

CLIENT ALERT

# NAIC Report: 2022 Summer National Meeting

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The 2022 Summer National Meeting of the National Association of Insurance Commissioners (the “Summer National Meeting”) was held from August 9–13, 2022 in Portland, Oregon with attendees participating virtually or in person.

NAIC President and Idaho Insurance Director Dean L. Cameron opened the Summer National Meeting by highlighting the key topics to be addressed during the meeting, including the NAIC’s work regarding the role of private equity ownership in the life insurance industry, efforts relating to the NAIC’s development of a revised bond definition for statutory accounting purposes, and the launch of the Innovation, Cybersecurity and Technology (H) Committee.

As discussed in more detail in this report, highlights from the Summer National Meeting include:

- The Executive (EX) Committee and Plenary adopted a plan to address the list of “Regulatory Considerations Applicable (But Not Exclusive) to Private Equity Owned Insurers”.
- The Statutory Accounting Principles (E) Working Group exposed for comment revisions to the bond definition, SSAP Nos. 26R and 43R, and the related issue paper. This is in addition to the group’s related exposure of reporting changes to Schedule D-1: Long-Term Bonds at an interim meeting held on July 18, 2022.
- The Executive (EX) Committee and Plenary adopted the Pet Insurance Model Act.

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- The Executive (EX) Committee adopted two Requests for Model Law Development to:
  - Replace the *NAIC Insurance Information and Privacy Protection Model Act* (#670) and the *Privacy of Consumer Financial and Health Information Regulation* (#672) with one new model, and
  - Revise the *Property and Casualty Insurance Guaranty Association Model Act* (#540) to ensure that policyholders do not lose guaranty fund coverage as a result of corporate division and insurance business transfer transactions.
- The Financial Condition (E) Committee adopted statutory and blanks revisions regarding related party investment transactions with a December 31, 2022 effective date.

The report below further summarizes key activities at the Summer National Meeting, and certain interim conference calls and other developments leading up to the Summer National Meeting, that may be of interest to our clients in the insurance industry.

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### GLOSSARY

“AI/ML” means artificial intelligence and machine learning.

“Bond Project” means the NAIC’s principles-based bond project, which aims to clarify what should be considered and reported as a bond on Schedule D-1 (Long-Term Bonds) of an insurance company’s statutory financial statement and to improve accounting and reporting.

“CLO” means collateralized loan obligation.

“ComFrame” means the Common Framework for the Supervision of Internationally Active Insurance Groups developed by the IAIS.

“Covered Agreements” means the U.S./EU Covered Agreement and the U.S./UK Covered Agreement, both as defined below.

“Dodd-Frank Act” means the Dodd-Frank Wall Street Reform and Consumer Protection Act.

“Federal Reserve” means the Board of Governors of the Federal Reserve System.

“FEMA” means the Federal Emergency Management Agency.

“FIO” means the Federal Insurance Office of the United States Department of the Treasury.

“FSB” means the Financial Stability Board, a nonprofit international body composed of representatives from international jurisdictions, as well as representatives from international financial institutions and international standard-setting, regulatory, supervisory and central bank bodies, that monitors and makes recommendations about the global financial system.

“GCC” means the group capital calculation that was developed by the Group Capital Calculation (E) Working Group and adopted by the NAIC in December 2020. It is a tool that uses an RBC aggregation methodology for all entities within the insurance holding company system, including non-U.S. entities.

“G-SII” means a Global Systemically Important Insurer, as designated by the FSB.

“Head of the IAIG” means the entity most responsible for the direct management/control of the insurance operations of the group, as designated by the group-wide supervisor, in consultation with other involved supervisors. The Head of the IAIG is not necessarily synonymous with the ultimate controlling person of the holding company system.

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“Holistic Framework” means the framework developed by the IAIS to assess and mitigate systemic risk in the global insurance sector.

“IAIG” means an internationally active insurance group.

“IAIS” means the International Association of Insurance Supervisors.

“ICS” means the Insurance Capital Standard being developed by the IAIS to apply to IAIGs.

“ITC” means innovation, technology and cybersecurity.

“LIBOR” means the London Inter-Bank Offered Rate.

“LST” means Liquidity Stress Test, which provides quantitative and qualitative insights for macroprudential surveillance designed to capture the impact on the broader financial markets of aggregate asset sales under a liquidity stress event.

“LTCI” means long-term care insurance.

“LTCI Framework” means LTCI Multistate Actuarial Rate Review Framework.

“ORSA” means an Own Risk and Solvency Assessment.

“P&P Manual” means the Purposes and Procedures Manual of the NAIC Investment Analysis Office.

“RBC” means risk-based capital.

“SOFR” means the Secured Overnight Financing Rate.

“SSAP” means Statement of Statutory Accounting Principles.

“SVO” means the NAIC’s Securities Valuation Office.

“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.

“VOSTF” means the Valuation of Securities (E) Task Force.

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### I. Private Equity Matters and the Insurance Industry

#### A. NAIC Adopts Private Equity Considerations and Work Plan

At its Summer National Meeting, the National Association of Insurance Commissioners (the “NAIC”) adopted a plan (the “Work Plan”) to address the list of “Regulatory Considerations Applicable (But Not Exclusive) to Private Equity Owned Insurers” (the “Considerations”). The Considerations were developed by the NAIC over the last year and pertain to the ability of state insurance regulators to effectively monitor the solvency of a legal entity insurer and to assess risks faced by the insurer’s holding company system, particularly in the acquisition context.

The Work Plan was previously adopted by the Financial Condition (E) Committee at the NAIC committee level in July 2022, as reported [here](#), and largely serves to refer the Considerations to other NAIC groups for action. Each Consideration, as published, and a summary of the applicable steps in the Work Plan, is listed below.

1. Regulatory Consideration One. Regulators may not be obtaining clear pictures of risk due to holding companies structuring contractual agreements in a manner to avoid regulatory disclosures and requirements. Additionally, affiliated/related party agreements impacting the insurer’s risks may be structured to avoid disclosure (for example, by not including the insurer as a party to the agreement).

**Work Plan:** This Consideration was referred to the Group Solvency Issues (E) Working Group (“GSIWG”) for actions, which may include creating optional disclosure requirements that regulators could use in cases when unresolved regulatory concerns exist with the acquisition. Such disclosures could, per the Work Plan, allow regulators to assess “the goal of the potential owner in acquiring the insurer, how the potential owner will be paid and in what amounts, and the ability of the potential owner to provide capital support as needed.” GSIWG reported at the Summer National Meeting that it plans to address each Consideration referred to it over the next several months.

2. Regulatory Consideration Two. Control is presumed to exist where ownership is greater than or equal to 10%, but control and conflict of interest considerations may exist with less than 10% ownership. For example, a party may exercise a controlling influence over an insurer through Board and management representation or contractual arrangements, including non-customary minority shareholder rights or covenants, investment management agreement (“IMA”) provisions such as onerous or costly IMA termination provisions, or excessive control or discretion given over the investment strategy and its implementation. Asset-management services may need to be distinguished from ownership when assessing and considering controls and conflicts.

**Work Plan:** This Consideration was also referred to GSIWG since it overlaps with Consideration One above. GSIWG may consider if questions should be included in Form A applications about less than 10% owners, or

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if additional disclosure requirements should be added to annual Forms B (Insurance Holding Company System Annual Registration Statement).

3. Regulatory Consideration Three. The material terms of the investment management agreement (“IMA”) and whether they are arm’s length or include conflicts of interest—including the amount and types of investment management fees paid by the insurer, the termination provisions (how difficult or costly it would be for the insurer to terminate the IMA) and the degree of discretion or control of the investment manager over investment guidelines, allocation, and decisions.

**Work Plan:** This Consideration was referred to the Risk-Focused Surveillance (E) Working Group, which is reviewing issues related to affiliated agreements and Form D filings but did not meet at the Summer National Meeting. Particular areas of focus regarding IMAs may include unique termination clauses and use of sub-advisors with the potential for additive fees. In addition, within this Consideration, the Risk-Focused Surveillance (E) Working Group may consider appropriate interest rates for surplus notes.

This Consideration was also referred to the Valuation of Securities (E) Task Force (“VOSTF”), which noted at its meeting on August 11, 2022 that it makes sense to tie this Consideration into the work of VOSTF and the Securities Valuation Office (“SVO”), given the increasing prevalence of “bespoke agreements” for investment management.

4. Regulatory Consideration Four. Owners of insurers, regardless of type and structure, may be focused on short-term results that may not be in alignment with the long-term nature of liabilities in life products. For example, investment management fees, when not fair and reasonable, paid to an affiliate of the owner of an insurer may effectively act as a form of unauthorized dividend in addition to reducing the insurer’s overall investment returns. Similarly, owners of insurers may not be willing to transfer capital to a troubled insurer.

**Work Plan:** At the Summer National Meeting, the NAIC adopted a new actuarial guideline for asset adequacy testing, *Actuarial Guideline LIII—Application of the Valuation Manual for Testing the Adequacy of Life Insurer Reserves* (“AG 53”), which addresses this Consideration and is described in greater detail in Section I.B of this report.

This Consideration was also referred to the Risk-Focused Surveillance (E) Working Group for review related to affiliated agreements and fees, including potentially suggesting guidance for the appropriate entities to provide capital maintenance agreements.



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5. Regulatory Consideration Five. Operational, governance and market conduct practices being impacted by the different priorities and level of insurance experience possessed by entrants into the insurance market without prior insurance experience, including, but not limited to, PE owners. For example, a reliance on TPAs due to the acquiring firm's lack of expertise may not be sufficient to administer the business. Such practices could lead to lapse, early surrender, and/or exchanges of contracts with in-the-money guarantees and other important policyholder coverage and benefits.

**Work Plan:** The Macroprudential (E) Working Group ("MWG"), which is charged with overseeing the Considerations, continues to review this Consideration and whether to refer it to another working group. The MWG is also considering whether to enhance the guidance currently in the NAIC Financial Analysis Handbook regarding Form A filings by PE acquirors of insurers.

6. Regulatory Consideration Six. No uniform or widely accepted definition of PE and challenges in maintaining a complete list of insurers' material relationships with PE firms. This definition may not be required as the considerations included in this document are applicable across insurance ownership types.

**Work Plan:** No action will be taken on this Consideration since regulators agree the focus should be on activities and not specific types of owners. This is consistent with the position that the NAIC has expressed throughout its development of the Considerations that the Considerations may apply to any insurer or owner engaged in the specified activities and not exclusively to private equity owned insurers.

7. Regulatory Consideration Seven. The lack of identification of related party-originated investments (including structured securities). This may create potential conflicts of interests and excessive and/or hidden fees in the portfolio structure, as assets created and managed by affiliates may include fees at different levels of the value chain—for example, a collateralized loan obligation ("CLO"), which is managed or structured by a related party.

**Work Plan:** The Statutory Accounting Principles (E) Working Group ("SAPWG") developed, and the NAIC adopted in June 2022, revisions to related party transaction reporting requirements effective for year-end 2022, as we previously reported [here](#). These revisions include new codes for reporting related party transactions that identify the role of the related party on new columns on insurers' year-end investment schedules. Regulators are comfortable with this as a first step to address this Consideration, although the Risk-Focused Surveillance (E) Working Group's work may also touch on this.

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8. Regulatory Consideration Eight. Although the NAIC's Annual and Quarterly Statement blanks include affiliated investment disclosures, it is not easy to identify underlying affiliated investments and/or collateral within structured security investments. Additionally, transactions may be excluded from affiliated reporting due to nuanced technicalities. Regulatory disclosures may be required to identify underlying related party investments and/or collateral within structured security investments. This would include, for example, loans in a CLO issued by a corporation owned by a related party.

**Work Plan:** The approach to this Consideration overlaps with Consideration Seven, above, regarding SAPWG's new reporting requirements, and Consideration Ten, below, related to privately structured securities.

9. Regulatory Consideration Nine. Broader considerations exist around asset manager affiliates (not just PE owners) and disclaimers of affiliation avoiding current affiliate investment disclosures.

**Work Plan:** A new Schedule Y, Part 3 is in effect for year-end 2021 to identify all entities with a greater than 10% ownership, regardless of whether a disclaimer is in place. Additionally, SAPWG's ongoing Bond Project, discussed further in Section II.A, addresses this Consideration. The Bond Project aims to clarify what should be considered and reported as a bond on Schedule D-1 (Long-Term Bonds) of an insurance company's statutory financial statement with a principles-based bond definition. Reporting changes are expected in 2024, on which we have reported in greater detail [here](#). No action was taken on this item at the Summer National Meeting, but comments on currently proposed reporting changes are due on October 7, 2022.

10. Regulatory Consideration Ten. The material increases in privately structured securities (both by affiliated and non-affiliated asset managers), which introduce other sources of risk or increase traditional credit risk, such as complexity risk and illiquidity risk, and involve a lack of transparency.

**Work Plan:** The new AG 53, discussed further in Section I.B, addresses this Consideration, since it includes disclosure requirements for these risks. This Consideration was also referred to VOSTF. As part of their overall work in assessing appropriate risk-based capital ("RBC") charges for CLOs, it was reported at VOSTF's August 11 meeting that the SVO and RBC Investment Risk and Evaluation (E) Working Group will proceed with working on a proposal to ensure that the aggregate RBC factor for owning all tranches of a CLO is the same as that required for owning all of the underlying loan collateral, in order to avoid RBC arbitrage. This change would be implemented at year-end 2023 at the earliest. VOSTF noted that the NAIC agrees with interested parties that CLOs are important to U.S. capital markets and said insurers will still be able to participate in the CLO market, while avoiding the risk of aggressive structuring that puts policyholders in jeopardy.

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The Examination Oversight (E) Task Force may also consider ways to allow regulators to obtain more information on CLO investments, such as monthly collateral reports or details regarding the underlying portfolio companies affiliated with a CLO manager.

11. Regulatory Consideration Eleven. The level of reliance on rating agency ratings and their appropriateness for regulatory purposes (e.g., accuracy, consistency, comparability, applicability, interchangeability, and transparency).

**Work Plan:** This Consideration was referred to VOSTF, which previously formed an ad hoc group to address this in what is expected to be a multi-year project. At its latest meeting, VOSTF discussed its proposal to add fixed income analytical measures to reporting requirements for bond investments (as an alternative way to measure a security's risk) and exposed a staff memorandum for comment regarding this proposal. In particular, VOSTF is considering whether the additional data should be gathered and reported to regulators by the SVO (which would require a significant investment of resources by the NAIC) or self-reported by insurers. Additional updates related to ongoing initiatives at VOSTF are discussed in Section II.C.

12. Regulatory Consideration Twelve. The trend of life insurers in pension risk transfer (PRT) business and supporting such business with the more complex investments outlined above.

**Work Plan:** This Consideration is intended to be addressed by the new AG 53 that generally aims to ensure claims-paying ability with respect to complex assets. There is also a new charge in the 2021 Life Risk-Based Capital Formula related to longevity risk transfer business, which regulators will monitor. The MWG will continue to review this Consideration.

13. Regulatory Consideration Thirteen. Insurers' use of offshore reinsurers (including captives) and complex affiliated sidecar vehicles to maximize capital efficiency, reduce reserves, increase investment risk, and introduce complexities into the group structure.

**Work Plan:** The new AG 53 addresses this Consideration because it requires a company to provide commentary on reinsurance collectability and counterparty risk in its asset adequacy analysis. The MWG is considering other actions with respect to this Consideration (such as additional holding company act requirements with respect to affiliated reinsurers), but has deferred specifying those actions pending meetings with industry representatives.

At the Summer National Meeting, MWG Chair Justin Schrader (NE) reported that the MWG plans to monitor the other NAIC groups' activities and provide periodic status updates on the Considerations. In addition, NAIC staff will post a document tracking the 13 Considerations and copies of the referral letters on the MWG website, available [here](#).

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### B. New Asset Adequacy Testing Guideline

The Executive (EX) Committee and Plenary also adopted AG 53, referenced above, as part of the NAIC's focus on overseeing the increase in private equity and complex assets in the life insurance industry. Approved earlier during the summer by the Life Actuarial (A) Task Force and Life Insurance and Annuities (A) Committee, AG 53 requires additional disclosures related to private equity and complex assets supporting annuities, pension risk transfers, and other life insurance products.

Specifically, AG 53:

- requires sensitivity testing and analysis of reserve adequacy and claims-paying ability in moderately adverse conditions;
- identifies expectations for valuing complex assets within asset adequacy analysis;
- clarifies elements in establishing margins on asset-related assumptions; and
- requires additional documentation of investment fee income relationships with affiliated entities or entities close to the insurer.

Due to the Life Actuarial (A) Task Force's aggressive timeline for adopting AG 53, further discussion and development is expected. AG 53 will apply to life insurers with (a) more than \$5 billion of general account actuarial reserves and non-unitized separate account assets, or (b) more than \$100 million of general account actuarial reserves and non-unitized separate account assets and over 5% of supporting assets that constitute "Projected High Net Yield Assets" as defined in AG 53. AG 53 will be effective for asset adequacy analysis of reserves reported in annual statements as of December 31, 2022 and thereafter.

### C. Other NAIC Macroprudential Initiatives

#### 1. Liquidity Stress Test

The MWG is encouraged by the initial results of the 2021 LST and will publish a summary of the results with in-depth analysis in the fall of 2022. At the Summer National Meeting, Mr. Schrader summarized the initial results of the 21 life insurance groups' filings, which were due on June 30 and are intended to provide insights for macroprudential surveillance and capture the impact on the broader financial markets of aggregate asset sales under a liquidity stress event. After aggregating the test results from the five stress scenarios, total assets sold by the groups increased for the baseline and adverse scenarios, but decreased for the other scenarios compared to last year's results. Notably, the amount of asset sales during the stress scenarios would not have been significant to the broader financial markets.

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With respect to LST and separate accounts, the MWG has created a study group to address which separate account products should be included in LST filings and how to do so appropriately. While the exact timing was not discussed, the goal is to determine the macroprudential impact of these products on the broader financial market.

For more information about the LST, see our 2021 Fall National Meeting report, available [here](#).

### 2. Macroprudential Risk Assessment

In April 2022, the Financial Stability (E) Task Force and the MWG jointly adopted the Macroprudential Risk Assessment, as previously reported [here](#), to allow insurance regulators to proactively identify and monitor risks that could impact the insurance industry and U.S. financial stability. The Macroprudential Risk Assessment uses a method that is consistent with an “activities-based” approach to systemic risk.

The MWG has since begun executing the steps outlined in the Macroprudential Risk Assessment process document, available [here](#), including by meeting with insurance regulators to discuss the risk assessment categories (e.g., credit and liquidity) and create risk indicators within each such category. Quantitative and qualitative inputs will be aggregated to create a baseline assessment of risk exposure in the insurance industry, and each risk category will be assigned an overall level and trend. The MWG intends to provide regulators with a detailed, confidential report in late September 2022 and to publish a public summary dashboard later this year. The MWG will then consider whether to take action based on the confidential report contents, such as asking the NAIC’s Center for Insurance Policy and Research to help assess climate change risks or sending referrals to other NAIC working groups.

## II. **Financial Condition Regulation**

### A. Bond Project Update

Work continues on the NAIC’s Bond Project, which aims to clarify what should be considered and reported as a bond on Schedule D-1 (Long-Term Bonds) of an insurance company’s statutory financial statement and to improve accounting and reporting. At a high level, the draft principles-based bond definition (the “Bond Definition”) starts by defining a bond as “any security representing a creditor relationship, whereby there is a fixed schedule for one or more future payments, and which qualifies as either an issuer credit obligation or an asset backed security,” and provides detailed instruction for applying this, including with respect to the meanings of a qualifying issuer credit obligation, asset backed security (“ABS”) and other terms used in assessing whether an investment may be considered a bond.

After exposing an updated Bond Definition in March 2022 and discussing comments received at the 2022 Spring National Meeting, SAPWG met on July 18, 2022 to discuss a package of revisions to the Bond Definition, relevant SSAPs and the

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related issue paper. At the Summer National Meeting, SAPWG voted to expose these items, as revised, for a comment period ending October 7, 2022. Revisions in this exposure include:

1. Minor revisions to the Bond Definition, including to clarify the treatment of securities with “plain-vanilla” inflation adjustment mechanisms (e.g., U.S. Treasury Inflation-Indexed Securities), and to revise the defining characteristics of an ABS to generally require pre-determined and contractual principal and interest payments (whereas this requirement had previously been limited to instances where the ABS issuer’s assets were equity interests);
2. Minor revisions to the related issue paper including a discussion of feeder funds and how the assessment should focus on the substance of the underlying investment in determining bond classification (i.e., feeder fund structures shall neither automatically be assumed to qualify for, nor automatically be precluded from, bond classification);
3. Revisions to SSAP No. 26R (*Bonds*) to incorporate the Bond Definition in its entirety; and
4. Revisions to SSAP No. 43R (*Asset Backed Securities*) to incorporate those portions of the Bond Definition related to asset backed securities and to change the name of the SSAP from “Loan-backed and Structured Securities” to “Asset Backed Securities.”

SAPWG is working to implement the new Bond Definition through appropriate revisions to the SSAPs, including through these revisions to SSAP Nos. 26R and 43R. Changes to align other SSAPs with the Bond Definition are expected to be proposed at future meetings, and SAPWG invites interested parties to notify NAIC staff of additional SSAPs that should be so conformed. Revisions to the SSAPs are not expected to be effective until January 1, 2024 at the earliest.

Also in connection with the Bond Project, on July 18, 2022, SAPWG exposed significant reporting changes for reporting bond investments, including a proposal for a Schedule D-1: Long-Term Bonds schedule with more granular reporting lines to separate issuer obligations and asset backed securities and revised reporting lines and instructions for investment classification. The comment deadline for these reporting revisions is also October 7, 2022.

### B. Update on Related Party Reporting Revisions

Following its discussion of proposed revisions to SSAP No. 25 (*Affiliates and other Related Parties*) and SSAP No. 43R (*Loan-backed and Structured Securities*) at the 2022 Spring National Meeting, SAPWG adopted these revisions on May 24, 2022. These revisions are intended to clarify the definition of control in the P&P Manual and create new financial statement reporting requirements for investment transactions with related parties.

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At the Summer National Meeting, subsequent to SAPWG's May 24, 2022 adoption of these revisions, the Accounting Practices and Procedures (E) Task Force and the Financial Condition (E) Committee formally adopted the changes. In conjunction with the adopted revisions to SSAP Nos. 25 and 43R, the addition of a new electronic reporting column will be effective at year end, starting with 2022 Annual Statement filings.

The revisions to SSAP No. 25 add a paragraph clarifying that control of an entity (including limited partnerships, trusts and other special purpose entities) may be found through arrangements other than voting interests. The revisions to SSAP No. 43R clarify that investments within the scope of SSAP No. 43R include investments issued by a related party or acquired through a related party transaction or arrangement subject to SSAP No. 25. Under corresponding changes adopted by the NAIC's Blanks (E) Working Group, related party transactions are now to be reported using new reporting codes that identify the role of the related party on new columns on the year-end investment schedules (Schedules B, BA, D, DA, DB, DL, and E) for life, accident and health/fraternal insurers; property and casualty insurers; health insurers; and title insurers. For additional background on these SSAP revisions, please see our Client Alert on the subject, published [here](#).

### C. Updates Related to Valuation of Securities and P&P Manual

In addition to topics related to investment management agreements, rating agency ratings and CLOs, as discussed in Section I.A of this report, VOSTF discussed initiatives related to the SVO's credit quality assessment of investments made by insurance companies.

1. VOSTF Adopts P&P Manual Amendment to Clarify Role of SVO. VOSTF adopted an amendment to the P&P Manual intended to confirm the SVO's role in working with statutory accounting colleagues in matters of interpreting insurers' accounting and reporting. The amendment states that the SVO may provide state regulators with its opinion of an insurer's statutory accounting and reporting, including whether a particular investment would not or might not be eligible for reporting on Schedule D or Schedule BA, although such opinion is not authoritative and may not reflect the opinion of the relevant state regulator. VOSTF rejected the interested parties' proposal that the SVO should be required to notify an insurer when it shares its opinion on any particular security with a regulator.
2. Related Party Reporting. At SAPWG's request, VOSTF is considering whether any amendments to the P&P Manual are needed to reflect the NAIC's adoption of revisions to related party reporting requirements, as discussed in Section I.A above.

### D. NAIC to Address RBC Treatment of CLO Investments

The Risk-Based Capital Investment Risk and Evaluation (E) Working Group adopted its updated working agenda for 2022 and will prioritize issues referred to it by the Financial Condition (E) Committee. In particular, the Working Group will

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focus on evaluating appropriate RBC charges for CLOs and other asset backed securities. Regulators' concerns with CLOs and other structured securities stem from what Chair Philip Barlow (DC) referred to as the possibility of "risk arbitrage," i.e., under present RBC formulas, an insurer's ownership of every tranche of a CLO has a lower risk weighting than ownership of the underlying assets, even if the insurer is in the same economic position as direct ownership. Moving forward, the Working Group is looking to consider the RBC treatment of structured securities more generally, beyond CLOs or residual tranches.

### III. Reinsurance Matters

The Reinsurance (E) Task Force met virtually on July 25, 2022 in lieu of the Summer National Meeting, and heard updates regarding the following developments.

#### A. Update on Reinsurance Collateral Reduction Applications and Passporting

At the July 25 interim meeting, the Reinsurance Financial Analysis (E) Working Group ("ReFAWG") reported to the Task Force on its continued assistance to states reviewing reinsurance collateral reduction applications to determine whether an applicant reinsurer meets the regulatory requirements to be recognized as a Certified Reinsurer and/or a Reciprocal Jurisdiction Reinsurer, and expressed confidence that the *ReFAWG Review Process for Passporting Certified and Reciprocal Jurisdiction Reinsurers* has been working well.

In May 2022, ReFAWG approved eight applications for Reciprocal Jurisdiction Reinsurer status and one application for Certified Reinsurer status. In total, 22 Reciprocal Jurisdiction Reinsurers have been approved for "passporting," the process giving a state discretion to defer to the collateral reduction (i.e., Certified Reinsurer and/or a Reciprocal Jurisdiction Reinsurer) status of a reinsurer by another state. ReFAWG plans to meet again in 2022 to approve additional applications. The NAIC publishes a complete list of Certified Reinsurers and Reciprocal Jurisdiction Reinsurers [here](#), along with a list of insurance department representatives best suited to answer questions about reinsurance collateral reduction applications in each state [here](#).

#### B. Updates Related to Qualified and Reciprocal Jurisdictions

The Mutual Recognition of Jurisdictions (E) Working Group (formerly the Qualified Jurisdictions (E) Working Group) recommended that all jurisdictions included on the *NAIC List of Qualified Jurisdictions* and the *NAIC List of Reciprocal Jurisdictions* should maintain their respective statuses. The Working Group noted that South Korea remains under consideration for inclusion on the *NAIC List of Reciprocal Jurisdictions*, but that its data localization requirements will need to be revised before it can move forward in the process of Reciprocal Jurisdiction Reinsurer recognition. Later in 2022, the Working Group plans to meet to discuss the efficacy of its review process.



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The Working Group also oversees the process for evaluating and maintaining the *NAIC List of Jurisdictions That Recognize and Accept the Group Capital Calculation*, which was adopted by The Financial Condition (E) Committee at the Summer National Meeting.

### C. State Implementation of the 2019 Revisions to the Credit for Reinsurance Models Nears Completion

Presenting to the Accreditation Financial Regulation Standards and Accreditation (F) Committee at the Summer National Meeting, Holly Weatherford (NAIC) reported that all 56 U.S. jurisdictions had adopted the equivalent of the 2019 amendments to the *Credit for Reinsurance Model Law* (#785), and 51 jurisdictions had adopted the *Credit for Reinsurance Model Regulation* (#786), with action pending or expected in the five remaining U.S. jurisdictions. Consistent with the messaging at the interim meeting of the Reinsurance (E) Task Force, she expressed optimism that both Credit for Reinsurance Models will be adopted across all jurisdictions by September 1, 2022—i.e., the date that, under both Covered Agreements, state credit for reinsurance laws may be federally preempted if they result in non-U.S. reinsurers subject to the Covered Agreements being treated less favorably than U.S. reinsurers. The amendments to the Credit for Reinsurance Models were adopted by the NAIC in June 2019 to conform to the requirements of the Covered Agreements. The amendments will become an NAIC accreditation standard as of September 1, 2022, with enforcement beginning on January 1, 2023.

The Dodd-Frank Act authorizes FIO to make federal preemption determinations, pursuant to the Covered Agreements, and the NAIC reported at the Summer National Meeting that it has been in frequent communication with FIO regarding its review of state laws and regulations in this regard. The NAIC reported that FIO has praised the efforts of both the NAIC and states, that FIO is working with states on “technical corrections” and that the NAIC is not concerned that interactions with FIO will result in federal preemption.

At its interim meeting in July, the Reinsurance (E) Task Force reminded states that they must also establish a website with information about the application process for Reciprocal Jurisdiction Reinsurers and a listing of Reciprocal Jurisdiction Reinsurers operating in the state, along with contact information for directing questions on the Reciprocal Jurisdiction Reinsurers recognition process (available [here](#)). Although not required by law, the Task Force recommended submission of applications to ReFAWG in order to ensure uniformity in the review process, which can better equip ReFAWG to answer questions from governments, foreign jurisdictions or other interested parties.

### D. Other Updates

The XXX Model Regulation, which is intended to establish uniform, national standards governing reserve financing arrangements for life insurance policies, becomes an accreditation standard on September 1, 2022 with enforcement beginning on January 1, 2023. Since the 2022 Spring National Meeting, ten additional states have adopted the XXX

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Model Regulation with four more states considering its adoption. The Task Force was reminded that if a state adopts the XXX Model Regulation, it also will need to adopt Section 5B(4) of the *Credit for Reinsurance Model Law* (#785).

The XXX Model Regulation mirrors Actuarial Guideline XLVIII—Actuarial Opinion and Memorandum Requirements for the Reinsurance of Policies Required to be Valued under Sections 6 and 7 of the NAIC Valuation of Life Insurance Policies Model Regulation (“AG 48”). Under the accreditation standards, a state may meet the requirements through an administrative practice, such as an actuarial guideline like AG 48. While 20 states have adopted the XXX Model Regulation as of July 8, 2022, others may be in compliance with the NAIC accreditation standard through this approach.

### IV. Innovation, Cybersecurity and Technology

Meeting for the second time at the Summer National Meeting after its inaugural meeting in the spring, the (H) Committee continues to develop the ITC Hub, announced in April 2022, which will serve as a portal where users can access ITC-related resources, and identify ongoing NAIC projects related to these topics. Additional updates regarding the (H) Committee’s work and related developments are described below.

#### A. NAIC to Develop New Privacy Model Law

At the Summer National Meeting, both the (H) Committee and the Executive (EX) Committee approved a Request for NAIC Model Law Development from the Privacy Protections (H) Working Group, seeking to replace two existing models—the *NAIC Insurance Information and Privacy Protection Model Act* (#670) and the *Privacy of Consumer Financial and Health Information Regulation* (#672)—with one new model. The existing models have not been broadly adopted by states and require extensive revisions, and replacing these with a single, new model is intended to promote efficiency and uniform protections across states. An exposure draft is expected by the 2023 Summer National Meeting.

##### 1. Federal Privacy Bill

The Privacy Protections (H) Working Group received an update on state and federal privacy-related legislation from Jennifer McAdam and Brooke Stringer of the NAIC. They reported that privacy bills are pending in six jurisdictions, and that on July 20, 2022, the U.S. House Committee on Energy and Commerce approved the American Data Privacy and Protection Act (the “ADPPA”) by a vote of 53 to 2. The ADPPA would allow a private right of action for consumers and preempt most of the states’ privacy laws with several nuanced exemptions. Despite its advancement from Committee, the ADPPA is facing strong headwinds prior to a full chamber vote including upcoming midterms and lack of support from key senators.

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### B. Developments Relating to Artificial Intelligence and Machine Learning

Key updates relating to AI/ML are summarized below:

- The (H) Committee remains focused on developing the “Collaboration Forum” as a platform for multiple NAIC committees to work together to identify and address foundational ITC-related issues, first announced in April 2022 as we reported [here](#). The Collaboration Forum’s first project addresses algorithmic bias – i.e., unfair discrimination by insurers during an insurance transaction resulting from bias in AI/ML-driven algorithms and complex predictive models. As part of this inaugural project, the (H) Committee established five goals: (i) to identify all NAIC working groups actively engaged in addressing algorithmic bias; (ii) to identify such groups’ projects and work products to promote awareness and information sharing; (iii) to provide foundational education about algorithmic bias and develop a common vocabulary; (iv) to identify foundational issues resulting in or causing algorithmic bias; and (v) to establish a regulatory framework to address the use of AI/ML in the insurance industry. These five goals are likely to culminate with a model regulation for AI/ML use, or some form of regulatory guidance.
- The Big Data and Artificial Intelligence (H) Working Group continues to analyze results of its AI/ML surveys in private passenger auto insurance and expects to provide a full report on the analysis at the 2022 Fall National Meeting. The Working Group is also developing AI/ML surveys for the homeowners and life insurance spaces. The homeowners survey is nearing completion, and a draft of the life insurance survey is expected to be circulated for public comment by the end of August 2022.
- The same Working Group is in the early stages of considering how to evaluate third-party data and model vendors and plans to report findings to the (H) Committee by the 2022 Fall National Meeting. Approaches may include creating a library of approved third-party vendors, or requiring that an actuary or other professional verifies the AI standards used by a third-party vendor before an insurance company contracts with the vendor.

### C. Cybersecurity Updates

Cybersecurity (H) Working Group Co-Chair Cynthia Amann (MO) reported that the NAIC *Insurance Data Security Model Law* (#668) has been adopted by twenty-one states, with additional states expected to adopt in the next two years.

In addition, the Working Group is developing a state insurance regulator cybersecurity survey to better understand each insurance department’s cybersecurity policies and resources, and may develop a response plan to aid regulators when a cybersecurity event occurs in the insurance industry.

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### V. Topics of Interest to the Life Insurance Industry

#### A. SOFR Replaces LIBOR for Swap Spreads

During the Summer National Meeting, the Executive (EX) Committee and Plenary adopted nine amendments to the 2023 NAIC Valuation Manual, previously adopted by the Life Insurance and Annuities (A) Committee at its July 20 interim meeting. Most notably, these included amendment proposal form (APF) 2022-04, naming SOFR as the official replacement for LIBOR in setting swap spreads, and providing the methodology that NAIC staff will use to set both short-term and long-term swap spreads. Although this amendment is set to take effect in 2023, NAIC staff submitted a recommendation to the Life Actuarial (A) Task Force to transition to SOFR for the remainder of 2022, upon finalizing contract work with the data providers that will provide SOFR data, which is expected in the coming months.

### VI. Topics of Interest to the P/C Insurance Industry

#### A. NAIC Adopts Pet Insurance Model Act

At the August 13 Joint Meeting of Executive (EX) Committee and Plenary, Executive (EX) and Plenary adopted the Pet Insurance Model Act. The Pet Insurance Model Act establishes a more uniform pet insurance framework for states, and defines a regulatory structure related to pet insurance, including issues such as producer licensing, policy terms, coverages, claims handling, premium taxes, disclosures, arbitration and preexisting conditions.

#### B. Corporate Division and Insurance Business Transfer Transactions: NAIC to Revise P&C Guaranty Association Model Act

The Executive (EX) Committee adopted a Request for Model Law Development to amend the *Property and Casualty Insurance Guaranty Association Model Act* (#540) to ensure that policyholders do not lose guaranty fund coverage as a result of corporate division (“CD”) and insurance business transfer (“IBT”) transactions. The referral stems from the Restructuring Mechanisms (E) Working Group’s efforts to draft a white paper on state laws regarding IBTs and CDs, during which one area of focus was the importance of policyholders retaining guaranty fund coverage after an IBT or CD. During that process, the National Conference of Insurance Guaranty Funds suggested that technical gap laws may exist in states that have adopted Model 540, and that revisions to state guaranty fund laws would be needed to address this issue.

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### C. Climate and Resiliency Updates

Key updates related to the work of the Climate and Resiliency (EX) Task Force are provided below:

- Since the 2022 Spring National Meeting, the Climate and Resiliency (EX) Task Force made referrals to the Financial Examiners Handbook (E) Technical Group, Financial Analysis Solvency Tools (E) Working Group and ORSA Implementation (E) Subgroup to consider making climate-related revisions to the NAIC's *Financial Condition Examiners Handbook*, the *Financial Analysis Handbook*, and the *ORSA Guidance Manual*, respectively. The referrals included recommendations that climate change risks be factored into insurers' investment portfolios, underwriting strategies and risk management frameworks.
- The Task Force will continue to monitor state use of the NAIC's Insurance Climate Risk Disclosure Survey, adopted by the NAIC at the 2022 Spring National Meeting as reported [here](#), although as of the Summer National Meeting it was unclear whether states have begun using the Climate Risk Survey since its April 2022 adoption.

### D. National Flood Insurance Program Reauthorization

The latest extension of the National Flood Insurance Program expires at the end of September, and another short term extension is expected. FEMA sent Congress a list of 17 legislative proposals, including a 10-year authorization, but they are widely viewed as aspirational given the political dynamics in Congress.

## VII. International Matters

### A. Public Consultation on the Comparability Criteria for Group Capital Standards

The International Insurance Relations (G) Committee heard updates on certain of the IAIS's key projects and priorities. Most notably, on June 15, the IAIS began its public consultation on the draft criteria that will be used to determine whether the aggregation method ("AM"), which forms part of the GCC, will produce comparable outcomes to the ICS. Comments were due on August 15.

Feedback on the IAIS draft criteria from the U.S. insurance industry has been critical. The (G) Committee heard a presentation on the "Potential Impact of the [IAIS's ICS] on the Life Insurance Industry, Policyholders and Markets in the United States" (the "IPAC Report," available [here](#)), which was provided to the Federal Reserve by the Insurance Policy Advisory Committee ("IPAC"), a group established by Congress in 2018 to advise the Federal Reserve on international capital standards.

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The IPAC Report was based on a study that used data from six large U.S. life insurers, with the goal of evaluating the impact of the ICS on U.S. insurers. The IPAC Report concluded that:

the ICS, in its present form, does not appropriately reflect the product and risk-mitigation features of long-duration life and retirement products sold in the U.S. and, perhaps just as important, it does not reflect how investment choices available in U.S. capital markets support such long duration products. ... [For instance, the] ICS fails to reflect several relevant asset classes and is overly reactive to credit spread movements[, and it] does not recognize dynamic hedging programs or the use of long-term alternative assets in liability management.

During a Q&A session, Romain Paserot, IAIS Deputy Secretary General and Head of Capital and Solvency, referred to the IPAC Report as an important contribution to the consultation process.

At the (G) Committee's interim meeting on July 21, interested parties were still reviewing the draft criteria, although several parties expressed concerns. They noted that the proposed criteria are too focused on quantitative data, rather than taking a more holistic approach of applying a certain level of judgment and considering both quantitative and qualitative aspects. The interested parties also expressed that the criteria disregard fundamental differences between the AM and ICS and set up a comparison which expects the AM to operate the same as the ICS.

The IAIS intends to finalize the criteria later this year, and for the comparability assessment to begin in the third quarter of 2023. The IAIS Secretariat, led by Secretary General Jonathan Dixon, will oversee the comparability assessment team that shares technical information with an IAIS task force that makes a recommendation to the IAIS's Executive Committee. The final decision on comparability will be made by the IAIS's Executive Committee. The ICS will also undergo a public consultation in 2023 in preparation for the ICS implementation as a group-wide prescribed capital requirement for IAIGs following the completion of the five-year monitoring period in 2024.

### B. Other IAIS Updates

A brief update on certain other key priorities at the IAIS is provided below.

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1. Holistic Framework. The Global Monitoring Exercise (“GME”), which is part of the Holistic Framework, will conclude this year. As part of the GME, the IAIS has completed numerous data calls, including data collections on climate risk and cybersecurity. In late 2022, the IAIS will submit a report to the FSB on the implementation assessment of the Holistic Framework, which will inform the FSB’s decision on whether to discontinue or reestablish the G-SII designation system.
2. Climate Risk. The IAIS’s Climate Risk Steering Group is studying how to monitor progress in addressing and mitigating climate risk, among other topics.
3. Cybersecurity. Deputy Secretary General Paserot noted that the insurance sector is uniquely positioned because it both faces risks posed by cybersecurity breakdowns and, at the same time, can be part of the solution by providing cybersecurity coverage.
4. Private Equity. The IAIS has created a workstream within the Macroprudential Supervision Working Group to monitor private equity ownership in the global insurance industry.
5. Diversity, Equity and Inclusion. The IAIS is reviewing the diversity, equity and inclusion initiatives underway by supervisors and insurance companies and will publish a paper at the end of the year.

### VIII. Briefly Noted

#### A. Update on ComFrame Revisions to NAIC Guidance Documents

The Group Solvency Issues (E) Working Group has been developing revisions to the NAIC Financial Condition Examiners Handbook, the NAIC Financial Analysis Handbook and the ORSA Guidance Manual to incorporate ComFrame elements deemed appropriate for the U.S. insurance regulatory system. At the Summer National Meeting, the Working Group adopted changes to these three documents. Changes to the ORSA Guidance Manual will be implemented in 2023, and revisions to the Financial Condition Examiners Handbook and Financial Analysis Handbook must be referred to the appropriate NAIC working groups for formal adoption and implementation.

- NAIC Financial Condition Examiners Handbook. Revisions to the Financial Condition Examiners Handbook incorporate elements from ComFrame relevant to the onsite examination of insurers and, importantly, are not meant to be prescriptive. In drafting the revisions, the Financial Exam Drafting Group’s goal was to highlight certain ComFrame elements that should be considered for an IAIG where a state insurance regulator acts as the global group-wide supervisor. The updated Financial Condition Examiners Handbook states that an examination team should consider addressing certain examination topics, such as risk management and investment policies, at a different level within an IAIG (e.g., at the head of the IAIG) since U.S. regulators are generally focused on a legal entity when conducting a financial examination.

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- ORSA Guidance Manual. Most revisions to the ORSA Guidance Manual pertain to IAIGs where a state insurance regulator is the global group-wide supervisor, and reflect IAIS guidance on the disclosure of liquidity and business strategies within an ORSA as well as considerations that are unique to IAIGs, as outlined in ComFrame. A new section of the ORSA Guidance Manual describes additional enterprise risk management expectations that should be discussed in an IAIG's ORSA Summary Report (e.g., enhanced liquidity considerations, and information on the diversity and geographical reach of the IAIG's activities).
- NAIC Financial Analysis Handbook. The updated Financial Analysis Handbook describes additional procedures for analyzing an IAIG's financial condition where a state insurance regulator is the global group-wide supervisor, noting that analysts should not duplicate efforts if the considerations are already addressed in other holding company analyses, corporate governance or ORSA review procedures. The additional procedures include, without limitation: (i) evaluating the complexity of an IAIG's group structure and considering its impact on the effectiveness of the IAIG's corporate governance framework; (ii) reviewing the IAIG's availability of capital to meet group-wide capital expectations, while considering each insurance legal entity's regulatory capital requirements; and (iii) determining whether the IAIG's risk management strategy and framework address certain topics, such as the geographical reach of the IAIG's activities and the degrees of risk in its entities/business lines.

### B. 2021 Holding Company Act Revisions Not Required for Accreditation

Because the *Insurance Holding Company System Regulatory Act* (#440) and *Insurance Holding Company System Model Regulation with Reporting Forms and Instructions* (#450) are part of the NAIC's accreditation standards, the Financial Regulation Standards and Accreditation (F) Committee is required to consider the impact of any changes to these models. Most recently, these models were amended in 2021 to address the continuation of essential services by affiliates of insurers undergoing receivership, as well as the receiver's access to data and records held by affiliates but belonging to the insurer, as we reported in greater detail [here](#). At the Summer National meeting, the (F) Committee adopted a recommendation from the Receivership and Insolvency (E) Task Force—the group that drafted 2021 amendments—that these receivership-related revisions be acceptable for accreditation, but not required.

### C. Other Updates

Additional, briefly noted updates from the Summer National Meeting are summarized at a high level below:

- Long-Term Care. The LTCI Multistate Actuarial Rate Review Framework, which was adopted by the NAIC at the 2022 Spring National Meeting and aims to create a voluntary and efficient multi-state actuarial review process, is still expected to be implemented in September 2022. For more information on the LTCI Multistate Actuarial Rate Review Framework, please refer to our report on the 2022 Spring National Meeting, available [here](#).



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- **Race & Insurance Workstreams.** The Special (EX) Committee on Race and Insurance did not announce any new actions or initiatives at the Summer National Meeting, but received updates on the continued efforts of its five workstreams. Most notably, Workstream Five, which focuses on identifying barriers to people of color and/or historically underrepresented groups obtaining health insurance and the role health insurance plays in health outcomes, plans to compile a guide by the end of 2022 that will provide tools and strategies to help state insurance regulators address such barriers.

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