

# **Financial Regulation Standards and Accreditation Program**

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**National Association *of*  
Insurance Commissioners**

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# The NAIC Financial Regulation Standards and Accreditation Program

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## THE NAIC FINANCIAL REGULATION STANDARDS AND ACCREDITATION PROGRAM

*(Note: The official standards, policies and procedures of the NAIC Financial Regulation Standards and Accreditation Program are contained in the Proceedings of the NAIC and should be consulted for complete, accurate and up-to-date information on the Program.)*

*This pamphlet contains only general information about the NAIC Financial Regulation Standards and Accreditation Program and is not a comprehensive statement of the official standards, policies and procedures of the Program. Although this pamphlet is periodically updated to reflect changes in the Program, the reader is advised that it may not reflect the current Program requirements.)*

### **Introduction**

#### ***What is accreditation?***

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In general, accreditation is the process by which a program has been certified as fulfilling certain standards by a national professional association. In the terms of the insurance industry, accreditation is a certification given to a state insurance department once it has demonstrated it has met and continues to meet an assortment of legal, financial, organizational, and licensing and change of control standards as determined by a committee of its peers.

#### ***Why is accreditation necessary?***

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The concept of accrediting state insurance departments began in the mid-to-late 1980s when several large insurance companies became insolvent. In May 1988, as a response to the insolvencies, a congressional inquiry began looking at the insolvencies. In turn, the NAIC began discussing and shaping the Financial Regulation Standards and Accreditation Program in September 1988.

It was apparent that a system of effective solvency regulation could provide crucial safeguards for America's insurance consumers. Insurance consumers benefit when the insurance industry is strong enough financially to be able to pay and settle claims in a timely manner, to provide diverse and competitively priced products, and to provide meaningful customer service.

An effective system of solvency regulation has certain basic components. It requires that regulators have adequate statutory and administrative authority to regulate an insurer's corporate and financial affairs. It requires that regulators have the necessary resources to carry out that authority. Finally, it requires that insurance departments have in place organizational and personnel practices designed for effective regulation.

After much discussion, the NAIC took a large step toward establishing a sound program that would aide state insurance departments and solvency regulation by adopting the Financial Regulation Standards (Standards) in June 1989. In an effort to provide guidance to the states regarding the baseline Standards and as an incentive to put them in place, the NAIC adopted in June 1990 a formal certification program. Under this plan, each state's insurance department will be reviewed by an independent review team whose job is to assess that department's compliance with the Standards. Departments meeting the Standards will be publicly acknowledged, while departments not in compliance will be given guidance by the NAIC to bring them into compliance.

The Financial Regulation Standards and Accreditation (F) Committee of the NAIC, consisting of regulators from across the country, ultimately decides whether a state meets the requirements set forth in the Standards. The meetings in which matters of state accreditation are discussed are held in a regulator only session to protect the states, regulators, and in some instances, insurers from disclosure of confidential information.

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***What is the program's mission statement?***

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The mission of the NAIC accreditation program is to establish and maintain standards to promote sound insurance company financial solvency regulation. The accreditation program provides a process whereby solvency regulation of multi-state insurance companies can be enhanced and adequately monitored with emphasis on the following:

1. Adequate solvency laws and regulations in each accredited state to protect consumers and guarantee funds.
2. Effective and efficient financial analysis and examination processes in each accredited state.
3. Appropriate organizational and personnel practices in each accredited state.
4. Effective and efficient processes regarding the review of organization, licensing and change of control of domestic insurers in each accredited state.

The accreditation program will accomplish its mission by continually evaluating the adequacy and appropriateness of accreditation standards in accordance with the changing regulatory environment and through continued monitoring of accredited states by conducting the following accreditation reviews:

- Pre-Accreditation Reviews to occur approximately one year prior to a state's full accreditation review. This review will entail a high-level review of the financial analysis and financial examination functions to identify areas of improvement.
- Full Accreditation Review to occur once every five years subject to interim annual reviews. This review will entail a full review of laws and regulations, the financial analysis and financial examinations functions, organizational and personnel practices, and organization, licensing and change of control of domestic insurers to assist in determining a state's compliance with the accreditation standards.
- Interim Annual Reviews to occur annually to maintain accredited status between full accreditation reviews. This review will entail a review of any law and regulation changes, the financial analysis and financial examination functions, and organizational and personnel practices to ensure continued compliance with the accreditation standards and to identify areas of improvement.

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***What are the benefits of accreditation?***

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The accreditation program allows for inter-state cooperation and reduces regulatory redundancies. That is, if a company is domiciled in an accredited state, the other states in which that company is licensed and/or writes business may be assured that, because of its accredited status, the domiciliary state insurance department is adequately monitoring the financial solvency of that company. In fact, each accredited state's laws or regulations on financial examinations contain a provision that all licensed companies are to be examined periodically; however, in lieu of performing its own examination, a state may accept the examination report prepared by an insurance department that was accredited at the time of examination. Therefore, the inter-state reliance that the accreditation program produces ultimately saves millions of dollars in duplicative examination costs.

The accreditation program is a key tool in promoting and maintaining state-based regulation of the insurance industry. The creation of the accreditation program was prompted by a congressional report that highlighted weaknesses in state-based regulation, to which the Program has aided states in correcting these deficiencies. States that maintain their accredited status demonstrate that the current scheme of regulatory monitoring is intact and continues to work effectively.

### ***Who is accredited?***

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As of April 2015, there are a total of 52 jurisdictions that are accredited. All fifty states, the District of Columbia and Puerto Rico are accredited, which includes—Alabama, Alaska, Arizona, Arkansas, California, Colorado, Connecticut, Delaware, District of Columbia, Florida, Georgia, Hawaii, Idaho, Illinois, Indiana, Iowa, Kansas, Kentucky, Louisiana, Maine, Maryland, Massachusetts, Michigan, Minnesota, Mississippi, Missouri, Montana, Nebraska, Nevada, New Hampshire, New Jersey, New Mexico, New York, North Carolina, North Dakota, Ohio, Oklahoma, Oregon, Pennsylvania, Puerto Rico, Rhode Island, South Carolina, South Dakota, Tennessee, Texas, Utah, Vermont, Virginia, Washington, West Virginia, Wisconsin and Wyoming. Moreover, since the program began, all 50 states, the District of Columbia and Puerto Rico have adopted laws and regulations designed to bring them closer to meeting the NAIC's accreditation standards.

## **How the Accreditation Program Works**

The accreditation program establishes requirements under which a state insurance department may seek accreditation. Additionally, the program establishes guidelines for states already accredited to maintain their accredited status.

### ***Accreditation Review Process***

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#### **Procedures in Preparation for an Accreditation Review**

1. A state requests an accreditation review by contacting the applicable NAIC staff.
2. The NAIC requests that the state submit a Self-Evaluation Guide. This Guide provides the state with the detailed requirements of the Standards including laws and regulations that must be adopted, financial analysis and examination procedures that must be in place and organizational and personnel practices that must be established.
3. The NAIC notifies the chair of Financial Regulation Standards and Accreditation (F) Committee (FRSAC) that the state has requested an accreditation review and provides the chair with a list of qualified Review Team candidates, comprised of experts in insurance regulation.
4. The Chair of FRSAC approves the Review Team and the Review Team Leader and appoints at least one NAIC Observer. Review Teams generally consist of three to six individuals depending upon the size of the state; however, the Chair of FRSAC may determine that a lesser number is sufficient when the size of the state's insurance industry and scope of the department's responsibilities are notably limited. The Review Team should include at least one disinterested former executive level regulator.
5. The NAIC notifies the state of the selection of the Review Team. The state is given the opportunity to object to any of the Review Team members.
6. The NAIC notifies the Review Team members. The Review Team members are paid by the NAIC at a set hourly rate for time spent on the accreditation review plus reasonable actual expenses incurred.
7. The NAIC works with the state to schedule the site visit and notifies the Review Team of the dates. Generally, a site visit requires three to five days depending upon the size of the state.

8. The NAIC sends copies of the state's completed Self-Evaluation Guide with any applicable supporting documentation to the Review Team.
9. The NAIC notifies the state of the data, documentation, staff interviews, and other needs of the Review Team for its on-site review.
10. The NAIC Legal Division reviews the Part A responses and other pertinent information received from the State, and to the extent necessary, may analyze the State's laws, to determine whether the State is in compliance with the Part A Standards and to confirm whether the citations provided by the State accurately identify the extent to which the State's laws and regulations evidence compliance with the Part A Standards. Questions or concerns are forwarded to the NAIC Accreditation Staff and, if not resolved, are discussed with the state and, in addition, may be brought to the attention of an accreditation review team leader.
11. The Report of the NAIC Legal Division on the Part A Standards (The Part A Report) reports the findings of the NAIC Legal Division and includes the NAIC Legal Division's conclusion on the state's compliance with the Part A: Laws and Regulations Standards. A management comments portion may highlight concerns, if any are noted during the review, together with recommendations for the state to consider enhancements to its laws and regulations providing for sound insurance regulation. The department is required to provide a formal response to the Management Comment Letter by the date indicated by NAIC staff. This response will be included in the accreditation report package provided to FRSAC for discussion during the National Meeting.
12. The Part A Report is made part of the documentation for the accreditation review. It is delivered to the Department and the Review Team no later than the commencement of the On-Site Review, and is included in the materials submitted to each member of FRSAC at the conclusion of the On-Site Review.

### **On-Site Accreditation Review Procedures**

1. The Review Team conducts the on-site review following a general outline of procedures to be performed to allow for uniformity in the evaluation process among the states. In addition, an NAIC staff representative is an observer on each site visit to help ensure uniformity and consistency in the on-site reviews. Before the on-site review, there is an initial meeting of the team members to discuss comments and concerns from review of the Self-Evaluation Guide and supporting documentation.
2. The on-site review consists of the following:
  - a. Review of examination reports and supporting work papers and analytical reviews.
  - b. Inspection of financial analysis and examination files for selected companies.
  - c. Interviews with department personnel.
  - d. Review of organizational and personnel practices.
  - e. Inspection of documentation regarding primary licensure applications and Form A filing for selected companies.
  - f. Walk-through of the department to gain an understanding of document and communication flows.
  - g. Meetings of the Review Team to discuss comments and findings from the review.
  - h. Team members vote using a scoring system to determine whether a state is in compliance with the accreditation standards.

- i. Closing conference with the state to discuss findings.
  - j. Draft copies of the Part A Compliance Report and the Parts B, C and D Compliance Report and Management Letter comments are provided to the state.
3. As a result of the site visit, a review team report, compliance report and management letter comments are prepared by the Review Team and submitted to the FRSAC by the Team Leader. The reports summarize the scope of the procedures performed during the site visit, document the findings on an exception basis, highlight major recommendations as a result of the review, and conclude with the Review Team's recommendation as to whether the state should be accredited by FRSAC. The department is required to provide a formal response to the Management Comment Letter by the date indicated by NAIC staff. This response will be included in the accreditation report package provided to FRSAC for discussion during the next National Meeting. In addition, a Part A Report is prepared by NAIC Legal and submitted to the Committee as well.

### **Committee Evaluation Process**

1. FRSAC normally meets at the NAIC National Meetings to discuss the Review Team's reports. FRSAC also has copies of the state's Self-Evaluation Guide and supporting documentation available. In addition, the Team Leader and the NAIC observer are present at the meeting, as needed. Representatives of the state are in attendance to respond to questions from FRSAC, or comment upon the Review Team's reports and recommendation.
2. FRSAC has the option to convene into a "private" session during its Regulator-to-Regulator session meeting, at the discretion of the Chair of FRSAC. The individuals in the private session would typically include only members of FRSAC and their representatives, applicable NAIC staff, and the Team Leader. This should only occur in rare and infrequent situations when FRSAC must discuss or inquire regarding sensitive issues. Examples of this could include the following:
  - a. Concern regarding the quality or competence of personnel employed by a state insurance department, or
  - b. To confer with NAIC staff on the process and results of a contentious issue that FRSAC has deliberated previously.
3. Representatives of the state are excused once FRSAC has no further questions for these individuals. Based on the recommendation of the Review Team and as a result of this meeting, FRSAC makes a decision as to whether or not the state should be accredited. If the state is already accredited, FRSAC makes a decision whether the state should retain its accreditation, or whether its accreditation should be placed on probation, suspended or revoked.
4. FRSAC informs the state of its decision:
  - a. If the decision is to retain the state's accreditation, which includes those states granted continued accreditation although they were also placed on probation, the state receives recognition via distribution of the "Daily News" publication at the NAIC National Meeting.
  - b. For those states not currently accredited: If the decision is unfavorable, the state has three options: withdraw its request for accreditation; ask FRSAC to hold its decision in abeyance pending legislative or other corrective action to bring the state into compliance with the standards; or appeal the decision of FRSAC. If the state received a failing score in Part B, the state may request and receive a copy of its Part B Scoring Sheet upon being informed of the unfavorable decision.



- c. For those states currently accredited:
- If the decision is to place a state's accredited status on probation, a letter setting forth the conditions of the probation should be sent to the state as soon as possible after the FRSAC meeting. The state does not have the option to appeal the decision of FRSAC.
  - If the decision is to suspend a state's accreditation, a letter setting forth the conditions of the suspension should be sent to the state as soon as possible after the FRSAC meeting. The state may either accept the decision or choose to appeal the decision of FRSAC. If the state received a failing score in Part B, the state may request and receive a copy of its Part B Scoring Sheet upon being informed of the unfavorable decision. In the case of an appeal, the state retains its full accredited status during the appeals process. Public acknowledgement that a state's accreditation has been suspended should only occur after the opportunity to appeal has lapsed and the state has not chosen to do so, or if the decision by FRSAC to suspend accreditation is upheld by the appeal hearing panel.
  - If the decision is to revoke a state's accreditation, the state may either accept the decision or choose to appeal the decision of FRSAC. If the state received a failing score in Part B, the state may request and receive a copy of its Part B Scoring Sheet upon being informed of the unfavorable decision. In the case of an appeal, the state retains its full accredited status during the appeals process. Public acknowledgement that a state's accreditation has been revoked should only occur after the opportunity to appeal has lapsed and the state has not chosen to do so, or if the decision by FRSAC to revoke accreditation is upheld by the appeal hearing panel.
5. Accreditation is for a five-year period, subject to annual reviews of the state's Self-Evaluation Guide. Once accredited, a state is subject to a full accreditation review every five years. If information comes to the attention of FRSAC that suggests that a state may no longer meet the Standards, a special review may be conducted. If FRSAC concludes that the state's accreditation should be placed on probation, suspended or revoked, the specific reasons are documented in a report to the state. The state would have the right to appeal a suspension or revocation decision of FRSAC utilizing the previously established procedures.

### **Interim Annual Reviews**

1. Annually, on the anniversary of the state's accreditation, the state shall submit an updated Self-Evaluation Guide (Interim Annual Reviews) to the NAIC Central Office.
2. The state's report in the first year after an on-site accreditation review shall provide a progress update to the Review Team's recommendations made in the report and/or management letter.
3. NAIC staff will review the Interim Annual Review report and supporting documentation submitted by the state and summarizes the information for presentation to FRSAC.
4. After hearing the report from the NAIC staff, FRSAC will determine whether the state remains in compliance with the Standards. (FRSAC may request that a representative of the state be present to answer questions, if desired.)
5. If FRSAC finds the state to be out of compliance with the Standards, the specific reasons will be documented in a letter to the state and the state's accreditation will be placed on probation, suspended or revoked. The state would have the right to appeal a suspension or revocation decision of FRSAC utilizing the procedures adopted by FRSAC.

## A Closer Look at the Standards

The Standards have been divided into four major categories: laws and regulations (Part A); regulatory practices and procedures (Part B); organizational and personnel practices (Part C); and organization, licensing and change of control of domestic insurers (Part D).

### **Part A: Laws and Regulations – Traditional Insurers**

#### *Preamble*

The purpose of the Part A: Laws and Regulations Standards is to assure that an accredited state has sufficient authority to regulate the solvency of its multi-state domestic insurance industry in an effective manner. The Part A standards are the product of laws and regulations that are believed to be basic building blocks for sound insurance regulation. A state may demonstrate compliance with a Part A standard through a law, a regulation, an established practice, which implements the general authority granted to the state or any combination of laws, regulations or practice, which achieves the objective of the standard.

The Part A standards apply to traditional forms of “multi-state domestic insurers.” This scope includes life/health and property/casualty/liability insurers and reinsurers that are domiciled in the accredited state and licensed, accredited or operating in at least one other state. This scope also includes insurers that are domiciled in the accredited state and operating or accepting business on an exported basis in at least one other state as excess and surplus lines insurers or as risk retention groups (RRGs); except that the term does not include RRGs incorporated as captive insurers. Part A standards for RRGs are included in the following section. It also does not include those insurers that are licensed, accredited or operating in only their state of domicile but assuming business from insurers writing that business that is directly written in a different state. The terms “insurer” and “insurers” used in the Part A standards fall within the definition of “multi-state domestic insurers.” For the purpose of this definition, the term “state” is intended to include any NAIC member jurisdiction, including U.S. territories.

#### **1. Examination Authority**

The Department should have authority to examine companies whenever it is deemed necessary. Such authority should include complete access to the company’s books and records and, if necessary, the records of any affiliated company, agent, and/or managing general agent. Such authority should extend not only to inspect books and records but also to examine officers, employees, and agents of the company under oath when deemed necessary with respect to transactions directly or indirectly related to the company under examination. The NAIC Model Law on Examinations or substantially similar provisions shall be part of state law.

#### **2. Capital and Surplus Requirement**

The Department should have the ability to require that insurers have and maintain a minimum level of capital and surplus to transact business. The Department should have the authority to require additional capital and surplus based upon the type, volume and nature of insurance business transacted. The Risk Based Capital (RBC) for Insurers Model Act or provisions substantially similar shall be included in state laws or regulations.

#### **3. NAIC Accounting Practices and Procedures**

The Department should require that all companies reporting to the Department file the appropriate NAIC annual statement blank, which should be prepared in accordance with the NAIC’s instructions handbook and follow those accounting procedures and practices prescribed by the NAIC’s *Accounting Practices and Procedures Manual*, utilizing the version effective January 1, 2001 and all subsequent revisions adopted by the Financial Regulation Standards and Accreditation (F) Committee.

**4. Corrective Action**

State law should contain the NAIC's Model Regulation to Define Standards and Commissioner's Authority for Companies Deemed to be in Hazardous Financial Condition or a substantially similar provision, which authorizes the Department to order a company to take necessary corrective action or cease and desist certain practices that, if not corrected, could place the company in a hazardous financial condition.

**5. Valuation of Investments**

The Department should require that securities owned by insurance companies be valued in accordance with those standards promulgated by the NAIC's Capital Markets and Investment Analysis Office. Other invested assets should be required to be valued in accordance with the procedures promulgated by the NAIC's Financial Condition (E) Committee.

**6. Holding Company Systems**

State law should contain the NAIC Insurance Holding Company System Regulatory Act or an Act substantially similar, and the Department should have adopted the NAIC's model regulation relating to this law.

**7. Risk Limitation**

State law should prescribe the maximum net amount of risk to be retained by a property and liability company for an individual risk based upon the company's capital and surplus. This limitation should be no larger than 10% of the company's capital and surplus.

**8. Investment Regulations**

State statute should require a diversified investment portfolio for all domestic insurers both as to type and issue and include a requirement for liquidity. Foreign companies should be required to substantially comply with these provisions.

**9. Liabilities and Reserves**

State statute should prescribe minimum standards for the establishment of liabilities and reserves resulting from insurance contracts issued by an insurer; including life reserves, active life reserves and unearned premium reserves, and liabilities for claims and losses unpaid and incurred but not reported claims. The NAIC's Standard Valuation Law, Actuarial Opinion and Memorandum Regulation and Property and Casualty Actuarial Opinion Model Law or substantially similar provisions shall be in place.

**10. Reinsurance Ceded**

State law should contain the NAIC Model Law on Credit for Reinsurance, the NAIC's Credit for Reinsurance Model Regulation and the NAIC Life and Health Reinsurance Agreement Model Regulation or substantially similar laws.

**11. CPA Audits**

State statute or regulation should contain a requirement for annual audits of domestic insurance companies by independent certified public accountants that is substantially similar to the NAIC's Annual Financial Reporting Model Regulation.

**12. Actuarial Opinion**

State statute or regulation should contain a requirement for an opinion on reserves and loss and loss adjustment expense reserves by a qualified actuary or specialist on an annual basis for all domestic insurance companies.

**13. Receivership**

State law should set forth a receivership scheme for the administration, by the insurance commissioner, of insurance companies found to be insolvent as set forth in the NAIC's Insurer Receivership Model Act.

**14. Guaranty Funds**

State law should provide for a regulatory framework such as that contained in the NAIC's model acts on the subject, to ensure the payment of policyholders' obligations subject to appropriate restrictions and limitations when a company is deemed insolvent.

**15. Filings with NAIC**

State statute, regulation or practice should mandate filing of annual and quarterly statements with the NAIC in a format acceptable to the NAIC except that states may exempt from this requirement those companies that operate only in their state of domicile.

**16. Producer Controlled Insurers**

States should provide evidence of a regulatory framework, such as that contained in the NAIC's Model Law for Business Transacted with Producer Controlled Property/Casualty Insurer Act or similar provisions.

**17. Managing General Agents Act**

States should provide evidence of a regulatory framework, such as that contained in the NAIC's Managing General Agents Model Act or similar provisions.

**18. Reinsurance Intermediaries Act**

States should provide evidence of a regulatory framework, such as that contained in the NAIC's Reinsurance Intermediary Model Act or similar provisions.

**19. Regulatory Authority**

State law should provide for a regulatory framework for the organization, licensing and change of control of domestic insurers.

*(Note: If a state can provide evidence that none of the entities contemplated in above standards 14, 16, 17 or 18, is either present or allowed to operate in the state, it will not need to demonstrate compliance with that standard.)*

**Part A: Laws and Regulations – Risk Retention Groups**

The following Part A standards apply to RRGs incorporated as captive insurers. This scope includes RRGs that are chartered in the accredited state and registered or operating in at least one other state. For the purpose of this definition, the term "state" is intended to include any NAIC member jurisdiction, including U.S. territories.

**1. Examination Authority**

The Department should have authority to examine RRGs organized as captive insurers whenever it is deemed necessary. Such authority should include complete access to the RRG's books and records and, if necessary, the records of any affiliated company, agent, and/or managing general agent. Such authority should extend not only to inspect books and records but also to examine officers, employees, and agents of the RRG under oath when deemed necessary with respect to transactions directly or indirectly related to the RRG under examination. The NAIC Model Law on Examinations or substantially similar provisions shall be part of state law.

**2. Capital and Surplus Requirement**

The Department should have the ability to require that RRGs have and maintain a minimum level of capital and surplus to transact business. The Department should have the authority to require additional capital and surplus based upon the type, volume, and nature of insurance business transacted. The Risk-Based Capital for Insurers Model Act or provisions substantially similar should be included in state laws or regulations.

**3. NAIC Accounting Practices and Procedures**

The Department should require that RRGs reporting to the Department file the appropriate NAIC Annual Statement Blank which should be prepared in accordance with the NAIC's Instructions Handbook, as applicable. The RRGs should follow those accounting procedures and practices prescribed by the NAIC Accounting Practices and Procedures Manual or another basis of accounting as permitted or prescribed by state law or regulation.

**4. Corrective Action**

State law should contain the NAIC's Model Regulation to Define Standards and Commissioner's Authority for Companies Deemed to be in Hazardous Financial Condition or a substantially similar provision which authorizes the Department to order a RRG to take necessary corrective action or cease and desist certain practices which, if not corrected, could place the RRG in a hazardous financial condition.

**5. Valuation of Investments**

The Department should require that securities owned by RRGs be valued in accordance with those standards promulgated by the NAIC's Capital Markets and Investment Analysis Office or, if a basis of accounting other than SAP is used, the state must have authority to determine the valuation of securities. For RRGs that use SAP, other invested assets should be required to be valued in accordance with the procedures promulgated by the NAIC's Financial Condition (E) Committee. For RRGs that use another basis of accounting, the state must have authority to determine valuation of securities.

**6. Holding Company Systems**

State law should contain the NAIC Model Holding Company Systems Act or an act substantially similar and the Department should have adopted the NAIC's model regulation relating to this law.

**7. Risk Limitation**

State law should provide the state insurance department with clear authority in statute or regulation to limit the net amount of risk retained for an individual risk.

**8. Investment Regulations**

State statute should require a diversified investment portfolio for RRGs both as to type and issue and include a requirement for liquidity.

**9. Liabilities and Reserves**

State statute should prescribe minimum standards for the establishment of liabilities and reserves resulting from insurance contracts issued by an RRG; including unearned premium reserves and liabilities for claims and losses unpaid and incurred but not reported claims.

**10. Reinsurance Ceded**

State law should contain the NAIC Model Law on Credit for Reinsurance, the NAIC's Credit for Reinsurance Model Regulation or substantially similar laws.

**11. CPA Audits**

State statute or regulation should contain a requirement for annual audits of domestic RRGs by independent certified public accountants that is substantially similar to the NAIC Annual Financial Reporting Model Regulation.

**12. Actuarial Opinion**

State statute or regulation should contain a requirement for an opinion on loss and loss adjustment expense reserves by a qualified actuary or specialist annually for all domestic RRGs.

**13. Receivership**

State law should set forth a receivership scheme for the administration, by the insurance commissioner, of RRGs found to be insolvent similar to the NAIC's Insurer Receivership Model Act.

**14. Filings with NAIC**

State statute, regulation or practice should mandate filing of annual and quarterly statements with the NAIC in a format acceptable to the NAIC except that states may exempt from this requirement those RRGs that operate only in their state of domicile.

**15. Producer Controlled Insurers**

States should provide evidence of a regulatory framework, such as that contained in the NAIC's Model Law for Business Transacted with Producer Controlled Property/Casualty Insurer Act or similar provisions.

**16. Managing General Agents Act**

States should provide evidence of a regulatory framework, such as that contained in the NAIC's Managing General Agents Act or similar provisions.

**17. Reinsurance Intermediaries Act**

States should provide evidence of a regulatory framework, such as that contained in the NAIC's Reinsurance Intermediary Model Act or similar provisions.

*(Note: If a state can provide evidence that none of the entities contemplated in above standards 15, 16, or 17, is either present or allowed to operate in the state (in relation to RRGs), it will not need to demonstrate compliance with that standard.)*

**Part B: Regulatory Practices and Procedures*****Preamble***

The purpose of Part B is to identify base-line regulatory practices and procedures required to supplement and support enforcement of the states' financial solvency laws in order for the states to attain substantial compliance with the core standards established in Part A. Part B identifies standards that are to be applied in the regulation of all forms of multi-state insurers.

Part B sets out standards required to ensure adequate solvency regulation of multi-state insurers. Each state must make an appropriate allocation of its available resources to effectively address its regulatory priorities. In addition to a domestic state's examination and analysis activities, other checks and balances exist in the regulatory environment. These include other states' regulation of licensed foreign companies, the appropriate application of FAST and IRIS ratios, the analyses by NAIC's staff, the NAIC Financial Analysis Working Group, the NAIC Analyst Team System project, and to some extent the evaluation by private rating agencies.

The scope of Part B is broader than the scope of Part A. "Multi-state insurer" as used in Part B encompasses all forms of insurers domiciled or chartered in the accredited state and licensed, registered,

accredited or operating in at least one other state. This scope also includes insurers that are domiciled in the accredited state and operating or accepting business on an exported basis in at least one other state as excess and surplus lines insurers. It does not include those insurers that are licensed, accredited or operating in only their state of domicile but assuming business from insurers writing that business that is directly written in a different state. The term “insurer” in Part B includes traditional insurance companies as well as, for instance, health maintenance organizations and health service plans, captive risk retention groups, and other entities organized under other statutory schemes. Although this scope includes risk retention groups organized as a captive insurer, it does not include any other type of captive insurer. While the unique organizational characteristics of some of these entities may require specialized laws, their multi-state activity demands solvency oversight that employs the base-line regulatory practices and procedures identified in Part B. For purposes of this definition, the term “state” is intended to include any NAIC member jurisdiction, including U.S. territories.

The accreditation program recognizes that complete standardization of practices and procedures across all states may not be practical or desirable because of the unique situations each state faces. States differ with respect to staff and technology resources that are available as well as the characteristics of the domestic industry regulated. For example, states may choose to emphasize automated analysis over manual or vice versa. Reliable results may be obtained using alternative, yet effective, financial solvency oversight methodologies. The accreditation program should not emphasize form over substance in its evaluation of the states’ solvency regulation.

*(NOTE: FRSAC has adopted Review Team Guidelines that provide detailed guidance to the review teams regarding how compliance with the Part B, Regulatory Practices and Procedures Standards should be assessed. These guidelines can also assist states in preparing for the accreditation review of their Department.)*

## **1. Financial Analysis**

### **a. Sufficient Qualified Staff and Resources**

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

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

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

### **c. Appropriate Supervisory Review**

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

### **d. Priority-Based Analysis**

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

### **e. Appropriate Depth of Review**

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

**f. Documented Analysis Procedures**

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

**g. Reporting of Material Adverse Findings**

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

**h. Action on Material Adverse Findings**

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

**2. Financial Examinations****a. Sufficient Qualified Staff and Resources**

The Department should have the resources to effectively examine all domestic insurers on a periodic basis in a manner commensurate with the financial strength and position of each insurer.

**b. Communication of Relevant Information to/from Examination Staff**

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

**c. Use of Specialists**

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

**d. Appropriate Supervisory Review**

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

**e. Use of Appropriate Guidelines and Procedures**

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

**f. Performance and Documentation of Risk-Focused Examinations**

The Department's performance and documentation of risk-focused examinations should generally follow the guidance set forth in the NAIC *Financial Condition Examiners Handbook*. Appropriate variations in method and scope should be commensurate with the financial strength and position of the insurer.

**g. Scheduling of Examinations**

In scheduling financial examinations, the Department should follow procedures such as those set forth in the NAIC *Financial Condition Examiners Handbook* that provide for the periodic



examination of all domestic companies on a timely basis. This system should accord priority to companies that exhibit adverse financial trends or otherwise demonstrate a need for examination.

**h. Examination Reports**

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

**i. Reporting of Material Adverse Findings**

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

**j. Action on Material Adverse Findings**

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

**3. Information Sharing and Procedures for Troubled Companies**

**a. Information Sharing**

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

**b. Procedures for Troubled Companies**

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

**Part C: Organizational and Personnel Practices**

**1. Professional Development**

The Department should have a policy that encourages the professional development of staff involved with financial surveillance and regulation through job-related college courses, professional programs, and/or other training programs.

**2. Minimum Educational and Experience Requirements**

The Department should establish minimum educational and experience requirements for all professional employees and contractual staff positions in the financial regulation and surveillance area, which are commensurate with the duties and responsibilities of the position.

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**3. Retention of Personnel**

The Department should have the ability to attract and retain qualified personnel for those positions involved with financial surveillance and regulation.

**Part D: Organization, Licensing and Change of Control of Domestic Insurers*****Preamble***

The focus of the Part D standards is on strengthening financial regulation and the prevention of unlicensed or fraudulent activities. The scope of this section only includes the licensing of new companies and Form A filings. The section applies to only traditional life/health and property/casualty companies, and this scope is narrower than that of Part B in that it does not include entities such as health maintenance organizations, health service plans, and captive insurers (including captive risk retention groups). These standards only deal with the department's analysis of domestic companies and do not include foreign or alien insurers. The initial company licensing process does not consider the "multi-state" concept since the company is in its initial licensing phase. The standards regarding Form A filings deal with only filings submitted related to multi-state insurers, as that term is defined in the Part B Preamble.

**1. Qualified Staff and Resources**

The department should have minimum educational and experience requirements for licensing staff commensurate with the duties and responsibilities for analyzing company applications. Staff responsible for analyzing applications should have an accounting, insurance, financial analysis or actuarial background.

**2. Sufficient Staff and Resources**

The department should have sufficient resources to effectively review applications for primary licensure or Form A filings in a timely manner.

**3. Scope of Procedures for Primary Applications**

The department should have documented licensing procedures that include a review and/or analysis of key pieces of information included in a primary licensure application.

**4. Scope of Procedures for Form A Filings**

The department should have documented procedures for the review of key pieces of information included in Form A filings.

**5. Use of the Form A Database**

The department should utilize the Form A Database as a means of obtaining information on prior filings made by an applicant and informing other states of the receipt and status of Form A filings in a timely manner.

**6. Documentation of Work Performed**

The department's files should include evidence that the department's procedures were adequately performed and well documented, including a conclusion regarding whether an application or filing is approved or denied.

## **Evolving Standards: The Impact of Changes in the Financial Regulation Standards**

As insurance industry practices evolve, so must solvency regulation. Therefore, the NAIC has anticipated that the Standards outlined above would not be static but would be dynamic.

### ***What is the process to add to or modify the Standards?***

In March 1998, the NAIC adopted a more flexible process when adding new standards or modifying the existing Standards. The process seeks extensive input from public officials, consumers, academics, regulators and industry representatives when changes in the Financial Regulation Standards and Accreditation Program are considered.

The procedures identify three ways in which the solvency standards may be modified:

1. The development of new models or amendment of existing models;
2. Additional or more specific requirements to Parts B, C and D of the Standards; or
3. Indirect modification of current requirements through changes in manuals or books incorporated by reference in the Standards, such as modification of the annual statement blank required to be filed by all companies.

The process uses a set schedule to complete the deliberation process, which allows all interested parties to clearly understand the decision timetable.

With regard to the development of new models or the amendment of existing models, the proposal would be discussed at the Spring National Meeting by FRSAC with public testimony taken at the Summer National Meeting. FRSAC will notify all interested parties including all regulators, industry, consumer groups, the National Conference of State Legislatures (NCSL), National Governors' Association (NGA), National Conference of Insurance Legislators (NCOIL), and others, both of the potential change in the model and the process for public comment.

Additionally, any suggested addition or change to the accreditation standards will be accompanied by the following:

1. A statement and explanation of how the standard is directly related to solvency surveillance and why the proposal should be included in the Standards.
2. A statement as to why ultimate adoption by every jurisdiction may be desirable.
3. A statement as to the number of jurisdictions that have adopted and implemented the proposal or a similar proposal and their experience to date.
4. A statement as to the provisions needed to meet the minimum requirements of the standard. That is, whether a state would be required to have "substantially similar" language or rather a regulatory framework. If it is being proposed that "substantially similar" language be required, the referring committee, task force or working group shall recommend those items that should be considered significant elements.
5. An estimate of the cost for insurance companies to comply with the proposal and the impact on state insurance departments to enforce it, if reasonably quantifiable.

After consideration of the testimony, FRSAC will determine whether the proposal should be exposed as a potential standard. At the Fall National Meeting, Executive Committee and Plenary will vote on the proposal.

If the proposal is adopted by Plenary, a one-year exposure period, commencing the following January 1, for laws and regulations standards will commence during which time all interested parties will evaluate the effectiveness of the proposal.

After the exposure period has ended, FRSAC will review the proposal at the Spring National Meeting to see what action, if any, should be taken to formally adopt the new proposal. At the Summer National Meeting, a public hearing will be held and FRSAC will decide whether to add the proposal to the standards with a 60% majority vote needed to adopt. At the Fall National Meeting, Executive Committee and Plenary would also take action with 60% required to adopt. Once adopted by Plenary, the standard will become effective two years immediately following the next January 1. This provides a total of at least four full years for all parties to consider amendments or additions to the laws and regulations standards.

For additional or more specific requirements to Parts B, C and D of the standards or indirect modification of current requirements through changes in manuals or books incorporated by reference in the standards, no seasoning period is required, and these changes become effective as deemed appropriate.

If FRSAC determines that a waiver of the above procedures is necessary to expeditiously consider modification or alteration of the Standards, it may upon a three-fourths (3/4) majority vote, move to recommend adoption of changes or modifications to the Executive Committee. The Report of FRSAC shall fully explain the necessity for expeditious action and attempt to summarize in an objective manner, the positions of the various interested parties. The Executive Committee and Plenary would vote on the Report, with a 60% majority required for adoption.

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#### ***What are some of the upcoming changes to the Program?***

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The risk-based capital filing is currently an accreditation standard for life and P/C companies. On January 1, 2015, the recommendation to make the *Risk-Based Capital for Health Organizations Model Act* (#315) an accreditation standard will be effective, thus requiring health organizations to file the risk-based capital as well.

The 2010 Revisions to the Insurance Holding Company System Model Act (#440) and Insurance Holding Company System Model Regulation (#450) was adopted by the F Committee at the 2013 Summer National Meeting, and the revisions primarily related to the Enterprise Risk Filing (Form F) and supervisory colleges. This will become applicable for accreditation as of January 1, 2016.

### **What the Future Holds: A Strong System of Solvency Regulation**

The regulation of the insurance industry for solvency stands as a unique example of how an effective regulatory system can be built. The strength of that system resides in the interdependence of independent state regulators, each responsible to his or her own constituencies, yet jointly responsible for the financial health of an entire industry. At every step along the way, state insurance regulators bear in mind their duty to safeguard consumers.

Governors, legislators and state insurance regulators, not content to rest on past success, have devised in the Financial Regulation Standards and Accreditation Program, a powerful means of achieving the necessary degree of consistency among states without sacrificing the multi-state diversity that has been instrumental to that success. Since 1990, every state, the District of Columbia and Puerto Rico have adopted legislative packages designed to bring their departments of insurance into compliance with the Standards. The partnership among state government officials has been key to the success of the accreditation program, solvency regulation, and effective consumer protection.