

CLIENT ALERT

NAIC Report: 2023 Spring National Meeting

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The 2023 Spring National Meeting of the National Association of Insurance Commissioners (the “Spring National Meeting”) was held from March 21–25, 2023 in Louisville, Kentucky with attendees participating virtually or in person.

The National Association of Insurance Commissioners (“NAIC”) President and Director of the Missouri Department of Commerce and Insurance Chlora Lindley-Myers opened the conference by highlighting the NAIC’s key priority areas for 2023, which include (i) oversight of insurer investments and solvency; (ii) monitoring cybersecurity and insurers’ use of artificial intelligence and automation; (iii) ensuring access to insurance and industry practices that could disadvantage underrepresented groups; and (iv) anticipating and planning for climate and catastrophe events to reduce negative impacts on consumers. Commissioner Marlene Caride (NJ), Chair of the NAIC’s Financial Stability (EX) Task Force, also made remarks at the Spring National Meeting regarding recent bank failures, stressing that regulators must “remain vigilant” against potential “contagion effects” in the insurance sector and that insurance companies must continually assess their risks.

Highlights from the Spring National Meeting include:

- **Insurer Investments**: The Financial Condition (E) Committee and its subgroups continued to focus on enhancing oversight of insurance company investments, including by (i) authorizing the SVO to financially model CLO investments, (ii) developing a proposal for the RBC treatment of residual tranches of structured security investments, and (iii) focusing on the appropriate role of rating agencies in assessing insurer investments.
- **Counterparty Risk**: The Macroprudential (E) Working Group is revitalizing a “counterparty initiative” that will focus on counterparty exposure risks to insurers from other financial sectors.
- **Banking Crisis Response**: Silicon Valley Bank and Signature Bank were removed from the SVO’s list of “qualified U.S. Financial Institutions” for reinsurance collateral purposes, and the SVO proposed new guidance to enhance its ability to remove troubled financial institutions from the list going forward.
- **Negative IMR Accounting Treatment**: The Statutory Accounting Principles (E) Working Group indicated that an interim solution for negative interest maintenance reserve (“IMR”) was an immediate priority for 2023 since the

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matter is time-sensitive for life insurers. NAIC staff was asked to prepare draft guidance that would allow insurers to admit negative IMR up to 5% of surplus.

- Affiliate Service Agreements: The Risk-Focused Surveillance (E) Working Group exposed changes to the Financial Analysis Handbook and the Financial Condition Examiners Handbook that provide additional guidance for the regulatory review of affiliate service agreements, particularly those with market-based fee structures.
- Consumer Privacy Protections: Interested parties voiced their concerns about the Privacy Protections (H) Working Group's initial draft of the new *Consumer Privacy Protections Model Act (#674)*.
- NAIC Leadership Changes: Michael Consedine is stepping down as CEO of the NAIC, effective April 30, after serving in the role for six years. Andrew Beal, who currently serves as the NAIC's COO and CLO, was appointed Acting CEO by the Executive (EX) Committee.

This report summarizes key activities at the Spring National Meeting, and certain interim conference calls and other developments leading up to the Spring National Meeting, which may be of interest to our clients in the insurance industry.

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GLOSSARY

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

“Algorithmic bias” refers to the unfair discrimination by insurers during an insurance transaction resulting from bias in AI/ML-driven algorithms and complex predictive models.

“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 statements and to improve accounting and reporting.

“Certified Reinsurer” means a reinsurer that is domiciled in a “Qualified Jurisdiction” (meaning a non-U.S. jurisdiction listed on the NAIC list of “Qualified Jurisdictions” established pursuant to the NAIC Process for Evaluating Qualified and Reciprocal Jurisdictions) that is eligible to qualify for reduced reinsurance collateral pursuant to the 2019 amendments to the Credit for Reinsurance Models.

“CLO” means collateralized loan obligation.

“Credit for Reinsurance Models” means the *Credit for Reinsurance Model Law* (#785) and the *Credit for Reinsurance Model Regulation* (#786).

“DE&I” means diversity, equity and inclusion.

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

“Financial Analysis Handbook” means the Financial Analysis Handbook published and maintained by the NAIC.

“Financial Condition Examiners Handbook” means the Financial Condition Examiners Handbook published and maintained by the NAIC.

“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.

“Holding Company Models” means the NAIC’s *Insurance Holding Company System Model Act* (#440) and the *Insurance Holding Company System Model Regulation with Reporting Forms* (#450).

“IAIG” means an internationally active insurance group.

“IAIS” means the International Association of Insurance Supervisors.

“ICS” means Insurance Capital Standard, which is the consolidated group-wide capital standard the IAIS is developing for IAIGs.

“LATF” means the Life Actuarial (A) Task Force.

“LST” refers to the Liquidity Stress Test, an annual filing by a life insurance company that satisfies the test’s scope criteria pursuant to the relevant state’s insurance holding company laws. The LST filing provides an insurance regulator with quantitative and qualitative insights for macroprudential surveillance.

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“Market Regulation Handbook” means the Market Regulation Handbook published and maintained by the NAIC.

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

“RBC” means risk-based capital.

“Reciprocal Jurisdiction Reinsurer” means a reinsurer that is domiciled in a “Reciprocal Jurisdiction” (meaning a non-U.S. jurisdiction listed on the NAIC list of “Reciprocal Jurisdictions” established pursuant to the NAIC Process for Evaluating Qualified and Reciprocal Jurisdictions) that is eligible to qualify for zero reinsurance collateral pursuant to the 2019 amendments to the Credit for Reinsurance Models.

“SEC” means U.S. Securities and Exchange Commission.

“SSAP” means Statement of Statutory Accounting Principles.

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

“Valuation Manual” means the Valuation Manual published and maintained by the NAIC.

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I. Macroprudential Risk and the Insurance Industry

A. Updates on the Private Equity Considerations Work Plan

In 2022, the NAIC's Macroprudential (E) Working Group (the "MWG") began work on a plan to address the list of "Regulatory Considerations Applicable (But Not Exclusive) to Private Equity Owned Insurers" (the "Considerations"). The MWG and other working groups shared updates regarding the status of certain of the Considerations at the Spring National Meeting, as set forth below.

- Consideration One (Structuring Contracts in a Holding Company System): Regulators may not be obtaining a clear picture of risk due to holding companies structuring contractual agreements in a manner to avoid regulatory disclosures and requirements. Related party agreements, which impact an insurer's risks, may also be structured to avoid disclosure (for example, by not including the insurer as a party to the agreement).
- Consideration Two (Control): Control is presumed to exist where ownership is greater than or equal to 10% of an insurer's voting securities, 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 insurer's investment strategy and its implementation.

Status: As reported [here](#), the MWG has referred Considerations One and Two to the Group Solvency Issues (E) Working Group, which has discussed enhancing regulator training and best practices surrounding insurance company acquisition transactions and "control" determinations. There has been no update since the 2022 Fall National Meeting.

- Consideration Three (IMAs): The material terms of an IMA and whether they are arm's length or include conflicts of interest—such as 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 investment manager's degree of discretion or control over investment guidelines, allocation and decisions.

Status: The MWG referred this Consideration to the Risk-Focused Surveillance (E) Working Group, which met at the Spring National Meeting and discussed its ongoing project to update guidance in the Financial Analysis Handbook and Financial Condition Examiners Handbook regarding affiliate service agreements, discussed in Section II.C below. The Working Group has deferred review of Consideration Three specifically until the handbook project is completed.

- Consideration Four (Asset-Liability Matching): 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 insurance products.

Status: In 2022, the NAIC adopted *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 [here](#). At the Spring National Meeting, Fred Andersen (MN) reported that the Valuation Analysis (E) Working Group expects to receive the first filings under AG 53 from in-scope life insurers on April 1 and has developed a plan for reviewing the filings and training reviewers on complex asset issues. After reviewing the filings, insurers may be asked to engage with domestic regulators on company-specific issues and aggregated results will be provided to the public. The MWG also referred this Consideration to the Risk-Focused Surveillance (E) Working Group for review, such as suggesting guidance for appropriate entities to provide capital maintenance agreements.

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- **Consideration Five (Operational Oversight):** 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, private equity (“PE”) owners. For example, reliance on third-party administrators due to the acquiring firm’s lack of expertise may not be sufficient to administer the insurer’s 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.

Status: There have been no updates on this Consideration since the 2022 Summer National Meeting because the MWG has been focused on Consideration Thirteen related to reinsurance, discussed below.

- **Consideration Six (PE Definition):** No uniform or widely accepted definition of PE and challenges in maintaining a complete list of insurers’ material relationships with PE firms.

Status: As previously reported, no action will be taken on this Consideration since regulators agree the focus should be on activities and not specific types of owners.

- **Consideration Seven (Related Party Investments):** 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 CLO, which is managed or structured by a related party.

Status: The financial statement related party transaction reporting requirements effective for year-end 2022, as reported on [here](#), address this Consideration. At the Spring National Meeting, the NAIC’s Statutory Accounting Principles (E) Working Group (“SAPWG”) adopted a clarification to these requirements in *SSAP No. 25—Affiliates and Other Related Parties*, which states that any invested asset held by a reporting entity which is issued by an affiliated entity, or which includes the obligations of an affiliated entity, is an affiliated investment.

The Risk-Focused Surveillance (E) Working Group’s work related to affiliate service agreements may also touch on this Consideration.

- **Consideration Eight (Affiliate Investments within Structured Securities):** Although the NAIC’s Annual and Quarterly Statement blanks include affiliate investment disclosures, it is not easy to identify underlying affiliate investments and/or collateral within structured security investments. Additionally, transactions may be excluded from affiliate reporting due to nuanced technicalities. Regulatory disclosures may be required to identify underlying related party and subsidiary, controlled and affiliated 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.

Status: The approach to this Consideration overlaps with Consideration Seven, above, regarding related party reporting requirements, and Consideration Ten, below, related to privately structured securities.

- **Consideration Nine (Disclaimers of Affiliation):** Broader considerations exist around asset manager affiliates (not just PE owners) and disclaimers of affiliation avoiding current affiliate investment disclosures.

Status: The MWG has stated that this Consideration is addressed by the Schedule Y, Part 3 reporting requirement, which went into effect for year-end 2021, to identify all entities with a greater than 10% ownership regardless of whether a disclaimer is in place. SAPWG’s ongoing Bond Project, discussed in Section II.A below (Insurance Company Investments), further addresses this Consideration.

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- **Consideration Ten (*Increased Risk from Certain Investments*):** The material increases in privately structured securities (both by affiliated and nonaffiliated 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.

Status: AG 53 addresses this Consideration, since it includes disclosure requirements for the referenced risks. The MWG also referred this Consideration to the NAIC's Valuation of Securities (E) Task Force ("VOSTF"), which (along with related NAIC groups) has been working on a project to determine appropriate RBC charges for CLOs held by insurers. Relevant updates are described in Section II.A below (Insurance Company Investments).

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

Status: The MWG referred this Consideration to VOSTF. Updates from the Spring National Meeting related to VOSTF's review of credit rating provider matters are discussed in Section II.A below (Insurance Company Investments).

- **Consideration Twelve (*Pension Risk Transfer Risks*):** The trend of life insurers engaging in pension risk transfer ("PRT") business and supporting such business with the more complex investments outlined above.

Status: As previously reported, the MWG expects that certain prior NAIC actions will address this Consideration, including (i) AG 53; (ii) the new charge added to the 2021 Life Risk-Based Capital Formula related to longevity risk transfer business, which regulators will monitor; and (iii) modifications to the reporting of PRT transactions adopted by SAPWG in May 2021. LATF is also considering the development of PRT/longevity risk mortality factors. In addition, NAIC staff is holding discussions with U.S. Department of Labor representatives and industry groups.

- **Consideration Thirteen (*Offshore Reinsurers*):** 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.

Status: At the Spring National Meeting, the Financial Stability (EX) Task Force voted to expose for comment a "reinsurance comparison worksheet" that the MWG developed following meetings with interested parties and U.S. and foreign insurance regulators. The worksheet is a tool intended for regulators to assess cross-border reinsurance treaties involving different regulatory systems and enhance state regulators' ability to monitor these activities by understanding the impacts of a reinsurance transaction. Regulators could require an insurer to complete the worksheet for a reinsurance treaty involving any line of business, including "new treaties when regulators are considering approvals," or "treaties already in place where there are significant and material questions/concerns." In addition, although the worksheet was designed for cross-border treaties, "if a regulator would find this information useful for a U.S. to U.S. transaction, there is no reason for the regulator to not pursue its completion." **Comments on the proposed worksheet (which is available [here](#)) are due by April 28, 2023.**

B. Other NAIC Macroprudential Initiatives

1. *Financial Sector and Counterparty Risk*

In her remarks regarding the recent failure of Silicon Valley Bank and Signature Bank, Commissioner Caride stated that U.S. insurance industry investments in the subject banks were relatively small and the Financial Stability (EX) Task Force does not anticipate any adverse impact on policyholders. While the U.S. insurance sector remains well capitalized, Commissioner Caride called on companies and state insurance regulators to remain vigilant about contagion effects from the banking sector.

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Commissioner Caride noted that state insurance regulators and the NAIC have many existing tools to monitor exposure to the banking sector and the impact of rising interest rates on insurers, such as the NAIC's macroprudential risk assessment process, the LST, IAIS statewide monitoring, the financial reporting system and actuarial analysis requirements. In addition, the MWG recently "revitalized" a "counterparty initiative." As background, "counterparty exposure/concentration" is one of four macroprudential considerations, along with liquidity risk, capital stress testing, and resolution and recovery, first identified by the NAIC's Macroprudential Initiative in 2017, and the Financial Stability (E) Task Force previously published [a list](#) of existing disclosure requirements relevant to counterparty exposure. The newly revitalized initiative will involve the "identification and aggregation of interrelated exposures from other financial sectors," with a goal to "assess reporting structure" and "determine if disclosure gaps exist." NAIC staff is currently working on identifying and aggregating all counterparty exposure data within current investment schedules and annual statements.

2. *Liquidity Stress Test*

Life insurers that were subject to the 2022 LST filing requirement recently completed a follow-up questionnaire so regulators could assess the impact of rising interest rates on their liquidity. The goal was to understand whether the life insurers' hypothetical asset sales reported in the 2022 LST submissions differed materially from their actual experience in 2022. Results from the questionnaire indicated that:

- The life insurers' actual assets sales in 2022 were comparable to the information provided in their LST filings.
- The life insurers all reported a decrease in market value and an increase in unrealized losses in bond portfolios, but not to an extent that would materially impact their liquidity profile.
- With respect to collateral calls on derivative contracts, most life insurers reported little to no impact on their liquidity profile. Net collateral pledged was minimal due to the companies' collateral netting agreements.

II. **Financial Condition Regulation**

A. Insurance Company Investments

As noted by President Lindley-Myers in her opening remarks, the NAIC is focused on oversight of insurance company investments and solvency. Over the past several years, concerns about potential risks to insurers arising from investments in complex assets has led to proposals to change how certain investments are assessed and reported, along with corresponding RBC treatment. This focus was evident at the Spring National Meeting, with various NAIC working groups sharing updates on existing workstreams along with new investment-related proposals.

1. *The Bond Project*

SAPWG continues to target an effective date of January 1, 2025 for changes related to the Bond Project, which aims to clarify which securities should be reported as a bond on Schedule D-1 (Long-Term Bonds) of an insurance company's statutory financial statements, and to improve accounting and reporting of these investments. Notably, the revisions would split Schedule D-1 into two sub-schedules: Schedule D-1-1 (issuer credit obligations) and Schedule D-1-2 (asset backed securities).

At the Spring National Meeting, SAPWG voted to expose updated revisions to *SSAP No. 26R—Bonds*, *SSAP No. 43R—Asset-Backed Securities*, *SSAP No. 21R—Other Admitted Assets* and other corresponding SSAP revisions. In addition, SAPWG exposed a proposal to revise the reporting lines on Schedule BA of an insurance company's annual statement to capture debt securities that do not qualify as bonds. **Each of these items is exposed for a public comment period ending June 9, 2023, available [here](#).**

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The proposed definition of “bond” is set forth in *SSAP No. 26R—Bonds* (along with related guidance), and at a high-level means “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.” Exposed revisions to *SSAP No. 26R—Bonds* include an edit to specify that the existing preclusion from bond treatment applicable to an issued security “with varying principal and interest payments based on the appreciation of referenced equity, real estate or other non-debt variable” is not intended to encompass nominal interest rate adjustments. The exposed edit also identifies sustainability-linked bonds (i.e., ESG bonds), where failure to achieve performance metrics could cause interest rate adjustments, as an example of adjustments that should not preclude a security from bond treatment.

SAPWG’s exposed revisions to *SSAP No. 21R—Other Admitted Assets*, which appear in a new, standalone document, are intended to address the accounting treatment of residual tranches that do not qualify for bond reporting, and include a request for industry input about how residual tranches have been amortized and assessed for other-than-temporary impairment.

NAIC staff advised that SAPWG will receive revisions to the issue paper exposed at the 2022 Fall National Meeting for consideration at a later date, and reported that the Blanks (E) Working Group is currently exposing for comment until June 30 a blanks proposal and investment schedule changes related to the Bond Project, available [here](#).

2. *Update on Modeling of CLO Investments*

The Financial Condition (E) Committee adopted an amendment to the P&P Manual to give the SVO’s Structured Securities Group responsibility for modeling CLO investments for purposes of assigning an NAIC Designation. Under the amendment, which will become effective on January 1, 2024 for year-end 2024 financial reporting, CLO investments will no longer be broadly exempt from filing with the SVO based on ratings from Credit Rating Providers (“CRP”). The amendment was adopted after the SVO raised concerns that CLOs have received inconsistent NAIC Designations when relying on CRP ratings, and recommended the change to ensure reporting consistency.

As a next step, VOSTF has formed an ad hoc group that includes interested parties to refine the proposed CLO modeling process. The group expects to run models based on proxy scenarios representing types of CLOs commonly held by insurance companies. VOSTF emphasized that the purpose of the ad hoc group is to resolve and clarify technical modeling issues, while regulatory policy issues continue to be discussed at VOSTF. Ad hoc group meetings are expected to start in April 2023 and be open to the public.

VOSTF will also coordinate with the NAIC’s Risk-Based Capital Investment Risk and Evaluation (E) Working Group’s (“RBCIRE WG”) work regarding the ultimate RBC factors for CLOs. At an interim meeting in February 2023, in response to interested parties’ concerns that the new modeling regime could result in “punitive” RBC treatment for CLOs, VOSTF Chair Carrie Mears (IA) suggested that VOSTF defer to the RBCIRE WG’s work in this area. As discussed in Section II.A.4 below, at the Spring National Meeting, the RBCIRE WG directed NAIC staff to prepare and expose an interim solution for residual tranches of structured security investments using a single factor. The RBCIRE WG also has a separate workstream dedicated to developing a long-term approach to RBC factors for CLOs. In addition, the American Academy of Actuaries’ C1 Working Group is reporting to the RBCIRE WG on related projects, which include (i) analyzing CLOs to develop considerations for establishing capital requirements, (ii) working on a “model specs document” that will provide guidance from the “bottom-up” on CLO modeling for RBC purposes without relying on prior approaches, and (iii) preparing a document that addresses various definitions used to discuss “RBC arbitrage” in order to avoid confusion in discussions among regulators, industry and interested parties, that may result from inconsistent uses of the term to date.

3. *Deferred Action on “Structured Equity and Funds” Proposal*

As we previously reported [here](#), in December 2022, VOSTF exposed for public comment an amendment to the P&P Manual with proposed instructions for the SVO’s assessment of “Structured Equity and Funds” investments. The proposed

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amendment resulted from SVO concerns that certain investment structures lack transparency and have relied on CRP ratings to qualify for an exemption from filing with the SVO for review. The proposed amendment states that investments meeting the definition of structured equity and funds would no longer be eligible for the filing exemption based on CRP ratings and would instead need to be filed with the SVO for credit quality assessment.

At the Spring National Meeting, VOSTF heard comments on the proposed amendment from interested parties who expressed concern about the scope of the proposal, the transparency of SVO's proposed analysis process, and overlap with other NAIC workstreams, including the Bond Project (discussed above) and the RBCIRE WG's projects (discussed below). In particular, certain interested parties argued that private letter rating rationales provide sufficient transparency about relevant investments to alleviate the SVO's concerns.

In response to this feedback, VOSTF agreed to defer action on the proposed P&P Manual amendment and directed SVO staff to create a process for the SVO to review and potentially challenge private letter ratings. Carrie Mears (IA), VOSTF Chair, described this approach as a "yellow light" between investments that are filing exempt and not filing exempt. A proposal will be prepared for discussion at a future meeting. VOSTF also agreed to send a referral to SAPWG to provide more information about how assets are reported by insurers for VOSTF to consider further. Ms. Mears emphasized that VOSTF agrees with certain of the SVO's concerns about structured equity and fund investments, but she recognized the feedback from interested parties that these investment types have also been important for insurers historically.

4. *Residual Tranches of Structured Securities*

At the 2022 Fall National Meeting, the RBCIRE WG received a referral from VOSTF to develop an "interim solution" to address RBC charges for residual tranches of structured securities. The residual tranche refers to the "lowest" tranche of an asset-backed security (e.g., CLOs and mortgage-backed securities) that has equity-like characteristics, meaning it has the highest potential yield but also absorbs the first losses. To address the perceived tail risk of such tranches, until the RBCIRE WG studies structured finance securities more fully, VOSTF asked the RBCIRE WG to consider adding three new NAIC Designation Categories (e.g., 6.A, 6.B and 6.C) with potential interim RBC factors of 30%, 75% and 100%, respectively. Under this approach, residual tranches would have an RBC factor that is equal to, and in some instances higher than, that for unaffiliated common equity.

The RBCIRE WG received comment letters from interested parties on the referral, which it discussed at its interim meeting on February 27, 2023. Comments were largely critical of the three-factor approach proposed by VOSTF but were divided on the appropriate alternative. Some commenters supported a single interim RBC factor for residual tranches of at least 45%, noting that, for CLOs specifically, it is appropriate for residuals to have a higher RBC charge than common equity since both the investments themselves and the counterparties of the underlying loans are highly leveraged. Others questioned the need for any interim solution, arguing that the residual tranches do not pose a sufficiently material risk to justify interim action. Working Group members responded by noting that while the risk posed by residual tranche investments may not be material to the industry on average, materiality should be considered on a company-by-company basis given that certain insurers have outsized holdings of these investments.

Although some RBCIRE WG members echoed concerns that an interim approach may not be necessary or appropriate, RBCIRE WG Chair Philip Barlow (DC) and other regulators expressed their intent to move forward with an interim solution, while potentially relaying commenters' concerns to the Financial Condition (E) Committee. The RBCIRE WG directed NAIC staff to prepare for exposure (i) a sensitivity test intended to allow regulators to determine whether any companies have material risk from their residual tranches, and (ii) an updated proposal for residual tranche RBC charges using a single factor rather than the three-factor approach initially presented by VOSTF. The RBCIRE WG anticipates adopting an interim structural change for residual tranches by the end of April 2023, then adopting all relevant factors by the end of June 2023. **The resulting exposures are available [here](#) for a comment period ending on April 12, 2023.**

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5. *Rating Agency Matters*

As noted in Section I. above, one of the Considerations of the NAIC's private equity-related initiative focuses on "the level of reliance on rating agency ratings and their appropriateness for regulatory purposes (e.g., accuracy, consistency, comparability, applicability, interchangeability and transparency)." In particular, as discussed in connection with the CLO and Structured Equity and Funds matters above, the SVO has expressed concerns about reliance on CRP ratings to assess the credit quality of insurer investments.

As a result, VOSTF has proposed to add additional market and analytical information to reporting requirements for bond investments (as an alternative way to measure a security's risk). Interested parties have proposed that the NAIC should be responsible for calculating this analytical information by utilizing commercially available data sources and investment models, instead of having each insurance company incur the costs to implement system changes. **VOSTF referred this proposal to the Financial Condition (E) Committee and certain of its subgroups, and requested feedback by May 15, 2023.**

Also at the Spring National Meeting, VOSTF shared [a list of questions](#) it has created to "reflect the range of issues" that VOSTF has discussed in ad hoc and regulator-only sessions regarding the role of credit ratings in insurer financial solvency regulation. VOSTF intends to use these questions in preliminary discussions that it will schedule with individual CRPs, and ultimately hopes to create a more formalized "due diligence" questionnaire for CRPs.

B. Accounting Treatment for Negative IMR

At the 2022 Fall National Meeting, SAPWG exposed a new agenda item detailing the history and current guidance on IMR and seeking industry comments on potential guardrails and unique considerations in allowing a net negative IMR balance as an admitted asset. This exposure was in response to the American Council of Life Insurers' ("ACLI") request for urgent action to address industry concerns with current statutory accounting guidance requiring the nonadmittance of negative IMR in a rising interest rate environment, as we reported in greater detail [here](#). Since then, during regulator-only meetings in January and February 2023, SAPWG has heard industry presentations on the topic, and it received an additional comment letter from the ACLI, available [here](#).

At the Spring National Meeting, SAPWG acknowledged the urgency of the issue, stating its intent to identify an interim solution as an immediate priority for 2023, in addition to developing a long-term solution even if future interest rate shifts reduce the urgency. Regulators discussed potential "safeguards" that may be implemented if a net negative IMR balance is treated as an admitted asset, including use of accounting and reporting guidance to separately list negative IMR as a "special surplus" on the financial statements; development of documentation (e.g., an attestation) to ensure that sales of bonds at loss were for reinvestment purposes; and limiting the amount of negative IMR that may be admitted based on a percentage of surplus. SAPWG directed NAIC staff to prepare guidance for the group's future consideration that would allow the admission of negative IMR up to 5% of surplus and provide for a downward adjustment if the company's RBC ratio is less than 300. This 5% limitation represents a starting point, and regulators indicated they will continue to discuss amongst themselves and with industry an appropriate percentage for any such limitation.

Additionally, SAPWG directed NAIC staff to prepare and recommend a referral to LATF to consider the asset adequacy implications of negative IMR, as well as a referral to the Capital Adequacy (E) Task Force to consider sensitivity testing with and without negative IMR and eliminating any admitted net negative IMR from total adjusted capital. The Capital Adequacy (E) Task Force subsequently referred these issues for consideration to the Life Risk-Based Capital (E) Working Group, with which it plans to partner in considering these issues moving forward.

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C. Update on NAIC Handbook Revisions Related to Review of Affiliate Service Agreements

The Risk-Focused Surveillance (E) Working Group continues to discuss proposed changes to the Financial Analysis Handbook and the Financial Condition Examiners Handbook that provide additional guidance for regulators when they review and monitor affiliate service agreements, particularly those with market-based fee structures. After addressing this topic in the fall of 2021 (as we reported [here](#)), the Working Group formed a joint Drafting Group comprising insurance regulators and interested parties. The updated draft of handbook revisions includes the following changes:

- Form D Procedures

- When additional steps in the Form D review process are warranted, a regulator should consider requiring interim reporting information from the insurer, including forecasted cash flows related to the affiliate agreement, “to evaluate [the] materiality of changes in year-to-year cash flows to the insurer, particularly if the agreement is market-based. ...”
- The information on which a Form D approval is based is subject to verification on examination of the insurer. An insurance department may reserve the right to review the affiliate agreement’s charges and fees for fairness and reasonableness as part of future financial examinations or at any time validation is warranted.

- Examination Process

If an examiner has concerns about a previously approved affiliate service agreement, at the insurer’s next examination, the examiner should coordinate with the financial analyst who approved the relevant Form D filing in order to gather more information.

The joint Drafting Group was unable to reach a consensus on developing guidance for “cost-plus” arrangements where affiliate services are not directly comparable to services offered in the open market. Several regulators remarked that additional research is needed before guidance on this topic can be developed. The Risk-Focused Surveillance (E) Working Group voted to expose the proposed handbook revisions as well as questions related to cost-plus arrangements (available [here](#)), such as the types of affiliate services that are appropriate for this payment structure and the tools regulators should use to assess its fairness and reasonableness. **The 45-day comment period ends on May 8, 2023.**

D. Receivership and Insolvency Matters

The Executive (EX) Committee adopted a Model Law Development request to consider proposed amendments to the *Property and Casualty Insurance Guaranty Association Model Act (#540)*, previously adopted by the Receivership and Insolvency (E) Task Force and the Financial Condition (E) Committee at the 2022 Fall National Meeting. The amendments would ensure that cyber insurance policyholders are provided with guaranty fund coverage.

The Receivership Law (E) Working Group is also developing amendments to Model #540 to ensure that policyholders do not lose guaranty fund coverage as a result of corporate division and insurance business transfer transactions. The Working Group will meet in April to continue this work.

At the Spring National Meeting, the Receivership and Insolvency (E) Task Force also took note of recent bank failures and discussed how insurance regulators and guaranty systems can produce the best outcomes for policyholders of troubled insurance companies. Although no action was taken on this matter, Task Force members and interested parties commented on the need for regulatory preparation generally and the potential for federal involvement in financial services typically regulated at the state level in light of the federal response to the bank failures.

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III. Reinsurance Matters

The Reinsurance (E) Task Force provided the following updates at its meeting on March 6, 2023, which was held in lieu of the Spring National Meeting. For a discussion of reinsurance developments under the NAIC's private equity-related initiative, see Section I, Consideration Thirteen, above.

A. Removal of Silicon Valley Bank and Signature Bank from the List of Qualified U.S. Financial Institutions

When a domestic insurer seeks statutory financial statement credit for ceding insurance exposure to an assuming insurer under a reinsurance arrangement, letters of credit are permitted to be used as collateral, so long as the issuing bank meets the criteria of a "qualified U.S. Financial Institution" ("QUSFI"). A financial institution that issues a letter of credit as collateral may request placement on the NAIC's *List of Qualified U.S. Financial Institutions* (the "QUSFI List") in order to be deemed a QUSFI for purposes of the NAIC's *Credit for Reinsurance Model Law* (#785).

Silicon Valley Bank and Signature Bank were removed from the QUSFI List as of March 13 and 14, 2023, respectively. When a financial institution that has provided a letter of credit for credit for reinsurance purposes subsequently loses its QUSFI status, the letter of credit continues to be acceptable as security until there is an opportunity in the normal course of business for the credit facility to be replaced. This guidance comes from a drafting note to Section 3 of Model #785.

At the Spring National Meeting, VOSTF discussed a memorandum prepared by the SVO, stating that under the P&P Manual's guidelines, Silicon Valley Bank and Signature Bank did not "reflect sufficient financial weakness" for the SVO to remove them from the QUSFI List prior to their failure. VOSTF proposed changes to the P&P Manual so that if a QUSFI "is closed by and/or placed in receivership or conservatorship, or notice is given of such action, by its primary regulator(s), the SVO shall promptly remove" the institution from the QUSFI List.

B. Update on Reinsurance Collateral Reduction Applications

The Reinsurance Financial Analysis (E) Working Group ("ReFAWG") continues to assist states with reviewing reinsurance collateral reduction applications to determine whether an applicant meets the requirements to be recognized as a Certified Reinsurer and/or a Reciprocal Jurisdiction Reinsurer. As of March 6, 2023, ReFAWG had approved 55 Reciprocal Jurisdiction Reinsurers and 41 Certified Reinsurers, and 39 states had "passported" at least one Reciprocal Jurisdiction Reinsurer, which is the process that gives states discretion to defer to the collateral reduction status of a reinsurer in another state. Although not required by law, the Reinsurance (E) Task Force continues to recommend submission of reinsurance collateral reduction 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.

The NAIC's complete list of Certified Reinsurers and Reciprocal Jurisdiction Reinsurers is available [here](#).

C. Proposed Enhancements to Bermuda Monetary Authority's Regulatory Regime

On February 24, 2023, the Bermuda Monetary Authority released a Consultation Paper on proposed enhancements to its regulatory and supervisory regime for commercial insurers (available [here](#)). The draft includes changes to the computation of the Bermuda Solvency Capital Requirement and certain prudential rules and reporting forms. The Reinsurance (E) Task Force and the Mutual Recognition of Jurisdictions (E) Working Group are reviewing the paper, which will be considered when Bermuda's status on the NAIC's *List of Reciprocal Jurisdictions* and *List of Qualified Jurisdictions* is up for reapproval later this year.

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IV. Innovation, Cybersecurity and Technology

A. Insurance Industry Voices Concerns About the Proposed Consumer Privacy Model Law

On February 1, 2023, the Privacy Protections (H) Working Group exposed an initial draft of the new *Consumer Privacy Protections Model Act* (#674), which is intended to replace two existing NAIC privacy models—the *Insurance Information and Privacy Protection Model Act* (#670) and the *Privacy of Consumer Financial and Health Information Regulation* (#672).

As we previously reported [here](#), the proposed draft includes several notable obligations for insurers, including (i) a new prior consent requirement for cross-border transfers of personal information; (ii) new diligence and oversight requirements for licensees and third-party service providers; (iii) a potential new private right of action; and (iv) significant data minimization, retention and notice requirements.

At the Spring National Meeting, interested parties raised several concerns with the current draft of the model law, including:

- i. the potential for increased consumer costs due to the prescriptive restrictions on the collection, processing or sharing of personal information;
- ii. certain consumer rights, such as the right to deletion, would require unmanageable and costly updates to legacy systems;
- iii. that there is overlap or inconsistency with certain existing regulatory requirements, such as the Health Insurance Portability and Accountability Act (HIPAA) and state data privacy laws;
- iv. that certain contractual requirements would be challenging for smaller businesses to comply with when doing business with larger counterparties and service providers; and
- v. that the proposed notice requirements would result in excessive distribution of privacy notices.

Given the large number of comments, the Privacy Protections (H) Working Group revised its work plan and will now send a draft of Model #674 to the Innovation, Cybersecurity, and Technology (H) Committee ahead of the 2023 Fall National Meeting. The Working Group will host a number of meetings for regulators and interested parties beginning on April 18, including a two-day in-person meeting in June, to work through the comments and revise the proposed [draft](#).

B. Regulators Continue to Focus on Big Data and Artificial Intelligence

1. *Ongoing Development of a Model Bulletin*

The Innovation, Cybersecurity, and Technology (H) Committee continues to develop a regulatory framework for the use of AI/ML by the insurance industry in the form of a model interpretive bulletin, where the process is being led by the NAIC's Collaboration Forum on Algorithmic Bias. The bulletin's standards will apply at a high level to decision-making that is supported by the use of artificial intelligence, and the document will contain four sections: (i) an introduction; (ii) definitions; (iii) regulatory expectations; and (iv) regulatory oversight. The third section will be the most substantial piece, focusing on regulators' expectations and standards for the use of AI/ML by the insurance industry, such as in regard to enterprise risk management. The (H) Committee's updated work plan is to publicly expose a complete draft of the model bulletin by early summer 2023.

2. *Update on AI/ML Surveys*

The Big Data and Artificial Intelligence (H) Working Group provided updates on its survey projects. Ten states participated in the survey on the use of AI/ML in the homeowners insurance industry, where formal examination call letters were issued to 194 insurers with at least \$50 million in national home insurance premium. The NAIC intends to share a summary report ahead of the 2023 Summer National Meeting.

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Fourteen states will participate in an AI/ML life insurance survey focused on pricing and underwriting, marketing and loss prevention. Formal examination call letters will be issued by the end of April and responses will be due in late May.

3. *Update on Regulatory Questions Project*

In December 2022, the Big Data and Artificial Intelligence (H) Working Group exposed a regulatory framework document with examination standards and questions that regulators can use to gather information about AI/ML models from insurers and third parties.

During the Spring National Meeting, interested parties voiced the following concerns with the proposed draft:

- i. the potential disclosure of confidential or proprietary information;
- ii. the burden on insurers to respond to the questions, including a disproportionate burden on smaller companies;
- iii. redundancy with financial examinations and other regulatory reporting requirements;
- iv. a lack of clarity with respect to the purpose of certain questions and the intended use by regulators; and
- v. an alleged lack of authority in state law.

Commissioner Doug Ommen (IA) acknowledged several of these concerns, and Working Group Chair Elizabeth Dwyer (RI) provided assurances that responses to the regulatory questions would be confidential under regulators' examination authority. The Working Group is coordinating with the Innovation, Cybersecurity, and Technology (H) Committee in "incredible detail" to reduce redundancy with other AI/ML-related projects at the NAIC, and the goal is to expose a further revised draft by the end of May.

4. *Colorado Proposes a Regulation to Implement the State's Law on External Consumer Data Use*

In July 2021, Colorado passed a law that prohibits use of external consumer data sources, algorithms or predictive models that unfairly discriminate against individuals based on protected classes, as we reported [here](#). At the Spring National Meeting, the (H) Committee heard a report that the Colorado Division of Insurance (the "[Colorado Division](#)") is drafting an implementing regulation focused on life insurance underwriting. The proposed regulation would require insurers to test whether their use of external consumer data sources, and the algorithms and predictive models that use these sources, results in unfairly discriminatory outcomes. The Colorado Division will expose a further revised draft of the regulation based on comments received, and it plans to continue its stakeholder engagement process when it turns to unfair discrimination in underwriting practices for private passenger auto insurance.

V. **Other Topics of General Interest**

A. *Update on NAIC Accreditation Standard for the Group Capital Calculation*

The proposed accreditation standard for the NAIC's 2020 amendments to the Holding Company Models, which implement the annual filing requirements for the GCC and LST, was exposed for a one-year comment period that ended on December 31, 2022. The accreditation standard, which includes a January 1, 2026 effective date, is expected to go to the Executive (EX) Committee and Plenary for approval at the 2023 Summer National Meeting. For more information, see our 2021 Summer National Meeting Report, available [here](#).

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B. Topics of Interest to the Life Insurance Industry

1. *Accelerated Underwriting Guidance Document Exposed*

At an interim meeting on February 22, 2023, the Accelerated Underwriting (A) Working Group exposed for comment a draft [guidance](#) document that provides questions and other considerations for insurance regulators when they review life insurers' accelerated underwriting programs. The goal is to ensure that these programs are fair, transparent and secure, especially since they impact the availability and affordability of life insurance for consumers. The proposed guidance suggests that regulators address certain topics with life insurers, such as (i) the external data or applicant information used by the accelerated underwriting program; (ii) how the life insurer discloses to applicants what external information is used in its accelerated underwriting program; (iii) whether the life insurer ensures that its models are based on sound actuarial principles; and (iv) how external data or applicant information is used, stored, and destroyed once the underwriting process is completed. **Comments are due by April 14, 2023.**

The Working Group also exposed a draft referral to the Market Conduct Examination Guidelines (D) Working Group asking it to consider adding similar guidance to the Market Regulation Handbook.

2. *Update on Actuarial Guideline 49-A*

On February 24, 2023, the Life Insurance and Annuities (A) Committee adopted revisions to *Actuarial Guideline XLIX-A—The Application of the Life Illustrations Model Regulation to Policies with Index-Based Interest to Policies Sold on or After December 14, 2020* (AG 49-A). These revisions are considered a “quick fix” to address concerns that some companies were illustrating non-benchmark indices more favorably in indexed universal life illustrations compared to benchmark indices. The Indexed Universal Life (IUL) Illustration (A) Subgroup is continuing to discuss larger-scale improvements for the long-term.

C. Topics of Interest to the Property and Casualty Insurance Industry

1. *(C) Committee Adopts the Amended Nonadmitted Insurance Model Act*

The Property and Casualty Insurance (C) Committee adopted the amended *Nonadmitted Insurance Model Act (#870)*, which was updated by the Surplus Lines (C) Task Force to align the model law with the Nonadmitted and Reinsurance Reform Act of 2010 (the “[NRRRA](#)”), part of Dodd-Frank. The key revisions to Model #870 address the following topics: (i) the role of the NAIC’s *Quarterly Listing of Alien Insurers* with respect to determining the eligibility of alien insurers; (ii) the collection of surplus lines tax; (iii) the regulation of domestic surplus lines insurers; and (iv) the incorporation of certain NRRRA concepts, such as “home state” and “exempt commercial purchaser.” The Task Force’s drafting group could not reach a consensus on the treatment of unaffiliated groups for the “home state” definition. The states’ different approaches are therefore addressed in a drafting note. The amended Model #870 is expected to go to the Executive (EX) Committee and Plenary for approval at the 2023 Summer National Meeting.

VI. **International Matters**

A. IAIS Finalizes the Comparability Criteria for the Group Capital Standards

The International Insurance Relations (G) Committee provided updates on certain of the IAIS’s key projects. On March 9, 2023, the IAIS published the final criteria that will be used to assess whether the Aggregation Method (“[AM](#)”) approach to a group capital standard, which forms part of the GCC, produces comparable outcomes to the ICS (available [here](#)). The IAIS will begin the comparability assessment in the third quarter of 2023, and a decision on whether the AM provides comparable outcomes to the ICS is expected in the third quarter of 2024.

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In other work related to the ICS, the IAIS will issue a public consultation in June on potential changes to the ICS before it becomes a prescribed capital requirement for IAIGs.

VII. Other Updates

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

A. Amending the Unfair Trade Practices Model Act to Address Lead Generator Concerns

The Executive (EX) Committee approved the Market Regulation and Consumer Affairs (D) Committee's request to amend the *Unfair Trade Practices Model Act* (#880) in order to provide insurance regulators with appropriate authority over health insurance lead generators and define lead generator prohibited practices. The Improper Marketing of Health Insurance (D) Working Group, which is charged with reviewing existing NAIC model laws that address the use of lead generators for sales of health insurance products, is drafting amendments to Model #880 that will be exposed for comment this spring.

B. Extension on Mortgage Guaranty Model Act Amendments

The Financial Condition (E) Committee granted an extension to the Mortgage Guaranty Insurance (E) Working Group on its charge to develop proposed changes to the *Mortgage Guaranty Insurance Model Act* (#630). The Working Group now has until Fall 2023 to finalize the Model #630 changes. At the Spring National Meeting, the Working Group heard comments on the current draft of proposed changes, available [here](#), which focused on a new section providing that there is no private right of action based upon compliance or noncompliance with any of the model law's provisions. The Working Group also discussed a letter from mortgage insurers highlighting concerns that proposed SEC conflict of interest rules would prohibit mortgage insurers from using mortgage insurance-linked notes as a risk management tool. The Working Group directed NAIC staff to coordinate with the SEC regarding this issue.

C. Long-Term Care Insurance

President Lindley-Myers stated that working to resolve inconsistent long-term care insurance rate review practices among state insurance departments and ensuring consistent regulatory oversight of reduced benefit options continue to be key NAIC priorities. The Long-Term Care Insurance (EX) Task Force, which met on March 13, 2023 in lieu of the Spring National Meeting, continues to focus on implementing the Long-Term Care Insurance Multistate Actuarial Rate Review Framework that the NAIC adopted in 2022.

D. Insurance Business Transfers and Corporate Divisions

The Restructuring Mechanisms (E) Working Group met on April 4, 2023 and continued to discuss comments on draft "Foundational Principles" and "Best Practices" for insurance regulators to use when reviewing insurance business transfer or corporate division transactions. Comments focused on the use of independent experts, the appropriate standard for regulatory approval, and "due process" considerations, such as policyholder communication and public hearing requirements. The Working Group will continue the discussion at a meeting next month with a goal to finalize the Foundational Principles and Best Practices by the 2023 Fall National Meeting.

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