

September 4, 2007

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RE: Risk-Focused Examination Round Tables

Dear Mike:

During the conference call of the Risk Assessment Working Group on August 29th, a request was made of interested parties to submit suggested topics to be considered for Round Table discussions. In that regard, I am glad to offer some suggestions.

Before doing so, however, I would like to share with you some observations that I hope will be helpful to the RAWG. First, there are some similarities between the experiences of the insurance regulators with regard to their implementation of the new risk-focused examination guidance, and that of the large registered accounting firms several years back in wrestling with what was then new SOX requirements. Those similarities include that:

- Some confusion and/or multiple interpretations as to the requirements.
- In the absence of clearer guidance by regulators, the policies and practices of audit /consulting firms fill the void to become defacto or proxy guidance.
- The requirements pertain to the auditor (examiner) community, not to the company being audited (examined) and, as a result, the companies have little ability to independently challenge what they are told about the process by those firms.

Another similarity relates to the use of Round Tables. In the SOX context, two types come to mind:

- Round Tables held by the Big-Four firms and with their clients to explore emerging issues, discuss responses and explore best practices.
- The Round Tables sponsored by the SEC and the PCAOB to jointly explore the experience of the first years of reporting under SOX and to consider the need for further guidance or clarification to both the audit and business communities.

As for the contemplated Round Tables to be orchestrated by the NAIC pertaining to the risk-focused examination guidance, I see these as being a blend of similar objectives. On the one hand, there are states considering implementation and they are trying to understand how to best go about that. On the other, there are other states that are now wrapping up their initial examinations and there is the opportunity to share and leverage what has been learned from those experiences.

Because of these similarities to the SOX experience, there is the opportunity to leverage what was learned then as the RAWG now works to support the needs of states as they implement the risk-focused approach. Having been a participant in some of the Big-Four Round Tables, and an attendee at the SEC Round Table, I offer the following suggestions, some of which were discussed on the conference call last week.

1. Find someone to chair the Round Table who has the perceived authority to do so, the lack of a personal agenda relative to the topics to be discussed, and the ability to keep the discussion moving while limiting the ability of anyone to monopolize the dialogue (in that regard, the SEC did some interesting things at their Round Tables which I would be glad to share with you if you are interested). That person would also make sure that the following suggested steps are taken.
2. Solicit ideas as to what participants want to discuss – what concerns them about the new approach, what problems have they faced, what questions do they have, etc. (that is underway).
3. Have a sub-group cluster those submissions around specific topics and triage that to a coherent but small list (4-6 items) that they believe reflect the priority issues and/or are representative of the majority of submissions submitted.
4. Send that small list of items back out to your members and ask for volunteers to champion the discussion of each topic at the Round Table. Depending upon the topic, it may be beneficial for those individuals to prepare before the Round Table, to refresh themselves on the pertinent guidance, and perhaps gain some additional context from those who submitted the topic. They would then be better able to suggest some questions to help propel the dialogue if need be.
5. At the Round Table, the topic Champion would spend about no more than 5 minutes to introduce the topic, but open it up for sharing and discussion after that. The Chair would intervene as need be to keep the discussion on track and on schedule, and if need be, to cut off discussion.
6. At the end of the Round Table, everyone would take five minutes or so to write down their comments and feedback about the process, while it is fresh in their mind. Armed with that, the RAWG can better decide if there is a rationale cost-benefit to holding additional sessions in the future, and how to further improve upon the process.

Unlike the RAWG's regular meetings, I do not believe that there is the need to necessarily resolve anything at these Round Table meetings. A topic does not have to be debated and voted on. Rather, the main objective is to better understand the questions and problems that examiners face, some of the solutions that are emerging, and then from there the RAWG can place specific topics on its ongoing agenda to address those in a more formal manner. Thus, everyone's point of view at the Round Table is valid and to be respected. Absent that, the discussion will be short-lived.

With that, I would like to submit the following suggested topics. These are in no particular order, nor is this intended to be an all-inclusive list. Rather, it represents a few ideas to help get the ball rolling.

- The interaction between enterprise-wide controls and controls and risk assessment at the activity level: If the former is very strong, what is the extent of work that is really required for the latter? What evidence about the effectiveness of enterprise-wide controls is most compelling?
- Extent of testing: For a company that is SOX-compliant, how much testing is really required? How much "credit" should be given to internal control documentation and testing performed by the company's own operational personnel? By its internal audit or SOX project management staff? By the external auditor? What degree of "re-testing", if any, is being done?
- ERM: presumably examiners are asking about these initiatives, but how deep should they dig? Should ERM metrics be subjected to some sort of testing if they are germane to the management's response to risk?
- Prospective risks: What are examiners really doing here? Is this a routine inquiry item only at a very high level; a pervasive consideration that one is simply mindful of throughout the exam; or should specific additional work be performed?
- Results: Of those who have been through an exam using the new guidance, what findings, observations, or other benefits resulted that might not have been identified under the former approach? Are tangible benefits being seen in terms of better insights with which to monitor the company in between exams?
- Meetings with Board Members or members of senior management: What kind of resistance to this has been experienced? How has it been overcome? What lessons have been learned?
- Key functional activities: How many "feels right"? In other words, how granular are examiners getting in identifying KFAs? What problems are being experienced in efficiently identifying KFAs?
- Exam substantive testing procedures – How is the scope and detail of substantive testing procedures changing under the new approach as compared to the prior SRA-based approach?

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I hope that you will find these comments and suggested topics helpful. I would be glad to respond to any questions you or the RAWG may have or provide further information.

Sincerely,



A. Thomas Finnell, Jr.
Managing Director

cc: Tim Nauheimer