assistance:

Consider requesting the following analytical reviews:

- Review of the insurer's investment portfolio
- Review of Investment Management Agreements

III.B.3.a. Liquidity Risk Repository – P/C Annual

Third-Party Investment Advisers:

Assess and determine if any concerns exist regarding third party investment advisers and associated contractual arrangements.

- Review Annual Financial Statement, General Interrogatories, Part 1, #28.05. Does the insurer utilize third party investment advisors, broker/dealer or individuals acting on behalf of the insurer with access to their investment accounts?

If “yes”, consider the following procedures:

- Review the results of the most recent financial examination work papers, follow-up and prospective risk information and the summary review memorandum provided by the examiners. Did the examination identify any issues with regard to investment advisers and associated contractual arrangements that require follow-up analysis or communication with the insurer? If “yes”, document the follow-up work performed.
- Compare Annual Financial Statement, General Interrogatories, Part 1, #28.05 for the current year to the prior year to determine if there have been any changes in advisors. If “yes”,
 - Consider obtaining an explanation for the change from the insurer.
 - Consider obtaining a copy of the new investment advisor agreement and review it for appropriate provisions.
- Using the information reported in Annual Financial Statement, General Interrogatories, Part 1, #28.05, obtain and review SEC Form ADV (if available), to determine if the investment advisor is in good standing with the SEC. If not in good standing, contact the insurer to request an explanation.
- If agreements with third party investment advisers are affiliated, have the appropriate Form D – Prior Notice of Transactions been filed and approved by the department? Were any concerns noted or follow-up monitoring recommended?
- Request information from the insurer regarding the background and expertise in structured securities of its investment advisors (in-house and/or contractual) and its analytical system capabilities. Determine whether the advisors and systems are adequate to allow the insurer to continuously monitor its structured securities investments.
- If the insurer uses an external asset manager, consider if investments on Schedule BA are invested in funds that are affiliated with the asset manager or are managed by that asset manager. Consider the following issues:
 - If any conflicts of interest exist
 - If the investment is appropriate for the insurer’s portfolio and is arm’s-length
 - If the insurer is paying double fees

Inquire of the Insurer:

If concerns exist, consider requesting information from the insurer regarding:

General Investment Inquiries:

- If management and the board of directors have adequately reviewed the investment portfolio and understands the yields, underlying collateral, cash flows and investment volatility
- Any additional concentration by collateral type
- Management’s process for valuing securities so as to assist the analyst in assessing if the securities are valued appropriately

III.B.3.a. Liquidity Risk Repository – P/C Annual

- Management’s intended use of certain riskier investments and purpose within the insurer’s portfolio
- If management has an appropriate level of knowledge and expertise with the type of securities being purchased/held
- If the insurer has controls implemented to mitigate the risks associated with this investment type
- Sources of liquidity, such as letters of credit (LOCs)
- Information/explanation of guarantees or other commitments to PSA
- Securities lending program (nature, size, reinvestment policies, etc.)
- Separate accounts plan descriptions and/or policy forms as they relate to its securities lending program

Investment Diversification:

- Planned asset mix and diversification strategies

Mortgages:

- Handling of foreclosed mortgage loans

BA Assets:

- Current Audited Financial Statements and other documents (partnership agreements, etc.) necessary to support the value of the insurer’s investment in partnerships and joint ventures
- Information necessary to support the value of significant other invested assets other than partnerships and joint ventures
- Current details on cash flows and returns for the different types of investments, especially hedge funds and private equity funds

RMBS, CMBS and LBaSS:

- Percentage distribution and amounts of each type of RMBS, CMBS and LBaSS held; planned amortization class (PAC), support bonds, interest only (IO) tranches, and principle only (PO) tranches to evaluate the level of prepayment risk in the portfolio
- Projected prepayment speeds on its RMBS portfolio and compare with historical prepayments, as well as the prepayment assumption at the time of purchase

Asset Liability Matching:

- If concerns are identified regarding overall liquidity of the asset portfolio, request a copy of the insurer’s asset/liability matching policy and/or liquidity stress testing/scenario analysis

Own Risk and Solvency Assessment (ORSA) Summary Report:

If the insurer is required to file an ORSA or is part of a group that is required to file an ORSA:

- Did the ORSA Summary Report analysis conducted by the lead state indicate any liquidity risks that require further monitoring or follow-up?
- Did the ORSA Summary Report analysis conducted by the lead state indicate any mitigating strategies for existing or prospective liquidity risks?
- For relevant business types, did the ORSA Summary Report analysis conducted by the lead state indicate any liquidity risks regarding catastrophic exposure and related mitigating strategies?

Holding Company Analysis:

- Did the Holding Company analysis conducted by the lead state indicate any liquidity risks impacting the

III.B.3.a. Liquidity Risk Repository – P/C Annual

insurer that require further monitoring or follow-up?

- Did the Holding Company analysis conducted by the lead state indicate any mitigating strategies for existing or prospective liquidity risks impacting the insurer?

Example Prospective Risk Considerations

Risk Components for IPS		Explanation of Risk Components
1	Overall liquidity is insufficient	The insurer does not hold sufficient liquid assets to meet current liabilities.
2	Illiquid assets are significant	Less liquid assets may be unavailable to pay policyholder claims as they are not easily or quickly marketable.
3	Significant affiliated investments balance	Investments in PSA may not be marketable and unavailable to pay policyholder claims.
4	Significant special deposits balance	Special deposit assets may be unavailable to pay policyholder claims.
5	Inability to produce positive cash flows from operations	Negative trends in cash flow from operations create liquidity needs that may result in the sale of investments at a loss.
6	Significant amount of [insert asset type] held with resale restrictions	Illiquidity of certain assets may be due to provisions of the asset, such as restrictions on resale. (E.g., certain BA assets, such as investment hedge funds, may have time restrictions on when investment can be sold/liquidated.)
7	Significant amount of Schedule BA assets held with commitments/ collateral requirements	Schedule BA assets may include commitments for additional funding, which is common in private equity funds. Schedule BA assets may have the potential to be required to post additional collateral, similar to variation margin for derivatives.
8	Expected cash flows from Schedule BA assets and types of other structured bonds	Certain Schedule BA assets and highly structured bonds—including RMBS, LBaSS and structured notes—may include liquidity risks where expected cash flows do not match actual.
9	Exposure to climate change, transition and asset devaluation risk	The insurer's investment portfolio is subject to prospective devaluation of the assets/changes in the asset return associated with its holdings of climate-affected assets.

III.B.3.a Liquidity Risk Repository - P/C Quarterly

Liquidity Risk: Inability to meet contractual obligations as they become due because of an inability to liquidate assets and/or obtain adequate funding without incurring unacceptable losses.

Note: The repository is not an all-inclusive list of possible procedures. Therefore, risks identified for which no procedure is available should be analyzed by the state insurance department based on the nature and scope of the risk. Also, note that key insurance operations or lines of business, for example, may have related risks addressed in different repositories. Therefore, analysts may need to review other repositories in conjunction with liquidity. For example, investment assets classes (Bonds, Mortgages, etc.) also are discussed in the Credit and/or Market Risk Repositories.

Analysis Documentation: Results of liquidity risk analysis should be documented in Section III: Risk Assessment of the insurer.

Liquidity of Investment Portfolio and Overall Liquidity

1. Determine if there are any concerns regarding the liquidity of the insurer's asset portfolio and overall liquidity.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Liquidity ratio: adjusted liabilities to liquid assets		>100%	[Data]	[Data]
b. Change in liquidity ratio	CR	>10 pts or <-10 pts from the prior quarter OR >20 pts or <-20 pts from the prior year- end	[Data]	[Data]
				<i>Other Risks</i>
c. Review the liquidity ratio within the Financial Profile Report, and document any unusual fluctuations over the last five years.				
d. If concerns are identified regarding overall liquidity of the asset portfolio, identify and assess other sources of liquidity available to the insurer. (Or, request information from the insurer if necessary. See Additional Analysis and Follow-Up Procedures below).				
e. Assess the impact of market conditions through consideration of industry and economic events (i.e., news, industry analytics). Is the analyst aware of any market conditions that may threaten the liquidity of insurers' investment portfolios (e.g., market dislocation or other events that could affect liquidity of assets classes such as structured securities, structured notes, Schedule BA assets and non-investment grade bonds).				

III.B.3.a Liquidity Risk Repository - P/C Quarterly

Exposure to Other Invested Assets (Schedule BA)**2. Determine whether there are concerns due to the level of investment in other invested assets (Schedule BA).**

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Ratio of BA assets owned to surplus	CR, MK	>10%	[Data]	[Data]
b. Increase in BA assets from the prior year-end, where the ratio of BA assets to surplus is greater than 5%	CR*, MK*	>10%	[Data]	[Data]

Securities Lending**3. Determine whether concerns exist regarding securities lending transactions.**

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Does the reporting entity engage in securities lending transactions?	OP	>0	[Data]	[Data]
i. Percentage of total securities lending collateral reinvested to total assets			[Data]	
ii. Aggregate total collateral received			[Data]	
				<i>Other Risks</i>
b. Review the Quarterly Financial Statement General interrogatories, Part 1, #16 and Notes to the Financial Statements, Note #5 (if reported) to gain an understanding of the scope of the securities lending program and to understand how the cash collateral is reinvested.				

Affiliated Investments**4. Determine whether investments in affiliates are significant.**

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Total of all investments in affiliates to surplus [Quarterly Financial Statement, General Interrogatories Part 1, #14]	CR, MK*	>20%	[Data]	[Data]
b. Change in total of all investments in affiliates from the prior year-end	CR, MK*	>20% or < -20%	[Data]	[Data]
c. Change in any category of affiliated investments from the prior year-end	CR, MK*	>10% or < -10%	[Data]	[Data]
				<i>Other Risks</i>
d. Review the results of the Holding Company Analysis completed by the lead state to determine if any concerns exist regarding affiliated entities.				CR, MK
e. Review Quarterly Financial Statement, Notes to the Financial Statements, #10 and #14, if reported, to identify if the insurer is subject to any guarantees or other commitments to				CR

III.B.3.a Liquidity Risk Repository - P/C Quarterly

parent, subsidiaries, or affiliates (PSA). If the guarantee or commitment is material to the insurer, assess the nature of the agreement and the financial strength of the PSA.

Cash Flow from Operations**5. Review cash flow from operations and determine if any concerns exist.**

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Net cash from operations to surplus		<-5%	[Data]	[Data]
b. Change in net cash from operations from prior year-to-date to surplus		>5% or <-5%	[Data]	[Data]
				<i>Other Risks</i>
c. Review the cash flow from operations to determine the underlying cause of the negative cash flow (if any).				
d. Review the trend in net cash from operations for the past five periods and note any unusual fluctuations or negative trends between quarters.				

III.B.3.b. Liquidity Risk Repository – Life/A&H/Fraternal Annual

Liquidity Risk: Inability to meet contractual obligations as they become due because of an inability to liquidate assets and/or obtain adequate funding without incurring unacceptable losses.

Note: The repository is not an all-inclusive list of possible procedures. Therefore, risks identified for which no procedure is available should be analyzed by the state insurance department based on the nature and scope of the risk. Also, note that key insurance operations or lines of business, for example, may have related risks addressed in different repositories. Therefore, the analyst may need to review other repositories in conjunction with liquidity risk. For example:

- Investment strategy is also discussed in Credit, Market, and Strategic Risk Repository.
- Investment asset classes (Bonds, Mortgages, etc.) are also discussed in Credit and/or Market Risk Repositories.

Analysis Documentation: Results of liquidity risk analysis should be documented in Section III: Risk Assessment of the insurer.

Liquidity of Investment Portfolio and Overall Liquidity

1. Determine if there are any concerns regarding the liquidity of the insurer's asset portfolio and overall liquidity.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Capital and surplus and AVR to total assets (excluding separate accounts). (See <i>Financial Profile Report</i>).		<7%	[Data]	[Data]
b. Change in liquid Assets.	CR	>80% or < -15%	[Data]	[Data]
c. Ratio of restricted assets to total cash and invested assets. [Annual Financial Statement, Notes to Financial Statements, Note #5-L]	OP	>10%	[Data]	[Data]
				<i>Other Risks</i>
d. Review the Annual Supplemental Investment Risks Interrogatories. Note any unusual items or areas that would indicate inadequate liquidity.				
e. Request and review the insurer's most recent investment plan. Determine if the investment plan is adequate to meet the liquidity needs of the insurer's liability structure.				
f. If there are concerns regarding liquidity or cash flows, review the Statement of Actuarial Opinion for comments regarding cash flow testing performed and the results obtained. (See the Statement of Actuarial Opinion Repository.)				
g. If an examination is in progress or recently completed, communicate with the examiner to determine if the insurer has recently provided responses to the stress liquidity inquiries and templates included in the NAIC <i>Financial Condition Examiners Handbook</i> . If such has occurred, review this information to ascertain whether the analyst's liquidity concerns have been alleviated. If not, request the insurer to submit responses to these inquiries.				
h. If restricted assets are material, gain an understanding and assess the types of investments, and products that may require collateral to be posted (e.g., derivatives, guaranteed investment contracts [GIC], Federal Home Loan Bank [FHLB], etc.)				

III.B.3.b. Liquidity Risk Repository – Life/A&H/Fraternal Annual

i. If concerns are identified regarding overall liquidity of the asset portfolio, identify and assess other sources of liquidity available to the insurer. (Or request information from the insurer if necessary. See Additional Analysis and Follow-up Procedures section below)	
j. Assess the impact of market conditions through consideration of industry and economic events (i.e., news, industry analytics). Is the analyst aware of any market conditions that may threaten the liquidity of insurers' investment portfolios (e.g., market dislocation or other events that could affect liquidity of assets classes, such as structured securities, structured notes, BA assets and non-investment grade bonds)?	

2. Assess the value and maturity of bond portfolio impact on liquidity.

	<i>Other Risks</i>
a. Review Annual Financial Statement, Schedule D – Part 1A – Section 2. i. Identify any material fluctuations/trends over the years. ii. Compared to a review of the insurer's most recent investment plan, determine if the bond maturity schedule adequately matches future liabilities.	
b. Review the Annual Financial Statement, Schedule D – Part 1 and determine the extent to which the fair value of bonds varies from the amortized cost. Assess the impact of such variance on the insurer's overall liquidity.	
c. Review Annual Statement disclosures, including Note #5, to assess if there are liquidity concerns due to a material exposure to highly structured bonds, including RMBS, loan-backed and structured securities (LBaSS) and structured notes.	

3. Determine whether there are concerns due to the level of investment in private-placement bonds.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Ratio of private-placement bonds to capital and surplus plus AVR.		>100%	[Data]	[Data]
b. Increase in private placement bonds from the prior year where the ratio of investments in private-placement bonds to invested assets is greater than 5%.		>15%	[Data]	[Data]
	<i>Other Risks</i>			
c. Review Annual Financial Statement, Schedule D – Part 1A – Section 1 and Schedule D – Part 1A – Section 2 by Major Type and Subtype, and determine the following: <ul style="list-style-type: none"> The total amount of privately-placed bonds owned. The types of issues with privately-placed bonds. The NAIC designations of the privately-placed bonds. The maturity distribution of the privately-placed bonds. The amount of total privately-placed bonds that are freely tradable under SEC Rule 144 or qualified for resale under SEC Rule 144A. 				

III.B.3.b. Liquidity Risk Repository – Life/A&H/Fraternal Annual

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|--|--|
| d. For the more significant privately-placed bonds, if rated by a chief risk officer (CRO), review the issuer's rating or request the Securities Valuation Office's (SVO) assessment of the designation to evaluate the issuer's financial position and ability to repay its debt. | |
|--|--|

4. Determine whether there are concerns due to the level of investment in other (Schedule BA) invested assets.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Ratio of Schedule BA assets to capital and surplus plus AVR.	CR*, MK*	>10%	[Data]	[Data]
b. Increase in Schedule BA assets from the prior year, where the ratio of Schedule BA assets to cash and invested assets is greater than 3.5%.	CR*, MK*	>10%	[Data]	[Data]
				<i>Other Risks</i>
c. Upon review of Annual Financial Statement, Schedule BA, is the insurer invested in any assets, such as hedge funds or private equity funds, that may include restrictions on an investor's ability to liquidate the assets, which may include commitments for additional funding, which is common in private equity funds, or which may have the potential to be required to post additional collateral, similar to the variation margin for derivatives?	ST, CR, MK			

5. Determine whether there are concerns due to the level of investment in collateral loans.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Ratio of collateral loans to capital and surplus plus AVR.	CR*	>20%	[Data]	[Data]
b. Increase in ratio of investments in collateral loans to cash and invested assets is greater than 3.5%, from the prior year.		>10%	[Data]	[Data]
				<i>Other Risks</i>
c. Review Annual Financial Statement, Schedule BA – Part 1 and Schedule DA – Part 1, and perform the following for each such loan: <ul style="list-style-type: none"> i. Determine whether the collateral for the loan is an acceptable asset. ii. Determine whether the collateral loan is to an officer, director, parent, subsidiary or affiliate. 	CR*			

Securities Lending**6. Determine whether concerns exist regarding securities lending transactions.**

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Does the reporting entity engage in securities lending transactions?	OP	>0	[Data]	[Data]

III.B.3.b. Liquidity Risk Repository – Life/A&H/Fraternal Annual

i. Percentage of total securities lending collateral reinvested to total assets.			[Data]	
ii. Aggregate total collateral received.			[Data]	
				<i>Other Risks</i>
b. Review the Annual Financial Statement, investment schedules, General Interrogatories and Notes to Financial Statements to gain an understanding of the scope of the securities lending program and restricted assets, and to understand how the cash collateral is reinvested (Schedule DL).				

Separate Accounts

7. Determine whether concerns exist regarding securities lending transactions within the separate accounts.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Does the reporting entity engage in securities lending transactions with separate account assets?	OP	>0	[Data]	[Data]
i. Percentage of total separate account assets to total assets.			[Data]	
ii. Aggregate total collateral received.			[Data]	
				<i>Other Risks</i>
b. Review the investment schedules, General Interrogatories and Notes to the Financial Statements to gain an understanding of the scope of the securities lending program and restricted assets, and to understand how the cash collateral is reinvested (Schedule DL).				
c. Does the reporting entity report Federal Home Loan Bank (FHLB) funding agreements within the separate account(s)? If so, assess the materiality of the FHLB agreements.				

Affiliated Investments

8. Determine whether investments in affiliates are significant.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Total of all investments in affiliates to capital and surplus. [Annual Financial Statement, Five-Year Historical Data]	CR, MK*	>20%	[Data]	[Data]
b. Change in total of all investments in affiliates from the prior year-end.	CR, MK*	>20% or < -20%	[Data]	[Data]
c. Change in any category of affiliated investments from the prior year-end.	CR, MK*	>10% or < -10%	[Data]	[Data]
				<i>Other Risks</i>
d. Review the results of the Holding Company Analysis completed by the lead state to determine if any concerns exist regarding affiliated entities.	CR			

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e. Review Annual Financial Statement, Notes to Financial Statements, Note #10 and Note #14 to identify if the insurer is subject to any guarantees or other commitments to parent, subsidiaries or affiliates (PSA). If the guarantee or commitment is material to the insurer, assess the nature of the agreement and the financial strength of the PSA.	CR
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Special Deposits

9. Review the Annual Financial Statement, Schedule E – Part 3

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Book/adjusted carrying value of total special deposits to assets.		>10%	[Data]	[Data]
b. Book/adjusted carrying value of all other special deposits (not for the benefit of all policyholders) to total special deposits.		>50%	[Data]	[Data]
c. Difference between the book/adjusted carrying value of total special deposits to the fair value of total special deposits.		>5%	[Data]	[Data]
				<i>Other Risks</i>
d. Review the listing of special deposits held by the insurer not for the benefit of all policyholders and there is overall liquidity risk regarding the insurer, consider: <ul style="list-style-type: none"> The number of states in which the insurer has these types of deposits. The greater the number, the more difficult it could be for the domiciliary state to call on these deposits in a rehabilitation. The amount of concentration in any one particular state. 				
e. Contact the domiciliary state or perform research to determine if any of the states have restrictions on the ability of those deposits to be called by the domiciliary state during a rehabilitation.				

Surrender and Withdrawal Activity

10. Determine whether concerns exist regarding the insurer's surrender and withdrawal activity.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Ratio of surrender benefits and withdrawals on deposit-type contracts to net premiums and deposits on deposit-type contracts.		>50%	[Data]	[Data]
b. Ratio of group surrenders to net group premiums in group annuities where group annuity surrenders exceed 20% of total surrenders.		>50%	[Data]	[Data]
c. Surrender benefits and withdrawals on deposit-type contracts to capital and surplus.		>20%	[Data]	[Data]
				<i>Other Risks</i>

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d. Review Annual Financial Statement, Notes to Financial Statements, Note #32. Determine if the insurer has a material amount of annuity reserves that can be withdrawn with minimal or no charge. <i>(See the Financial Profile Report.)</i>	
e. Determine which lines of business had significant surrender activity during the year or if there appears to be a negative trend in surrender activity over the past five years.	
f. Review the insurer's plan descriptions and/or policy forms to better understand the types of plans offered and the specific policy withdrawal features and surrender charges.	

Cash Flow from Operations

11. Review cash flow from operations and determine if any concerns exist.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Net cash from operations to capital and surplus.		<-5%	[Data]	[Data]
b. Prior year net cash from operations to capital and surplus.		<-5%	[Data]	[Data]
c. Net cash from operations to premium income			[Data]	
d. Net transfers to or from separate accounts to capital and surplus.		>20%	[Data]	[Data]
e. "Other cash provided (applied)" changed by more than 10% of capital and surplus.		>10% or < -10%	[Data]	[Data]
f. "Other cash provided (applied)" to capital and surplus.		>10%	[Data]	[Data]
g. "Other cash provided (applied)" to net cash from operations.		>150% or < -150%	[Data]	[Data]
				<i>Other Risks</i>
h. Review the cash flow from operations to determine the underlying cause of the negative cash flow.				
i. Review the trend in cash flow from operations for the past five years and note any unusual fluctuations or negative trends between years. Also review trend in transfer to/from separate account for unusual fluctuation, such as: <ul style="list-style-type: none"> Significant reliance on cash provided from separate accounts. Significant trends in providing cash to separate accounts. 				
j. Describe any material commitments for capital expenditures as of the end of the reporting period indicating the purpose, source of funds, changes in equity and debt, and any off-balance sheet financing arrangements.				
k. Compare cash flow from operations with the industry in order to identify significant deviations.				

Related Party Exposure in the Investment Portfolio

#12. Assess related party exposure in the investment portfolio.

	Other Risks
<p>a. Review the Annual Financial Statement investment schedules, as disclosed in the column “Investments Involving Related Parties” and utilizing iSite+ tools, determine if the insurer has material related party exposures in its investment portfolio.</p> <p>This disclosure is included in:</p> <ul style="list-style-type: none"> • Schedule B • Schedule BA • Schedule D • Schedule DA • Schedule DB • Schedule DL • Schedule E, Part 2 <p>Consider exposure by asset class and in aggregate, and by the role of the related party in the investment as designed by the “Investments Involving Related Parties” disclosure.</p>	LQ, MK
<p>b. If concerns exist regarding a material related party exposure in the investment portfolio, assess the credit quality of those investments involving related parties by reviewing designations, assessing historical default experience, etc.</p>	LQ, MK

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<p>c. If concerns exist regarding a material related party exposure in investment management or advisory services, consider the following:</p> <ul style="list-style-type: none"> i. Review the procedures in the “Additional Procedures” section below regarding Third Party Investment Advisors and consider their application to related party advisors in that role. ii. In addition to the additional analysis procedures regarding third party investment advisors, consider the following: <ul style="list-style-type: none"> 1. Review the insurer’s investment policy guidelines and determine whether the related party investments follow the guidelines and are in compliance with regulatory requirements. 2. Review whether the fee structure for asset management is fair, reasonable, and appropriately recognized as investment expenses. 3. If the related party asset manager also originates/securitizes investments held by the insurer, consider requesting additional information from the insurer to determine the following: <ul style="list-style-type: none"> a. Whether the asset manager has adequate experience and knowledge in originating and managing the types of investments; b. Whether the asset manager follows appropriate underwriting practices and applicable regulatory requirements in originating investments; and c. Whether the fee structures embedded in securities (if applicable) are fair, reasonable, and appropriately account for potential duplication of fees or conflicts of interest. 	OP
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Invested Asset Exposure to Climate Change Risk

13. Assess the potential impact of material climate change and/or transition and asset devaluation risk on the insurer’s invested asset portfolio.

	<i>Other Risks</i>
a. Review information provided in the insurer’s response to the NAIC’s Climate Risk and Disclosure Survey (if available) on its exposure to material climate change/energy transition risk and related mitigation activity in this area.	CR*, MK*
b. Review relevant information provided in the Own Risk and Solvency Assessment (ORSA) Summary Report, and/or U.S. Securities and Exchange Commission (SEC) 10-K or 10-Q filings (if available) that discusses the insurer’s exposure to material climate change/energy transition risk and related mitigation activity in this area.	CR*, MK*
c. Review information provided in the NAIC’s U.S. Insurance Industry Climate Affected Investment Analysis to identify potential concentrations in insurer exposure.	CR*, MK*

III.B.3.b. Liquidity Risk Repository – Life/A&H/Fraternal Annual

Assessments Against Policy Benefits (Fraternal Societies Only)**14. Assess the materiality of a Fraternal Society's liens on policyholder benefits.**

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. For fraternal societies, did the society report outstanding assessments in the form of liens against policy benefits that have increased surplus?	OP	>0	[Data]	[Data]
i. Assess the materiality of outstanding assessments Total Liens as a percentage of total current year surplus	OP		[Data]	[Data]
b. Were new assessments imposed in the current year? Review any information the department has on the nature and duration of the liens. [Annual Financial Statement, General Interrogatories – Part 2 – #35.2]	OP	>0	[Data]	[Data]

Additional Analysis and Follow-Up Procedures**Request and Assess the Insurer's Investment Policies and Strategies:**

If concerns exist regarding the level of liquidity risk, request and review the insurer's investment strategy to determine if it is appropriately structured to support its ongoing business plan and cash flow needs. Review the guidelines outlined in the plan for:

- Quality of issues invested in and diversification standards pertaining to issuer, industry, duration, liquidity, geographic location, and issues/sectors exposed to material climate change, transition, and asset devaluation risks.
- Expected rate of returns on investments (projected investment income) compared to actual results.
- Planned increases in investment types, sectors, markets, etc.
- Appropriateness of the investment plan for the liability structure of the insurer. (This may require a review of asset adequacy analysis for asset liability matching and discussion with the insurer's management to better understand its plan.)
- Upon review of the investment plan, compare the plan to actual results. Does the insurer and its investment manager(s) appear to be adhering to the investment policies and guidelines in the investment plan?

Examination Findings:

Review the most recent examination report and Summary Review Memorandum (SRM) for any findings regarding liquidity risks associated with

- Asset liability matching (ALM) and cash flow stress testing.
- Investment returns.
- Climate change, transition, and asset devaluation.
- Effective management of the insurer's liquidity position.
- Other-than-temporary impairments (OTTI).

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- Investment valuation issues.
- Adherence to investment policies and strategies.
- Investment management and use of and monitoring of external investment managers.
- Determine if liquidity concerns identified during the last exam have been addressed.

NAIC Capital Market's Bureau Analytical Assistance:

Consider requesting the following analytical reviews:

- Review of the insurer's investment portfolio.
- Review of Investment Management Agreements.

Third-Party Investment Advisers:

Assess and determine if any concerns exist regarding third party investment advisers and associated contractual arrangements.

- Review Annual Financial Statement, General Interrogatories – Part 1 – #29.05. Does the insurer utilize third party investment advisors, broker/dealer or individuals acting on behalf of the insurer with access to their investment accounts?

If “yes”, consider the following procedures:

- Review the results of the most recent financial examination work papers, follow-up and prospective risk information and the summary review memorandum provided by the examiners. Did the examination identify any issues with regard to investment advisers and associated contractual arrangements that require follow-up analysis or communication with the insurer? If yes, document the follow-up work performed.
- Compare Annual Financial Statement, General Interrogatories – Part 1 – #29.05 for the current year to the prior year to determine if there have been any changes in advisors.
- If “yes”,
 - Consider obtaining an explanation for the change from the insurer.
 - Consider obtaining a copy of the new investment advisor agreement and review it for appropriate provisions.
- Using the information reported in Annual Financial Statement, General Interrogatories, Part 1 – #29.05, obtain and review SEC Form ADV (if available), to determine if the investment advisor is in good standing with the SEC. If not in good standing, contact the insurer to request an explanation.
- If agreements with third party investment advisers are affiliated, have the appropriate Form D – Prior Notice of Transactions been filed and approved by the department? Were any concerns noted or follow-up monitoring recommended?
- Request information from the insurer regarding the background and expertise in structured securities of its investment advisors (in-house and/or contractual) and its analytical system capabilities. Determine whether the advisors and systems are adequate to allow the insurer to continuously monitor its structured securities investments.
- If the insurer uses an external asset manager, consider if investments on Schedule BA are invested in funds that are affiliated with the asset manager or are managed by that asset manager. Consider the following issues:

III.B.3.b. Liquidity Risk Repository – Life/A&H/Fraternal Annual

- If any conflicts of interest exist.
- If the investment is appropriate for the insurer’s portfolio and is arms-length.
- If the insurer is paying double fees.

Inquire of the Insurer:

If concerns exist, consider requesting information from the insurer regarding:

General Investment Inquiries

- If management has adequately reviewed the investment portfolio and understand the yields, underlying collateral, cash flows and investment volatility.
- Any additional concentration by collateral type.
- Management’s process for valuing securities to assist the analyst in assessing if the securities are valued appropriately.
- Management’s intended use of certain riskier investments and purpose within the insurer’s portfolio.
- If management has an appropriate level of knowledge and expertise with the type of securities being purchased/held.
- If the insurer has controls implemented to mitigate the risks associated with this investment type
- Sources of liquidity, such as letters of credit (LOCs).
- Information/explanation of guarantees or other commitments to PSA.
- Securities lending program (nature, size, reinvestment policies, etc.).
- Separate accounts plan descriptions and/or policy forms as they relate to its securities lending program.

Investment Diversification

- Planned asset mix and diversification strategies.

Mortgages

- Handling of foreclosed mortgage loans.

BA Assets

- Current Audited Financial Statements and other documents (partnership agreements, etc.) necessary to support the value of the insurer’s investment in partnerships and joint ventures.
- Information necessary to support the value of significant other invested assets other than partnerships and joint ventures.
- Current details on cash flows and returns for the different types of investments, especially hedge funds and private equity funds.

RMBS, CMBS and LBaSS

- Percentage distribution and amounts of each type of RMBS, CMBS and LBaSS held; planned amortization class (PAC), support bonds, interest only (IO) tranches, and principle only (PO) tranches to evaluate the level of prepayment risk in the portfolio.
- Projected prepayment speeds on its RMBS portfolio and compare with historical prepayments, as well as the prepayment assumption at the time of purchase.

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Own Risk and Solvency Assessment (ORSA) Summary Report:

If the insurer is required to file an ORSA or is part of a group that is required to file an ORSA,

- Did the ORSA Summary Report analysis conducted by the lead state indicate any liquidity risks that require further monitoring or follow-up?
- Did the ORSA Summary Report analysis conducted by the lead state indicate any mitigating strategies for existing or prospective liquidity risks?
- For relevant business types, did the ORSA Summary Report analysis conducted by the lead state indicate any liquidity risks regarding catastrophic exposure and related mitigating strategies?

Holding Company Analysis:

- Did the Holding Company Analysis conducted by the lead state indicate any liquidity risks impacting the insurer that require further monitoring or follow-up?
- Did the Holding Company Analysis conducted by the lead state indicate any mitigating strategies for existing or prospective liquidity risks impacting the insurer?

Asset Liability Matching (ALM):

- Did the review of the Statement of Actuarial Opinion or other actuarial filings indicate any concerns regarding the adequacy of ALM, cash flow stress testing and the sufficiency of assets to meet the business obligations of the insurer?
- If concerns are identified regarding overall liquidity of the asset portfolio, request a copy of the insurer's ALM policy and/or liquidity stress testing/scenario analysis.

Example Prospective Risk Considerations

Risk Components for IPS		Explanation of Risk Components
1	Overall liquidity is insufficient.	The insurer does not hold sufficient liquid assets to meet current liabilities.
2	Illiquid assets are significant.	Less liquid assets may be unavailable to pay policyholder claims as they are not easily or quickly marketable.
3	Negative economic impact on separate account liquidity.	Market decline results in the need for policyholder cash, resulting in the potential negative impact or a "run on the bank" scenario.
4	Illiquidity of separate account assets.	That liquid assets are insufficient to meet surrender benefits, resulting in insufficient cash flows.
5	Significant affiliated investments balance.	Investments in PSA may not be marketable and unavailable to pay policyholder claims.
6	Liquidity strain of surrenders and withdrawals.	Liquidity strain of surrenders and withdrawals may be the result of: <ul style="list-style-type: none"> • Market decline results in the need for policyholder cash, resulting in the potential negative impact or a "run on the bank" scenario. • That liquid assets are insufficient to meet surrender benefits, resulting in insufficient cash from operations. • Poor asset-liability matching and the potential negative impact.
7	Significant special deposits balance.	Special deposit assets may be unavailable to pay policyholder claims.

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8	Inability to produce positive cash flows from operations.	Negative trends in cash flow from operations create liquidity needs that may result in the sale of investments at a loss.
9	Significant amount of [insert asset type] held with resale restrictions.	Illiquidity of certain assets may be due to provisions of the asset, such as restrictions on resale. (e.g., certain BA assets, such as investment hedge funds, may have time restrictions on when investment can be sold/liquidated.)
10	Significant amount of Schedule BA assets held with commitments/collateral requirements.	BA assets may include commitments for additional funding, which is common in private equity funds. BA assets may have the potential to be required to post additional collateral, similar to variation margin for derivatives.
11	Expected cash flows from BA assets and types of other structured bonds.	Certain BA assets and highly structured bonds—including RMBS, LBaSS and structured notes—may include liquidity risks where expected cash flows do not match actual.
12	Fraternal policyholder assessments.	Material liens imposed against policyholder benefits.
13	Exposure to climate change, transition and asset devaluation risk	The insurer's investment portfolio is subject to prospective devaluation of the assets/changes in the asset return associated with its holdings of climate-affected assets.

III.B.3.b. Liquidity Risk Repository – Life/A&H/Fraternal Quarterly

Liquidity Risk: Inability to meet contractual obligations as they become due because of an inability to liquidate assets and/or obtain adequate funding without incurring unacceptable losses.

Note: The repository is not an all-inclusive list of possible procedures. Therefore, risks identified for which no procedure is available should be analyzed by the state insurance department based on the nature and scope of the risk. Also, note that key insurance operations or lines of business, for example, may have related risks addressed in different repositories. Therefore, the analyst may need to review other repositories in conjunction with liquidity risk. For example, investment asset classes (Bonds, Mortgages, etc.) also are discussed in Credit and/or Market Risk Repositories.

Analysis Documentation: Results of liquidity risk analysis should be documented in Section III: Risk Assessment of the insurer.

Liquidity of Investment Portfolio and Overall Liquidity

1. Determine if there are any concerns regarding the liquidity of the insurer's asset portfolio and overall liquidity.

	Other Risks	Benchmark	Result	Outside Benchmark
a. Capital and surplus plus asset valuation reserve (AVR) to total assets (excluding separate accounts).		<7%	[Data]	[Data]
b. Change in Liquid Assets from prior quarter-to-date or prior year-end.	CR	>80% or < -15%	[Data]	[Data]
				Other Risks
c. Review liquidity within the Quarterly Financial Profile Report for any unusual fluctuations or negative trends between quarters.				
d. If concerns are identified regarding overall liquidity of the asset portfolio, identify and assess other sources of liquidity available to the insurer. (Or request information from the insurer if necessary. See below.)				
e. Assess the impact of market conditions through consideration of industry and economic events (i.e., news and industry analytics). Is the analyst aware of any market conditions that may threaten the liquidity of insurers' investment portfolios (for example, market dislocation or other events that could affect the liquidity of assets classes, such as structured securities, structured notes, BA assets and non-investment grade bonds)?				

2. Determine whether there are concerns due to the level of investment in other (Schedule BA) invested assets.

	Other Risks	Benchmark	Result	Outside Benchmark
a. Ratio of Schedule BA assets owned to net admitted assets.	CR*, MK	>5%	[Data]	[Data]
b. Increase in Schedule BA assets from the prior year-end, where the ratio of BA assets to cash and invested assets is greater than 3.5%.	CR*, MK*	>10%	[Data]	[Data]

III.B.3.b. Liquidity Risk Repository – Life/A&H/Fraternal Quarterly

Securities Lending**3. Determine whether concerns exist regarding securities lending transactions.**

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Does the reporting entity engage in securities lending transactions?	OP	>0	[Data]	[Data]
i. Percentage of total securities lending collateral reinvested to total assets.				
ii. Aggregate total collateral received.			[Data]	
				<i>Other Risks</i>
b. Review the Quarterly Financial Statement, General Interrogatories, Part 1, #16 and Notes to the Financial Statements, Note #5 (if reported) to gain an understanding of the scope of the securities lending program and to understand how the cash collateral is reinvested.				

Affiliated Investments**4. Determine whether investments in affiliates are significant.**

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Total of all investments in affiliates to capital and surplus.	CR, MK*	>20%	[Data]	[Data]
b. Change in total of all investments in affiliates from the prior year-end.	CR, MK*	>20% or < -20%	[Data]	[Data]
c. Change in any category of affiliated investments from the prior year-end.	CR, MK*	>10% or < -10%	[Data]	[Data]
				<i>Other Risks</i>
d. Review the results of the Holding Company Analysis completed by the lead state to determine if any concerns exist regarding affiliated entities.				CR
e. Review Quarterly Financial Statement, Notes to Financial Statements, Note #10 and Note #14, if reported, to identify if the insurer is subject to any guarantees or other commitments to parent, subsidiaries or affiliates (PSA). If the guarantee or commitment is material to the insurer, assess the nature of the agreement and the financial strength of the PSA.				CR

Surrender and Withdrawal Activity**5. Determine whether concerns exist regarding the insurer's surrender and withdrawal activity.**

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Ratio of surrender benefits to net premiums.		>30% or <0	[Data]	[Data]
b. Surrender benefits to capital and surplus.		>20%	[Data]	[Data]

III.B.3.b. Liquidity Risk Repository – Life/A&H/Fraternal Quarterly

c. Change in surrender benefits to capital and surplus ratio.		> +/- 5 percentage points	[Data]	[Data]
				<i>Other Risks</i>
d. Review Quarterly Financial Statement, Notes to Financial Statements, Note #32, if reported, to determine if the insurer has a material amount of annuity reserves withdrawable with minimal or no charge.				
e. Review the Quarterly Financial Profile Report to determine if there appears to be a negative trend in surrender activity over the past five quarters.				
f. If concerns exist, review the insurer's plan descriptions and/or policy forms to better understand the types of plans offered and the specific policy withdrawal features and surrender charges.				

Cash Flow from Operations

6. Review cash flow from operations and determine if any concerns exist.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Ratio of net cash from operations to capital and surplus.		<-5%	[Data]	[Data]
i. Ratio of net cash from operations to premium income.			[Data]	
b. Change in net transfers to or from separate accounts from the prior quarter-to-date.		>10% or < -10%	[Data]	[Data]
c. Ratio of net transfers to or from separate accounts to capital and surplus.		>20%	[Data]	[Data]
d. Change in "Other cash provided (applied)" to capital and surplus.		>10% or < -10%	[Data]	[Data]
e. "Other cash provided (applied)" to capital and surplus.		>10%	[Data]	[Data]
f. "Other cash provided (applied)" to net cash from operations.		>150% or < -150%	[Data]	[Data]
				<i>Other Risks</i>
g. Review the cash flow from operations to determine the underlying cause of the negative cash flow.				
h. Review the trend in cash flow from operations for the past five periods and note any unusual fluctuations or negative trends between quarters.				

III.B.3.b. Liquidity Risk Repository – Life/A&H/Fraternal Quarterly

Assessments Against Policy Benefits (Fraternal Societies Only)

7. Assess the materiality of a Fraternal Society's liens on policyholder benefits.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. For fraternal societies, did the society report outstanding assessments in the form of liens against policy benefits that have increased surplus? [General Interrogatories – Part 2 – #6.1]	OP	= YES	[Data]	[Data]
i. Assess the materiality of outstanding assessments Total liens as a percentage of total current year surplus	OP		[Data]	[Data]
b. Were new assessments imposed in the current year? Review any information the department has on the nature and duration of the liens. [Quarterly Financial Statement, General Interrogatories – Part 2 – #6.2]	OP	>0	[Data]	[Data]

III.B.3.c. Liquidity Risk Repository – Health Annual

Liquidity Risk: Inability to meet contractual obligations as they become due because of an inability to liquidate assets or obtain adequate funding without incurring unacceptable losses.

Note: The repository is not an all-inclusive list of possible procedures. Therefore, risks identified for which no procedure is available should be analyzed by the state insurance department based on the nature and scope of the risk. Also, note that key insurance operations or lines of business, for example, may have related risks addressed in different repositories. Therefore, analysts may need to review other repositories in conjunction with liquidity risk. For example:

- Investment strategy is also discussed in Credit, Market and Strategic Risk Repository.
- Investment assets classes (Bonds, Mortgages, etc.) are also discussed in Credit and/or Market Risk Repositories.

Analysis Documentation: Results of liquidity risk analysis should be documented in Section III: Risk Assessment of the insurer.

Liquidity of Investment Portfolio and Overall Liquidity

1. Determine if there are any concerns regarding the liquidity of the insurer's asset portfolio and overall liquidity.

	Other Risks	Benchmark	Result	Outside Benchmark
a. Total liabilities to liquid assets		>100%	[Data]	[Data]
b. Change in liquid assets	CR	>75% or <-15%	[Data]	[Data]
c. Liquid assets and receivables to current liabilities ratio (excluding non-investment grade bonds)		<200%		
d. Ratio of restricted assets to total cash and invested assets. [Annual Financial Statement, Notes to Financial Statements, Note #5 – L]	OP	>10%	[Data]	[Data]
e. Aggregate write-ins for other than invested assets to capital and surplus	CR	>10%	[Data]	[Data]
				Other Risks
f. Review the Annual Supplemental Investment Risks Interrogatories. Note any unusual items or areas that would indicate inadequate liquidity.				
g. Review changes in the total liabilities to liquid assets ratio in past years for unusual fluctuations or negative trends between years.				
h. Review changes in the liquid assets and receivables to current liabilities ratio in past years for unusual fluctuations or negative trends between years. (See Financial Profile Report.)				
i. Compare the insurer's liability to liquid assets ratio or liquid assets and receivables to current liabilities ratio with industry and peer group averages in order to identify significant deviations.				
j. Request and review the insurer's most recent investment plan. Determine if the investment plan is adequate to meet the liquidity needs of the insurer's liability structure.				

III.B.3.c. Liquidity Risk Repository – Health Annual

k. If there are concerns regarding liquidity or cash flows, review the Statement of Actuarial Opinion for comments regarding cash flow testing performed and the results obtained. (See Statement of Actuarial Opinion Repository.)	
l. If restricted assets are material, gain an understanding and assess the types of investments and products that may require collateral to be posted (e.g., derivatives, guaranteed investment contracts [GICs], Federal Home Loan Bank [FHLB], etc.).	
m. If concerns are identified regarding overall liquidity of the asset portfolio, identify and assess other sources of liquidity available to the insurer. (Or, request information from the insurer if necessary. See Below.)	
n. Assess the impact of market conditions through consideration of industry and economic events (i.e., news, industry analytics). Is the analyst aware of any market conditions that may threaten the liquidity of insurers' investment portfolios (e.g., market dislocation or other events that could affect the liquidity of assets classes, such as structured securities, structured notes, BA assets and non-investment grade bonds)?	

2. Assess the value and maturity of bond portfolio impact on liquidity.

	<i>Other Risks</i>
a. Review Schedule D – Part 1A – Section 2. i. Identify any material fluctuations/trends over years. ii. Compared to a review of the insurer's most recent investment plan, determine if the bond maturity schedule adequately matches future liabilities.	
b. Review Annual Financial Statement, Schedule D – Part 1 and determine the extent to which the fair value of bonds varies from the amortized cost. Assess the impact of such variance on the insurer's overall liquidity.	
c. Review Annual Statement disclosures, including Note #5, to assess if there are liquidity concerns due to a material exposure to highly structured bonds, including RMBS, loan-backed and structured securities (LBaSS) and Structured Notes.	

3. Determine whether there are concerns due to the level of investment in private-placement bonds.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Ratio of private-placement bonds owned to capital and surplus		>15%	[Data]	[Data]
b. Increase in private placement bonds over the prior year where the ratio of investments in private-placement bonds to invested assets is greater than 5%		>15%	[Data]	[Data]
				<i>Other Risks</i>

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c. Review Annual Financial Statement, Schedule D – Part 1A – Section 1 and Schedule D – Part 1A – Section 2 by Major Type and Subtype, and determine the following: <ul style="list-style-type: none"> • The total amount of privately-placed bonds owned • The types of issues with privately-placed bonds • The NAIC designations of the privately-placed bonds • The maturity distribution of the privately-placed bonds • The amount of total privately-placed bonds that are freely tradable under SEC Rule 144 or qualified for resale under SEC Rule 144A 	
d. For the more significant privately-placed bonds, if rated by a chief risk officer (CRO), review the issuer’s rating or request the Securities Valuation Office’s (SVO) assessment of the designation to evaluate the issuer’s financial position and ability to repay its debt.	

4. Review the Z-Score Analysis included in the Financial Profile Report.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Total Z-Score		<2.6	[Data]	[Data]
b. Decrease in Z-Score from the prior year where the total Z-Score is 6.0 or less in the current year		<-1.5 pts	[Data]	[Data]
c. Decrease in the Z-Score over the past three years if the Z-Score is 6.0 or less in the current year		<-2.0 pts	[Data]	[Data]
d. Ratio of working capital to total assets		<30%	[Data]	[Data]
				<i>Other Risks</i>
e. Review the working capital to total assets ratio for past years and review any unusual fluctuations or negative trends between years.				

5. Determine whether there are concerns due to the level of investment in other (Schedule BA) invested assets.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Ratio of Schedule BA assets to capital and surplus	CR*, MK*	>10%	[Data]	[Data]
b. Increase in Schedule BA assets from the prior year, where the ratio of Schedule BA assets to capital and surplus is greater than 5%	CR*, MK*	>10%	[Data]	[Data]
				<i>Other Risks</i>
c. Upon review of Schedule BA, is the insurer invested in any assets, such as hedge funds or private equity funds, that may include restrictions on an investor’s ability to liquidate the assets, which may include commitments for additional funding, which is common in private equity funds, or which may have the potential to be required to post additional collateral, similar to the variation margin for derivatives?				CR, MK, ST

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Affiliated Investments**6. Determine whether investments in affiliates are significant.**

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Total of all investments in affiliates to capital and surplus [Annual Financial Statement, Five-Year Historical Data]	CR, MK*	>20%	[Data]	[Data]
b. Change in total of all investments in affiliates from the prior year-end	CR, MK*	>20% or <-20%	[Data]	[Data]
c. Change in any category of affiliated investments from the prior year-end	CR, MK*	>10% or <-10%	[Data]	[Data]
				<i>Other Risks</i>
d. Does the company have an interest in the capital stock of another insurance company or other insurer? i. If “yes,” did the insurer fail to properly disclose the investment on Schedule Y?				CR
e. Review the results of the Holding Company Analysis completed by the lead state to determine if any concerns exist regarding affiliated entities.				CR
f. Review Annual Financial Statement, Notes to Financial Statements, Note #10 and Note #14 to identify if the insurer is subject to any guarantees or other commitments to parent, subsidiaries or affiliates (PSA). If the guarantee or commitment is material to the insurer, assess the nature of the agreement and the financial strength of the PSA.				CR

Other Receivables**7. Review and assess furniture, equipment and supplies and EDP equipment.**

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Ratio of admitted furniture, equipment and supplies to capital and surplus		>5%	[Data]	[Data]
b. Change in the admitted balance of furniture, equipment and supplies from the prior year		>10% or <-10%	[Data]	[Data]
c. Ratio of admitted EDP equipment and software to capital and surplus		>3%	[Data]	[Data]
d. Change in the admitted balance of EDP equipment and software from the prior year		>25% or <-25%	[Data]	[Data]
				<i>Other Risks</i>
e. Review the reporting distribution of furniture, equipment and supplies. [Annual Financial Statement, Exhibit 8]				
f. If there are concerns regarding furniture, equipment and supplies, request and review: <ul style="list-style-type: none"> Clarification of any unusual responses from its independent auditor. 				

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<ul style="list-style-type: none"> Information regarding depreciation and review for reasonableness. Determine if the depreciation period exceeds three years. 	
g. Regarding EDP equipment, review disclosures in the Notes to the Audited Financial Report for reasonableness.	
h. Regarding EDP equipment, perform a review to determine whether the minimum capitalization amount, depreciable life and admissibility are in compliance with statutory limitations.	
i. Regarding EDP equipment, request a description of the methodology used to compute depreciation. <ul style="list-style-type: none"> Determine if the period of depreciation exceeds three years. Determine if the insurer non-admitted non-operating software. 	
j. Review the management or service agreements, if any, which provide for EDP services and evaluate whether the charges appear reasonable for the services provided.	
k. If the insurer did not report an asset for EDP equipment and operating system software, does a management or service agreement exist that provides for electronic data processing services?	

Special Deposits

8. Review the Annual Financial Statement, Schedule E, Part 3.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Book/adjusted carrying value of total special deposits to assets		>10%	[Data]	[Data]
b. Book/adjusted carrying value of all other special deposits (not for the benefit of all policyholders) to total special deposits		>50%	[Data]	[Data]
c. Difference between the book/adjusted carrying value of total special deposits to the fair value of total special deposits		>5%	[Data]	[Data]
				<i>Other Risks</i>
d. Review the listing of special deposits held by the insurer not for the benefit of all policyholders and there is overall liquidity risk regarding the insurer, consider: <ul style="list-style-type: none"> The number of states in which the insurer has these types of deposits. The greater the number, the more difficult it could be for the domiciliary state to call on these deposits in a rehabilitation. The amount of concentration in any one particular state. 				
e. Contact the domiciliary state or perform research to determine if any of the states have restrictions on the ability of those deposits to be called by the domiciliary state during a rehabilitation.				

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Cash Flow from Operations**9. Review cash flow from operations and determine if any concerns exist.**

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Net cash from operations to capital and surplus		<-5%	[Data]	[Data]
b. Prior year net cash from operations to prior year capital and surplus		<-5%	[Data]	[Data]
c. Net cash from operations to net premium income			[Data]	
d. Change in “Other cash provided (applied)” to capital and surplus		>10% or <-10%	[Data]	[Data]
e. “Other cash provided (applied)” to capital and surplus		>10%	[Data]	[Data]
f. “Other cash provided (applied)” to net cash from operations		>20%	[Data]	[Data]
g. Ratio of benefits and loss related payments to premiums collected net of reinsurance		>85%	[Data]	[Data]
h. Average number of days of unpaid claims	LG*	>30 Days	[Data]	[Data]
				<i>Other Risks</i>
i. Review the cash flow from operations to determine the underlying cause of the negative cash flow.				
j. Review the trend in cash flow from operations for the past five years and note any unusual fluctuations or negative trends between years.				
k. Review changes in the average number of days of unpaid claims in past years for unusual fluctuations or negative trends between years.				
l. Describe any material commitments for capital expenditures as of the end of the reporting period indicating the purpose, source of funds, changes in equity and debt, and any off-balance sheet financing arrangements.				
m. Compare cash flow from operations with the industry in order to identify significant deviations.				
n. Review other sources, including the Management’s Discussion and Analysis (MD&A) and the Asset Adequacy Analysis from the Statement of Actuarial Opinion (if required). Do concerns exist relating to cash flow and liquidity or asset adequacy?				

Related Party Exposure in the Investment Portfolio

#10. Assess related party exposure in the investment portfolio.

	Other Risks
<p>a. Review the Annual Financial Statement investment schedules, as disclosed in the column “Investments Involving Related Parties” and utilizing iSite+ tools, determine if the insurer has material related party exposures in its investment portfolio.</p> <p>This disclosure is included in:</p> <ul style="list-style-type: none">• Schedule B• Schedule BA• Schedule D• Schedule DA• Schedule DB• Schedule DL• Schedule E, Part 2 <p>Consider exposure by asset class and in aggregate, and by the role of the related party in the investment as designed by the “Investments Involving Related Parties” disclosure.</p>	LQ, MK
<p>b. If concerns exist regarding a material related party exposure in the investment portfolio, assess the credit quality of those investments involving related parties by reviewing designations, assessing historical default experience, etc.</p>	LQ, MK

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<p>c. If concerns exist regarding a material related party exposure in investment management or advisory services, consider the following:</p> <ul style="list-style-type: none"> i. Review the procedures in the “Additional Procedures” section below regarding Third Party Investment Advisors and consider their application to related party advisors in that role. ii. In addition to the additional analysis procedures regarding third party investment advisors, consider the following: <ul style="list-style-type: none"> 1. Review the insurer’s investment policy guidelines and determine whether the related party investments follow the guidelines and are in compliance with regulatory requirements. 2. Review whether the fee structure for asset management is fair, reasonable, and appropriately recognized as investment expenses. 3. If the related party asset manager also originates/securitizes investments held by the insurer, consider requesting additional information from the insurer to determine the following: <ul style="list-style-type: none"> a. Whether the asset manager has adequate experience and knowledge in originating and managing the types of investments; b. Whether the asset manager follows appropriate underwriting practices and applicable regulatory requirements in originating investments; and c. Whether the fee structures embedded in securities (if applicable) are fair, reasonable, and appropriately account for potential duplication of fees or conflicts of interest. 	OP
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Invested Asset Exposure to Climate Change Risk

11. Assess the potential impact of material climate change and/or transition and asset devaluation risk on the insurer’s invested asset portfolio.

	<i>Other Risks</i>
a. Review information provided in the insurer’s response to the NAIC’s Climate Risk and Disclosure Survey (if available) on its exposure to material climate change/energy transition risk and related mitigation activity in this area.	CR*, MK*
b. Review relevant information provided in the Own Risk and Solvency Assessment (ORSA) Summary Report, and/or U.S. Securities and Exchange Commission (SEC) 10-K or 10-Q filings (if available) that discusses the insurer’s exposure to material climate change/energy transition risk and related mitigation activity in this area.	CR*, MK*
c. Review information provided in the NAIC’s U.S. Insurance Industry Climate Affected Investment Analysis to identify potential concentrations in insurer exposure.	CR*, MK*

Additional Analysis and Follow-Up Procedures

Request and Assess the Insurer's Investment Policies and Strategies:

If concerns exist regarding the level of liquidity risk, request and review the insurer's investment strategy to determine if it is appropriately structured to support its ongoing business plan and cash flow needs. Review the guidelines outlined in the plan for:

- Quality of issues invested in and diversification standards pertaining to issuer, industry, duration, liquidity, geographic location, and issues/sectors exposed to material climate change, transition, and asset devaluation risks.
- Expected rate of returns on investments (projected investment income) compared to actual results.
- Planned increases in investment types, sectors and markets, etc.
- Appropriateness of the investment plan for the liability structure of the insurer. (This may require a review of asset adequacy analysis for asset liability matching (ALM) and discussion with the insurer's management to better understand its plan.)

Upon review of the investment plan, compare the plan to actual results. Does the insurer and its investment manager(s) appear to be adhering to the investment policies and guidelines in the investment plan?

Examination Findings:

Review the most recent examination report and Summary Review Memorandum (SRM) for any findings regarding liquidity risks associated with:

- Asset liability matching (ALM) and cash flow stress testing.
- Investment returns
- Climate change, transition, and asset devaluation.
- Effective management of the insurer's liquidity position.
- Other-than-temporary-impairments (OTTI)
- Investment valuation issues.
- Adherence to investment policies and strategies.
- Investment management, and use of and monitoring of external investment managers.
- Determine if liquidity concerns identified during the last exam have been addressed.

If outstanding issues are identified, perform follow-up procedures as necessary to address concerns.

NAIC Capital Market's Bureau Analytical Assistance:

Consider requesting the following analytical reviews:

- Review of the insurer's investment portfolio
- Review of Investment Management Agreements

Third-Party Investment Advisers:

Assess and determine if any concerns exist regarding third party investment advisers and associated contractual arrangements.

- Review Annual Financial Statement, General Interrogatories, Part 1, #29.05. Does the insurer utilize third party investment advisors, broker/dealer or individuals acting on behalf of the insurer with access to their

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investment accounts?

If “yes,” consider the following procedures:

- Review the results of the most recent financial examination work papers, follow-up and prospective risk information and the summary review memorandum provided by the examiners. Did the examination identify any issues with regard to investment advisers and associated contractual arrangements that require follow-up analysis or communication with the insurer? If “yes,” document the follow-up work performed.
- Compare Annual Financial Statement, General Interrogatories, Part 1, #29.05 for the current year to the prior year to determine if there have been any changes in advisors. If “yes,”
 - Consider obtaining an explanation for the change from the insurer.
 - Consider obtaining a copy of the new investment advisor agreement and review it for appropriate provisions.
- Using the information reported in Annual Financial Statement, General Interrogatories, Part 1, #29.05, obtain and review SEC Form ADV (if available), to determine if the investment advisor is in good standing with the SEC. If not in good standing, contact the insurer to request an explanation.
- If agreements with third party investment advisers are affiliated, have the appropriate Form D–Prior Notice of Transactions been filed and approved by the department? Were any concerns noted or follow-up monitoring recommended?
- Request information from the insurer regarding the background and expertise in structured securities of its investment advisors (in-house and/or contractual) and its analytical system capabilities. Determine whether the advisors and systems are adequate to allow the insurer to continuously monitor its structured securities investments.
- If the insurer uses an external asset manager, consider if investments on Schedule BA are invested in funds that are affiliated with the asset manager or are managed by that asset manager. Consider the following issues:
 - If any conflicts of interest exist
 - If the investment is appropriate for the insurer’s portfolio and is arm’s-length
 - If the insurer is paying double fees

Inquire of the Insurer:

If concerns exist, consider requesting information from the insurer regarding:

General Investment Inquiries:

- If management has adequately reviewed the investment portfolio and understand the yields, underlying collateral, cash flows and investment volatility.
- Any additional concentration by collateral type.
- Management’s process for valuing securities to assist analysts in assessing if the securities are valued appropriately.
- Management’s intended use of certain riskier investments and purpose within the insurer’s portfolio.
- If management has an appropriate level of knowledge and expertise with the type of securities being purchased/held.
- If the insurer has controls implemented to mitigate the risks associated with this investment type.

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- Sources of liquidity, such as letters of credit (LOCs).
- Information/explanation of guarantees or other commitments to PSA.
- Securities lending program (nature, size, reinvestment policies, etc.).
- Separate accounts plan descriptions and/or policy forms as they relate to its securities lending program.

Investment Diversification:

- Planned asset mix and diversification strategies

Mortgages:

- Handling of foreclosed mortgage loans

BA Assets:

- Current Audited Financial Statements and other documents (partnership agreements, etc.) necessary to support the value of the insurer's investment in partnerships and joint ventures.
- Information necessary to support the value of significant other invested assets other than partnerships and joint ventures.
- Current details on cash flows and returns for the different types of investments, especially hedge funds and private equity funds.

RMBS, CMBS and LBaSS:

- Percentage distribution and amounts of each type of RMBS, CMBS and LBaSS held; planned amortization class (PAC), support bonds, interest only (IO) tranches, and principle only (PO) tranches to evaluate the level of prepayment risk in the portfolio.
- Projected prepayment speeds on its RMBS portfolio and compare with historical prepayments, as well as the prepayment assumption at the time of purchase.

Own Risk and Solvency Assessment (ORSA) Summary Report:

If the insurer is required to file ORSA or part of a group that is required to file ORSA:

- Did the ORSA Summary Report analysis conducted by the lead state indicate any liquidity risks that require further monitoring or follow-up?
- Did the ORSA Summary Report analysis conducted by the lead state indicate any mitigating strategies for existing or prospective liquidity risks?
- For relevant business types, did the ORSA Summary Report analysis conducted by the lead state indicate any liquidity risks regarding catastrophic exposure and related mitigating strategies?

Holding Company Analysis:

- Did the Holding Company analysis conducted by the lead state indicate any liquidity risks impacting the insurer that require further monitoring or follow-up?
- Did the Holding Company analysis conducted by the lead state indicate any mitigating strategies for existing or prospective liquidity risks impacting the insurer?

Actuarial Filings, Including Asset Liability Matching (ALM):

- Did the review of the Statement of Actuarial Opinion or other actuarial filings indicate any concerns regarding the adequacy of ALM, cash flow stress testing and the sufficiency of assets to meet the business obligations of the insurer?
- If concerns are identified regarding overall liquidity of the asset portfolio, request a copy of the insurer's ALM policy and/or liquidity stress testing/scenario analysis.

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Example Prospective Risk Considerations		
Risk Components for IPS		Explanation of Risk Components
1	Overall liquidity is insufficient	The insurer does not hold sufficient liquid assets to meet current liabilities.
2	Illiquid assets are significant	Less liquid assets may be unavailable to pay policyholder claims as they are not easily or quickly marketable.
3	Significant affiliated investments balance	Investments in PSA may not be marketable and unavailable to pay policyholder claims.
4	Significant special deposits balance	Special deposit assets may be unavailable to pay policyholder claims.
5	Inability to produce positive cash flows from operations	Negative trends in cash flow from operations create liquidity needs that may result in sale of investments at a loss.
6	Trend of extraordinary dividends	High reliance by affiliated companies on dividends paid by the insurer representing an ongoing liquidity need.
7	Significant amount of [insert asset type] held with resale restrictions	Illiquidity of certain assets may be due to provisions of the asset, such as restrictions on resale (e.g., certain BA assets, such as investment hedge funds, may have time restrictions on when the investment can be sold/liquidated).
8	Significant amount of Schedule BA assets held with commitments/collateral requirements	BA assets may include commitments for additional funding, which is common in private equity funds. BA assets may have the potential to be required to post additional collateral, similar to variation margin for derivatives.
9	Expected cash flows from Schedule BA assets and types of other structured bonds	Certain BA assets and highly structured bonds— including RMBS, LBaSS and structured notes—may include liquidity risks where expected cash flows do not match actual.
10	Exposure to climate change, transition and asset devaluation risk	The insurer's investment portfolio is subject to prospective devaluation of the assets/changes in the asset return associated with its holdings of climate-affected assets.

III.B.3.c. Liquidity Risk Repository – Health Quarterly

Liquidity Risk: Inability to meet contractual obligations as they become due because of an inability to liquidate assets or obtain adequate funding without incurring unacceptable losses.

Note: The repository is not an all-inclusive list of possible procedures. Therefore, risks identified for which no procedure is available should be analyzed by the state insurance department based on the nature and scope of the risk. Also, note that key insurance operations or lines of business, for example, may have related risks addressed in different repositories. Therefore, analysts may need to review other repositories in conjunction with liquidity risk. For example:

- Investment assets classes (Bonds, Mortgages, etc.) are also discussed in Credit and/or Market Risk Repositories.

Analysis Documentation: Results of liquidity risk analysis should be documented in Section III: Risk Assessment of the insurer.

Liquidity of Investment Portfolio and Overall Liquidity

- Determine if there are any concerns regarding the liquidity of the insurer's asset portfolio and overall liquidity.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Change in liquid assets from prior year-end	CR	>75% or <-15%	[Data]	[Data]
b. Liquid assets and receivables to current liabilities ratio (excluding non-investment grade bonds)	CR	<200%		
c. Ratio of working capital to total assets	CR	<30%	[Data]	[Data]
				<i>Other Risks</i>
d. Review the Quarterly Financial Profile Report for changes in the ratio of total liabilities to liquid assets for unusual fluctuations or negative trends between years.				
e. If concerns are identified regarding overall liquidity of the asset portfolio, identify and assess other sources of liquidity available to the insurer. (Or, request information from the insurer if necessary. See Additional Analysis and Follow-Up Procedures below.)				
f. Assess the impact of market conditions through consideration of industry and economic events (i.e., news and industry analytics). Is the analyst aware of any market conditions that may threaten the liquidity of insurers' investment portfolios (e.g., market dislocation or other events that could affect the liquidity of assets classes, such as structured securities, structured notes, BA assets, non-investment grade bonds)?				

- Determine whether there are concerns due to the level of investment in Other (Schedule BA) invested assets.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Ratio of Schedule BA assets to capital and surplus	CR, MK	>5%	[Data]	[Data]
b. Increase in Schedule BA assets from the prior year-end, where the ratio of BA assets to capital and surplus is greater than 5%	CR*, MK*	>10%	[Data]	[Data]

III.B.3.c. Liquidity Risk Repository – Health Quarterly

Affiliated Investments

3. Determine whether investments in affiliates are significant.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Total of all investments in affiliates to capital and surplus [Quarterly Financial Statement, General Interrogatories, Part 1, #14]	CR, MK*	>20%	[Data]	[Data]
b. Change in total of all investments in affiliates from the prior year-end	CR, MK*	>20% or <-20%	[Data]	[Data]
c. Change in any category of affiliated investments from the prior year-end	CR, MK*	>10% or <-10%	[Data]	[Data]
				<i>Other Risks</i>
d. Review the results of the Holding Company Analysis completed by the lead state to determine if any concerns exist regarding affiliated entities.				CR, MK
e. Review Quarterly Financial Statement, Notes to Financial Statements, #10 and #14, if reported, to identify if the insurer is subject to any guarantees or other commitments to parent, subsidiaries or affiliates (PSA). If the guarantee or commitment is material to the insurer, assess the nature of the agreement and the financial strength of the PSA.				CR

Other Receivables

4. Review and assess furniture, equipment and supplies and EDP equipment.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Ratio of admitted furniture, equipment and supplies to capital and surplus		>5%	[Data]	[Data]
b. Change in admitted balance of furniture, equipment and supplies from the prior year-end		>10% or <-10%	[Data]	[Data]
c. Ratio of admitted EDP equipment and software to capital and surplus		>3%	[Data]	[Data]
d. Change in admitted balance of EDP equipment and software from the prior year-end		>25% or <-25%	[Data]	[Data]

Cash Flow from Operations

5. Review cash flow from operations and determine if any concerns exist.

	<i>Other Risks</i>	<i>Benchmark</i>	<i>Result</i>	<i>Outside Benchmark</i>
a. Ratio of net cash from operations to capital and surplus		<-5%	[Data]	[Data]
b. Decline in net cash flow from operations from the prior year-to-date to capital and surplus		>5%	[Data]	[Data]

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c. Ratio of benefits and loss related payments to premiums collected net of reinsurance		>85%	[Data]	[Data]
				<i>Other Risks</i>
d. Review the cash flow from operations to determine the underlying cause of the negative cash flow (if any).				
e. Review the trend in cash flow from operations for the past five periods and note any unusual fluctuations or negative trends between years.				

Liquidity Risk Assessment

Liquidity Risk: Inability to meet contractual obligations as they become due because of an inability to liquidate assets or obtain adequate funding without incurring unacceptable losses.

The objective of the Liquidity Risk Assessment analysis is focused primarily on overall liquidity, liquidity of investments, receivables, and cash flow from operations. The following discussion of procedures provides suggested data, benchmarks and procedures analysts can consider in his/her review. In analyzing liquidity risk, analysts may analyze specific types of investments and receivables held by insurers. An analyst's risk-focused assessment of liquidity risk should take into consideration the following areas (but not be limited to):

- Liquidity ratios/metrics
- Liquidity of certain investments, including private placement bonds and common stock, highly structured investments, investments on Schedule BA, and affiliated investments
- Liquidity of certain receivables, including health care receivables and special deposits
- Cash flow from operations
- Stockholder dividends
- Surrender and withdrawal activity for life insurers

Overview of Investments

Refer to IV.A. Supplemental Analysis Guidance – Financial Analysis and Reporting Considerations for general information and a primer on derivatives.

Overview of Cash Flows

Cash Flow is one of several core financial statements presented in the Annual Financial Statement of property/casualty insurers. It provides information about the primary sources of cash (inflow) and applications of cash (outflow). Cash Flow is organized to readily identify the net cash flow from operations separately from the net cash flow from investments. Other important sources and applications of cash are also shown, such as dividends to stockholders. The net change in cash and short-term investments, as reflected on Cash Flow, reconciles to the change in the balance sheet accounts of cash and short-term investments for the year.

While Cash Flow provides information about historical sources and applications of cash, analysts should analyze the liquidity of the balance sheet in its entirety in order to evaluate the insurer's ability to fund loss reserves and other demands for cash in the future. One common way of accomplishing this is to compare the total adjusted liabilities of the insurer in relation to its liquid assets.

Liquidity of Health Entities

There are a number of situations that can elevate the risk of a negative impact on a health entity's cash flow and liquidity including the credit risk of receivables, the level of borrowed money and other liabilities, and dividends to shareholders. For example, if a health entity relies heavily on risk transfer arrangements with provider groups and the parties involved in the arrangements are unable to meet their obligations, the collectability of those obligations could negatively impact the liquidity of the health entity. Credit risk is a concern for other receivables as well, including amounts due from affiliates and reinsurance receivables. An analyst should be aware of the domiciliary state's requirements for downstream risks such as provider groups and reinsurance. Other situations involve significant increases in liabilities such as unpaid claim reserves or borrowed money, which can increase the health entity's short-term cash requirements. Additional cash would also be needed in order for the health entity to pay dividends to a parent company or other shareholder.

III.B.3.d. Liquidity Risk Repository – Analyst Reference Guide

Health entities have a shorter benefit payout period than other insurers, and consequently understanding the need for liquidity is an important issue for management. Because a health entity writes short-tail business, it will generally have a shorter average maturity on its bonds and hold more cash and short-term investments than other insurers. The key liquidity risks to a health entity include substantial declines in enrollment, underpricing, and spikes in claims. If this were to occur, the entity's cash outflows for claims payments would exceed its inflows from newly received premiums. However, a health entity with a relatively stable enrollment and claims experience within expectations may feel it can safely accept some durational mismatch between its assets and liabilities and may invest in more long-term invested assets in order to increase its investment yield. Those health entities writing long-tailed business may also own long-term invested assets to support those lines' liabilities.

Discussion of Annual Procedures

Using the Repository

The liquidity risk repository is a list of possible quantitative and qualitative procedures, including specific data elements, benchmarks and procedures from which analysts may select to use in his/her review of liquidity risk. Analysts are not expected to respond to all procedures, data or benchmark results listed in the repository. Rather analysts and supervisors should use their expertise, knowledge of the insurer and professional judgement to tailor the analysis to address the specific risks of the insurer and document completion of the analysis. The repository is not an all-inclusive list of possible procedures. Therefore, risks identified for which no procedure is available should be analyzed by the state insurance department based on the nature and scope of the risk.

In using procedures in the repository, analysts should review the results in conjunction with the Supervisory Plan and Insurer Profile Summary and the prior period analysis. Communication and/or coordination with other internal departments are a critical step in the overall risk assessment process and are a crucial consideration in the review of certain procedures in the repository.

Analysts should also consider the insurer's corporate governance which includes the assessment of the risk environment facing the insurer in order to identify current or prospective solvency risks, oversight provided by the board of directors and the effectiveness of management, including the code of conduct established by the board.

The placement of the following data and procedures in the liquidity risk repository is based on "best fit." Analysts should use their professional judgement in categorizing risks when documenting results of the analysis. Key insurance operations or lines of business, for example, may have related risks addressed in different repositories. Therefore, analysts may need to review other repositories in conjunction with liquidity risk.

ANALYSIS DOCUMENTATION: Results of liquidity risk analysis should be documented in Section III: Risk Assessment of the insurer. Documentation of the risk assessment analysis should be sufficiently robust to explain the risks and reflect the strengths and weaknesses of the insurer. Analysts are not expected to respond to procedures, data or benchmark results directly in the repository document.

Quantitative and Qualitative Data and Procedures

Liquidity of Investment Portfolio and Overall Liquidity

<i>Property & Casualty #</i>	<i>Life/A&H/Fraternal #</i>	<i>Health #</i>
1, 2, 3, 4	1, 2, 3, 4, 5	1, 2, 3, 4, 5

EXPLANATION: The procedures assist analysts in evaluating the insurer's overall liquidity. The primary method of accomplishing this is to review changes in the insurer's liquid assets and results of liquidity ratios/metrics.

III.B.3.d. Liquidity Risk Repository – Analyst Reference Guide

ADDITIONAL REVIEW CONSIDERATIONS: Assess how the insurer's liquidity trends over years. An analyst may also consider liquidity results compared to industry averages (some ratios are included in the Financial Profile Report) and peer companies that have similar business mix, asset size, and asset composition.

FOR PROPERTY/CASUALTY (P/C) INSURERS: The liquidity ratio calculation (#1a) compares the insurer's adjusted liabilities with its liquid assets available to fund such liabilities in the future. Affiliated holdings are removed from liquid assets because these investments are considered less liquid and may not be readily converted to cash for paying claims. Analysts should also consider reviewing the five-year trend of liquidity within the Financial Profile Report and identifying any significant fluctuations and the underlying cause(s) for those fluctuations.

FOR LIFE INSURERS: #1g advises that analysts should be aware that stress liquidity inquiries and templates are included in the NAIC *Financial Condition Examiners Handbook*. Information captured in these templates is considered confidential; therefore, it is not captured within the annual financial statements. In order to obtain this information, regulators must request that reporting entities complete the forms. As noted in the *Examiners Handbook*, requests for reporting entities to complete these templates may occur at any time and are not limited to instances of comprehensive statutory examinations. Analysts should communicate with the examiner to determine if the insurer has recently submitted responses to the stress liquidity inquiries and templates or if a request should be made to the insurer for the information.

FOR HEALTH ENTITIES:

- #1 assists analysts in evaluating the health entity's overall balance sheet liquidity. The primary method of accomplishing this is to compare the health entity's liabilities with its liquid assets available to fund such liabilities in the future. However, as previously mentioned, various other comparisons can be used to help assess liquidity or potential liquidity concerns. Liquid assets in this calculation include all bonds but exclude affiliated investments.
- #1a and 1g assist analysts in determining a health entity's ability to pay maturing obligations with cash and invested assets. A significant increase in the liabilities to liquid assets ratio could indicate the health entity's growing inability to satisfy its financial obligations without having to sell long-term investments. Liquid assets in this calculation include all bonds but exclude affiliated investments.
- #1b alerts analysts to fluctuations in total liquid assets. A significant increase in total liquid assets could indicate that the health entity has been unable to collect on receivables. If the change is significant, an analyst may consider a more detailed review of the change in the asset mix from the prior period to determine the cause of the fluctuation.
- #1c measures the health entity's ability to pay current obligations with current assets including marketable securities. Results of less than 200 percent may not pose a serious threat to the health entity if it has access to other assets that can be liquidated. This ratio excludes non-investment grade bonds and affiliated investments but includes certain receivables not included in the two procedures above.

FOR HEALTH ENTITIES: #4 requires analysts to review the Z-Score analysis included in the Annual Financial Profile. The Z-Score is a way to measure and monitor financial performance by analyzing specific ratios over a period of time. If a result of less than 2.6 occurs, analysts should consider reviewing the individual ratios within the Z-Score. An unstable trend of the Z-Score or a low Z-Score may indicate increased risk to the solvency of the health entity and analysts should take a closer look at each of the ratio results in the Financial Profile. There are four ratios in the Z-Score; however, the Z-Score places the most emphasis on working capital and earnings. The following briefly explains each ratio within the Z-Score, although more detail is available in the link to the *Z-Score Document* on iSite+.

- Working Capital to Total Assets measures the ability of a health entity to manage working capital, which is fundamental for all business. While a health entity may have sufficient surplus, they may have insufficient working capital to pay claims due to related party transactions and other non-liquid long-term investments. Analysts should also consider that while working capital may be above the threshold, it may still not provide a sufficient cushion for significant unexpected losses. Refer to the discussion of procedure #1c above.

III.B.3.d. Liquidity Risk Repository – Analyst Reference Guide

- Retained Equity to Total Assets reflects the age of the business and the philosophy of management. This assumes that a more mature business would normally have more capital and surplus. Companies that have been in business fewer years and have insufficient management experience tend to have higher failure rates.
- Earnings Before Interest & Taxes (EBIT) to Total Assets measures a health entity's earnings performance. This ratio is weighted the highest for several reasons including the following: 1) significant shifts in earnings may indicate a highly risky industry with unstable cash flows; 2) health entities must balance consumer demands with cost management; and 3) Medicare and Medicaid programs and other outside factors can have a significant impact on the health entity's financial condition.
- Capital and Surplus to Total Liabilities is the leverage measure within the Z-Score and is the inverse of the traditional debt to equity ratio.

RESTRICTED ASSETS (LIFE #1C, P/C #1C, HEALTH #1D): Assessment of materiality of restricted assets is intended to determine if any liquidity concerns exist regarding the level of assets not under the insurer's exclusive control. Analysts should review General Interrogatories and Notes to the Financial Statement #5 to determine the reason the assets are not under the insurer's exclusive control (e.g., loaned to others, subject to repurchase or reverse repurchase agreements, pledged as collateral, placed under option agreements) and who holds the assets in order to evaluate whether there are liquidity concerns. Analysts should also consider the potential for pledging additional assets, as in variation margin requirements for derivatives transactions.

PRIVATE PLACEMENT BONDS (#3): Significant investments in privately-placed bonds may cause concerns regarding the insurer's liquidity because some of these investments cannot be resold, while those that can be resold have restrictions on whom they can be sold to, including restrictions under securities laws. There is no structured market for privately-placed bonds like there is for publicly-traded bonds. Therefore, even if the privately-placed bonds can be sold, it may be difficult to find a willing buyer.

ADDITIONAL REVIEW CONSIDERATIONS FOR PRIVATE PLACEMENT BONDS: Review Annual Financial Statement, Schedule D – Part 1A – Section 1 to determine the amount, issue type, NAIC designations, maturity distribution of privately-placed bonds owned, and the amount of privately placed bonds that are freely tradeable under U.S. Securities and Exchange Commission (SEC) Rule 144 or qualified for resale under SEC Rule 144A.

Securities Lending

<i>Property/Casualty #</i>	<i>Life/A&H/Fraternal #</i>	<i>Health #</i>
5	6	N/A

EXPLANATION: The procedure assists analysts in determining if concerns exist regarding the materiality of securities lending activity and the nature of the reinvested collateral.

Separate Accounts

<i>Property/Casualty #</i>	<i>Life/A&H/Fraternal #</i>	<i>Health #</i>
N/A	7	N/A

EXPLANATION: The procedure assists analysts in determining the materiality of separate account assets in order to determine the potential impact on the liquidity of the insurer in the event of large withdrawals from separate accounts.

III.B.3.d. Liquidity Risk Repository – Analyst Reference Guide

Affiliated Investments

<i>Property & Casualty #</i>	<i>Life/A&H/Fraternal #</i>	<i>Health #</i>
6	8	6

EXPLANATION: The procedure assists analysts in determining whether investments in affiliates are significant. The procedure measures the extent to which capital and surplus relies on assets that are due from affiliated entities because affiliated investments are often illiquid. Excessive affiliated investments and receivables may indicate the insurer has invested heavily in affiliated stock and bonds instead of cash or short-term investments and may also indicate an affiliate's inability to pay current amounts due. Analysts may consider reviewing and understanding the financial statement of the affiliate.

Other Receivables

<i>Property/Casualty #</i>	<i>Life/A&H/Fraternal #</i>	<i>Health #</i>
N/A	N/A	7

EXPLANATION: The procedures assist analysts in reviewing assets of a health entity that may have limited marketability.

FURNITURE AND EQUIPMENT:

Furniture and equipment includes not only administrative furniture and equipment but also health care delivery assets such as furniture, medical equipment and fixtures, pharmaceuticals and surgical supplies, and durable medical equipment.

Statement of Statutory Accounting Principles (SSAP) No. 73—Health Care Delivery Assets and Leasehold Improvements in Health Care Facilities describes health care delivery assets as those assets that are used in connection with the direct delivery of health care services in facilities owned or operated by the health entity. SSAP No. 73 further provides that these types of assets shall be admitted provided they meet the definitions of health care delivery assets as set forth in the SSAP. As a result of this accounting guidance, it is possible that a health entity with these types of assets will have a much different mix of assets than other health entities that do not use these types of assets in its operations. It should be noted that the depreciation period for health care delivery assets is limited to three years, which varies from the depreciation period for similar assets that are non-admitted.

Analysis of these assets should consist primarily of ongoing monitoring of the balances, the relative change, and the relationship of that change with what is expected based upon other trends/activity within the health entity.

ELECTRONIC DATA PROCESSING EQUIPMENT AND SOFTWARE:

As discussed in SSAP No. 16R—*Electronic Data Processing Equipment and Software*, electronic data processing (EDP) equipment and operating system software are admitted assets to the extent they conform to the requirements of SSAP No. 4—*Assets and Nonadmitted Assets*. The admitted asset is limited to three percent of capital and surplus; adjusted to exclude any EDP equipment and software, net deferred tax assets and net positive goodwill. However, SSAP No. 16R provides that non-operating system software is a non-admitted asset. EDP equipment and software depreciated for a period not to exceed three years using methods detailed in SSAP No. 19—*Furniture, Fixtures, Equipment and Leasehold Improvements*.

EDP assets generally are subject to various state specific limitations, such as a minimum amount that can be capitalized as an asset, a maximum depreciable life, and/or limits that may be admitted as a percentage of total admitted assets or capital and surplus. These limitations are put in place to avoid undue concentrations of assets that have less marketability than other admitted assets and rapid technological obsolescence. Because of this, the amount reported by a health entity is generally limited to an amount that is not significantly material to the health entity's financial position. It is also common to find that the health entity reports no EDP assets. In these