



INSURANCE LAW BULLETIN

Re: Assessment of Corporate Governance by Insurance Regulators

Assessment of insurance company governance is undergoing a modernization process, evidently in response - at least in part - to national discussions on corporate governance. In light of recent actions taken by the National Association of Insurance Commissioners, the current procedures for assessment, as part of an insurer's financial examination, are likely to change.

In June 2004, the NAIC adopted the *Risk-Focused Surveillance Framework*, a tool specifically tailored to the insurance industry to prospectively assess risk management processes. The *Framework* is a statement of sound risk management principles. As a regulatory tool, it supplements the current retrospective assessment of corporate governance, a process that occurs through annual statement reporting and financial examinations. The *Framework* anticipates that boards and their individual directors take an affirmative role in measuring, managing, and monitoring the risks associated with the insurance business.

After adoption of the *Framework*, the NAIC set out to incorporate *Framework* principles into the financial examination process. Consequently, in December 2006, the NAIC adopted revisions to its Financial Condition Examiners Handbook that were being drafted during the two years that had elapsed since adoption of the *Framework*. Recently, the NAIC published and distributed the new edition of the Examiners Handbook, which incorporates the revisions. As a next step toward adoption of the revisions as uniform standards, the NAIC's Financial Standards and Accreditation Committee will consider mandatory use of the 2007 Examiners Handbook in accredited jurisdictions beginning on January 1, 2010. The implementation date coincides with implementation of the recently adopted NAIC Annual Financial Reporting Model Regulation, which renames the Model Regulation Requiring Annual Audited Financial Reports (Model Audit Rule) and revises it to impose new corporate governance requirements similar to those applicable to public companies under the federal Sarbanes-Oxley Act.

Unless and until use of the 2007 Examiners Handbook becomes a uniform standard for financial regulation, its application in any particular state is discretionary.

The concepts underlying the 2007 Examiners Handbook are the same ones that form the basis for current guidelines in the 2006 Examiners Handbook. However, the level of scrutiny of governance, management, and the enterprise as a whole, is more intense than the level heretofore applied by insurance regulators to a healthy insurer.

It is anticipated that mandatory use of the 2007 Examiners Handbook will be considered at the Spring National Meeting of the NAIC.

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