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1. This is an NAIC working document which includes general concepts and proposed technical specifications and options to be used for field testing and analysis of the NAIC’s proposed Group Capital Calculation (GCC)

General Comments

2. Criteria in this document are intended to provide uniform guidance to field test Volunteers, their respective Lead State Regulator and field test analysts as to the Scope of Application for the specific purpose of the GCC. The “Scope of Application” (i.e., for purposes of the GCC specifically) may be narrower, i.e., comprise a subset of, the entities controlled by the Ultimate Controlling Person of the insurer(s) (Broader Group).

3. The initial identification of the Insurance Group and the determination of the Scope of Application is made by a field test Volunteer for submission to its Lead State Regulator, following the principles and steps discussed herein, However, the final decisions as to the identification of the Insurance Group and the determination of the Scope of Application remain the ultimate responsibility of the Lead State Regulator, cooperating and coordinating with other involved regulators. In particular, in the case of Insurance Groups that operate on a cross-border basis, the Lead State Regulator should be able to explain the appropriateness of the identification of the Insurance Group and the determination of the Scope of Application to involved supervisors in other jurisdictions. The Lead State Regulator, in cooperation with other involved regulators, should review the appropriateness of the Scope of Application at least annually and to confirm continued relevance.

4. The fundamental reason for state insurance regulation is to protect American insurance consumers\(^1\). Therefore, the objective of the GCC is to assess quantitatively the collective risks to, and capital of, the entities within the Scope of Application. This assessment should consider risks that originate within the Insurance Group along with risks that emanate from outside the Insurance Group but within the Broader Group. The overall purpose of this assessment is to better understand the risks that could adversely impact the ability of the entities within the Scope of Application to pay policyholder claims consistent with the primary focus of insurance regulators. Consistent with sound regulation, the benefits of the quantitative analysis facilitated by the GCC should exceed the cost of implementation. Such an approach could be achieved by leveraging existing statutory information filed with the Lead State Regulator wherever practical.

Definitions

5. **Broader Group**: The entire set of legal entities that are controlled by the Ultimate Controlling Person of insurers within a corporate group.

6. **Field Test Volunteer, or Volunteer**: An Insurance Group that is participating with its Lead State Regulator and the NAIC in the development of the GCC through the submission of confidential data and field testing exercises.

7. **Financial Entity**: A non-insurance financial institution that makes or facilitates financial intermediary operations (accepting deposits, granting of credits and loans, investments, etc.). The primary examples of financial entities are commercial banks, intermediation banks, investment banks, saving banks, credit unions, savings and loan institutions, investment companies, private funds, commodity pools, swap dealers etc.

8. **Insurance Group**: For purposes of the GCC, a group that is comprised of two or more entities of which at least one is an insurer, and which includes all of the insurers in the Broader Group. Another (non-insurance) entity may exercise significant influence on the insurer(s), i.e. a holding company or a mutual holding company; in other cases, such as mutual insurance companies, the mutual insurer itself may be the Ultimate Controlling Person. The exercise of significant influence is determined based on criteria such as (direct or indirect) participation, influence and/or other contractual obligations; interconnectedness; risk exposure; risk concentration; risk transfer; and/or intragroup agreements, transactions and exposures. An Insurance Group may include entities which facilitate, finance or service the group’s insurance operation, such as holding companies, branches, non-regulated entities, and other regulated financial institutions. An Insurance Group could be headed by:
   - an insurance legal entity;
   - a holding company; or
   - a mutual holding company.

   An Insurance Group may be:
   - a subset/part of bank-led or securities-led financial conglomerate; or
   - a subset of a wider group.

   An Insurance Group is thus comprised of the head of the Insurance Group and all entities under its direct or indirect control.

9. **Lead State Regulator**: as defined in the NAIC’s Financial Analysis Handbook, i.e., generally considered to be the one state that “takes the lead” with respect to conducting group-wide supervision within the U.S. solvency system.

10. **Reciprocal Jurisdiction**: as defined in the Model Law for Credit for Reinsurance.

   **Drafting Note**: The term “Reciprocal Jurisdiction” is from the proposed revisions incorporated to the exposure draft dated June 21, 2018 to the Credit for Reinsurance Model Law (#785) and the Credit for Reinsurance Model Regulation (#786). The content of this reference may need to be modified if it does not incorporate the mutual recognition of group supervision concept.

**Question 1**- For purposes of field testing, since a decision to participate in field testing is voluntary between an Insurance Group and its lead state, should a group assume that groups with Group-Wide Supervisors in current qualified jurisdictions (e.g., Bermuda, Japan, Switzerland, Ireland and the EU (including the UK, France and Germany specifically) would not
be required to complete the NAIC Group Capital Calculation, and therefore influence their
decision in volunteering? If yes, are further changes to paragraph 13 needed?

11. **Scope of Application**: Refers to the entities that meet the criteria listed herein for inclusion in the
GCC. Depending on the facts and circumstances involving a specific group, the application of such
criteria may result in the Scope of Application being the same as, or a subset of, the entities
controlled by the Ultimate Controlling Person of the insurer(s).

12. **Ultimate Controlling Person**: As used in the NAIC’s Insurance Holding Company System
Regulatory Act.

**Groups Exempted from the GCC**

13. A non-U.S. based group (a group with a non-U.S. group-wide supervisor) may be exempt from the
GCC if:

i. The non-U.S. based group is based in a Reciprocal Jurisdiction that recognizes the U.S.
regulatory regime and accepts the GCC from U.S. based groups to satisfy the Reciprocal
Jurisdiction’s group capital requirement;

ii. The non-U.S. Group-Wide Supervisor’s home jurisdiction requires a group capital calculation
be applied at a level that includes the same (or substantially similar) Scope of Application as
would otherwise be determined by the Lead State Regulator in the absence of this
exemption; and

iii. The Lead State Regulator can obtain information from the foreign group’s Group-Wide
Supervisor either through a Supervisory College or otherwise, that allows the Lead State
Regulator to understand the financial condition of the group and complete the expectations
of other states in its Group Profile Summary (GPS).

14. A U.S. based group is exempt from the GCC if it is not required to file an ORSA with its Lead State
Regulator.

**Question 2** - For purposes of field testing, since a decision to participate in field testing is
voluntary between an Insurance Group and its lead state, should paragraph 14 be deleted?

**Guiding Principles and Steps to Determine the Scope of Application**

15. The Scope of Application is initially determined by the Insurance Group in a series of steps, listed
here and then further explained as necessary in the text that follows:

- Develop an initial inventory of potential entities using the Inventory of the Group template
  (Schedule 1)
- Denote in the Inventory of the Group template the following entities as “included in the Scope of
  Application”:
  - All of the entities within the Insurance Group
  - All other Financial Entities that are outside the Insurance Group but within the Broader
    Group
  - All non-Financial Entities that are outside the Insurance Group but within the Broader
    Group and that pose material risks to the Insurance Group
- Denote in the Inventory of the Group template all other entities as “excluded from the Scope of
  Application”
• Submit the completed Inventory of the Group template to the Lead State Regulator, who would then review and discuss as necessary with the Insurance Group and consult with other involved regulators to determine the final Scope of Application

**Question 3** - For purposes of field testing, do regulators or members of the industry believe any further definitions of materiality should be added to the “Guiding Principles and Steps to Determine the Scope of Application” to increase consistency in application between groups and lead-states?

**Document the Inventory of the Group**

16. When developing an initial inventory of all potential entities, the Field Test Volunteer shall complete the Inventory of the Group template (Schedule 1), which includes all the entities in the insurer’s most recent Schedule Y, along with other relevant Holding Company Filings pertaining to entities directly or indirectly owned by the Ultimate Controlling Person.

   i. This will require entities to complete basic information about each entity, including assets, revenue and net income for each entity on an annual basis. A Volunteer may agree with its Lead State Regulator to provide the data on a sub-grouping basis (see also paragraph 26).

**Question 4** - The attached includes a proposed list of items for an inventory (Schedule 1), which already contemplates within paragraph 25 that the group and the lead state should work together to determine how the inventory of companies (but including all) such should be aggregated, but are there other alternatives such as those proposed by Cigna/Aetna (US regulated entities, Non-US regulated entities, Material Non-Regulated Entities) or some variation of Schedule Y that can be used instead to avoid duplicative reporting?

**Question 5** - For purposes of maximizing the usefulness of field testing and the calculation, NAIC staff proposes adding elements to the Schedule 1 for “Written Premiums” and “Debt.” Are you opposed to this additional information, or do you have any proposed definitions that you think are necessary to be included with these, or any of the other items in Schedule 1 to assist with Field Testing (such definitions may be submitted at a later date)?

**Identify the Insurance Group**

17. Include all entities that fit the criteria identified in the definition of the Insurance Group, above, and denote as such (i.e., included or excluded in the Scope of Application) in the Inventory of the Group template.

**Identify and Include all Financial Entities**

18. Financial Entities within the Inventory of the Group template shall be included in the Scope of Application regardless of where they reside within the Broader Group.

**Identify Risks from the Broader Group**

19. An Insurance Group may be a subset of a Broader Group, such as a larger diversified conglomerate with insurance legal entities, Financial Entities and non-financial entities.

   i. In considering the risks to which the Insurance Group is exposed, it is important to take account of those material risks to the Insurance Group from the Broader Group within which the Insurance Group operates. Entities within the Broader Group but outside the Insurance Group that pose such risks to the Insurance Group should be included within the Scope of Application.
Expedited Approaches

20. To avoid duplicative capital measures for approaches that are essentially similar to the NAIC’s aggregation approach and to address cost/benefit considerations, an expedited alternative is available for the following classes of insurance groups:

i. U.S. groups subject to the Federal Reserve Board’s group capital requirement may provide that capital assessment measure as an acceptable alternative; or

**Question 6** - Should groups that will submit a group capital calculation to the Federal Reserve be allowed to be exempt from the NAIC calculation, and therefore not considering volunteering for Field Testing, and a decision made after testing?

ii. U.S. groups where the Ultimate Controlling Party is an underwriting company that directly or indirectly owns all of the other entities within the Broader Group may provide its Annual RBC report as an acceptable alternative.

**Question 7** - For purposes of field testing, since a decision to participate in field testing is voluntary between an Insurance Group and its lead state, should paragraph 20ii be deleted, and a decision made after testing?

Documentation and on-going assessment

21. The Lead State Regulator should review the Inventory of the Group template to determine if there are entities excluded by the Volunteer that the Lead State Regulator nonetheless believes create other than a non-material risk to its insurance operations. Additional information may be requested by the Lead State Regulator to facilitate this analysis.

22. The exclusion or inclusion of entities within the Scope of Application should be regularly re-assessed.

23. The Field Test Volunteer, together with the Lead State Regulator and with technical support from the field test analysts, would use the above steps, which includes considering the Lead State Regulator’s understanding of the group, including inputs such as Form F, ORSA, and other information from other involved regulators, to determine the Scope of Application.

Considerations for Subsequent Field Test Exercises

24. The Scope of Application should be considered for update on an ongoing basis throughout the field testing exercise, but at least annually. To assist the Lead State Regulator in assessing the Scope of Application, the Inventory of the Group template will be completed by participants to provide information and certain financial data on all the entities in the group for the Lead State Regulator’s and field test analyst’s use in assessing if the entities excluded from the Scope of Application are appropriate. The Lead State Regulator and the Insurance Group should agree on a designation of entities from the inventory that may pose risk of a material adverse impact on the group’s insurance entities and operations. This may allow the GCC to reflect a more risk-sensitive approach and allow the Lead State Regulator to better understand the group.

25. The Lead State Regulator should work with the group in determining whether the inventory should list all entities individually, or whether some should be grouped in a specified way in future iterations of the field test exercise to better illuminate potential areas of risk. For example, groupings of non-insurance, non-Financial Entities with some common traits (business unit, purpose, e.g.) could allow the Lead State Regulator to better understand the group and how they are managed. Thus, while the inventory would include the full combined financial results/key financial information (net
premiums for insurers, total revenues, total net income, total assets, total debt, total capital or equity) for all entities of the Ultimate Controlling Person and all of its controlled entities, such data may be reported based upon major groupings of entities to maximize its usefulness and allow the Lead State Regulator to better understand trends. Annually the Lead State Regulator and the Insurance Group should agree on such groupings.

**Determine Risk Factors for Non-Insurance Entities within the Scope of Application**

26. Non-insurance entities not directly owned by an insurer but within the Scope of Application should use the following methodology to determine the appropriate risk charge to be applied.

**Non-Insurance Testing**

27. Non-insurance entities that have been determined to be within the Scope of Application should include within the template the required risk charges and available capital amounts determined by either the respective regulator of the entity, the methodology outlined below or as modified for captives or scalars. Such entities must be individually listed in the template, and will be tested based upon the following:

A. **Regulated Financial Entities**

   i. **All banks and other depository institutions** - Minimum required by their regulator. Test both a) unscaled; and b) scaled to an RBC equal to 300% ACL.

   ii. **All asset managers and registered investment advisors** – Test both a) 22.5% of Book/Adjusted Carrying Value (BACV); and b) 12% of three-year average revenue based upon ACLI suggestion (BASEL operational risk). In addition to an unscaled calculation, test the BASEL operational risk methodology scaled to an RBC equal to 300% ACL.

   iii. **All other financially regulated entities** - Minimum required by their regulator (not scaled)

B. **Unregulated Financial Entities**

   i. **Other entities that engage in financial activities or services that support the insurer(s)** – Because these entities can pose more risk of a material adverse impact on the group’s insurance entities and operations than other non-regulated entities, a 22.5% charge on the BACV should be tested. These entities are not subject to a minimum capital requirement.

   ii. **Other Financial Entities** - For purpose of the GCC, unregulated Financial Entities include those which create financial risks through products or transactions such as a mortgage, other credit offering, a derivative, corporate guarantees, intercompany indebtedness, operational interdependence, materiality to the application of credit rating methodologies to the overall group rating and other financial links. Because these entities can pose more risk of a material adverse impact on the group’s insurance entities and operations than other non-regulated entities, apply the greater of the following factors:

   - 22.5% of the BACV
   - Notional value of the contract (e.g. a net worth guaranty/indemnification/guaranty multiplied by a probability factor as determined by the company based upon past historical experience)
   - Other proposed factors suggested by testing participants
Grouping of like entities in type 27 Aii and 27 Bi above would be allowed, assuming that the members of the group all use the same accounting rules (e.g., all GAAP), and are at least consistent with the way the group manages their business.

C. Other Non-Insurance, Non-Financial Entities

Non-insurance, non-Financial Entities (including holding companies that are not insurance legal entities) may not be as risky as regulated entities and other Financial Entities. The Lead State Regulator and the group may decide together how best to group such entities and subject them collectively to the following charges for field testing. The agreed-upon basis for such groupings should be disclosed to the field test analysts.

**Test 1-Principle-Past Income/Loss is a sound predictor of risk**
Test a factor that considers the specific net losses/fluxuation in profitability over an economic cycle, where five years is used as a proxy for an economic cycle. This factor will be risk-based not only to the industry, but to the individual company since it considers past performance. The calculation would be determined based upon the following (for each entity or group of entities):

**Test 1a** - Factor to Apply = (Absolute value of the greatest net loss in the past five years/Gross revenue in that year for that entity or grouped entities) Multiplied by the current year gross revenue for the same entity or grouped entities

**Test 1b** - Same as Test 1a, except subject to a minimum charge that assumes a net loss equal to 2% of total gross revenues. The minimum is expected to cover the fact that the group is not consistently profitable or that the losses are not material, but it covers this risk in this way as opposed to requiring a calculation that considers this dependence through the use of a more complex standard deviation of profits over a period of time.

**Test 2- Principle-Potential Capital Needs of Non-Financial Entities is Equivalent to an Operational Risk Charge**
Test a factor that considers non-financial entities as operational risk.

**Test 2a** - Non-regulated entities should be subject to either an operational risk charge as used in Basel III or a 22.5% charge on the BACV. The 12% Basel charge should be scaled to convert to U.S. RBC, thus the scaled factor becomes 2.47% for life insurers (based upon an average RBC Company Action Level ratio of 486%) and a factor of 3.64% for property/casualty (P/C) insurers (based on an average RBC Company Action Level ratio of 332%). A life factor of 3.7% and P/C factor of 5.4% should also be tested, which corresponds to the 300% RBC trend test calibration.

**Test 2B** - Test 3% of BACV.

**Test 3- Principle-Simplicity and Consistency with RBC Requirements**
Test a simpler method specifically, a factor applied to the absolute value of the entities BACV. The relevant RBC charge (22.5% for P&C and Health and 19.5% (post tax) for Life) applied to BACV (post-covariance) should be tested, as well as other alternatives that may be more appropriate for risks posed by entities not owned by an insurer. Consider using the relevant RBC charge applied to BACV, provided groups do so consistently from one year to the next and across all of their entities.

**Question 8** - Should the participating groups and lead states be able to consider other tests that provide information that helps inform the Working Group on whether other considerations to the proposed calculation are appropriate (e.g. that the amount of business
within the group’s foreign insurers is so small [e.g., some of the health insurers] that the impact of the scalars can be shown to be immaterial, and utilized to develop thresholds that could be used for eliminating this requirement if met)?
Schedule 1

The following columns are taken from a proposed Schedule 1 (excel file) and included herein within this format to make readability of what is expected to be included in the Schedule 1 more easily read.

| NAIC #           | FEIN #           | Name of Securities Exchange if Publicly Traded (U.S. or International) | Name of Parent, Subsidiaries or Affiliates | Domicile | Primary Regulator and Contact | Primary Regulator E-Mail | Description & Purpose of Entity | Business Segment | Intercompany Guarantee | Capital Maintenance Agreement (if yes, describe) | Contractual Relationship with Affiliates (if yes, describe) | Basis of Accounting | Assets | Liabilities | Capital | Revenue | Net Income | AM Best Rating | Moody’s Rating | S&P Rating | Prospective Risks | Scope of Application (Y=Include, X=Exclude) | Required Capital |
|------------------|------------------|-------------------------------------------------------------------------|--------------------------------------------|----------|-----------------------------|--------------------------|---------------------------------|-------------------|---------------------|-------------------------------|-------------------------------------------------|--------------------|--------|-------------|---------|---------|-----------|---------------|---------------|-----------|------------|-----------------|------------------------|------------------|
