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NAIC Capital & Surplus Relief Working Group to Hold Public Hearing on Proposals to Revise Accounting Procedures and Reserve Standards for December 31, 2008 Life Insurer Financial Statements

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The National Association of Insurance Commissioners ("NAIC") Capital & Surplus Relief Working Group has scheduled a public hearing on January 27, 2009, in Washington, D.C., to consider proposed revisions to certain rules and accounting procedures intended to provide capital and surplus relief to life insurers on their December 31, 2008, statutory financial statements. The hearing will be held at the Marriott Wardman Park Hotel, 2660 Woodley Road, beginning at 10 a.m.

The changes in question were originally proposed by the American Council of Life Insurers ("ACLI") in November of last year. The ACLI had requested that they be implemented for December 31, 2008 statutory financial statements, which are required to be filed on or before March 1, 2009. Life insurers have traditionally operated in an environment where capitalization and rating agency ratings are important factors. However, current market conditions have negatively impacted insurers' ability to readily access outside capital. Investors, rating agencies, and prospective purchasers of life insurance products have made increased demands on these insurers for strong capital levels and a high degree of liquidity.

The proposed changes are intended to provide life insurers with near-term relief from certain regulatory requirements and standards that are viewed as overly conservative in their operation. (One of the proposed changes, relating to recognition of deferred tax assets, would have implications for property-casualty insurers as well.) The proposals focus on

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accounting issues, reserve requirements and associated actuarial guidelines, and the application of certain risk-based capital requirements. In response to a contraction of letter of credit capacity and large decreases in trust assets, a request was also made for insurance commissioners to exercise their discretionary authority to allow alternatives to letters of credit and trust agreements as security for their reinsurance. This would permit U.S. insurers to take reserve credit on their statutory financial statements for reinsurance placed with insurers not licensed or accredited in the United States.

In response to this proposal, the NAIC created the Working Group, which in turn has drawn on the technical expertise of NAIC committees and task forces in its work to date. There were preliminary discussions held and reports made at the December 2008 NAIC meeting, and initial draft recommendations were subsequently circulated. A teleconference meeting was held on January 2, 2009, to review the preliminary report and recommendations. The scheduling of a public hearing was announced on the call. There was no vote on any of the proposals at the teleconference meeting.

At this point there appears to be general sympathy for the position of the life insurance industry, but a number of significant hurdles exist. Implementing the requested relief for the 2008 year-end financial statements presents a major challenge in and of itself. The hearing process can be expected to involve substantial written comments and testimony. (The January 2 teleconference had over 200 participants.) Consumer groups have already objected to the perceived truncation of the review process and dilution of regulatory control at a time of deteriorating financial condition on the part of many insurers. Moreover, certain changes require formal consideration and adoption by NAIC committees and technical working groups or amendments to published standards and manuals, and are therefore not likely to be accomplished before the filing deadline for the 2008 financial statements. Even in areas where existing state insurance laws and regulations afford discretionary authority to the regulator, there are concerns regarding the propriety and workability of having some states adopt procedures and other states being unwilling (or lacking statutory authority) to do so.

The NAIC has made clear that any measures ultimately adopted to provide requested relief would not dilute any of the existing solvency standards for insurers or impact upon their ability to pay claims and meet other financial obligations. Reconciling the competing positions and objectives will clearly

present a formidable task. It may also be viewed as a measure of how the existing state regulatory system faces problems and issues that are national in scope and impact.

Additional information regarding the Working Group and its activities, including the ACLI request, the Working Group's report and comments submitted by interested parties, can be found at http://www.naic.org/committees_ex_capital_surplus_relief.htm.

We will be monitoring this issue and reporting on significant developments.

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FOR ADDITIONAL INFORMATION ON THIS ISSUE, CONTACT:



Jeremiah P. Sheehan Mr. Sheehan has had extensive experience in insurance and regulatory matters and has represented a broad range of clients in connection with the financing, acquisition and regulation of life, health and property-casualty insurers and related entities. He has represented clients on a wide range of matters before state insurance departments. He has also advised clients in connection with product development, financial and market conduct examinations, investment law issues, insurance holding company transactions, formation and licensing of insurers and related entities, reinsurance matters, insurer liquidation and rehabilitation proceedings and insurance agency and broker operations.