

To: Group Solvency Issues (EX) Working Group
From: Louis K. Quan, Chief, Financial Analysis Division, California Department of Insurance
Date: October 11, 2010
Re: Request for Comment - Group Capital Assessment Options

Please find below California's comments:

Option One - Legal Entity RBC Adjustments

We would think that RBC needs to account for the risks of being in a group. We are not sure how this can be quantified, but the risk, including reputational risk does exist.

Option Two – Group Capital Analysis through ORSA

We think that that ORSA can be a solvency tool, but it should be one of a package a tools rather than the determinative tool of a group RBC calculation. The individual company must still comply with the individual insurer.

Option Three – Group Capital Calculations

In the case of a parent holding company, we agree with this method of analysis leading to discussions with the group relative to its risk. We do not think that we can currently favor use of a group RBC due to the open issue of “fungibility of capital”.

To: Group Solvency Issues (EX) Working Group

From: Jim Hanson, Illinois Department of Insurance

Date: October 14, 2010

Subject: Response to NAIC group capital assessment proposal

With regard to the three options, IL responses are:

Option 1 – Disagree

Option 2 – Disagree

Option 3 – Disagree with first bullet, agree with the second bullet

To: Group Solvency Issues Working Group

From: Ken Abitz, Kansas Department of Insurance

Date: October 11, 2010

Subject: Response to NAIC group capital assessment proposal

With regard to the three options, KS responses are:

1. Agree
2. Agree
3. Disagree

To: Group Solvency Issues (EX) Working Group

From: Dan Kosmicki, CFE, Assistant Chief Examiner, Nebraska Department of Insurance

Date: Oct. 13, 2010

RE: Group Capital Assessment Options

Option 1 – yes, the current legal entity RBC assessment of insurers should not be ignored in a group-wide assessment, the current RBC measurement would need some significant adjustments to account for the many various risks exposures by the various industry sectors that are a part of many diverse holding company structures. There is some validity to such an approach, although such an approach may not be a practical or a consistent measurement assessment but simply a good measurement of a group over a long period of time, and may not be able to provide much of a take on what is happening within all or each of the specific legal entities comprising the group.

Approach likely to end up being merely another tool to identify trends (after the fact) based on historical data if done on a summarized group data .

Option 2 – yes, as a useful tool although not as a sole assessment measure. There is some validity to such approach. This approach may be able to provide insight into various risk exposures within the various sectors/industries within a group. A Company might be able to explain in narrative form its risks which exist today or are anticipated in the future and which cannot otherwise be easily quantified in today's terms.

Option 3 – No, comments similar to option 1 plus it would be difficult to justify and to impose insurance industry capital standards on other industries that compromise a large diverse holding company structure. The time and effort to do this type of assessment approach may provide an end product which lacks consistency, usefulness and meaning. Would likely require many years of calculations adjustments to develop the formulas in order to arrive at a workable product for one year results, and would require many annual changes thereafter to the formula based on the ever changing world we live in. If such an approach is utilized, are insurance regulators going to debate the validity of non-insurance and other changes environmental factors on a regular basis?

From: Tim Nauheimer, New York State Insurance Dept
To: Group Solvency Issues Working Group
Subject: Request for Comment - Group Capital Assessment Options
Date: Oct 12, 2010

I would like to explore Group Capital Calculations combined with ORSA. Where the parent is a Holding Co. the material or significant risks of the non-insurance entities could be quantified by applying ORSA. Where the parent is an insurer, we can use the existing RBC and incorporate other countries' capital requirements akin to Canada's MCCSR. Additionally, as far as the consolidated method vs the aggregation method, the aggregation method would be preferred with an adjustment for alien entities that have different capital requirements.

To: Group Solvency Issues (EX) Working Group

From: Jim Odiorne, Deputy Insurance Commissioner, Washington State Office of the Insurance Commissioner

Date: Oct. 4, 2010

RE: Comments on a document containing three possible options for group capital assessment.

Based on information currently available and our best estimate of resource availability in the next five years, we believe that a rules based approach to group capital assessment is a more viable option. Of the two rules based options presented, it appears to us that option 3 may present the best possibility of adoption and implementation.

Washington, and we believe a majority of other states, is currently facing significant budget short fall. Even though the short fall (currently estimated to be at least \$4 billion) is only in the general fund, not affecting OIC funding, the atmosphere is such that any increase in our resources is highly unlikely in the near term.

We must also recognize that all three options presented will also require resource commitments from the regulated community. That community, like regulators, is suffering the effects of a financial crisis, from which recovery appears to be very slow.

We believe that the more focus is placed on principles based regulation, the more resources, both regulator and regulated, will be required for development, implementation, and maintenance. A principles based approach will likely require skill sets not generally available to U.S. insurance regulators. Obtaining those skill sets will be resource intensive.

Option 3 seems to us to build on tools and skill sets currently available. This option seems to be less resource intensive, which suggests a better possibility for adoption and implementation.

Option 3 also sends the message that we are willing to change, even if slowly. This option also lends itself as an interim step toward more principles based regulation, if that is the direction ultimately taken by SMI. It seems that we could move from Option 3 to a more principles based approach in the future.



AMERICAN ACADEMY *of* ACTUARIES

October 11, 2010

Ann M. Frohman, Co-Chair
Danny Saenz, Co-Chair
Group Solvency Issues (EX) Working Group
Via email: David Vacca (dvacca@naic.org)

Re: Comments on Group Capital Assessment Options paper

The American Academy of Actuaries¹ Risk Management and Solvency Committee and its Enterprise Risk Management Subcommittee are pleased to present comments on the Group Capital Assessment Options Paper. These comments also include input from other interested Academy groups. Our comments are brief in recognition that this project is just beginning.

We agree with the IAIS core principles that there are numerous valid approaches to group capital assessment. It will be a challenge to identify and measure insurance risks from non-insurance members of a group unless those risks originate under an insurance holding company. However risk professionals must be able to assess the risk exposure if that risk can affect the insurance entity. If they are part, for instance, of a parent holding company then capital assessment would most likely treat those risks separately from any calculation of capital for the subsidiary insurance company. This is especially true when the differences between the general purposes accounting statements of the holding company are not necessarily consistent with the statutory statements of the US insurer affiliates/subsidiaries. The concept of an ORSA or some similar report could be adopted to address these issues.

Due to the uniqueness of groups of entities that include insurers, we believe that the ORSA-approach is the most logical of the options being considered for group capital assessment. Groups and holding companies will have different characteristics regarding centralization, management controls, board expertise, non-insurance entities, and non-US enterprises. None of the other options offer the flexibility to address each of these differences.

We feel strongly that any proposed option must require that each insurance subsidiary have enough capital to meet the minimum requirements of its regulatory domicile. Permitting lower capital in one subsidiary in recognition of higher capital in another or at the parent level would seem unwise to us. Customers need to be treated equally in the case of wind up; a firm, legally enforceable agreement among the companies in the group must exist so that regulators can, without interference, have access to capital in another company. However, when dealing with individual scenarios, the needs of capital in one insurer may create additional (or reduced) capital or increased (or decreased) margins in other insurers or affiliates. This issue of diversification is complex, but should not just be ignored.

¹ The American Academy of Actuaries (“Academy”) is a 17,000-member professional association whose mission is to serve the public on behalf of the U.S. actuarial profession. The Academy assists public policymakers on all levels by providing leadership, objective expertise, and actuarial advice on risk and financial security issues. The Academy also sets qualification, practice, and professionalism standards for actuaries in the United States.

An adjustment to RBC would not be sufficient in our view to address the individual and complex nature of the access to capital and diversification issues. For these issues and such risks as reputational risk, contagion risk, and enterprise risk, evaluations are better handled outside of formulaic RBC using tools similar to ORSA. A regulator could consider aggregating all insurance entities whether they are in the same holding company or not, but we don't think this would provide significant useful insight.

With regard to expanding the use of other countries' capital requirements beyond Canada, that is a question that could be researched. For now, however, we don't recommend a move in this direction.

While the "phantom" Parent Holding Company is feasible, it is unclear what benefits would exist without the regulator having solvency authority over an additional legal entity and the ability to mandate how the capital is determined. In using this option, evaluations should be based on direct interaction between a company and its regulator rather than incorporated into the RBC calculation.

A significant concern will be exactly how groups are supervised. Which regulator will have jurisdiction? Does the NAIC have jurisdiction to address group solvency? Will all regulators follow the direction of the lead regulator?

If you have any questions, or would like to discuss this further, please contact Tina Getachew, Senior Policy Analyst, Risk Management and Financial Reporting Council, by phone (+1 202/332-5958) or email (getachew@actuary.org). Thank you again for this opportunity to provide input.

Sincerely,



Thomas Herget
Chair, Risk Management and Solvency Committee
Risk Management and Financial Reporting Council
American Academy of Actuaries



Robert Neill

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October 11, 2010

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Nebraska Department of Insurance
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Sr. Associate Commissioner Danny Saenz
Texas Department of Insurance
P.O. Box 149104
Austin, TX 78714-9104

Via E-mail

Re: Comments on the NAIC Request for Comment on Group Capital Assessment Options

Dear Director Frohman and Senior Associate Commissioner Saenz:

We appreciate the opportunity to respond to the NAIC Group Solvency Issues Working Group's Request for Comment on Group Capital Assessment Options. We support careful consideration and a full discussion of the need for and an appropriate approach to group capital assessment and we suggest such be conducted in consultation with the NAIC International Solvency Task Force, Capital Adequacy Task Force, Principles-Based Reserving Working Group, and the industry.

Overview

As recognized by the IAIS, ACLI believes that any group capital assessment must take into account how an insurer operates, *i.e.*, on a legal entity or on a consolidated group basis. Under any approach group-wide solvency assessment should be applied in a way that properly aligns with the risk and operational characteristics of the group and its members. Diversification benefits should be recognized to the full extent they can be demonstrated to the group supervisor.

The primary focus of prudential regulation in the U.S. should be on the setting of the total financial resources requirement necessary to substantially ensure the solvency of the insurer so that it can continue to meet its insurance obligations at all times. It would be useful for regulators in their overall risk assessment of insurers to understand and consider the full range of capital management techniques and methodologies available to and used by insurers. We further suggest regulators should rely upon CRO risk assessments, with details available upon request, rather than mandating broad initial filings that would inundate insurance departments with volumes of detailed assumptions and other technical analysis.

ACLI Solvency Principles and Application Guidance contain principles important to our members that relate to group capital assessment:

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- Solvency assessment standards for insurance groups should recognize the interaction and correlation of all risks across an insurance group and the degree of capital mobility within an insurance group.
- A solvency assessment system should require an insurer to have a sound process for assessing its capital adequacy in relation to its risk profile. That process should be qualitative, forward-looking, judgment-based, iterative, and appropriate to the nature, scale, and complexity of each insurer.
- The solvency assessment system should also reward insurers by providing incentives for insurers to embed such a process in their cultures.
- We believe that detailed prescriptive standards are inappropriate.

Group Capital Assessment Options

We offer the following comments on the various group capital assessment options identified by the Working Group.

Legal Entity RBC Adjustments

We believe that requiring the legal entity to take into consideration the risk of being part of a group is already largely being addressed through recent changes to the risk-focused surveillance process incorporated into the NAIC Financial Examiners Handbook effective this year and currently being implemented in the states. We suggest that acquiring and sharing examiner's and insurer's experience with this new exam process is a critical first step in assessing risks that membership in a group may pose to an insurer. Further, if regulators are currently modifying legal entity capital requirements to "measure the material risks arising from being part of a group" as indicated in the background on U.S. state insurance group capital considerations we urge that the assumptions and methods used to do so be disclosed and discussed. We question the practicality of quantifying reputational or contagion risks in setting capital standards and suggest that a reference to enterprise risk is more appropriate.

We don't believe the foundation for a productive discussion of a group capital requirement exists currently; thus we also question the need for the creation of a "uniform and consolidated group statement" and strongly encourage careful consideration of any consolidated statement in light of existing examination authority and voluminous financial filings already submitted. Insurers should not be required to create new financial statements that would not otherwise be prepared, and are potentially duplicative of existing statements. ACLI member companies are committed to providing necessary financial information to their regulators; however, creating such new financial statements where they are not already available could require an unnecessary, multi-year massive dedication of resources and expense.

Group Capital Analysis through ORSA

ACLI recently submitted comprehensive preliminary comments on the currently titled "Own Risk and Solvency Assessment" (ORSA) being developed by the NAIC International Solvency (EX) Working Group (attached). In the letter, ACLI urges further discussion of its definition, value added, and related costs within the context of the current and evolving framework of U.S. insurance regulation.

We suggest that first a gap analysis should be conducted identifying any gaps in current U.S. insurance regulation, and that an ORSA be tailored to any identified gaps. That process would help our collective understanding of any such tool and therefore improve its usefulness to all. We are concerned that, absent such a process, an ORSA may add to the cost and complexity of U.S. regulation without providing commensurate benefits to policyholders. In light of the recent changes to the risk-focused exam

process that NAIC has already implemented this year that already supplement insurance regulators' access to information in a financial exam, an ORSA analysis is premature.

Group Capital Calculation

We suggest that the group capital calculation approach is not workable in the near term. It appears to be a concept that would require significant advance work to implement and that raises practical questions about the definitions of key terms and how the calculations would be applied under the current RBC framework.

Conclusion

We look forward to further discussions with Working Group of an appropriate approach to group capital assessment.

Sincerely,

A handwritten signature in black ink, appearing to read "Robert H. Neill, Jr.", written in a cursive style.

Robert H. Neill, Jr.

cc: David A. Vacca, CPA
Assistant Director, Insurance Analysis and Information Services Department
NAIC Regulatory Services Division



Financial Security. For Life.

Carolyn Cobb

Vice President & Associate General Counsel

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October 4, 2010

Director Christina Urias

Chair of the NAIC International Solvency (EX) Working Group

kdefrain@naic.org

Dear Director Urias:

The American Council of Life Insurers (ACLI) represents more than 300 legal reserve life insurer and fraternal benefit society member companies operating in the United States. These member companies represent over 90% of the assets and premiums of the U.S life insurance and annuity industry. We appreciate the opportunity to offer our comments on the Working Group's Consultation Paper (CP) on Own Risk and Solvency Assessment (ORSA) on their behalf.

ACLI commends the NAIC on undertaking the Solvency Modernization Initiative. Our members welcome the deliberative process that you and the Working Group have adopted for considering the value to U.S. insurance regulators of aspects of other solvency regimes. That is particularly true with respect to an ORSA, as we have some reservations about its necessity within the context of U.S. insurance regulation. While we have not opposed the IAIS's high-level endorsement of an ORSA, we urge further discussion of its definition, value added, and related costs within the context of the current and evolving framework of U.S. insurance regulation. We note that the IMF's May 2010 Detailed Assessment of Observance of IAIS Insurance Core Principles did not include any recommendation for an ORSA.

Prior to implementing a procedure designed under a different regulatory regime, we suggest that the Working Group (WG) begin with a gap analysis, that is, by clearly identifying the gaps in current U.S. insurance regulation that the WG believes should be filled. Once the gaps are clearly identified, the next step would be to propose a definition of an ORSA tailored to any identified gaps. That process would help our collective understanding of any such tool and therefore improve its usefulness to us all. We are concerned that, absent such a process, an ORSA (however defined) may add to the cost and complexity of U.S. regulation without providing commensurate benefits to policyholders.

ACLI has previously shared with you our Solvency Principles and Application Guidance. It contains views that may be related to issues raised in the CP—

- A solvency assessment system should require an insurer to have a sound process for assessing its capital adequacy in relation to its risk profile. That process should be qualitative, forward-looking, judgment-based, iterative, and appropriate to the nature, scale, and complexity of each insurer.
- The solvency assessment system should also reward insurers by providing incentives for insurers that embed such a process in their cultures
- We believe that detailed prescriptive standards are inappropriate for an ORSA.

If the gap analysis shows need for an ORSA, we hope to refine these views and those in the attached responses in discussion with you and the Working Group. We wish to be as constructive as we can,

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given the breadth of our membership and the importance of these issues to them and to the perception of the quality of U.S. insurance regulation.

We look forward to discussing these important issues with you and with the Working Group.

NAIC Questions:

- 1) A. Content: What content should be included in the ORSA/ERM tool about RISK MANAGEMENT?
Risk and Risk Management "Description"
- a. Description of risk management and the process used to assess, monitor, and communicate risk. Explanation of how (or if) the report and its results ties to a company's management of the business. Note: Whether the report is required to tie to the company's management is identified as a topic for future decision.
 - b. Risk appetite, tolerances, and/or limits
 - c. Identification of significant risks faced by the insurer (underwriting, marketing, credit, investment, catastrophe, operational – including disaster recovery/business continuity risks, contagion, reputation, liquidity – including asset-liability management and cash flow and market value volatility, legal, reinsurance, reserving, concentration, and operational risk.)
 - d. Identification of emerging risks
 - e. New actions taken by the company that will impact the risk profile.
 - f.1. Recent changes that have occurred to the risk profile.
 - f.2. Risk Mitigation description – reinsurance, securitization, pooling, etc.
 - g. Contingency plans (actions the company expects to take under different circumstances).

ACLI: The factors listed above (a through g) might be part of an individual insurer's overall, judgment-based evaluation of its risks. We might discuss, for example, whether a certification from an insurer's chief risk officer—written at a very high-level—might be an appropriate means of assuring a domiciliary regulator that the insurer has incorporated such a process. Confidentiality of any such information would be key, and our members believe that the submission process must be flexible enough to accept insurers' reports as they exist currently.

ACLI: We believe that risk sensitive regulatory financial requirements should provide the incentive for optimal alignment of risk and capital management by the insurer and by the regulator. We view this feature as critical. We might discuss, for example, rewarding insurers that have successfully incorporated the risk management process into their cultures.

Risk "Quantitative"

- h. Quantification/Assessment of each significant risk, assumptions used, sensitivity of assumptions, changes made to assumptions and the impact of such, etc.
- i. Forward-looking Stress Testing, Description and Results
- j. Forward-looking Scenario Testing, Description and Results
- k. Trends
- l. Documentation of any internal models used (e.g. overview of model, impact of significant assumptions)
- m. Identification of any insurers in the group that have triggered an RBC action or control level and how that is considered in the insurer's risk management.

ACLI emphasizes that an ORSA, as we have described it, would be essentially and fundamentally a qualitative assessment—not a quantitative process. The primary tool of prudential regulation in the U.S. should be on the setting of the total financial resources requirement that is necessary to substantially ensure the solvency of the insurer so that it can continue to meet its insurance obligations at all times. It would be useful for regulators in their overall risk assessment of insurers to understand and consider the full range of capital management techniques and methodologies available to and used by insurers.

As above, we suggest that we should discuss relying upon CRO risk assessment, with detail available upon request, rather than inundating insurance departments with large volumes of detailed assumptions and other technical analysis, would be the most effective and efficient way to incorporate this perspective.

Risk and Risk Management “Other?”

m. Are there any other risk/risk management items that should be included?

B. Content: What should be included in the ORSA/ERM tool about SOLVENCY ASSESSMENT?

aa. A company’s view of the short- and long-term significant risks and the amount of funds necessary to cover them. (“Short- and long-term” would require definition).

bb. Upon reflection of the significant risks the company identifies, does the company believe the RBC is too low?

cc. Prospective (forward-looking) solvency assessment to attest to the ability to maintain a going concern.

·Qualitative assessment

·Quantitative calculations

dd. The company’s own target capital

ee. Explanation and documentation of the internal models used by the company, including the extent of reliance on outside models.

ff. Description of the reflection of significant interrelationships between risks and diversification effects considered.

gg. Basis for the calculations (e.g. economic valuation)

hh. Other solvency assessment?

ACLI strongly urges that detailed prescriptive standards are inappropriate. In our view, insurers should be given the flexibility to shape their risk management frameworks in the way most suited to their business objectives, consistent with a range of guidance published by risk management organizations in recent years.

Consider, for example, the question (bb) above. In our view, the purpose of required capital is to identify weakly capitalized companies. We suggest that the WG should take a position on the purpose of required capital before our industry can answer this question. This is another example of why we think a full discussion is needed.

Frequency: How often should the insurer perform this process (e.g. quarterly, annually, prior to financial examinations, when there is a significant change in the risk profile of a company)? How often should the insurer report on this process?

ACLI believes that an insurer should apply the insight gained from its internal risk management process to its ongoing and long-term management and decision making. An ORSA should not be designed solely to enable the insurer to complete as-requested information for the supervisor. Rather, the culture of the business should embrace an active internal risk assessment and risk management process. We believe that an insurer should not be required to report metrics.

If we were to agree on a CRO risk assessment, for example, we might recommend that it occur once every 3-5 years. More frequent updates could be triggered upon the domiciliary commissioner’s request based on objective economic factors.

Confidentiality: How should confidentiality be maintained (e.g. through examination process or via a new law/regulation)? Which component(s) of the content identified in #1 is not proprietary and could be made public?

ACLI believes that it is vitally important that all components of an ORSA review process should be viewed as confidential and protected from requests under state Freedom of Information Acts.

Group / Legal Entity / Pool: At what level should regulators require this tool (e.g. group, legal entity, intercompany pool)? Should the tool be required based upon “how the enterprise is managed?”

a. How should non-insurance entities be considered?

b. Should international entities be included?

ACLI believes that any ORSA must be based on how an insurer chooses to operate, *i.e.*, on a legal entity or on a consolidated group basis. Under any approach (*i.e.*, legal entity, consolidated or hybrid), group-

wide solvency assessment should be applied in a way that properly aligns with the risk and operational characteristics of the group and its members.

Proportionality: How should U.S. regulators implement proportionality (e.g. size, nature/scale/complexity, extent of international activity, certain lines of business, etc.)? What exclusions from the requirements or simplified reporting would you recommend, and for whom?

ACLI considers that the proportionality principle is essential and should be expressly endorsed in any ORSA. All insurers should not be required to perform either an ORSA or exactly the same ORSA. It and any similar requirement would have to be proportionate to the nature, size, and complexity of an insurer's risks.

Should the U.S. implement a questionnaire or a minimum level of standardized reporting? If so, should the reporting be an abbreviated reporting, with the full report available for review at the company upon request? Should a "sample report" or template be provided for educational purposes?

ACLI: The NAIC should not seek to develop prescriptive standards for risk management by insurers; rather, insurers should be given the flexibility to shape their risk management frameworks in the way most suited to their business objectives, consistent with a range of guidance published by risk management organizations in recent years. Companies should have the option of providing existing reports or analysis, to the extent that they are responsive to high level regulatory inquiries.

Should the tool be entirely driven by the company or should the regulators specify items such as specific stress tests or safety levels?

- a) If regulators specify stress or scenario tests, what should be the focus of the tests (e.g. major interest rate shift, major changes in lapse rates, misestimation of parameters, large adverse development in loss reserves (including adverse court decisions, etc.)?
- b) If regulators specify a safety level (e.g. 99.0% TVar) and time horizon for solvency assessment, what should those be?

ACLI believes that the NAIC should not seek to develop prescriptive standards for risk management by insurers; rather, insurers should be given the flexibility to shape their risk management frameworks in the way most suited to their business objectives, consistent with a range of guidance published by risk management organizations in recent years. On the other hand, we can understand that regulators may desire to make sure all companies are meeting a minimum ORSA standard. We suggest discussing the concept that an ORSA could be an assessment tool if its framework provided some incentives to insurers. For example, if a company was performing its risk management adequately and provided a comprehensive ORSA to its regulator as part of the financial examination process, there would be a greatly shortened financial examination at the company. If its risk management is inadequate and the ORSA is incomplete, then the company would have to do more to support the financial examiners in their assessment of the financial condition and the risk management of the company.

Should the Board be responsible for the ORSA/ERM? If so, to what extent? Should there be a sign off or certification requirement (by an actuary, chief risk officer, risk professional)? Should there be a required report to the Board (e.g. on stress tests)?

ACLI emphasizes that an ORSA is a process, not an "answer." Further, while the board of an insurer has ultimate oversight of that process, implementation should remain the responsibility of management.

How great will the need be for additional resources? Do states need to hire more risk experts? Do they need these experts on staff, or should they hire consults or share resources?

ACLI: We share the concern about staffing, training, and resources. That concern is among the reasons that we recommend discussing a CRO certification process once every 3-5 years. We acknowledge that non-routine, particularly complex situations could trigger the use of independent consultants.

What should we name this tool?

Should the gap analysis show need for an ORSA, **ACLI** suggests Insurer Solvency and Risk Assessment Profile (**ISRAP**).

Sincerely,


Carolyn Cobb



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October 11, 2010

Group Solvency Issues Working Group
c/o Mr. David Vacca
National Association of Insurance Commissioners
2301 McGee Street, Suite 800
Kansas City, MO 64108-2662
Via E-mail: dvacca@naic.org

Re: *Request for Comment on Group Capital Assessment Options*

The American Insurance Association (AIA) submits this letter in response to a request from NAIC's Group Solvency Issues Working Group (GSIWG) to provide comments on possible options for the group capital assessment. AIA is a trade association of approximately 300 property-casualty insurers that write more than \$117 billion in premiums each year. Many of our members are part of an affiliated group of companies that operate within and outside the United States. Consequently, we are interested in any matter that could lead to a proposal for determining capital requirements at a group level.

At the outset, we would like to make a few general comments about the request from the GSIWG. In order to generate meaningful discussion on the options presented in the request, the Working Group must also address certain threshold questions:

1. What is meant by the phrase "group capital assessment"? To clarify the use of that phrase, it is also necessary to define what is meant by "group". The term "group" has been used to praise and chide the insurance regulatory structure in the United States, but no consistent definition has been offered.
2. Assuming an adequate definition is eventually provided, what is the regulatory objective of a "group capital assessment"? In other words, what higher purpose would be served with a group capital assessment? When asking for feedback, there ought to be a clearly articulated regulatory objective in mind to justify the diversion of resources in providing the requested feedback. It is difficult to provide a meaningful response about any of the options (or to provide alternative approaches) without first understanding the desired end result.
3. How is a group capital assessment relevant to the U.S. regulatory framework? On behalf of the NAIC, Dr. Mary Weiss completed a summary of the current U.S. regulatory framework for insurance; yet, the request from the Working Group makes no reference to that summary document and it is noticeably silent on how the potential options would fit within the existing regulatory framework.

There should be a context against which responses can be provided. Without more, we can only respond based on the system that exists today, and that regulatory system is state-based and driven by the single entity concept.

Review of the Options

1. *Legal Entity RBC Adjustments.* Under a state-based/single-entity regime, this first option appears to be the most conceptually sound approach, though it is not simple to apply. Aggregating all the insurance activity into one consolidated risk-based capital (RBC) report might ease the process for determining RBC that would apply to the group of insurers since RBC is designed to specifically evaluate risks that apply to an insurer. However, this approach does not work very well for a diversified group of companies since insurance-specific factors should not be applied to non-insurance elements. To address this possible incongruity, the GSIWG comment request indicates that the non-insurance companies could be excluded from the group RBC calculation. This rationale, however, creates another conundrum: the non-insurance portions of the group could possibly contain contagion risk that could affect the insurance members of the group, in which case, the exclusion might undercut the objective of using RBC as a mechanism to protect against risk from the rest of the group.
2. *Group Capital Through ORSA.* The GSIWG request appears to suggest that the NAIC “is developing a risk management assessment tool that is currently titled an “Own Risk and Solvency Assessment” (ORSA)”. However, we are not aware of any decision by the NAIC to proceed with the development of an ORSA. In fact, there has been significant debate among regulators as to the purpose and benefit of an ORSA, given existing tools in the U.S. regulatory system. The International Solvency Working Group has recently asked for comments regarding an IAIS consultation paper on ORSA, and in that request, it rightfully acknowledges the risk-focused surveillance system that already exists in the U.S. for evaluating risks at the entity level (the Mary Weiss paper also lauds the existing risk-based surveillance framework, which necessarily causes us to question why a separate ORSA would be necessary). We think it is misleading at this juncture to suggest that NAIC is pursuing an ORSA methodology for groups when significant questions still remain about its relevance to the U.S. system.

Under a state-based regulatory system, it is not clear how a state insurance regulator could compel a diversified group of companies to perform an ORSA. Given the structural limitations of the existing state-based system, we would need more information on how this option could work before we can provide sufficient feedback to the GSIWG.

3. *Group Capital Calculation.* This option is not clear with respect to a parent that is also an insurance company. Is this option suggesting that risk-based capital could be calculated on a consolidated basis and reported on the parent company’s RBC report? If that is the case, it raises a question of how the individual companies in the group would be regulated for RBC purposes. Additionally, how should the non-insurance companies that are held by the parent insurance company be treated for RBC purposes? This option either assumes insurance regulators can assert authority over non-insurance companies, or it ignores the reality that many groups of companies are diverse structures and do not fall neatly into preconceived notions for regulating groups. As we stated earlier, it is imperative to first identify the regulatory objective in order to properly evaluate the options presented in the GSIWG request for comment, and, if necessary, to develop more appropriate options.

The fact that the GSIWG request for comment makes a distinction between control levels and action levels is not meaningful, in that there is a more fundamental issue of jurisdiction: an insurance regulator would not normally have authority over non-insurance companies, or insurance companies domesticated or operating in other jurisdictions. Under a state-based system, therefore, we do not understand the basis for an insurance regulator to require an RBC report of a parent, over which the regulator has no authority. Likewise, it is unclear as to why an action level or control level at the group level would be meaningful or relevant to the single entity over which the regulator would have jurisdiction. This third option is particularly confusing and requires clarification. As presented, it suggests numerous conceptual and legal problems that cannot be readily addressed under the current state-based, single entity system.

In summary, we are unable to provide more detailed comments because there are fundamental questions that the GSIWG must first answer. Most importantly, the GSIWG must provide clarification about the desired regulatory objective for using any of the proposed options. Once the GSIWG clearly articulates the regulatory objectives of group capital assessment, AIA will be happy to provide more detailed analysis of the options.

Thank you again for this opportunity to comment. We look forward to discussing the GSIWG comment request during the Fall 2010 NAIC meeting.

Sincerely,

A handwritten signature in cursive script that reads "Phillip L. Carson". The signature is written in dark ink and is positioned above the printed name.

Phillip L. Carson
Assistant General Council

To: Group Solvency Issues Working Group

From: Livesay, Milum D (Genworth)

Date: October 11, 2010

Subject: Response to NAIC group capital assessment proposal

Genworth Financial appreciates the opportunity to comment on the group capital assessment options. We have read both the ACLI and GNAIE responses to the NAIC request for comment on the group capital assessment options. Genworth agrees with the conclusions reached in both of those organization's letters.

While we conceptually agree with the NAIC's windows and walls approach to group supervision, we share the concerns expressed in the ACLI and GNAIE letters regarding the specific proposals under consideration by the NAIC. We feel that any project along the lines of group capital assessment must focus on the legal entity analysis where state regulators have jurisdiction. We have legitimate concerns about group analysis potentially involving non-public information. We advocate that the group considerations be deferred until the extensive modernization actions at the legal entity level, such as principles based reserving, the future of statutory accounting, RBC modernization, and reinsurance collateral reduction, are completed.

We would be happy to discuss our reservations further during the NAIC proceedings in Orlando.

Signed for Genworth Financial,

David Sloane
Milum Livesay

cc: Rob Vrolyk
Shekar Jannah
Dennis LaGanza

GNAIE Response on Group Capital Assessment Options Final

You have proposed for our consideration three possible group capital assessment options:

1. Legal Entity RBC Adjustments

To comply with IAIS standards, the legal entity RBC needs to account for the risks of being part of a group, such as reputational, contagion, or enterprise risks that could have an impact on the insurance company itself. This concept differs from “group-level capital” because the capital requirements do not require any capital levels for any non-insurers in the group. The non-insurer could be in dire financial condition, but there would be no impact to the insurer’s legal entity RBC unless that insolvency would have an impact on the financial position of the insurer.

To do this analysis, NAIC would need financial data from the group. Thus, a uniform and consolidated group statement would need to be considered.

GNAIE believes the information necessary for the NAIC to perform a group analysis is already available and could easily be provided on an annual basis. Consolidated financial reports could be provided for public companies while non-public companies, which do not prepare consolidated financial reports, provide combined annual statements which offer an aggregate view of all insurance and non-insurance activities within the group. In addition, holding company filings provide useful information regarding affiliate transactions and relationships. GNAIE opposes the creation of an additional consolidated group financial statement requirement which would be costly to generate and provide little value over the current information available.

2. Group Capital Analysis through ORSA

The International Solvency (EX) Working Group is developing a risk management assessment tool that is currently titled an “Own Risk and Solvency Assessment” (ORSA). U.S. state insurance regulators could develop the ORSA to provide information to perform an analysis of the group’s financial condition and risks.

GNAIE supports a review of group’s financial condition and risks and believes the risk focused financial examination process is the appropriate tool to facilitate such a review. Use of the examination process provides the necessary confidentiality protection for the sensitive information that an ORSA would contain. The International Association of Insurance Supervisors’ version of ORSA requires an insurer to determine the amount of financial resources needed based on its own risk tolerance, business plans and to demonstrate that the insurer is able to continue in business over the next few years. These are exercises that any prudent insurer is already undertaking either as part of its Enterprise Risk Management (ERM) function or some version thereof. We believe that it is appropriate for regulators to examine these existing processes and procedures tied to how a group manages its business, through the existing examination process, rather than to create a separate regulatory tool.

3. Group Capital Calculation

- *Parent Insurer*

When the parent is an insurer, the RBC currently applies. The RBC use of other countries' capital requirements could be expanded beyond the use of Canada's MCCSR for life insurers. This might require some determination, country by country, of the comparability of capital requirement calculations.

GNAIE supports mutual recognition between jurisdictions and would encourage the US to participate in such agreements, however, we have concerns that the unique use of the Canadian MCCSR in the RBC system works because the products in the US and Canada are similar. We are not sure that a similar integration of other methodologies would work as well for jurisdictions in which the product mix is different. That being said, a better understanding of the comparability of capital requirements in other jurisdictions could be helpful in assessing the appropriateness of RBC charges for foreign subsidiaries.

- *Parent Holding Company*

A group capital calculation and analysis could be created. This group capital calculation could be similarly calculated as the RBC, with adaptation for non-insurance companies deemed "significant" in the group. But the Group RBC would be significantly different than the legal entity RBC given there would be no control levels, but only action levels. Regulatory action with the group capital calculation could be focused on the need to have risk discussions with a group rather than any concrete required action or control. That would leave all control ladders of intervention in the legal entity capital requirements.

GNAIE believes that capital requirements should continue to be set on an insurance legal entity basis. This position is in line with the "windows and walls" approach adopted by the NAIC which aligns the capital requirements with the legal authority to act at the legal entity level. As previously noted, GNAIE supports the review of risks imposed on legal entities from being part of a group as part of the overall risk focused examination process. Through this process, along with required reporting under the Model Holding Company Act, regulators have sufficient tools to appropriately evaluate the risk of the group in its entirety, without performing a group capital calculation. The proposal suggests that regulatory action at the group capital level could result in the need for risk discussions at that level. It is our belief that the previously mentioned regulatory tools currently in place allow for such discussions and, if used as intended, would ensure regulators are well aware of any concerns before they become significant.



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October 11, 2010

Mr. David Vacca, CPA
Group Solvency Issues (EX) Working Group
National Association of Mutual Insurance Companies
2301 McGee Street, Suite 800
Kansas City, Missouri 64108

Dear Mr. Vacca:

We respond here to the Working Group's "Request for Comment on Group Capital Assessment Options" about several aspects of solvency regulation for insurers that are part of a group of insurers or a group of one or more insurers and other entities. NAMIC is a trade association with more than 1,300 mutual insurer members domiciled throughout the United States. Those members write approximately 37 percent of the property-casualty premium in this country and have clear interest in solvency regulation as it may affect their conduct of business.

As a representative of mutual insurers, some of which are organized as groups, NAMIC has concerns with the overall direction of the group-capital assessment options as suggested by the questions posed in this inquiry.

The foundation and center of solvency regulation is the legal entity. To the extent that regulation presumes to integrate the capital and risks of another, related entity into the capital of a subject insurance entity, we suspect that the probability of regulatory mistakes increases. To the extent such integration is formulaic, we further suspect that such probability of error may be aggravated. We admit the relevance of group capital to the regulatory process, yet we caution against fixed formulae or algorithms for determination of the adequacy of capital of a subject insurer.

Existing law, admittedly varying among states, constraining intra-group investment and, separately, the application of risk-based capital are rational and acceptable means for limiting group-capital problems and for assessing capital for regulatory intervention. Both operate at the legal-entity level. The Holding Company Act, as applied by the states and being modified by this Working Group is an additional and powerful supervisory tool relevant to group capital.

The difficulty finding consensus on formulae that produce quantitative measures of group capital for application to an insurer member of a group would appear formidable, if not wholly intractable. Quantifying contagion or reputational risk as between an insurer and some other species of business in a group—e. g. a manufacturer or other financial services unit—would seem subject to any number of subtle and essentially unquantifiable risks.

We offer the following responses or comments on the numbered options in the “Request for Comment ...”:

1. Legal Entity RBC Adjustments: For those mutual insurers organized as a group there exists no requirement in our knowledge for consolidated filing of financial statements, as opposed to most group situations in the GAAP world. Groups of mutual insurers, however, file combined annual statements. These, plus additional information on inter-company transactions can be obtained from information filed under the states’ holding company acts. We suggest additional regulation is not the answer to this concern.
2. Group Capital Analysis through ORSA: In our separate comments to the International Solvency (EX) Working Group on the matter of an “Own-Risk Solvency Assessment,” we stated our reluctance to see an ORSA or ORSA-like requirement added to the current solvency regime. We rehearse from those comments the fact that recent and severe turmoil in the capital markets did not bring the insurance industry in this country to its knees or result in material numbers of regulatory interventions. Perhaps other shoes will drop, but we believe we see from empirical results great strength in the existing solvency regulation system. With respect to an ORSA solving regulators’ group-capital problems, it is reasonable to recall that virtually every state allows its insurance regulator to legitimately demand data on the risks for a subject insurer that attend being in a group. Given that power, imposing an ORSA for the purpose of monitoring group capital would not seem advisable.

Already suggested in other forums under the SMI umbrella is use of the financial examination process to gather and/or consolidate such information. The process can be sharpened or focused to include group risks and their interactions.

3. Group Capital Calculation:

Parent Insurer—We hope that “equivalence” and other pressures do not impel rapid resolution of this question or set of questions. Instead, we suggest there is every reason—Solvency II not yet operating—to make deliberate and careful comparison of other jurisdictions’ capital requirements in practice. The dynamic at the group level is sure to be different and complex. Let this process of comparison of other jurisdictions’ methods for settling group capital be a project for the longer term.

Parent Holding Company—Again, we hope resolution or creation of some construct for this purpose is not forced by outside pressures. We reiterate that the holding

company with diverse interests presents great difficulty with respect to calculating capital requirements for the insurer or insurers within. This Working Group has fostered use of the “windows and walls” concept, which seems to be a viable method centered at the legal entity.

Finally, we believe the state regulatory regime has most of the information it may need to regulate solvency of insurers that are in a group and that, where information is not present, unquestionable authority to cause it to be produced. Finally, the legal-entity approach, combined with good judgment on the effects of risks from the group, is the best regulatory formula.

Respectfully,

Signature

A handwritten signature in cursive script that reads "William D. Boyd". The signature is written in black ink and is positioned above the printed name.

William D. Boyd
Financial Regulation Manager

Stephen W. Broadie
Vice President, Financial Policy

October 11, 2010

David Vacca, CPA
Assistant Director, Insurance Analysis & Information Systems
National Association of Insurance Commissioners
2301 McGee Street, Suite 800
Kansas City, MO 64108-2604

Re: Request for Comment on Group Capital Assessment Options

Dear Mr. Vacca:

The Property Casualty Insurers Association of America (PCI) appreciates the opportunity to comment on the Group Solvency Issues (EX) Working Group's paper on Group Capital Assessment Options. PCI is composed of more than 1,000 member property/casualty insurance companies, representing the broadest cross-section of insurers of any national trade association. PCI members write over \$174 billion in annual premium, 37.1 percent of the nation's property/casualty insurance.

As our members have considered the issues raised in this paper, the following principles appear clear to us:

- Groups should be assessed as they are managed, and a significant consideration in the definition of a group for capital assessment purposes should be whether there is capital support between the members of the group.
- Quantitative assessment of group risks (those risks to which members of a group are subject because they are members of the group) in an objective and verifiable way is extremely difficult. Analysis of these risks will always require judgment. Therefore we question the reliability and usefulness of a separate group capital calculation, especially when non-insurers are members of the group. Regulators should be interested in the potential effects of the capitalization of non-insurer members on the insurer members of the group, but we don't see how this can be objectively quantified.
- In a system like the U.S. system, in which regulation is based upon legal entities, what regulators really need to be concerned about is the effect of group risks on insurer legal entity capital.
- These questions are appropriate for review under the NAIC's risk-focused financial analysis and examination process.

With these principles in mind, here are our responses to the questions in the paper.

1. Legal entity RBC adjustments – We question whether this would be helpful, because of the difficulty in objectively quantifying group risks.
2. Group capital analysis through ORSA (Own Risk and Solvency Assessment) – Insurer members of groups should be taking group risks into account in their own enterprise risk management. As we stated in our comments on the NAIC's ORSA consultation paper, however, regulator analysis should be carried out through the risk-focused examination and analysis process.
3. Group capital calculation – With respect to groups where non-insurers are the parents, at this time we are skeptical of the value of a group capital calculation.

We are continuing to develop our positions on these issues, and we look forward to working with the Working Group as it does the same. If you have any questions or comments about our letter, please contact me at your convenience. We look forward to further discussing these issues with you at the Working Group's October meeting.

Sincerely,

A handwritten signature in black ink, appearing to read "Step W Brodie". The signature is fluid and cursive, with the first name "Step" and last name "Brodie" clearly legible.

Stephen W. Brodie