WILLKIE FARR & GALLAGHER LLP

CLIENT ALERT

NAIC Report: 2019 Summer National Meeting

August 27, 2019

AUTHORS

Leah Campbell | Michael Groll | Donald B. Henderson, Jr. | Allison J. Tam
Elizabeth B. Bannigan

The 2019 Summer National Meeting of the National Association of Insurance Commissioners was held in New York City on August 3 through 6, 2019.

NYDFS Superintendent Linda A. Lacewell greeted meeting attendees and spoke at the opening session of the Summer National Meeting. In her comments, Superintendent Lacewell emphasized New York's leading role in addressing key issues facing state insurance regulators today. She cited New York's cybersecurity rules applicable to insurance licensees as an example, as well as the NYDFS's recent amendment to Regulation 187, applying to insurers and producers the "best interest" standard of care with respect to the sale of life insurance policies as well as annuity products. In November 2018, the best interest rule was challenged in court by New York insurance producer groups. Immediately prior to the Summer National Meeting, the New York State Supreme Court dismissed the plaintiffs' legal challenge and upheld the NYDFS's authority to extend the rule to life insurance products. Superintendent Lacewell also emphasized New York's focus on consumer protection, as evidenced by the recent combining of the Enforcement and Financial Frauds Division with the Consumer Protection Division of the NYDFS. This change has resulted in a new division called the Consumer Protection and Financial Enforcement Division. In addition, a consumer advocate will be named by the NYDFS to work across its divisions in order to put the consumer first in everything the NYDFS does.

Areas of focus for NAIC members at the Summer National Meeting included a number of initiatives related to innovation and technology and continued work on such important NAIC projects as the group capital calculation. This report summarizes some of these key activities at the Summer National Meeting and, as indicated, NAIC interim meetings and conference calls and other developments leading up to the meeting that may be of interest to our clients in the insurance industry.

GLOSSARY

Definitions used in this report include the following:

- "ComFrame" means the Common Framework for the Supervision of Internationally Active Insurance Groups being developed by the IAIS.
- "Covered Agreements" means the U.S./EU Covered Agreement and the U.S./UK Covered Agreement.
- "Credit for Reinsurance Models" means the NAIC Credit for Reinsurance Model Law and the NAIC Credit for Reinsurance Model Regulation.
- "Federal Reserve" means the Board of Governors of the Federal Reserve System.
- "FSB" means the Financial Stability Board, a nonprofit international body, currently composed of 59 representatives from 25 jurisdictions (including representatives from international financial institutions and international standard-setting, regulatory, supervisory and central bank bodies), which monitors and makes recommendations about the global financial system.
- "FSOC" means the Financial Stability Oversight Council of the United States Department of the Treasury.
- "G-SII" means Global Systemically Important Insurer, as designated by the FSB.
- "IAIG" means an internationally active insurance group.
- "IAIS" means the International Association of Insurance Supervisors.
- "NAIC" means the National Association of Insurance Commissioners.
- "NYDFS" means the New York State Department of Financial Services.
- "Qualified Jurisdiction" means a non-U.S. jurisdiction that the NAIC deems to be included on its list of "Qualified Jurisdictions" using the *NAIC Process for Developing and Maintaining the NAIC List of Qualified Jurisdictions*, whereby the NAIC evaluates the appropriateness and effectiveness of the reinsurance supervisory system within such non-U.S. jurisdiction through an evaluation methodology that considers the rights, benefits and the extent of reciprocal recognition afforded by the jurisdiction to reinsurers licensed and domiciled in the United States. The NAIC List of Qualified Jurisdictions is not binding on the states, and each state may also evaluate a non-U.S. jurisdiction to determine if it is a Qualified Jurisdiction. Although individual states must consider the NAIC List of

Qualified Jurisdictions, the ultimate regulatory authority to recognize a Qualified Jurisdiction resides solely in each state.

- “Reciprocal Jurisdiction” means a jurisdiction in which an eligible reinsurer is required to be domiciled in order to qualify for zero reinsurance collateral pursuant to the 2019 revisions to the Credit for Reinsurance Models.
- “SEC” means the United States Securities and Exchange Commission.
- “SIFI” means a systematically important financial institution designated by FSOC.
- “U.S./EU Covered Agreement” means the Bilateral Agreement Between the United States and the European Union on Prudential Measures Regarding Insurance and Reinsurance entered into by such parties on September 22, 2017.
- “U.S./UK Covered Agreement” means the Bilateral Agreement Between the United States and the United Kingdom on Prudential Measures Regarding Insurance and Reinsurance entered into by such parties on December 11, 2018.

I. Topics of General Interest

a. Group Capital

i. Field Testing of Group Capital Calculation Tool Is Underway by the NAIC; More Work to Follow

The Group Capital Calculation (E) Working Group finalized its work on the template for the Group Capital Calculation ("GCC") tool for U.S. insurance groups earlier this year, and field testing of the GCC tool has now commenced. It is currently expected that this field testing process will conclude later this year. Working Group Chair and Florida Insurance Commissioner David Altmaier indicated that the Working Group's goal is to adopt the GCC in 2020, although this timing may be impacted by the results of the field testing.

One of the key areas for the Working Group's future consideration is to determine whether the GCC data will be filed by insurance groups with the NAIC or state regulators after the GCC is adopted. If this occurs, it will be important for a process to be developed pursuant to which this data would be kept confidential. One approach currently under consideration is an amendment to the NAIC Insurance Holding Company System Regulatory Act (Model #440) (the "Model HCA") to include submissions of GCC data in the list of filings granted confidential treatment by regulators. Such an approach would, by its nature, incorporate a lengthy time line for the NAIC's adoption of an amendment to the Model HCA, to be followed by state legislative enactment of such model act amendment—a process that could take up to several years to complete. The Working Group will engage in further discussions of confidentiality for submissions of GCC data over the next few months.

ii. International Developments

A. Update on Development of the ICS

The IAIS is currently in the final stages of policy development with respect to its "International Capital Standard," or "ICS." This work, which is part of ComFrame, is expected to culminate with the adoption of ComFrame and ICS Version 2.0 by the IAIS in November of this year. The ICS will then proceed to a five-year "monitoring period," during which it will not be deemed a prudential capital requirement ("PCR") for IAIGs. The concept that will be "monitored" during the monitoring period is the performance of the ICS itself, and not capital adequacy of the IAIGs. Indeed, the IAIS has repeatedly stated that the ICS Version 2.0 for the monitoring period is not intended to be a tool for decision-making by insurance supervisors or a capital standard on which third parties (which would include, e.g., rating agencies) should rely. After the end of this monitoring period (which will include a further public consultation period), the ICS is expected to be implemented as a PCR starting in 2025.

In preparation for the ICS's expected adoption in November 2019, the IAIS has been engaging in a significant amount of work this year—including field testing of the ICS (with data collection completed earlier this summer and analysis of this data underway); development of further specific criteria relating to monitoring of the ICS during the monitoring period; and early discussions concerning criteria for considering other capital regimes "comparable" to the ICS. The latter initiative is in its early stages, with further discussions to be held by the IAIS concerning comparability over the next few months, prior to expected adoption of the ICS Version 2.0 in November 2019.

B. No Clarity on Comparability

While U.S. regulators continue developing group capital rules for U.S. insurance groups (including the development of the GCC by the NAIC and the development of the "Building Block Approach," or the "BBA," by the Federal Reserve), the key question continues to be whether these group capital rules will be considered "comparable" to international capital standards developed by the IAIS. The answer is far from clear.

At the Summer National Meeting, IAIS representatives reiterated that the IAIS will not commit to determining whether a particular jurisdiction's group capital standard is comparable to the ICS until 2024, which is the end of the five-year ICS monitoring period. Consequently, U.S.-based insurance groups with operations abroad will face regulatory uncertainty during this monitoring period. As noted by U.S. industry members during the Summer National Meeting, the IAIS has not described in official guidance the criteria pursuant to which a group capital regime would be considered "outcome-equivalent" with the ICS.

The IAIS has stated that in order for an aggregation method—such as the GCC and the BBA—to be considered comparable to the ICS, it must provide "substantially the same—in the sense of the ultimate goal" outcomes to the ICS (i.e., an approach that is "outcome-equivalent" to the ICS). Industry members have expressed concern that the IAIS's criteria will be limited to a quantitative exercise that compares one number to another, and will not focus on qualitative aspects of the other jurisdiction's approach to capital or its supervisory framework.

In a May 2019 letter (the "May 2019 Letter"), 42 U.S. senators requested that the Federal Reserve, among other things, urge the IAIS to issue a public letter expressly defining "outcome equivalence" and recognizing both qualitative and quantitative criteria in determining comparability.

Unsurprisingly, the topic of comparability was also the subject of much discussion both at the session of the International Insurance Relations (G) Committee and the IAIS Secretariat Q&A session with interested parties. During these discussions, two new pieces of information emerged regarding comparability—first, IAIS representatives stated that the comparability criteria will likely incorporate both quantitative and qualitative elements, and second, IAIS representatives stated that the decision as to whether a particular jurisdiction's capital standard is comparable to the ICS will be made by the IAIS membership, and not by the IAIS Secretariat.

C. Other Concerns with the ICS Remain

Comparability is far from being the only issue with the ICS that has raised concerns both with members of "Team USA" (i.e., the NAIC, state insurance regulators, the Federal Reserve and the Federal Insurance Office) and with the U.S. insurance industry. As part of his remarks at the NAIC International Forum in May of this year, Eric Cioppa, NAIC President and Superintendent of the Maine Bureau of Insurance, noted that certain members of the industry believe that the ICS is "currently not fit for [its] purpose," and that no amount of technical tweaks can address the fatal design flaws with the ICS. Superintendent Cioppa also stated that IAIS initiatives such as the ICS often "confuse sight for vision" by having a single-minded focus on validating particular approaches or perspectives instead of pursuing outcomes or objectives with which regulators of multiple jurisdictions fundamentally agree. In line with these remarks, the U.S. senators' May 2019 Letter to the Federal Reserve questions the need for the ICS and urges the Federal Reserve to publicly state that a global capital standard for insurers is not required.

In addition to these general concerns, more specific concerns with the ICS abound. For example, the consolidated Market Adjustment Valuation ("MAV") approach used in the ICS is considered by some members of the industry to be unsuitable for calculating capital requirements for insurance groups. Speaking at the NAIC International Forum in May of this year, U.S. Secretary of the Treasury Steven Mnuchin emphasized that the MAV approach in particular can negatively impact the insurance industry's ability to provide long-term savings products, which are especially critical to Americans entering retirement.

Finally, some concern exists that the IAIS is focused on implementing the ICS as a PCR by an agreed-upon date instead of focusing on developing a substantively correct framework prior to its adoption. In line with this concern, U.S. Secretary of the Treasury Steven Mnuchin noted during his remarks at the NAIC International Forum that "getting the ICS right" should be more important to the IAIS than meeting any fixed schedule mandating completion of the ICS at a specific point in time.

Overall, U.S. stakeholders believe that an ICS that is not implementable in the United States—which is a key insurance market—does not constitute a true global capital standard. Time will tell to what extent this message will resonate with the IAIS.

b. Systemic Risk

i. Update on the IAIS's Holistic Framework

Since late 2017, the IAIS has been working on the draft Holistic Framework for Systemic Risk in the Insurance Sector (the "Holistic Framework"). The Holistic Framework would replace the "entity-based approach" to systemic risk, which was the IAIS's initial attempt to address systemic risk after the 2007-2008 financial crisis, with a holistic approach that includes an "activities-based approach" ("ABA") that focuses on potential systemic industry activities and focuses on a broader portion of the insurance sector. However, the Holistic Framework also retains some elements of the previous entity-based approach in recognizing that systemic risk may arise from activities undertaken by a single large insurance company or group. Speaking at the Summer National Meeting, IAIS representatives stated that certain remnants of the entity-based approach are a "permanent feature" of the Holistic Framework, and that the IAIS does not currently intend to remove them.

As with the ICS Version 2.0, the IAIS's goal is to have the Holistic Framework adopted at the IAIS's Annual General Meeting in November 2019. Thereafter, starting in 2020, implementation of the Holistic Framework will commence, including the implementation by jurisdictional supervisory authorities of the revised Insurance Core Principles ("ICPs") and ComFrame related to the Holistic Framework, as well as an annual global monitoring exercise coordinated by the IAIS. The global monitoring exercise is intended to detect the possible build-up of systemic risk in the global insurance sector, and will involve annual data collection and analysis by the IAIS. In light of this, interested parties have urged the IAIS to leverage existing data collection processes and information in regulatory filings instead of requiring the insurance sector to submit significant additional data to the IAIS as part of this global monitoring exercise. As part of the implementation of the Holistic Framework, the IAIS will also assess the implementation of the supervisory material contained in the ICPs and ComFrame that are related thereto.

Because the IAIS's work on the ABA started in 2017, the FSB did not publish a list of G-SIIs in 2017 or 2018. It is expected that if the IAIS adopts the Holistic Framework in November, the FSB will suspend the G-SII identification process until 2022. In 2022, the FSB will review the Holistic Framework and the role of an annual identification of G-SIIs in order to assess whether the Holistic Framework is meeting its objectives. As a result of this review, the FSB may determine that the annual identification of G-SIIs is no longer required.

The IAIS's shift away from the entity-based approach has found support among members of "Team USA." Speaking at the NAIC International Forum, U.S. Secretary of the Treasury Steven Mnuchin stated that the U.S. Treasury supports shifting the focus of systemic risk analysis away from individual insurance groups and towards activities undertaken in the insurance sector. In addition, as described below, FSOC is developing guidance on designating non-bank SIFIs that is based on the ABA.

ii. Update on NAIC'S Macroprudential Initiative

One of the NAIC's top priorities is the Macroprudential Initiative ("MPI"), which is intended to enhance risk identification efforts by building on the state-based regulation system. Key components of the MPI include liquidity; resolution and recovery; capital stress-testing; and counterparty exposure.

As part of the MPI, the NAIC is continuing to develop a liquidity stress-testing framework for certain large U.S. life insurers and insurance groups (likely to be based on amounts of certain types of business written or material exposure to certain investment transactions, such as derivatives and securities lending) as a regulatory tool. This effort is being led by the Liquidity Assessment (EX) Subgroup, which has engaged in significant technical work this year in order to provide a recommendation on the liquidity stress-testing framework to the Financial Stability (EX) Task Force. This work is ongoing, and the Subgroup expects to recommend an approach on liquidity stress-testing to the Task Force by the end of the year.

Separately, the Receivership and Insolvency (E) Task Force received recommendations from its drafting group relating to the MPI referral on recovery and resolution that the Receivership and Insolvency (E) Task Force received from the Financial Stability (EX) Task Force. Among other things, the drafting group has recommended that the Receivership and Insolvency (E) Task Force consider methods to encourage states to adopt key areas of NAIC model receivership law to enhance efficiencies and effectiveness of insurer receivership processes across states. The Receivership and Insolvency (E) Task Force expects to begin work on these recommendations in 2020.

iii. U.S. Federal Developments

A. FSOC Update

During the meeting of the Financial Stability (EX) Task Force, Vice Chair of the Task Force and Superintendent of the Maine Bureau of Insurance Eric Cioppa noted that FSOC is continuing to evaluate comments received on its proposed guidance regarding a revised process for designating non-bank SIFIs. This proposed guidance provides, among other things, that FSOC will identify, assess, and address potential risks and threats to U.S. financial stability through a process that emphasizes an ABA, and that FSOC will pursue entity-specific determinations that an entity should be designated as a non-bank SIFI only if a potential risk or threat cannot be addressed through an ABA. This shift in focus to an ABA is occurring on a parallel track to the development and potential adoption by the IAIS of the Holistic Framework—which recognizes that systemic risk may arise both from the distress of individual entities (i.e., the current entity-based approach) and from collective activities on an industry-wide level (i.e., an ABA).

iv. International Developments

A. IAIS Releases Its Strategic Plan for 2020 - 2024

In June 2019, the IAIS released its Strategic Plan for 2020 through 2024, which states that the IAIS will focus heavily on the following key themes during this five-year period: technological innovation, including FinTech; cyber resilience (including both exposure of the insurance sector to cyber risks and underwriting of cyber risks by insurers); climate risk; "conduct and culture," including potentially developing a "holistic approach to market conduct and prudential supervision"; and financial inclusion and sustainable economic development. This indicates a shift in the IAIS's policy development initiatives from capital, solvency and group supervision matters towards key emerging trends and risks in the insurance market.

c. Innovation and Technology

i. Reconciling Anti-Rebating Laws and Innovation

A predominant focus of the Innovation and Technology (EX) Task Force was how to address concerns shared by regulators and industry members alike that anti-rebating language in the NAIC Unfair Trade Practices Model Act—and inconsistent interpretations of that language across states—may impede innovation designed to prevent or mitigate the risk of loss for consumers. The Unfair Trade Practices Model Act prohibits insurers and producers from providing to insureds/policyholders "anything of value whatsoever not specified in the policy." North Dakota Insurance Commissioner and Task Force Chair Jon Godfread explained that the Unfair Trade Practices Model Act, first introduced over a century ago to protect insurer solvency and to prevent discrimination and unethical sales practices, now presents obstacles to both start-ups and insurers seeking to create and utilize technologies designed to prevent or mitigate loss. A small group of volunteer states that reviewed the language and application of anti-rebating provisions throughout the country found that interpretation and enforcement of such laws varies greatly across states.

At the National Meeting, Commissioner Godfread presented a draft North Dakota Guidance on Rebating document (the "North Dakota Guidance") as "food for thought," and as a possible alternative to formally revising the Model Act. Specifically, the North Dakota Guidance highlights insurers' lack of clarity as to whether innovative benefits that prevent or mitigate risk would be considered impermissible inducements or rebates, and sets forth criteria for "value-added products, services or programs" that insurers may permissibly offer in connection with an insurance policy. The Task Force exposed the North Dakota Guidance for comments to be submitted by September 5, 2019.

The Task Force also discussed a recent bulletin issued by the Ohio Department of Insurance concerning interpretations of anti-rebating language (the "Ohio Bulletin"). Whereas the North Dakota Guidance retains from the Model Act a consideration as to whether the value-added products, services or programs "are specified in the insurance policy," the Ohio Bulletin explicitly sets forth criteria for when such products that "are not specified in the policy" can nonetheless be offered or provided by insurance companies to policyholders.

Notwithstanding discussion of both the North Dakota Guidance and the Ohio Bulletin, the general consensus among regulators was that regulatory guidance alone "might not be enough" to remedy ingrained and inconsistent interpretations of what one regulator described as "archaic" rebating laws. Some regulators noted that the Task Force could develop model guidance and pursue amendments to the Model Act on parallel tracks, and the Task Force passed a motion to develop a Model Law Request to amend the NAIC's Unfair Trade Practices Model Act.

ii. States to "Lead or Be Led" on Data Privacy and Cybersecurity Initiatives

The Innovation and Technology (EX) Task Force also heard an update on data privacy and security initiatives from Director for the South Carolina Department of Insurance Raymond G. Farmer, including state implementation of the

Insurance Data Security Model Law. As of early August 2019, seven states had adopted data security laws modeled on the Insurance Data Security Model Law. Making an NAIC model law an “accreditation” standard for U.S. states encourages adoption of the model act/regulation and results in a measure of state-by-state uniformity. We understand that the NAIC’s accreditation authority, however, does not extend to all model laws—it is focused on model laws affecting financial regulation. Therefore, although state implementation of data security laws is a high priority for the NAIC, the Insurance Data Security Model Law is not an accreditation standard for states. At the Summer National Meeting, NAIC legal staff reported that the U.S. Congress is focused on data privacy and suggested that in connection with regulating data security, the U.S. Congress will look to state regulators to either “lead or be led” in this area.

Further to the Task Force’s encouragement that states implement data privacy and cybersecurity measures, the Task Force approved a motion to refer to the Market Regulation and Consumer Affairs (D) Committee a new and related charge to review state insurance privacy protections regarding the collection, use and disclosure of information obtained from consumers as part of insurance transactions and to recommend any necessary revisions to privacy-related NAIC model laws by the 2020 Summer National Meeting.

iii. Formation of Artificial Intelligence (EX) Working Group

Following an innovator presentation on the use of artificial intelligence to evaluate insurance regulatory compliance, the Innovation and Technology (EX) Task Force voted to form an Artificial Intelligence (EX) Working Group. The Artificial Intelligence (EX) Working Group is charged with studying the development, use and impact of artificial intelligence, and will focus on its role in consumer protection and privacy, marketplace dynamics, and the state-based insurance regulatory framework. The Working Group is charged with providing the Innovation and Technology (EX) Task Force with guidance and recommendations by the 2020 Summer National Meeting.

iv. Formation of Accelerated Underwriting (A) Working Group

The Life Insurance and Annuities (A) Committee voted to form a new Accelerated Underwriting (A) Working Group, which is charged with considering the use of external data and data analytics in accelerated life insurance underwriting. In discussing this item, NYDFS Deputy Superintendent for Insurance James Regalbuto suggested that this Working Group should consider what, if any, diligence insurers perform on the data practices of the insurers’ vendors, such as credit reporting agencies, which are not regulated in the same fashion as insurers, as well as the extent of information that consumers receive upon being entered into or removed from an accelerated underwriting program. Commissioner Godfread (North Dakota) also offered that while forming the Accelerated Underwriting (A) Working Group is a “great step” for the Life Insurance and Annuities (A) Committee, the NAIC will likely need to explore the same issues beyond the context of life and health insurance in the future.

d. Reinsurance

On June 25, 2019, the NAIC adopted revisions to the Credit for Reinsurance Models after over a year of work and multiple exposures of, and comment periods on, draft revisions that followed the execution of the Covered Agreements. For more information on the key provisions of these revisions and their impact, please see our previous client alert on this subject, which is available here.

The Covered Agreements may preempt an inconsistent state law that treats a qualified non-U.S. reinsurer more favorably than a U.S. insurer licensed in that state. The Federal Insurance Office is required under the Covered Agreements to commence this preemption analysis in April 2021 and to complete this analysis in September 2022. This effectively means that each U.S. state will need to enact the revisions to the Credit for Reinsurance Models by September 2022, or face possible federal preemption of those provisions in its credit for reinsurance laws that are inconsistent with the Covered Agreements.

The Credit for Reinsurance Models were reopened by the NAIC several times in the recent past (including in 2011 to permit reinsurers qualifying as certified reinsurers to post reduced reinsurance collateral and in 2016 to permit the adoption of regulations setting forth additional requirements for XXX, AXXX and other business typically ceded to captives). As a result, there is some concern at the NAIC that legislatures in certain states may be delayed in enacting the revised Credit for Reinsurance Models. In order to ensure that states begin their respective processes for adopting the revised Credit for Reinsurance Models as early as possible, the Financial Regulation Standards and Accreditation (F) Committee encouraged the states to begin adopting the revised Credit for Reinsurance Models before the formal process to add these provisions as an accreditation standard begins in Spring 2020.

At the National Meeting, the Reinsurance (E) Task Force heard a report from the Qualified Jurisdiction (E) Working Group, which must reevaluate the current list of NAIC Qualified Jurisdictions (Bermuda, France, Germany, Ireland, Japan, Switzerland and the UK), each of which must be reapproved by the end of 2019. In addition, as a result of the revisions to the Credit for Reinsurance Models, the Qualified Jurisdiction (E) Working Group must now revise the process by which it updates and maintains the NAIC List of Qualified Jurisdictions to additionally consider which Qualified Jurisdictions also satisfy the Reciprocal Jurisdiction requirements of the newly revised Credit for Reinsurance Models, thus entitling reinsurers from those jurisdictions to potentially post zero, as opposed to reduced, collateral. Because France, Germany, Ireland and the UK are currently subject to Covered Agreements, these jurisdictions will automatically be eligible for collateral elimination as Reciprocal Jurisdictions once states begin adopting the amendments to the Credit for Reinsurance Models and thereby incorporating them into their own credit for reinsurance laws and regulations. A process must be developed, however, for evaluating those Qualified Jurisdictions that are not subject to Covered Agreements (Bermuda, Japan and Switzerland) to determine whether they too may be deemed Reciprocal Jurisdictions. Chair of the Qualified Jurisdiction (E) Working Group Robert Wake (Maine) emphasized the importance of developing an evaluation process that will achieve parity of treatment among Bermuda, Japan and Switzerland and the Qualified Jurisdictions subject to the Covered Agreements.

One of the key purposes of the Covered Agreements is to remove certain barriers to reinsurance transactions that were in effect in certain participating jurisdictions before the Covered Agreements were adopted (e.g., local presence requirements for alien reinsurers). These local barriers to reinsurance transactions are also in place in a number of international jurisdictions that are not currently parties to any Covered Agreements, and certain jurisdictions have also enacted laws that have required domestic retention of reinsurance risks, resulting in forced localization of reinsurance. At the Summer National Meeting, a number of interested parties encouraged attending IAIS representatives to have the IAIS consider this issue, with the goal of reducing or eliminating forced localization of reinsurance in particular. In response, IAIS representatives noted that the IAIS has not formally discussed this issue yet, but that there is some understanding at the IAIS that it may be prudent to encourage local supervisors to consider that a governmental policy requiring localization of reinsurance may pose additional prudential risks.

e. Insurance Business Transfer and Division Laws

Since its formation on February 19, 2019, the Restructuring Mechanisms (E) Working Group has heard a number of presentations from state insurance regulators and interested parties concerning corporate division and business transfer laws adopted in various states; the benefits and potential drawbacks of these laws; and business transfer mechanisms that are in effect in certain non-U.S. jurisdictions (e.g., the Part VII transfer mechanism that exists under UK law). At the Summer National Meeting, certain interested parties made presentations to the Working Group concerning the potential benefits of having business transfer laws adopted in the United States, citing in particular the advantages and the positive track record of the UK Part VII transfer mechanism.

Prior to the Summer National Meeting, on an interim conference call, the Working Group heard a presentation from the Connecticut Insurance Department ("CID") regarding Connecticut's corporate division law and the CID's plans to develop a checklist with guidance on what the CID will look for in reviewing division transactions. The Working Group also heard a presentation from the Illinois Department of Insurance ("IL DOI") regarding how the IL DOI plans to review corporate division transactions. The CID and IL DOI both noted that they may be issuing regulations with respect to their respective division laws in the future, but the CID will not issue any regulations until the Working Group has completed its work and the IL DOI would like to review some division transactions before implementing any regulations. To date, the regulators noted, there have not been any division plans submitted in either jurisdiction.

These presentations are intended to aid the Working Group with its development of a white paper including a summary of the current restructuring laws, a discussion of the perceived need for these laws, the issues these statutes are designed to address, and other alternatives available to insurers. The Working Group's goal is to finalize this white paper by the

2020 Summer National Meeting. In furtherance of this goal, the Working Group anticipates developing a draft of this white paper by early 2020.

II. Topics of Interest to the Life Insurance Industry

a. Update on Revisions to the Suitability in Annuity Transactions Model Regulation

The Annuity Suitability (A) Working Group is continuing its work on developing proposed revisions to the Suitability in Annuity Transactions Model Regulation that are intended to elevate the standard of care in existing suitability standards for the sale of annuities and to make consumers aware of any material conflicts of interest. In June 2019, the SEC adopted its final Regulation Best Interest, which sets forth what the SEC calls a "best interest" standard for sales of securities by broker-dealers. As a result, the Working Group is once again considering incorporating a "best interest" standard into the Model Regulation. During the Working Group's meeting, it was emphasized that the Working Group's purpose is to develop a definition of "best interest" (which will be less than a fiduciary standard, but more than a suitability standard), and that the Working Group understands that not every state will support this definition. With this objective in mind, the Working Group will begin drafting revisions to the Model Regulation shortly, with the goal of exposing these revisions in mid-September 2019 and addressing comments in October and November 2019. This would enable the Working Group to provide a recommendation to the Life Insurance and Annuities (A) Committee at the Fall National Meeting.

The NYDFS does not believe that the SEC's Regulation Best Interest truly establishes a "best interest" conduct standard. During the meeting, the NYDFS's representative stated that he is hopeful that the Working Group will have the courage to adopt a "real" standard, which will go farther than the standard in Regulation Best Interest. He also noted that the NYDFS's "best interest" regulation went into effect on August 1, 2019 and survived a challenge in a New York state court. With that in mind, the NYDFS's representative encouraged members of the Working Group to take advantage of the opportunity to purchase a life insurance policy or annuity contract while staying in New York during the Summer National Meeting.

III. Topics of Interest to the P/C Insurance Industry

a. Surplus Lines

The Surplus Lines (C) Task Force exposed a proposal to modify Schedule T in insurance company financial statements to include a new "Part 3," which would include detail on "Home State" premiums written. This proposal would go into effect starting with 2020 annual financial statements. The intent of this proposal is to enable state insurance regulators to reconcile surplus lines premiums reported by surplus lines brokers with surplus lines premium tax information reported by insurance companies, with the goal of ensuring that states are receiving the proper amounts of surplus lines premium taxes.

b. Cannabis Insurance

The Property and Casualty (C) Committee adopted a new white paper, *Regulatory Guide: Understanding the Market for Cannabis Insuranc*e, which was the product of many drafting sessions of the Cannabis Insurance (C) Working Group and much research conducted by regulators. As U.S. states continue to legalize cannabis for medical and recreational purposes, cannabis remains a Schedule 1 substance under federal law, making it illegal to manufacture, distribute or sell. Given the conflicting directives of state and federal laws, banks and insurers largely hesitate to service participants in the cannabis space, which is expected to become a $21 billion industry by 2021. Illustrating the impact of this, the white paper points out that approximately 70 percent of businesses in the cannabis industry have “no relationship with a financial institution,” leaving businesses operating entirely in cash and their crops, property, employees and operations lacking adequate insurance coverage. In this context, the white paper is intended to educate regulators, cannabis industry participants and the broader public about the cannabis industry, to identify the insurance needs and gaps in the industry, and to highlight best practices for insurance regulators.

IV. Briefly Noted

a. Pet Insurance

The Executive (EX) Committee and Plenary adopted a new white paper, *A Regulator’s Guide to Pet Insurance*, which provides an overview of the history, coverage options and other information related to current pet insurance offerings and regulatory requirements. The Pet Insurance (C) Working Group will utilize the white paper in drafting a model law, a development request for which was also adopted by the Executive (EX) Committee at the Summer National Meeting.

b. Formation of New Retirement Group

The Life Insurance and Annuities (A) Committee voted to form a new Retirement Security (A) Working Group that will be dedicated to implementing the Committee’s charge to promote retirement security and will be chaired by Commissioner Stephen C. Taylor (DC). In his comments to the Committee, Commissioner Taylor discussed possible tasks for the Working Group, including drafting a white paper on retirement challenges, reviewing relevant model laws, and developing a public campaign and curriculum regarding the importance of retirement security and financial literacy.

If you have any questions regarding this client alert, please contact the following attorneys or the attorney with whom you regularly work.

Leah Campbell
212 728 8217
lcampbell@willkie.com

Michael Groll
212 728 8616
mgroll@willkie.com

Donald B. Henderson, Jr.
212 728 8262
dhenderson@willkie.com

Allison J. Tam
212 728 8282
atam@willkie.com

Elizabeth B. Bannigan
212 728 8135
ebannigan@willkie.com