DAVE JONES
Insurance Commissioner

July 5, 2017

Hon. Tom Daly, Chair
Assembly Insurance Committee
1020 N Street, Room 369
Sacramento, CA 95814

Hon. Tony Mendoza, Chair
Senate Insurance, Banking
& Financial Institutions Committee
State Capitol, Room 2195
Sacramento, CA 95814

Recommendations Regarding Changes in the Law Necessary to Protect the Members of Firefighters', Police Officers', or Peace Officers' Benefit and Relief Associations, pursuant to Assembly Bill 1072 (Daly 2015)

Dear Chairman Daly and Chairman Mendoza:

Assembly Bill 1072 (Daly 2015) required firefighters', police officers', and peace officers' benefit and relief associations ("Associations") that provide long term care or long term disability benefits to file an actuarial opinion with the Insurance Commissioner. The law also provided that the Commissioner may make recommendations to the Legislature on changes in the law necessary to protect the interests of members of such associations.

The Department of Insurance identified 7 Associations (5 self-funded, one hybrid plan that is partially self-funded, and one that is fully-insured but was self-funded until the start of 2016) subject to the legislation.[1]

A review of the actuarial reports provided by these Associations revealed that because the self-funded Associations do not have to comply with the financial requirements of a licensed insurer, such as investment restrictions, capital requirements, or reserve valuation factors, they may be able to offer cheaper rates than their fully-insured competitors. While this may allow self-funded Associations to grow their membership ranks more quickly, there is also a greater danger such Associations will have to reduce promised future benefits, or even become insolvent, which would harm tens of thousands of public safety officers. As such, I believe that the current laws governing such Associations are inadequate to protect the interests of their members.

Therefore, I have developed the recommendations below to strengthen the current laws. Please refer to the Supplement for more detailed information regarding the recommendations, the Associations' historical role, and comparisons with the regulatory

[1] A "fully-insured" Association contracts with a licensed insurer to provide benefits to its members. A "self-funded" Association is directly responsible for providing benefits.

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oversight over similar entities to Associations such as traditional fraternal benefit societies and multiple employer welfare arrangements.

I. Recommendations Based on Review of Actuarial Filings from Associations

Associations should be subject to investment restrictions limited to U.S. Treasury securities and highly rated corporate bonds. Associations should also be required to conservatively estimate the assets necessary to pay future claims. This will provide a steady and reliable stream of income that can confidently be planned around.

To ensure Associations are financially sound, Associations should be required to submit an opinion signed by a qualified actuary every two years, certifying that the reserves held in support of contractual obligations are reasonable and in accordance with accepted actuarial standards of practice. Associations should also be required to submit an annual financial statement audited by a certified public accountant to ensure assets are held in secure investments.

II. Other Recommendations Based on Recent Experience and Best Practices

- Annual renewal of an Association's certificate of authority.
- Exempt Associations that are either fully-insured **or** do not offer long term care or long term disability benefits from all recommendations in Sections I and II, other than annual renewal of a certificate of authority.
- Associations must disclose financial reports and the benefit plan contract to members upon request.
- Apply the Commissioner's examination power of an entity's operations and financial condition to Associations.
- Apply the Commissioner's stop order power to issue an order to correct or eliminate actions that threaten solvency to Associations.
- Establish a procedure to allow Associations to cease operating to ensure an orderly winding up of its financial affairs.
- Associations must continue to provide benefits to former members that became entitled to benefits prior to the end of membership.
- Associations must be subject to the unfair practices laws that currently apply to insurers.
- The Commissioner should be able to review and investigate complaints by members against Associations.

- The Commissioner should be able to conduct public hearings to determine whether an Association has violated the applicable law, and impose penalties such as suspension or revocation of an Association's certificate of authority.

III. Conclusion

The recommendations above strike the proper balance between adequate supervision and allowing the Associations to compete for members through the promise of guaranteed benefits.

As a whole, I believe that the recommendations presented in this report provide far greater protection for the safety officer members of Associations than is currently offered by the inadequate laws in force today. Thank you.

Sincerely,

Dave Jones

DAVE JONES
Insurance Commissioner

SUPPLEMENT TO RECOMMENDATIONS

I. Background on Benefit and Relief Associations

Firefighter, police officer, and peace officer benefit and relief associations are a type of fraternal benefit society that have existed for more than a century. Such Associations typically started as local organizations that administered rudimentary "Widows and Orphans" funds to provide members and their dependents with benefits in the event of an illness, injury or death.

As these funds were a simple form of insurance, California's statutory scheme, found in Insurance Code § 11400 *et seq*, loosely regulated such Associations. These statutes provide that as long as these Associations obtain a certificate of authority, have qualified members, do not pay for members to join, elect its officers, pay benefits only to members or dependents, and are supported mainly by contributions from its members, they are **completely exempt** from any laws regulating insurance.

Currently, there are 83 Associations with a certificate of authority from the Department of Insurance, providing coverage to approximately 100,000 firefighters, police officers, peace officers, and their spouses. Some Associations do not have a certificate of authority, but are organized as an ERISA-authorized trust subject to Department regulation.[2]

II. Recent expansion into Long Term Care and Long Term Disability

Prior to 2016, the statutes regulating Associations had been essentially unchanged for more than 80 years, as they were already in place when the state's insurance laws were codified to create the modern Insurance Code in 1935.

In the past few decades, while many Associations have stayed true to their modest beginnings as local operators of Widows and Orphans funds, eight have evolved into sophisticated statewide organizations offering complex insurance products such as long term care (LTC) coverage (similar to that offered by an entity like CalPERS) and long term disability (LTD) coverage (similar to that offered by an entity like AFLAC).

LTC and LTD coverage produces liabilities that are long term in nature. Since the claim payments are expected to be made 30-70 years into the future, claims are paid using a combination of member contributions and the investment income generated by those contributions. Members make contributions for a specified number of years or until the member goes on claim, in which case contributions are waived.

[2] The Department has a range of regulatory authority over benefit plans subject to ERISA, depending on whether the benefit plan is "self-funded" or "fully-insured," and whether the plan is administered by a bona fide "employer" or "employee organization" as defined by ERISA.

When valuing liabilities, Associations utilize a "discount rate" to calculate the amount of assets necessary to pay future claims. Especially in the case of long-term liabilities, the present value of future liabilities is sensitive to the chosen discount rate, with a higher discount rate forecasting greater future returns, and requiring a lower present value. Alternatively, assuming a discount rate that is less than the expected earned rate provides a layer of protection in case investments perform worse than their average expected rate of return; a strong possibility for an Association holding assets with substantial volatility such as stocks and real estate. In order for an Association to be confident that it has sufficient funds, it must use a reasonable and conservative discount rate when valuing its liabilities.

If the discount rate used is too high and the projected investment earnings are not realized, Associations have the right to force active members to make increased contributions in order to pay for the claims of disabled members who are no longer making contributions. Unlike traditional insurers, these associations do not pay into, nor do they receive payment from, any insurance guarantee associations. Members are therefore exposed to financial risk through the investment activities of the Association. It is therefore very important that the discount rate used in valuing liabilities is sufficiently conservative to protect against this risk. Additionally, it is important that investments be safe enough that they can reliably grow at a rate that will allow them to cover future liabilities.

One way that an Association can compensate for this risk is by holding additional assets, beyond what is expected to be able to pay out future liabilities, in a surplus fund, similar to the practice of other entities that provide insurance. This provides an additional cushion that protects members from poor market performance. In order to determine an adequate surplus, the liabilities must be valued by discounting expected costs into present day dollars. An Association may choose to invest aggressively and seek the highest rate of return on their investments in an attempt to keep member contribution rates lower, but if these risky investments perform poorly, then the Association must either increase contribution rates or decrease benefits to members. Coupled with the fact that those on claim no longer make contributions, this gives rise to an intergenerational inequity. Increases in contribution rates for active members to cover current claimants unfairly and disproportionally impact current contributors, especially if the number of current contributing members is lower than the number of claimants.

Some Associations have contracted with licensed insurers to provide benefits to their members, which is referred to as a "fully-insured" arrangement. As insurers are subject to the entire scope of insurance regulation, such arrangements provide sufficient indirect regulation of these kinds of Associations.

Other Associations remain directly responsible for providing benefits, which is referred to as a "self-funded" arrangement. These self-funded Associations are outside the reach of any meaningful regulation, which has created the following problems, among others:

- Lack of financial transparency due to inability to access actuarial reports.
- Payment of benefits conditioned only on availability of assets.

- Underfunded claim reserves for current claims and underfunded policy reserves for future claims.

- Investment in improper assets and failure to have sufficient safeguards for adverse financial market changes.

- Retaliation against members who leave to join other Associations by discontinuing benefits to these former members, even if they were already on claim.

- Members unaware that benefits are not protected against insolvency by insurance guarantee association.

Because the self-funded Associations do not have to comply with the financial requirements of a licensed insurer, such as investment restrictions, capital requirements, or reserve valuation factors, they may be able to offer cheaper rates than their fully-insured competitors. While this may allow self-funded Associations to grow their membership ranks more quickly, there is also a greater danger such Associations will have to reduce promised future benefits, or even become insolvent, due to poor financial oversight, which will harm tens of thousands of public safety officers.

III. <u>Comparison With More Highly-Regulated Similar Entities</u>

Other entities that sell similar products to those of Associations, such as traditional fraternal benefit societies, multiple employer welfare arrangements, life insurers, and continuing care retirement communities, have restrictions imposed upon their investment activities, and each must maintain a minimum level of capital and surplus beyond their liabilities in order to operate. Associations are not subject to these, and other requirements, listed below.

A. Traditional Fraternal Benefit Societies

Perhaps the most similar entities to Associations are traditional fraternal benefit societies ("Society"), such as the Knights of Columbus, Modern Woodmen of America, or B'nai B'rith. Insurance Code § 10990 defines a Society as follows:

- Any incorporated society, order or supreme lodge, without capital stock;

- Conducted solely for the benefit of its members and their beneficiaries and not for profit;

- Operated on a lodge system with ritualistic form of work;

- Having a representative form of government; and

- Which makes provision for the payment of benefits in accordance with the Insurance Code.

Societies may offer life and disability benefits to their members. Among other responsibilities, Societies are required to:

- Provide a valuation report and such other information as the Commissioner deems proper to receive a certificate of authority;
- Renew their certificates of authority annually, ensuring that the Commissioner is aware of which Societies are active and which are dissolved;
- Respond to an Order to Show Cause from the Commissioner as to why its certificate of authority should not be suspended or revoked for conducting business in a manner that is hazardous to its members or not complying with other provisions of the laws regulating Societies, with a possible penalty of being enjoined from transacting business by the Attorney General;
- Be subject to the same insolvency and delinquency proceedings as other insurers, including the right of the Commissioner to seize assets until a further court order;
- Attend, testify, and produce documents in response to a subpoena from the Commissioner;
- Invest only in the types of securities that life insurers are permitted to invest in, and calculate the value of such securities according to the methods used by life insurers;
- File an annual financial statement with the Commissioner, who may address any additional inquiries related to the Society's operations, and is entitled to receive a written response under oath;
- Maintain adequate reserves, with the ability of the Commissioner to require additional reserves as deemed necessary and prohibit the Society from operating until it reaches an adequate financial standing;
- Notify its members of the Society's financial condition annually;
- Allow the Commissioner to examine its financial affairs at the Society's expense;
- Refrain from causing or permitting to be made, issued, or circulated in any form any misrepresentation or false or misleading statement concerning any matter related to any Society.

B. Multiple Employer Welfare Arrangements

A multiple employer welfare arrangement ("MEWA") is an arrangement between a group of employers in which the employers pool contributions for a self-run benefits plan for their employees. These arrangements allow small employers to offer group health benefits to their employees with the protection afforded by being part of a large risk pool. MEWAs were established in 1974 through the Employee Retirement Income Security Act (ERISA) as an alternative to traditional insurance programs or HMOs. In order to be eligible for a certificate of compliance, MEWAs must operate in accordance with sound actuarial principles and maintain aggregate stop loss insurance that takes effect at not greater than 125% of annual expected claims. They must submit a quarterly report certifying that they maintain assets in a claim reserve account sufficient to meet its contractual obligations. Additionally, they must maintain a minimum level of capital and surplus in addition to what is needed to meet contractual obligations, currently amounting to $4 million.

Investment activity restrictions for MEWAs are largely focused on surplus funds, which must be primarily secure investments due to the liability profile of these arrangements. (See Appendix 1 for authorized investments for MEWAs.) Surplus, along with aggregate stop-loss insurance, helps to ensure that the company can remain solvent even if claims increase drastically during a given year.

C. Life Insurers/Continuing Care Retirement Communities

See Appendix 2 for a description of the characteristics and regulatory oversight of life insurers and continuing care retirement communities, which share some similarities in their products and liabilities with Associations.

See Appendix 3 for a comparison of the factors relating to solvency between Associations, Societies/Life Insurers, and MEWAs.

IV. Department's Actions Following 2016 Statutory Change

Due to the concerns expressed in Section II of this Supplement, the Legislature enacted a new statute in 2016 (Insurance Code § 11401.5) requiring every self-funded Association that issued LTC or LTD coverage to submit to the Commissioner an actuarial report completed no earlier than December 31, 2013. This report, written by a qualified actuary, was required to discuss whether reserves were expected to satisfy contractual provisions, whether they were based on reasonable assumptions, and whether they were based on published actuarial standards of practice. The report also had to include supporting memoranda discussing administrative or operating expenses.

The Department of Insurance found 83 Associations operating in the state, and notified them of this requirement. As a result, the current status of the Associations operating in this state is as follows:

- 5 offer self-funded LTC/LTD, and submitted an actuarial report.

- 1 offers LTC/LTD through a hybrid plan that is partially self-funded and partially insured, and submitted an actuarial report.

- 2 offer LTC/LTD through a fully-insured mechanism. One Association submitted an actuarial report, as it only transferred to a fully-insured mechanism at the start of 2016. The other Association has been fully-insured for several years, and was not required to submit an actuarial report.

- 32 affirmatively replied that they do not offer LTC/LTD.

- 16 are dissolved or suspended. The Department recommends cancelling the certificate of authority of these Associations (See Appendix 6).

- 27 did not respond to the Department's notice or repeated follow-up. The Department attempted to contact these Associations via letter, telephone call, and by contacting similarly named police departments, fire departments, and public safety unions. Some of these Associations may be members of one of the eight large statewide Associations, and do not issue LTC/LTD on their own accord. Others may be dissolved or suspended. The Department recommends cancelling the certificate of authority of these Associations (See Appendix 7).

V. <u>Review of Actuarial Reports Pursuant to Insurance Code § 11401.5</u>

The chief life actuary of the Department of Insurance reviewed 7 actuarial reports filed pursuant to Insurance Code § 11401.5. The chief life actuary concluded that some Associations have appropriately provided for future liabilities, while others have serious challenges meeting future obligations. Problems noted at one or more associations include:

- Claims reserves that are insufficient to allow merger with another relief association, or converting to a fully insured plan; unless the amount of the reserve is increased;

- Multimillion dollar deficit if optimistic investment returns are off by even 0.5%;

- Assumptions that claims longer than twelve months will be paid with fees charged in the future; rather than establish a claim reserve for the full liability;

- Estimated liability on open claims is too low because the present value of future claim payments is discounted at too high of an interest rate; and

- Excessive assets that could be used to expand coverage, waive fees, or provide a dividend to members.

The Department has provided those Associations that it determined to have problems with their current operations with detailed findings and recommendations for corrective measures. The Department has also made its staff available to meet further with such Associations to discuss specific concerns.

VI. <u>Detailed Recommendations Based on Review of Actuarial Filings from Associations</u>

After reviewing the Associations' actuarial findings, the Commissioner believes that the current laws governing such Associations are inadequate to protect the interests of their members. In order to do so, the Commissioner makes the following actuarial recommendations for self-funded Associations that offer LTC/LTD:

- Recommendation 1: Investment restrictions and a conservative basis for reserves.
    - Creating investment restrictions and requiring a conservative basis for reserves will work together to ensure that Associations invest in a responsible manner, and will decrease the likelihood that members will unexpectedly see their contributions increase as a result of poor investment performance. Conservative allocation of assets provides a steady and reliable stream of income that can confidently be planned around. Assets used to back reserves should be restricted to U.S. Treasury securities and highly rated corporate bonds. Treasuries should make up the bulk of assets, representing an amount not less than 80% of assets used to back reserves. Holdings in investment grade corporate bonds should be limited to 20% of assets backing reserves.
    - The discount rate used in reserve valuation should be limited to the current long-term Treasury rate. A conservative valuation of reserve liabilities provides members with protection against new assessments, which unfairly shift costs to current paying members when Association management is too optimistic with earnings projections.
- Recommendation 2: Regular submission of actuarial opinion, financial statement, and other documents.
    - Every two years, Associations should be required to submit an opinion signed by a qualified actuary certifying that the reserves held in support of contractual obligations are reasonable and in accordance with actuarial standards of practice published by the American Academy of Actuaries and the Actuarial Standards Board.
    - Associations should be required to submit an annual financial statement audited by a certified public accountant to ensure assets are in secure investments. Such

financial statements should also include all compensation or stipends paid to trustees, and other administrative costs.

- Associations should be required to submit all documents to the Department of Insurance that they submit to the U.S. Department of Labor, such as Form 5500, the Annual Return/Report of Employee Benefit Plan

VII. Other Detailed Recommendations Based on Recent Experience and Best Practices

Along with reserve/investment standards and financial reporting requirements, the Commissioner has developed the following recommendations regarding further changes in the law necessary to protect Association members:

- Recommendation 3: Annual renewal of certificate of authority.
    - Many Associations with an active certificate of authority are suspended or dissolved. Other Associations received their certificates of authority so long ago that they are unaware they even possess one.
    - A requirement to annually renew an Association's certificate of authority, along with a fee, would allow the Department to maintain a current address, and help fund oversight activity.
    - Associations that are fully-insured or do not offer LTC/LTD may only be subject to a nominal renewal fee compared to other Associations.
    - The Commissioner recommends developing a procedure to cancel a certificate of authority for an Association whose status is suspended or dissolved, as there are many active certificates of authority for organizations that may no longer be in existence. (See Appendix 6 for Associations that are currently suspended or dissolved, and Appendix 7 for Associations believed to be inactive.)
- Recommendation 4: Exempt Associations that are fully-insured or do not offer LTC/LTD from all recommendations in Sections VI and VII, other than annual renewal of a certificate of authority.
    - There is far less regulatory concern with fully-insured Associations as the insurers that the Associations contract with are subject to the full regulatory authority of the Department. Exempting such Associations from the recommendations discussed in this Supplement would also encourage current self-funded Associations to transition to a fully-insured model. For example, Standard Insurance Company, Reliance Standard Life Insurance Company, and possibly other insurers provide LTC/LTD coverage for Associations. Currently, two

statewide Associations operate on a fully-insured model, and another partially insures its benefits.

There is also far less regulatory concern with Associations that do not offer LTC/LTD, which supports exempting such Associations from the recommendations discussed in this Supplement.

- Recommendation 5: Disclosure to members.
    - So that members are aware of the nature of the benefits that they stand to receive, Associations should disclose that they do not participate in any insurance guarantee funds.
    - Associations should also be required to provide its members with copies of financial reports and the benefit plan contract upon request.
- Recommendation 6: Examination.
    - To further the goal of consumer protection, the Commissioner recommends extending the existing examination power to Associations, by being given the ability to examine the operations and financial condition of an Association, through access to relevant records. The Commissioner should also have the ability to examine officers or agents of an Association under oath in relation to the operations and condition of the Association.
    - For such examinations to be effective, Associations should be required to maintain business records for at least five years after the transactions described within them.
    - The Commissioner should have the ability to recover the costs associated with examinations.
- Recommendation 7: Stop order power.
    - The Commissioner recommends extending the stop order power to Associations, by being given the ability to issue an order to Associations to correct or eliminate actions that threaten solvency.
- Recommendation 8: Ceasing operations.
    - As currently applied to insurers, the Commissioner recommends establishing a procedure to allow Associations to cease operating to ensure an orderly winding up of its financial affairs. Such a procedure would also protect members from the negative consequences of the Association ceasing operations in a haphazard manner.

- Recommendation 9: Continuation of benefits.
    - To prevent Associations from retaliating against former members who join new Associations, the Commissioner recommends requiring Associations to continue to provide long term benefits to any individual or entity that is no longer a member, but became entitled to benefits prior to the end of membership.
    - An Association may stop providing benefits to a former member upon written confirmation from a successor Association or admitted insurer that the former member will begin receiving the benefits that they are entitled to without lapse.
- Recommendation 10: Associations subject to unfair practices laws.
    - The Commissioner recommends requiring Associations to comply with the unfair practices laws that currently apply to insurers. This would allow members to pursue remedies against Associations that misrepresent the terms of a contract for benefits, or engage in unfair claims settlement practices, such as discontinuing benefits as a form of retaliation for a member leaving the Association.
- Recommendation 11: Complaint procedure
    - Members cannot currently take advantage of the established complaint procedure available to other California consumers aggrieved by the actions of an insurer or agent. The Commissioner recommends extending the established complaint procedure to encompass the acts of Associations so that members may have recourse to submit complaints, and the Commissioner may have the ability to investigate such complaints.
- Recommendation 12: Enforcement Authority
    - An important component of the Commissioner's regulatory powers is the authority to conduct hearings and determine whether an entity has violated the provisions of the Insurance Code. The Commissioner recommends extending the established enforcement authority to encompass the acts of Associations so that the Commissioner may conduct public hearings, make findings, and determine possible penalties, including suspension or revocation of an Association's certificate of authority.
    - An Association should have the right to judicial review of any penalties or remedies following a hearing establishing that the Association violated the provisions of the Insurance Code.

Appendix 1

Summary of Authorized Investments for MEWAS

Self-funded or partially self-funded MEWAs in California must abide by the following restrictions:

- At least 25% of required surplus (the current amount is $4,000,000) must be made in investments specified for life insurance company general funds (see Appendix 4) or in bank deposits and debt obligations.

- An amount up to 75% of the excess of invested assets over the sum of reserves and required surplus may be invested in:

    - At least three U.S. domiciled, open-ended, and diversified management companies registered with the Securities and Exchange Commission, whose investments consist of common and preferred stocks and cash.

    - Exchange traded U.S. or Canadian corporate notes, bonds, and preferred stocks rated investment grade or better by at least two rating agencies (Standard & Poor's, Moody's, or Fitch). No single investment in this category may comprise more than 10% of the funds described in this section.

- The balance of the assets may be invested in at least three U.S. domiciled, open-ended, and diversified management companies that are registered with the Securities and Exchange Commission, and whose assets consist of investment grade debt instruments and cash.

Appendix 2

Life Insurance

Life insurers carry similar liabilities to Associations. Life insurers collect premiums over the course of many years before they expect to make payments on a policy. A larger portion of their assets are set aside as reserves, in comparison to health insurers and MEWAs, due to the long-term nature of their liabilities. Since reserve assets are held for so long, the return that can be generated through investment is very important. If life insurers overestimate their investment income, they can find themselves insolvent in the future when the value of their assets is not enough to cover the cost of claims. As a result, life insurers are restricted in their investment activity and have a mandatory minimum paid-in capital and surplus requirement. The mandatory minimum paid-in capital is subject to heavy restrictions—these assets are limited to low risk, fixed-instrument investments such as government bonds. Funds held beyond the minimum paid-in capital requirement are given more leeway in where they may be invested, with larger insurers having additional options such as purchasing call options under certain conditions, or making foreign investments. A summary of authorized investments for life insurers is provided in Appendix 4. Large companies with lots of available capital and multiple product lines are allowed additional leniency because their size and diversification have an insulating effect on the risk that their policy holders are exposed to. In addition, life insurers are regularly required to submit an actuarial opinion on the state of reserves in light of the assets held indicating that those funds will be sufficient to cover claims under moderately adverse conditions.

Continuing Care Retirement Communities

Continuing care retirement communities are another group of entities that offer products similar to insurance and are regulated by state law. In California, these entities are regulated under the Health and Safety Code. The types of care provided by these communities and the financial liabilities associated with that care are similar to those of LTC and LTD insurance products. Communities are required to hold reserves to cover debt services and operating expenses that must be backed by qualifying high-quality and liquid assets. A summary of authorized investments in California, as well as in the states of New York and Florida, is included in Appendix 5. Additionally, communities are required to file an actuarial opinion as to the financial condition of the provider's continuing care operations at least once every 5 years. If their regulator, the California Department of Social Services, has reason to believe that the provider is insolvent or in danger of becoming insolvent, it may increase the amount of assets that the provider is required to hold in liquid reserves or may require that the reserves be placed into an escrow account.

Appendix 3

Comparison of Factors Relating to Solvency of Similar Entities

	MEWA	Fraternal Society/Life Insurer	Benefit Association
Duration of liabilities	Short-term	Long-term	Long-term
Primary Allocation of Assets	Surplus	Backing reserves	Backing reserves
Source of Assets	Contributions from members, investment income	Premiums, investment income	Contributions from members, investment income
Recourse in case reserves are insufficient to cover claims	Mandated surplus, mandated aggregate stop-loss insurance	Mandated surplus, cross-subsidization, guarantee associations	Assessment of members, reduction of future benefits
Financial reporting requirements	Yearly actuarial opinion and supporting memoranda	Yearly actuarial opinion and supporting memoranda	Single actuarial opinion and supporting memoranda submitted on or before July 1, 2016

Appendix 4

Summary of Authorized Investments for Life Insurers

General Fund [Insurance Code §§ 1170-1182]
These funds are used to finance required minimum paid-in capital for life insurance companies. Domestic incorporated insurers may invest their assets in securities that conform to the following conditions:

- Securities must not be in default at the date of investment
- The purchase price must be less than or equal to the market value at the date of investment.
- In the case of non-mortgage loans, the amount loaned must not exceed 85% of market value at the date of investment.

Companies may invest in bonds backed by:

- The U.S. Government
- The U.S. Postal Service
- The Canadian Government or the Commonwealth of Puerto Rico, or any political subdivision thereof, as long as that subdivision has not defaulted on any payments of any obligations for more than 90 days in the past ten years.
- Any county, municipality, or school district in the U.S. or Canada, as long as it has not defaulted for more than 90 days in the past two years.
- Any state in the U.S., as long as it has not defaulted for more than 90 days in the past ten years.
- Any permanent road division or district in California, when such bonds are considered legal investments for savings banks, or with approval from the Commissioner.
- Any county water district operating under Division 12 of the Water Code.
- The "Servicemen's Readjustment Act of 1944."
- A mortgage guaranteed as to payment by a policy of mortgage insurance.
- Collateral trust bonds or notes.
- Any obligation issued under the Federal Farm Loan Act.
- The "Home Owners' Loan act of 1933."
- Registered warrants of California.
- Bank accounts to the extent that the accounts are insured by an agency or instrumentality of the federal government. This includes certificates of deposit.

Excess Fund [Insurance Code §§ 1190-1202]
These funds are investments made beyond the amount required for minimum paid-in capital. Companies may invest excess funds in:

- Stock of any corporation in the U.S. or Canada.
- Exchange traded call options on common stock for the purpose of a closing purchase transaction. Companies may only sell exchange traded call options with respect to stock which it owns.
- Interest-bearing obligations issued by a nonaffiliated institution.
- Bonds, notes, or obligations assumed or guaranteed by the International Bank for Reconstruction and Development, the Inter-American Development Bank, the Government Development Bank for Puerto Rico, the Asian Development Bank, the International Finance Corporation, or the African Development Bank. These investments shall not exceed the lesser of 2.5% of admitted assets or 25% of the total capital and surplus for the insurer.
- Securities of a first lien on unencumbered leasehold on real property.
- < 10% of capital and surplus may be invested in stock of corporations organized under the laws of Canada.
- Deposits and debt obligations of banks whose accounts are insured by an agency of the federal government.
- Mortgages, mortgage-backed bonds, or mortgage participations or pass-throughs.
- Shares of an investment company provided that it is/has:
    - Registered with and reporting to the Securities and Exchange Commission.
    - Domiciled in the United States.
    - Assets in excess of $100 million or is affiliated with other companies that have, in aggregate, assets in excess of $1 billion.
    - No more than 33% invested in foreign investments unless:
        - If more than 50% of total investments consist of foreign investments, some companies may invest in the fund as a foreign investment as defined by Insurance Code § 1240.
    - Borrowings that may not exceed 33 ⅓% of total assets, derivative instruments outstanding that may not exceed 10% of total assets, and may not invest in commodities or direct ownership of real estate.
    - Expense ratios that may not exceed 100 basis points for money market funds, 200 basis points for bond funds, or 300 basis points for a stock or mixed stock/bond fund.
- Investment pools
- Stock in Federal Home Loan Banks.
- Insurers with admitted assets over $25 million may invest in real estate and make improvements on that real estate as an investment for the production of income.
    - If the Commissioner determines that an insurer is carrying upon its books any real estate at values that exceed a sound market value, the insurer may be ordered to create a reserve against the book value of the property or to reduce the book value of the property.
- Notes or bonds secured by second mortgages or other second liens.

No excess fund investment:

- May be in an investment company that makes up more than 3% of admitted assets.
- May be in an affiliate group of investment companies that makes up more than 7% of admitted assets.
- May exceed more than 25% of total assets invested in the excess fund.
- May be worth more than the company's surplus in regard to policyholders.
- May be in any single investment company that would make up greater than 10% of the assets of that company.
- Of all medium and lower grade bond obligations may exceed 20% of admitted assets.
    - No more than 10% of admitted assets may consist of NAIC 4, 5, or 6-rated bonds
    - No more than 3% of admitted assets may consist of NAIC 5 or 6-rated bonds.
    - No more than 1% of admitted assets may consist of NAIC 6-rated bonds.

The Commissioner may deny credit for all or any part of an investment in an investment company if he or she finds the investment to be unsound or hazardous on the grounds that:

- The investment company's investment adviser lacks sufficient investment experience to render investment advice or lacks good standing with securities licensing authorities.
- The portfolio turnover rate of the investment company is deemed excessive in relation to its goals.
- Management fees or other fees are not reasonable.
- The investment company does not substantially mirror any security index upon which its investment policy is based.

Appendix 5

Summary of Authorized Investments for Continuing Care Retirement Communities in California, New York, and Florida

California (Health and Safety Code §§ 1770-1793.91)

Providers shall maintain at all times qualifying assets as a liquid reserve. The amount of this reserve is the sum of the debt service reserve (HSC § 1792.3) and the operating expense reserve (HSC § 1792.4). If the Department of Social Services has reason to believe that the provider is insolvent, in imminent danger of becoming insolvent, in a financially unsound or unsafe condition, or in a condition such that it may otherwise be unable to fully perform its obligations pursuant to continuing care contracts, the Department may increase the amount that a provider is required to hold or may require that the provider place its liquid reserve into an escrow account. Qualifying assets include (HSC § 1792.2):

- Cash and cash equivalents (certificates of deposit and U.S. treasuries with a maturity of 5 years or less)

- Investment securities:
  - Direct obligations of the U.S. government.
  - Obligations backed by the Federal Home Loan Bank, Export-Import Bank of the U.S., Federal Financing Bank, Government National Mortgage Association, Farmers Home Administration, Federal Home Loan Mortgage Corporation of the Federal Housing Administration, or any agency or department of the United States if they are rated in one of the two highest rating categories.
  - Bonds of California or any county or city of this state if they are rated in one of the two highest rating categories.
  - Commercial paper of finance companies and banking institutions if rated in one of the two highest rating categories.
  - Repurchase agreements fully secured by collateral security.
  - Long-term investment agreements rated in one of two highest rating categories.
  - Banker's acceptances or certificates of deposit rated in one of the two highest rating categories and insured by the Federal Deposit Insurance Corporation.
  - Taxable money market government portfolios restricted to obligations guaranteed by the U.S. government.
  - Bonds with at least an "A" Moody's rating that are listed on a national exchange.
  - Bonds traded over-the-counter that are rated at least "Aa" by Moody's or "AA" by Standard and Poor's or Fitch.
- Equity securities, including:
  - Shares of mutual funds that hold portfolios consisting predominantly of qualifying assets.
  - Large and mid-capitalization corporate stocks that are publicly traded and readily liquidated for cash.
- Lines or letters of credit under certain conditions

Providers that enter into contracts that have an up-front entrance fee and include a provision for housing, residential services, amenities, and unlimited specific health-related services with little or no substantial increases in monthly charges (type–A contracts) shall file an actuarial opinion as to the financial condition of the provider's continuing care operations at least once every 5 years.

New York (11 Codes, Rules, and Regulations § 350.6)

Continuing care retirement communities in New York must hold a debt reserve fund as well as an operating reserve fund. Eligible liquid assets include:

- Cash
- Demand accounts at any solvent national or state chartered bank or savings and loan association valued at surrender value.
- Commercial paper with original maturity 270 days or less which is rated by at least one NRSRO and valued at market value with equivalent of A-1+ or A-1 by Standard and Poor's or P-1 by Moody's.
- Non-negotiable certificates of deposit with a remaining maturity of one year or less valued at surrender value.
- Common or preferred stock. No investment shall be more than 5% of the market value of total assets supporting reserve liabilities and no more than 25% of assets in excess of those supporting reserve liabilities.
- U.S. government or Canadian government-issued or guaranteed bonds, bills, or notes, or U.S. government money market funds
- Other fixed income assets, provided that at least 90% of the market value of those assets consists of publicly traded obligations rated among the top four rating categories by either Standard and Poor or Moody's rating services. Any obligations rated lower will be valued at 90% of market value. No more than 10% of assets supporting reserve liabilities shall be invested in fixed income securities of any one issuer and no more than 5% of the securities of any one issuer will be included among the assets supporting reserve liabilities.
- Capital (fixed) assets.
- Any other asset which the operator can demonstrate as appropriate, subject to the approval of the superintendent.

Florida (Statute 651.035)

Providers must maintain in escrow a minimum liquid reserve consisting of a debt service reserve and operating expense reserve. Funds must be invested in a letter of credit following certain conditions or according to the rules set forth for insurance companies in Part II of Chapter 625 of the Florida Statutes. Allowable investments include:

- Cash and deposits
- U.S. government obligations, state obligations, Canadian obligations, and obligations of counties, municipalities, and districts of Florida.
- Loans guaranteed by the U.S.
- Public improvement bonds and public utility obligations
- Securities of certain government agencies
- Public housing obligations and obligations of the state board of education
- International development banks
- Corporate bonds

- Religions institution obligations
- Equipment trust certificates
- Building and loan or savings and loan association accounts
- Policy loans, collateral loans, or ship loans
- Corporate stocks (limited to 10% of insurer's admitted assets, no more than 3% in any one investment)
- Investments in subsidiaries and related corporations (limited)
- Capital participation instruments
- State of Israel obligations
- Mortgage loans (each limited to the lesser of 5% of admitted assets and 10% of capital and surplus. In aggregate must be less than 40% of admitted assets for life insurers; continuing care communities are not specified)
- Real estate (<5% of assets)

Appendix 6

Associations Currently in Suspended/Dissolved Status

- Albany Police and Fire Civil Service Club
- Anaheim Firemen's Benevolent Association
- Chico Police and Firemen's Association
- Compton Police Officers Association
- Firemen's Relief Fund Association of the Alameda Fire Department
- Hillsborough Firemen's Welfare Club
- Huntington Park Firemen's Relief Association
- Inglewood Firemen's Benefit Association
- Salinas Police Benefit Association
- San Bernardino Firemen's Benefit Association
- San Bernardino Police Department Benefit Association
- San Luis Obispo-Santa Barbara Bi-Counties Peace Officers Association
- Ventura Firemen's Relief Association
- Whittier Police Department Welfare Association
- Widows' and Orphans' Aid Association of the San Francisco Fire Department
- Widows and Orphans and Mutual Aid Fund of the Millbrae Volunteer Fire Department

Appendix 7

Associations Believed to be Inactive

- Chula Vista Police Relief Association
- Combined District Mutual Association of the San Francisco Fire Department
- Long Beach Firemen's Mutual Benefit Association
- Los Angeles Police Relief Association
- Los Angeles Police Retirement Benefits and Insurance Association
- Martinez Police Officers' Benefit and Relief Association
- Monterey Helmet Club of Fire Fighters
- Pasadena Firemen's Relief Association
- Redlands Fireman's Relief Association
- Sacramento County Firemen's Association Mutual Benefit Fund
- Sacramento Fire Department Relief Association
- San Diego Firemen's Relief Association
- San Mateo County Sheriff's Office Association
- Santa Barbara County Sheriff's Relief and Benefit Association
- Santa Barbara Firemen's Relief Association
- Santa Rosa Police and Fire Department Mutual Aid Association
- Sheriffs' Relief Association of Los Angeles County
- Stockton Fire Fighters Relief Association
- Torrance Fire-Fighters Benevolent Fund
- Vallejo Police and Fireman Benefit Association
- Ventura County Sheriff's Association
- Veteran Firemen's Association of San Francisco Incorporated
- Widows' and Orphans' Aid Assoc. of the Central Fire Protection District of Santa Clara
- Widows and Orphans Aid Association of the Oakland Police Department
- Widows' and Orphans' Aid Association of the Police Department of San Francisco, CA
- Widows' and Orphans' Aid Assoc. of the So. San Francisco Fire Dept. of San Mateo City.
- Widows and Orphans and Mutual Aid Association of the San Mateo Fire Department