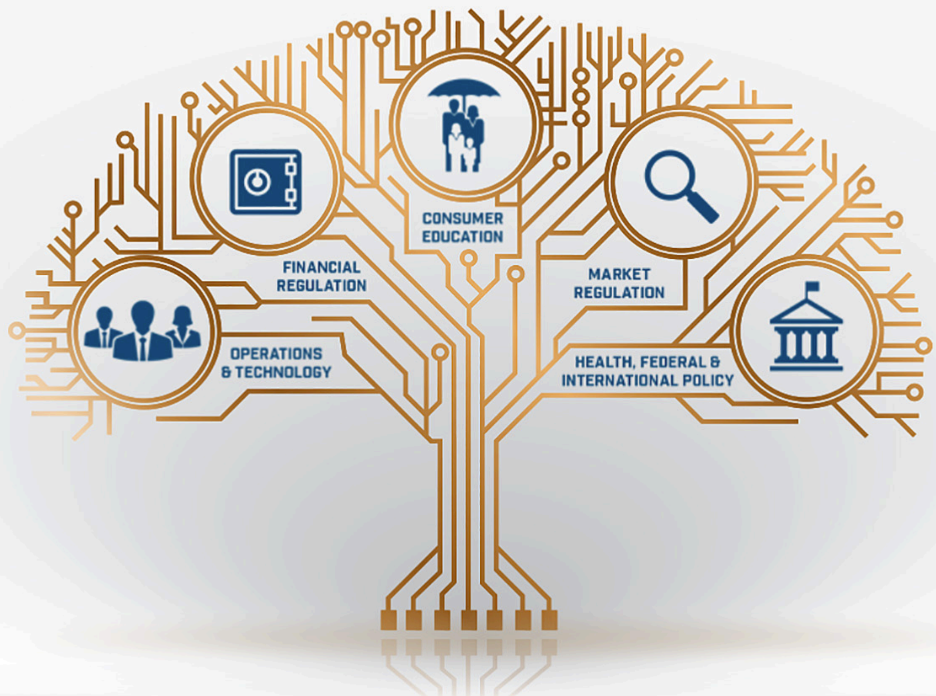
NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS **2016 ANNUAL REPORT**

INSPIRING **INNOVATION**



OPERATIONS, DATA & TECHNOLOGY

Association Highlights

The NAIC is the U.S. standard-setting and regulatory support organization created and governed by the chief insurance regulators from the 50 states, the District of Columbia and five U.S. territories. Through the NAIC, state insurance regulators establish standards and best practices, conduct peer review and coordinate their regulatory oversight. Its staff supports these efforts and represents state regulators' collective domestic and international views. NAIC members, together with the central resources of the association, form the national system of state-based insurance regulation in the U.S.

The NAIC provides its members a national forum for discussing common issues and interests, while working cooperatively on matters shared across jurisdictions. Collectively, commissioners work to develop model legislation, rules, regulations and white papers to coordinate regulatory policy. The overriding objective is to protect consumers and help maintain the financial stability of the insurance marketplace.

With its wide range of services, the NAIC supports the work of its committees, the state insurance departments, state and federal officials and the public. The association maintains three offices: the Executive Office in Washington, D.C.; the Central Office in Kansas City, Mo.; and the Capital Markets & Investment Analysis Office in New York City.

Home of the world's largest insurance financial database, the NAIC maintains extensive systems linking all state insurance departments and provides financial, actuarial, legal, research, technology, market conduct and economic expertise. Staff research and create standard and custom reports, develop uniform statutory financial statements, monitor federal activity, submit legal briefs, conduct educational training programs and much more.

The Center for Insurance Policy and Research (CIPR) leverages resources to collect and analyze information provided to officials, agencies and policymakers in the U.S. and abroad. Through seminars, presentations and publications, CIPR efforts strengthen: coordination with federal, state and international agencies and regulators; understanding of insurance-related topics and issues by thought leaders; information exchange between the states and the federal government; and state regulator participation in public policy decisions affecting insurance and the broader financial services sector.

NAIC Operations

Providing the highest quality of member service requires a talented and dedicated workforce. The NAIC is dedicated to creating a work environment that results in high job satisfaction for our employees. The association provides flexible work options — including flex scheduling and work-from-home opportunities, which promote work-life balance. The association also has an *Infants in the Workplace* program that allows parents to bring their newborn to work. In the program's 19th year, the NAIC welcomed 10 new babies to its office, meaning 150 babies have accompanied their parents to work since the program's inception.

The NAIC was honored with the Constangy, Brooks Smith & Prophete Excellence in Work-Life Balance Award, which recognized the association for promoting specific policies and programs that allow for workplace flexibility.

To promote wellness and team spirit, the NAIC's Kansas City office finished fourth in the Kansas City Corporate Challenge Division. The association's participation level increased to 205 employee participants from 78 in 2015.

The NAIC implemented a new Student Loan Repayment Program to facilitate the recruitment and retention of highly qualified candidates and employees.

One of the results of the association's culture is a low employee turnover rate. The NAIC had a net turnover of just 7.59% this year.

2016 NAIC Organizational Chart

Andrew J. Beal, Chief Operating Officer & Chief Legal Officer

Kay Noonan
General Counsel

Jim Woody
Chief Financial Officer

Scott Morris
Chief Technology Officer

Frosty Mohn
Chief Security & Information Officer

Christina Urias
Managing Director, International Insurance Regulatory Affairs

Jeff Johnston
Senior Director, Financial Regulatory Affairs, Domestic Policy & Implementation

Elise Liebers
Senior Director, Financial Regulatory Affairs, International Policy & Market Surveillance

Ethan Sonnichsen
Managing Director, Government Relations

Eric Nordman
Director, Regulatory Services and Center for Insurance Policy & Research

Trish Schoettger
Director, Member Services

Scott Holeman
Director, Communications

Todd Sells
Director, Financial Regulatory Policy & Data

Dan Daveline
Director, Financial Regulatory Services

Charles Therriault
Director, Securities Valuation Office

Eric Kolchinsky
Director, Structured Securities Group

Ed Toy
Director, Capital Markets Bureau

Ramon Calderon
Director, International Policy

Denise Matthews
Director, Data Coordination & Statistical Analysis

Kris DeFrain
Director, Research & Actuarial Services

Tim Mullen
Director, Market Regulation

Brent Roper
Director, Human Resources

Member Services

The NAIC is dedicated to providing the best possible services to its members through education and training, new member orientation and sponsorship of regulator travel for NAIC business.

The association hosted three national meetings — in New Orleans, San Diego and Miami — with a total of 5,974 attendees. The NAIC also held 60 interim meetings and 4,171 meetings via conference call. NAIC funding made it possible for each state insurance department to send a second senior regulator to NAIC-sponsored meetings at no cost to the state insurance departments.

The NAIC provided more than 88 free education and training courses for state regulators.

Insurance Summit

The NAIC hosted its inaugural Insurance Summit in Kansas City, combining several annual meetings and trainings into one large conference. More than 800 insurance regulators, industry professionals and consumer representatives attended a variety of sessions, organized by track – market regulation, financial regulation, communications, technology, producer licensing and CIPR.

The NAIC saved approximately $70,000 by consolidating the meetings into one weeklong summit.

CIPR Events

The CIPR hosted several well-attended symposiums. Events included *Technology and Insurance* at the Spring National Meeting, *Gearing Up for Autonomous Vehicles* at the Summer National Meeting, *The Impact of Rating Agencies on the Insurance Industry* in October and Regulatory Evaluation 2.0 – *Meeting the Challenges of Innovation* at the Fall National Meeting.

CIPR also published three editions of the CIPR Newsletter.

Data & Technology

NAIC Cybersecurity Enhancements

Cybersecurity continued to be one of the NAIC's primary focuses. The NAIC adopted the National Institute of Standards and Technology's (NIST) approach to managing information security risk as outlined in *NIST Special Publication 800-37*. Adoption of this Risk Management Framework has helped the NAIC identify and confront information security risks throughout the organization. The Risk Management Framework is a foundational element of the NAIC's Information Security program, and policies are built on the control framework platform. These policies bring together security, compliance and business requirements into one integrated framework.

The NAIC continued to implement new and more advanced security and privacy controls, as well as assess the continued effectiveness of established controls. Moving forward into 2017, the NAIC will continue to identify areas to mature and enhance security. With the ongoing heightened cybersecurity awareness within the insurance industry, cybersecurity will continue to be of paramount importance for the NAIC for the foreseeable future.

Life Insurance Policy Locator

A major consumer focus was creating and implementing the Life Insurance Policy Locator. Many life insurance benefits go unclaimed because beneficiaries have difficulty finding and accessing policy information. This project is designed to give consumers a tool to search for lost insurance policies and annuities.

Consumers provide information via an online tool to begin a search with participating life insurance companies. If matching information is discovered, the company will report back to the NAIC any relevant findings. In addition, a regulator application allows state department staff to search for pending requests and run reports.

Big Data

The NAIC has a long-standing role as a data collector for the states for statutory financial statements, Market Conduct Annual Statements (MCAS) and complaints data. Now the association is expanding its services to include regulators' ad hoc data collection needs, such as disaster reporting and mortality experience data collection from life insurers to assist regulators with the transition to principle-based reserving (PBR). As part of this expanded service, the NAIC is utilizing new technologies to develop the appropriate systems for collecting various regulatory data sets in a timely and cost-effective manner.

Business Intelligence

The NAIC started with a goal of building a secure, manageable and robust Business Intelligence (BI) framework for a group of internal and external users. Users will be able to discover value in the data that was unattainable before. The initiative started with a pilot group of around 20 internal staff with the idea of going into full production sometime in late 2017. After evaluating five tools, the decision was made to utilize the Tableau tool suite.

The BI pilot group also created several dashboards for experience data reporting, security of actuaries, the Life Insurance Policy Locator and many operational dashboards.

Enterprise Project Management Office

The NAIC created an Enterprise Project Management Office (EPMO) in March and is using portfolio management techniques to facilitate the integration of strategy, project management, resources and performance at an enterprise level. One of the goals was to standardize monthly reporting of all strategic projects. This was accomplished with the active and closed portfolio summary reports and roadmap overview. Standard status reports are used to provide the project's overall health, milestones and risk mitigation.

A new process was created for project proposals and project change requests. A project change request is required if an official adjustment to a strategic project's schedule, budget or critical success factors are needed. The EPMO meets monthly to review the status of projects, project change requests, new proposals and proposed process updates.

State Based Systems

The State Based Systems (SBS) team entered the transition phase of the SBS 2016 rewrite project and transitioned 12 of 26 jurisdictions from the legacy SBS system to the newly rewritten system. The SBS 2016 project is a multiyear project updating the SBS architecture and toolset to provide enhanced performance, stability and scalability.

The 12 jurisdictions transitioned this year were Delaware, Florida, Illinois, Kansas, Maryland, Montana, North Dakota, Puerto Rico, Rhode Island, Virginia, the Virgin Islands and Washington, D.C. To transition a jurisdiction, the SBS team completed the code, data migration, configurations and testing for core and state-specific requirements for all the services used by that insurance department.

The following services were deployed in the new application: Producer, Company, Continuing Education, Revenue, Consumer Services, Enforcement, Investigations, Senior Health Insurance Program (SHIP), Prescription Connection (PC), joint service of SHIP/PC, Arbitration, Projects, Market Exam and Market Analysis. This included completing the code, data migration, configurations, internal and user testing for core and state specific-requirements for each service and jurisdiction.

Information Technology Infrastructure Libraries

The NAIC and NIPR have begun to adopt consistent Information Technology Infrastructure Libraries (ITIL) methodologies throughout both organizations. The first two components of ITIL that will be implemented are Change Management and Incident Management. The new Change Management process includes increasing transparency across all teams in the organizations, increasing throughput and productivity by using the same process for all change types and gaining more control changes through approvals and workflows built into the JIRA Service Desk module. The new processes have been set and approved by senior leadership in order to enforce the policies across all business areas. Other goals include decreasing risk, negative impact, cost and surprises for both organizations.

The Incident Management implementation of ITIL is a joint effort by both the NAIC and NIPR to standardize and improve customer and technical support of their combined information technology (IT) platforms, products and services. Incident Management will enable greater flexibility and transparency through the use of standardized processes, customer support procedures, communication methods and powerful reporting tools. Incident Management is scheduled to go live during the second quarter of 2017.

VISION

The VISION project is a rewrite of the existing Integrated Securities Information System (ISIS) to include major enhancements using JAVA technology. The system is used by the Securities Valuation Office (SVO) and the Financial Regulatory Services (FRS) team, as well as industry customers who file their securities with the NAIC for a ratings designation. After undergoing two years of design and development, along with an extensive data migration, the new product launched in early September.

The system provides improved pricing capabilities; dashboards for filers and analysts; subsidiary, controlled and affiliated (SCA) company filing improvements; sharing of support documentation; faster uploads; and an overall improved customer experience. Following the initial delivery of the product, point releases were made on a monthly basis to clean up data anomalies and continue improvements to the system. The release schedule shifted to a five-week interval in November and the team continues to make improvements to the software as guided by the SVO and FRS groups.

Training Process Improvement

In the first quarter, the NAIC and NIPR embarked on a joint effort to implement IT Service Management (ITSM) best practices, using the ITIL framework. The Change Management and Incident Management ITIL processes were selected for initial evaluation and implementation to align the entire organization into a common set of tools, processes and coordination methodologies.

FINANCIAL REGULATION

Financial examinations and analysis processes are central to effective solvency oversight. By employing sophisticated analytical tools and expert resources, regulators minimize insolvencies and their profound impact on policyholders and the marketplace.

The Financial Condition (E) Committee and the Financial Regulation Standards and Accreditation Program work in tandem to maintain the U.S. system of solvency regulation.

Group Supervision

All 50 states, the District of Columbia and Puerto Rico have passed key amendments to their holding company statutes, which will aid in assessing the potential contagion risks present in the business enterprise that includes insurers. Updating the NAIC's *Insurance Company System Regulatory Act* (#440) was one of the NAIC's initial responses to the financial crisis to improve group supervision. In just six years since developing the model, states have passed this flagship legislation nationally, bolstering the NAIC's approach to group supervision.

Forty states have adopted legislation based on the NAIC *Risk Management and Own Risk and Solvency Assessment (ORSA) Model Act* (#505), which requires insurance groups above a certain size to file an annual ORSA Summary Report with their lead state. In 2014, the NAIC adopted additional revisions to Model #440, which provide clear legal authority for a state insurance commissioner to act as a group-wide supervisor for a defined class of internationally active insurance groups and further defines the activities the commissioner may engage in related to such authority.

The Financial Condition (E) Committee formed the Group Capital Calculation (E) Working Group and was charged to construct a U.S. group capital calculation using a risk-based capital (RBC) aggregation methodology. The working group has tentatively agreed to utilize an "inventory" approach to serve as its desired form of this aggregation. For much of the year, the working group explored methods for addressing various issues before finalizing the calculation. Ongoing work is expected throughout 2017 and into 2018. State insurance regulators continue to enhance their group supervisory framework through these efforts and their ongoing involvement in U.S. and non-U.S. lead supervisory colleges.

Reinsurance

Under the 2011 revisions to the NAIC *Credit for Reinsurance Model Law and Regulation* (Revised Reinsurance Models), reinsurers from a qualified jurisdiction are eligible to be certified for reduced reinsurance collateral requirements. To date, 35 states have passed the revised *Credit for Reinsurance Model Law* (#785), with 27 jurisdictions also adopting the revised *Credit for Reinsurance Model Regulation* (#786), covering approximately 69% of the direct insurance premium written in the U.S. across all lines of business. The NAIC voted to make the certified reinsurer provisions a uniform accreditation standard requirement for all NAIC-accredited jurisdictions effective Jan. 1, 2019.

The Reinsurance Financial Analysis (E) Working Group of the Financial Condition (E) Committee provides a peer review process for certified reinsurer designations. The Reinsurance Financial Analysis (E) Working Group's mission is to facilitate consistency among the states and to coordinate multi-state efforts. To date, the NAIC has approved 23 certified reinsurers. The working group also adopted the Uniform Application Checklist for Certified Reinsurers, to provide further guidance and ensure consistency across the states' certification processes.

Principle-Based Reserving

The NAIC continued to implement principle-based reserving (PBR), including addressing regulatory and NAIC staff resources, developing analysis and examination procedures, making changes to the statutory blanks and creating a Valuation Analysis (E) Working Group to provide consistent oversight and application across each jurisdiction. More than 42 states adopted the Standard Valuation Laws, triggering the threshold of 75% of U.S. premium volume.

Use of Captives by Life Insurers

In 2014, the NAIC adopted a conceptual reinsurance framework for life insurers' use of captives for business subject to Regulation AXXX and/or the *Valuation of Life Insurance Policies Model Regulation* (#830), commonly referred to as Regulation XXX. Several important components of this framework were adopted in 2014 and almost all other components were adopted in 2015, including new RBC requirements and additional disclosure within the annual audit report.

The NAIC adopted the *Term and Universal Life Insurance Reserve Financing Model Regulation* (#787) and revisions to the *Credit for Reinsurance Model Law* (#785), which collectively provide insurance departments with specified authority with regard to captive reinsurance transactions on certain term and universal life insurance business.

The NAIC focused on captive reinsurance used by life insurers known as variable annuities this year. The NAIC formed a Variable Annuities Issues (E) Working Group and by year-end, developed and adopted a structure to make changes to the statutory framework for variable annuities. The NAIC commissioned a quantitative impact study, which resulted in possible specific proposed changes to the statutory framework for variable annuities.

Financial Regulation Standards and Accreditation Program

The NAIC Financial Regulation Standards and Accreditation Program was established to maintain standards to promote effective financial solvency regulation. NAIC accreditation allows non-domestic jurisdictions to rely on the accredited domestic regulator to fulfill baseline financial regulatory oversight. Currently, all 50 states, the District of Columbia and Puerto Rico are accredited, making regulation more efficient and coordinated. Accreditation also creates far greater efficiencies for insurance companies, which are then not subject to overlapping regulation.

The NAIC conducted nine full accreditation reviews, 43 interim annual reviews and 10 pre-accreditation reviews. In addition, the NAIC adopted revisions to modernize the Accreditation Program to focus the program toward the substance and quality of work performed, ensuring the program continues to meet the needs of an increasingly complex and sophisticated regulatory environment. Further, various accreditation guidelines continue to be reviewed and revised, as appropriate, for updates to financial solvency regulation and the risk-focused surveillance process.

International Insurers Department

The International Insurers Department (IID) functions as a national gatekeeper for non-U.S. insurers seeking to gain access to the U.S. excess and surplus lines market. This function includes solvency monitoring and trust account maintenance of all NAIC-listed insurers, as well as oversight and analysis for considering new applications. Nine new insurers were added during the year, offset by four withdrawals, resulting in an increase to 149 listed entities at Jan. 1, 2017. The most recent financial statistics (2015) reflect that listed insurers wrote direct surplus lines' premiums of more than $11.6 billion, or about 28% of the $41.4 billion in total U.S. surplus lines premiums. As of Sept. 30, 2016, listed insurers maintained $4.9 billion in trust assets, which are held as collateral against an estimated $17 billion of gross claim liabilities as of year-end 2015.

Securities Valuation Office

The NAIC's Securities Valuation Office (SVO) is comprised of investment professionals who assess the credit risk of insurer investments. The SVO assigns an NAIC designation, a measure of credit risk, to filed insurer investments. The SVO received filings from 1,435 insurers. These filings covered 13,586 securities with an insurer total carrying value of approximately $346 billion. This unique capability allows the NAIC to assess investment credit risks through its own independent regulator-driven process instead of relying exclusively on nationally recognized statistical rating organizations. The NAIC designation and other analysis produced by the SVO are used in regulatory processes to monitor insurers, including the appropriateness of the RBC investment charges.

Mortgage-Backed Securities

The NAIC's Structured Securities Group (SSG) is an internal team of investment professionals that builds upon the NAIC's technical expertise to provide specialized analysis, valuation, research and reporting for structured securities. The NAIC first began modeling expected losses for non-agency residential mortgage-backed securities (RMBS) owned by insurance companies in 2009. This project was successful and expanded in 2010 to include commercial mortgage-backed securities (CMBS).

The SSG modeled 5,272 unique CMBS and 21,891 unique RMBS Committee on Uniform Security Identification Procedures (CUSIP) this year. The book values of these securities were approximately $152 billion for CMBS and $101 billion for RMBS.

Capital Markets

The NAIC Capital Markets Bureau (CMB) provides a macroprudential view in support of the efforts of state insurance regulators. The CMB monitors trends, developments and activity in financial markets around the world while analyzing the potential impact on investment activities and portfolios of U.S. insurance companies. The CMB then reports these results to state insurance regulators, in addition to publishing reports available to both regulators and the general public.

The group published 17 Capital Markets Special Reports. These reports include updates on U.S. insurer exposures to different investment markets and strategies, such as below investment grade investments and securities lending. Topical issues are also covered, such as the use of credit derivative index products, the shifting role of U.S. insurers in the investment ecology and the impact of diverging international economies.

The CMB also provides quick updates on more specific situations in the capital markets through periodic Hot Spots. Flurries of market volatility this year that were often event driven created a greater need for these alerts. They focused on market reactions to the U.K. referendum to leave the European Union and the U.S. presidential election, the implications of flat yield curves and negative government bond yields, as well as ongoing issues such as oil price volatility and the Puerto Rican debt crisis.

CONSUMER EDUCATION

Celebrating its 10th year, Insure U is the NAIC's primary public education program. Insure U has successfully employed a variety of tactics to target and educate consumers about a wide range of insurance-related issues through traditional and social media channels. Insure U provides materials organized by life event, life stage and insurance type. Additional special sections support mini-campaigns for specific targets, such as retirement security, modern families, young singles and disaster preparation.

The NAIC's websites had an outstanding year, with Insure U totaling more than 332,000 visits, while NAIC.org attracted more than 8.8 million visits. NAIC social media ended the year with more than 12,700 Twitter followers, 6,650 Facebook likes, 3,800 LinkedIn followers and 3,030 LinkedIn group members. More than one billion total media impressions were generated during the year's various campaigns.

Consumer Outreach

Consumer outreach focused on technology, modern households, the sharing economy and financial literacy for students. As part of the NAIC's retirement security initiative, consumer outreach to seniors — with an emphasis on preparing for retirement — was included in outreach plans.

Rita Moreno Sets the Stage

The NAIC partnered with legendary entertainer Rita Moreno to help communicate the needs of seniors. While Moreno has been successful on the stage and screen, she relied on her husband to make most financial decisions. When he passed away, she was left with many questions regarding her finances and insurance coverage.

Moreno's personal story helped promote retirement planning, which was a key initiative for the members. A native Puerto Rican, Moreno recorded radio public service announcements (PSA) in English and Spanish that spoke to the importance of smart retirement planning and other issues facing senior citizens. She also recorded social media videos and made an appearance at the NAIC's Summer National Meeting in San Diego, where she discussed the importance of planning ahead.

RJ Mitte Continues to Connect With Millennials

"Breaking Bad" star RJ Mitte led the NAIC's millennial outreach efforts for the second year. Mitte highlighted his own "Bad Breaks" that taught him firsthand the importance of insurance. He recorded three videos for the NAIC that were promoted on social media. His candid dialogue about personal experiences with theft, car accidents and the importance of talking with parents about insurance planning resonated with younger audiences. He also led two live Twitter chats to engage with young people about insurance. This unique campaign targeting a hard-to-reach audience generated more than 128 million impressions. Mitte, who has an impressive social media following, shared personal comments and Insure U content about a variety of important insurance issues.

Kimberly Williams-Paisley Wraps Up Campaign

Actress Kimberly Williams-Paisley first partnered with the NAIC in 2015 to share her family's experience with her mother's diagnosis of dementia and urge consumers to plan for the unexpected. In a radio PSA, she underscored the need for baby boomers and established families to have a plan. Her story was also featured in People and SPRY Living magazines. This campaign wrapped in early 2016, earning more than 414 million media impressions, with an estimated ad value of $5.4 million.

Financial Literacy Outreach

The NAIC continued its partnership with the Jump$tart Coalition for Personal Financial Literacy — a non-profit organization committed to advancing financial literacy among pre-school through college-age youth and working collaboratively toward effective financial education. The NAIC partnered with the Pennsylvania Insurance Department to develop *Insurance 101 for Teen Drivers*, an insurance curriculum for high school teachers. Teachers started using these materials about auto insurance in May.

Professional Recognition

The NAIC's consumer education programs were recognized for excellence with several awards. The Greater Kansas City Chapter of the Public Relations Society of America (PRSA) honored the NAIC with six PRISM awards, one for each of the entries the NAIC submitted. The NAIC was also recognized at the PR News Platinum PR Awards with an honorable mention for the 2015 Annual Report and at the PR News Digital PR Awards for the "Bad Breaks" social media campaign with RJ Mitte.

MARKET REGULATION

State insurance regulators protect and serve consumers through many channels, but much of this work is streamlined through the Market Regulation and Consumer Affairs (D) Committee. Here, regulators monitor all aspects of the marketplace for continuous improvement.

The NAIC held its third Market Regulation Summit in May as part of the inaugural Insurance Summit, where state insurance regulators set priorities for market conduct regulatory activities. Attendees exchanged perspectives on regulatory best practices and discussed shared challenges and insights into industry practices. A key area of focus was insurers' use of big data and predictive analytics in rating, underwriting, marketing and claims. The summit included an exchange of perspectives on how big data use and predictive analytics are changing how insurers operate in the marketplace, the insurance purchasing experience for consumers and regulatory issues arising from these changes.

Life Insurance Policy Locator

The NAIC launched the Life Insurance Policy Locator in August — a national service that helps consumers search for a deceased person's life insurance policies and annuities. Through the end of the year, consumers submitted more than 5,000 requests and recovered more than $3.7 million in lost benefits.

Market Conduct Annual Statement

The Market Conduct Annual Statement (MCAS) provides a uniform system of collecting market conduct information for personal lines annuities, life insurance, homeowners insurance, private passenger automobile insurance and long-term care insurance. There were 47 participating jurisdictions this year, up from 29 when the program launched in 2009. In addition, the NAIC adopted a new health MCAS blank to facilitate the collection of 2017 health insurance data in 2018. The NAIC assists members by receiving MCAS filings, validating data and enhancing the analysis of market conduct information. The NAIC received 30,051 MCAS filings to be centrally stored this year.

Complaints Database System

The NAIC's 56 member jurisdictions submitted a total of 248,471 complaints to the Complaints Database System (CDS) this year. This database contains information about closed consumer complaints filed against insurance entities and producers. The CDS automates the collection and storage of complaint data submitted by state insurance departments. Regulators can then leverage nationwide information from this database.

Regulatory Information Retrieval System

The Regulatory Information Retrieval System (RIRS) contains records of regulatory actions finalized by state insurance departments against entities engaged in the business of insurance. States entered 8,027 actions into the database this year.

Online Fraud Reporting System

Increased reporting to state insurance departments helps reduce fraud, which cut insurers' expenses, protects consumers and reduces costs that otherwise lead to higher premiums. Jurisdictions use the Online Fraud Reporting System (OFRS) to receive referrals of suspected fraud from consumers and the insurance industry. The NAIC also receives reports from the National Insurance Crime Bureau (NICB). The NAIC received 66,110 reports this year that were made available to members.

State regulators actively engage in consumer protection by verifying insurance policy provisions comply with state law, are reasonable and fair, and do not contain major gaps in coverage that might be misunderstood by consumers and leave them unprotected.

HEALTH, FEDERAL & INTERNATIONAL POLICY

Government Relations

Consumer protection and market stability are hallmarks of the U.S. system of state-based insurance regulation. State insurance departments working collectively through the NAIC demonstrate their effectiveness by working with Congress, the administration and international standard-setting bodies to promote sound policy to best serve the needs of consumers. Through our commitment at the federal and international levels, the NAIC collaborates with regulators and lawmakers in the U.S. and around the world to achieve our policy goals.

Federal Engagement

State insurance regulators engaged a number of federal agencies on several financial policy issues. The NAIC submitted comment letters to Congress supporting legislation, including the Senior $afe Act, which passed the House, and provided guiding principles for reauthorization of the National Flood Insurance Program.

The NAIC also made recommendations to the administration on various financial regulatory issues, including enhanced prudential standards for systemically significant insurers and capital standards for insurers under Federal Reserve supervision. The association also submitted comments to the Federal Reserve and the Bureau of Consumer Financial Protection, among other agencies.

Former North Dakota Insurance Commissioner Adam Hamm served as the designated state insurance commissioner on the Financial Stability Oversight Council (FSOC) until September, when he was succeeded by Peter L. Hartt, Director of New Jersey's Insurance Division.

In April, the NAIC submitted an amicus brief in the United States Court of Appeals of MetLife, Inc. v. Financial Stability Oversight Council in support of MetLife's challenge to its designation as a systemically important financial institution. Hamm previously dissented on the action of FSOC during the designation process and the NAIC supported Congressional review of the process.

Working with Congress

Through the NAIC, state regulators work closely with Congress through member-to-member meetings and during congressional hearings. Pennsylvania Insurance Commissioner Teresa D. Miller testified during a congressional hearing on Jan. 13 before the U.S. House Financial Services Subcommittee on Housing and Insurance. As chair of the NAIC Property and Casualty Insurance (C) Committee, she spoke in favor of H.R. 2901, the Flood Insurance Market Parity and Modernization Act supported by the NAIC. The legislation subsequently passed the House.

Hamm — who chaired the NAIC Cybersecurity (EX) Task Force — testified before Congress on known and emerging issues affecting cybersecurity in the insurance sector on March 22. He also spoke about the importance of protecting consumer data and developing a strong cyber insurance market.

Nearly 40 chief state insurance regulators traveled to Washington, D.C. for the NAIC's Commissioner Fly-In in the spring. The members were briefed by Sen. Susan Collins (R-Maine) and Rep. Sean Duffy (R-Wis.) before scheduled meetings with their congressional delegations. Political analyst Stuart Rothenberg also gave a presentation on the potential impact of the 2016 elections.

Oklahoma Insurance Commissioner John D. Doak attended the White House Forum on Smart Finance for Disaster Resilience on behalf of the NAIC in September. Senior presidential advisor Brian Deese — who oversees climate, conservation and energy policy — and Federal Emergency Management Agency Director Craig Fugate briefed the audience. The forum gave participants an opportunity to learn about new approaches and programs and leveraging resources regarding disaster-recovery financing.

Also in September, former Missouri Insurance Director John M. Huff participated in a panel discussion on emergency preparedness hosted by The Hill in Washington, D.C. The forum, *Preparing For The Next Disaster: A Policy Discussion on Community Resilience*, examined the role of the federal, state and local government in pre-event mitigation.

Tennessee Insurance Commissioner Julie Mix McPeak testified before Congress in September on the NAIC's engagement with the European Union (EU). Her testimony detailed marketplace dynamics in the U.S. and EU, developments in Europe's transition to Solvency II, the ongoing EU-U.S. Dialogue Project and negotiations for a covered agreement for reinsurance collateral.

NAIC members actively promoted sensible cyber policies in Washington, D.C. during National Cybersecurity Awareness Month in October. Huff attended a White House meeting on cybersecurity with members of the administration, the National Security Council and representatives of the U.S. Department of the Treasury to discuss emerging cyberthreats and implications of a potential significant incident. Participants addressed the importance of coordination and procedures for organization among financial sector companies. Leaders from the government, financial regulators and the private sector reiterated their commitment to improving cybersecurity through public-private collaboration.

Health Policy

Six years after the passage of the Affordable Care Act (ACA), state regulators continue to coordinate through the NAIC to navigate health insurance reforms and regulatory challenges. The NAIC continues to work with federal agencies on health reform rule-making activities.

Federal Engagement

Maryland Insurance Commissioner Al Redmer Jr. testified before Congress on behalf of the NAIC in September. The hearing, held by the U.S. House Oversight and Government Reform Committee, examined rising health insurance premiums under the ACA. His testimony focused on the challenges facing state health insurance exchanges.

Several insurance regulators provided state perspectives during testimony before the U.S. Senate during the State of Health Insurance Markets hearing also in September. Lieutenant Governor and Director of the Ohio Insurance Department Mary Taylor, former Iowa Insurance Commissioner Nick Gerhart, Washington State Insurance Commissioner Mike Kreidler and Wisconsin Deputy Insurance Commissioner J.P. Wieske testified before the Committee on Homeland Security and Governmental Affairs.

The NAIC commented on several proposed regulations and facilitated regular oversight calls with state and federal regulators. In addition, the NAIC promoted legislative language that would allow states to regulate air ambulances to restrict balance billing.

The association also provided comments on implementation issues to Congress and federal agencies including: the Internal Revenue Service, Health and Human Services, and the Centers for Medicare & Medicaid Service.

Long-Term Care

The NAIC held a public hearing in August to examine the future of private solutions to long-term care financing. The Long Term Care Innovation (B) Subgroup held the hearing during the NAIC's Summer 2016 National Meeting. Presenters from state insurance departments, consumer groups and insurance industry professionals covered topics ranging from innovation to affordability and availability as well as consumer education. The subgroup also held a series of calls to receive more input. The NAIC continues to examine potential product modifications, reductions of regulatory barriers and appropriate incentives to strengthen the insurance market.

International Activities

The NAIC is committed to maintaining our position as a world leader and standard-setter in the insurance market. Through robust dialogues with counterparts around the globe, U.S. insurance regulators are well-positioned to protect American consumers and companies.

International Association of Insurance Supervisors

The International Association of Insurance Supervisors (IAIS) is a component of the NAIC's interaction with foreign regulators. In this venue, regulators coordinate with colleagues on global standards and best practices, while maintaining a focus on safeguards for U.S. insurance consumers and companies.

The NAIC welcomed members of the IAIS to Kansas City in January while hosting a meeting of its Executive (EX) Committee. Highlights included the continuing development of an international capital standard for insurance and prioritizing IAIS activities. Other discussion topics were stakeholder engagement, cybersecurity, reinsurance, the impact of low interest rates on insurer investments and the long-term care insurance market. The attendees ended their visit with a tour of the NAIC Central Office, which serves as a clearinghouse for data collection and analysis of the insurance industry in the U.S.

In June, NAIC members traveled to Budapest, Hungary, to participate in IAIS committee meetings and stakeholder dialogue. During the proceedings, Tennessee Insurance Commissioner Mix McPeak was elected as one of the committee's two vice chairs.

The IAIS also formally approved Wisconsin Insurance Commissioner Ted Nickel and Texas Insurance Commissioner David Mattax as members of ExCo during the meeting. Connecticut Insurance Commissioner Katharine L. Wade was appointed to the IAIS Financial Stability and Technical Committee, joining Commissioner Mix McPeak, Director Hartt and Senior Director of Financial Regulatory Affairs for the NAIC Elise Liebers.

International Forum

Federal Reserve Governor Daniel Tarullo gave the keynote address during the second day of the 10th annual International Insurance Forum in May. During Tarullo's speech, he highlighted the importance of different regulatory approaches. Another keynote address came from Victoria Saporta, chair of the IAIS Executive Committee.

The two-day forum drew more than 300 attendees and featured panels on systemic risk and insurance regulation, insurance company investments in a volatile marketplace, cybersecurity and cyberinsurance, and managing catastrophic risk using insurance and reinsurance.

International Fellows

In its 12th year, the NAIC's International Fellows Program welcomed nine international fellows from six countries in April. The spring class included members from Bermuda, India, Nigeria, Saudi Arabia, South Korea and Taiwan, hosted by Louisiana, Missouri, Oklahoma, Puerto Rico, Texas, Vermont and Washington, D.C. The NAIC welcomed nine participants to the fall class in October. Countries represented were Bermuda, China, India, Saudi Arabia, Thailand and Taiwan.

Since the program began in 2004, 36 U.S. jurisdictions have hosted nearly 260 participants from 32 countries.

Bilateral and Regional Dialogues

Nearly two-thirds of the global insurance market is comprised of the Pacific Rim and Latin American regions. This includes the top three largest national markets — the U.S., Japan and China. These regions show promise for expansion, as U.S. insurers seek opportunities for growth.

The NAIC hosted the Third Annual Asia-Pacific International Forum prior to the Summer National Meeting in San Diego. The forum served as an opportunity to strengthen relationships between regulators from the U.S. and the Asia-Pacific region. More than 35 regulators from the region and the U.S., joined senior-level industry representatives in attendance at the event.

In October, the NAIC participated in the Sixth Insurance Regulatory Dialogue between U.S. and Japanese regulators. Members met with representatives from the Financial Services Agency of Japan to discuss key issues, including cybersecurity, principle-based reserving and the group capital calculation.

Other bilateral and regional dialogues took place throughout the year, including Bermuda, China, Japan and Thailand along with Latin America and the EU. In addition to the IAIS, the NAIC participated in meetings of the Organisation for Economic Co-operation and Development. The NAIC also continues to build relationships through participation in and leadership of international supervisory colleges of regulators, where regulatory cooperation is practiced to the benefit of all participants.

AUDITED FINANCIAL REPORTS
DECEMBER 31, 2016

National Association of Insurance Commissioners

Financial Report
December 31, 2016

THE POWER OF BEING UNDERSTOOD
AUDIT | TAX | CONSULTING

RSM

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RSM US LLP

Independent Auditor's Report

Honorable Members
National Association of Insurance Commissioners
Kansas City, Missouri

Report on the Financial Statements
We have audited the accompanying financial statements of the National Association of Insurance Commissioners, which comprise the statements of financial position as of December 31, 2016 and 2015, the related statements of activities and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements
Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation and maintenance of internal controls relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility
Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion
In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the National Association of Insurance Commissioners as of December 31, 2016 and 2015, and the changes in its net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

RSM US LLP

Kansas City, Missouri
February 16, 2017

THE POWER OF BEING UNDERSTOOD
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National Association of Insurance Commissioners

Statements of Financial Position
December 31, 2016 and 2015

	2016	2015
Assets		
Current assets:		
Cash and cash equivalents	**$ 10,548,197**	$ 8,353,628
Accounts receivable, less allowance for doubtful accounts of 2016—$2,111,578 and 2015—$3,308,171	**8,595,280**	10,048,092
Interest receivable	**69,079**	81,015
Incentive receivable (Note 4)	**201,013**	189,635
Prepaid expenses	**3,204,823**	3,076,917
Inventories	**97,276**	83,862
Investments (Note 2)	**101,606,317**	98,629,348
Total current assets	**124,321,985**	120,462,497
Operating note receivable (Note 6)	**3,227,696**	3,155,950
Incentive receivable (Note 4)	**1,201,114**	1,402,127
Property and equipment, net (Note 3)	**26,993,702**	27,591,550
Total assets	**$ 155,744,497**	$ 152,612,124
Liabilities and Net Assets		
Current liabilities:		
Accounts payable	**$ 3,580,409**	$ 1,482,717
Accrued expenses and other current liabilities	**11,167,500**	13,948,242
Deferred revenue	**6,069,411**	6,300,587
Total current liabilities	**20,817,320**	21,731,546
Deferred lease incentive (Note 4)	**10,020,665**	11,373,018
Deferred pension liability (Note 5)	**5,644,037**	5,134,063
Total liabilities	**36,482,022**	38,238,627
Unrestricted net assets:		
Allocated	**117,476,818**	112,730,294
Unallocated	**1,785,657**	1,643,203
Total unrestricted net assets	**119,262,475**	114,373,497
Total liabilities and net assets	**$ 155,744,497**	$ 152,612,124

See notes to financial statements.

National Association of Insurance Commissioners

Statements of Activities
Years Ended December 31, 2016 and 2015

	2016	2015
Revenues:		
Member assessments	**$ 2,109,914**	$ 2,193,791
Database fees	**26,700,694**	26,344,370
Publications and insurance data products	**15,092,720**	14,549,758
Valuation services	**27,069,520**	26,625,927
Transaction filing fees	**9,200,422**	9,058,068
National meeting registration fees	**2,153,060**	2,095,850
Education and training	**594,168**	683,603
Administrative services/license fees	**14,323,946**	12,984,007
Other	**96,673**	49,820
Total revenues	**97,341,117**	94,585,194
Expenses:		
Salaries	**46,041,296**	45,482,446
Temporary personnel	**414,852**	443,379
Employee benefits	**13,960,587**	11,956,752
Professional fees	**15,073,405**	15,148,778
Travel	**4,310,805**	4,454,152
Rental and maintenance	**7,166,983**	6,627,264
Depreciation and amortization	**5,079,912**	3,870,014
Insurance	**494,104**	510,496
Supplies	**2,021,281**	2,058,153
Printing expense	**74,949**	127,772
Meetings	**2,653,759**	2,293,529
Education and training	**1,196,153**	1,732,619
Bad-debt expense	**199,984**	286,590
Other	**917,911**	851,223
Total expenses	**99,605,981**	95,843,167
Changes in net assets before investment income (loss) and pension adjustment	**(2,264,864)**	(1,257,973)
Investment income (loss) (Note 2)	**7,228,909**	(2,400,640)
Changes in net assets before pension adjustment	**4,964,045**	(3,658,613)
Pension adjustment	**(75,067)**	(1,711,816)
Changes in net assets	**4,888,978**	(5,370,429)
Net assets, beginning of year	**114,373,497**	119,743,926
Net assets, end of year	**$ 119,262,475**	$ 114,373,497

See notes to financial statements.

National Association of Insurance Commissioners

Statements of Cash Flows
Years Ended December 31, 2016 and 2015

	2016	2015
Cash flows from operating activities:		
Changes in net assets	**$ 4,888,978**	$ (5,370,429)
Adjustments to reconcile changes in net assets to net cash provided by operating activities:		
Interest income included in operating note receivable	**(71,746)**	(70,152)
Depreciation and amortization	**5,079,912**	3,870,014
Net realized and unrealized losses (gains) on investments	**(4,269,596)**	5,357,100
(Gain) loss on sale of property and equipment	**58**	(880)
Changes in operating assets and liabilities:		
Accounts receivable, net	**1,452,812**	1,124,654
Incentive receivable	**189,635**	178,900
Interest receivable	**11,936**	12,127
Prepaid expenses	**(127,906)**	(323,987)
Inventories	**(13,414)**	4,244
Accounts payable	**2,097,692**	(1,215,492)
Accrued expenses and other current liabilities	**(2,780,742)**	(2,045,884)
Deferred revenue	**(231,176)**	527,409
Deferred lease incentive	**(1,352,353)**	(688,406)
Deferred pension liability	**509,974**	1,455,624
Net cash provided by operating activities	**5,384,064**	2,814,842
Cash flows from investing activities:		
Purchase of property and equipment	**(4,482,225)**	(7,999,165)
Proceeds from disposition of property and equipment	**103**	2,776
Purchase of investments	**(31,542,704)**	(27,694,173)
Proceeds from disposition of investments	**32,835,331**	29,956,968
Net cash used in investing activities	**(3,189,495)**	(5,733,594)
Net increase (decrease) in cash and cash equivalents	**2,194,569**	(2,918,752)
Cash and cash equivalents:		
Beginning of year	**8,353,628**	11,272,380
End of year	**$ 10,548,197**	$ 8,353,628
Supplemental disclosures of investing activities:		
Property and equipment in accounts payable	**$ -**	$ 249,979
Property and equipment in accrued expenses	**$ -**	$ 263,994

See notes to financial statements.

Note 1. Nature of Operations and Summary of Significant Accounting Policies

Nature of operations: The National Association of Insurance Commissioners (the NAIC) is the U.S. standard-setting and regulatory support organization created and governed by the chief insurance regulators from the 50 states, the District of Columbia and five U.S. territories. Through the NAIC, state insurance regulators establish standards and best practices, conduct peer reviews, and coordinate their regulatory oversight. The NAIC staff supports these efforts and represents the collective views of state regulators domestically and internationally. The NAIC members, together with the central resources of the NAIC, form the national system of state-based insurance regulation in the U.S.

Cash and cash equivalents: The NAIC considers all liquid investments with original maturities of one year or less to be cash equivalents. At December 31, 2016 and 2015, cash equivalents consisted of money market funds and discount notes. The NAIC, at times, maintains deposits with banks in excess of the insured limits, but has not experienced any losses in such accounts.

Accounts receivable: Accounts receivable are stated at the amounts billed to customers. The NAIC provides an allowance for doubtful accounts, which is based upon a review of outstanding receivables, historical collection information and existing economic conditions. Past-due accounts are periodically reviewed by management. Delinquent and/or uncollectible receivables are written off based on individual credit evaluation and specific circumstances of the customer.

Inventory pricing: Inventories are stated at the lower of cost, determined by the first-in, first-out (FIFO) method, or market.

Investments: The NAIC carries its investments in marketable securities with readily determinable fair values, and all investments in debt securities, at their fair values determined by reference to public exchanges. The NAIC reports the fair value of alternative investments using the practical expedient. Unrealized gains and losses are included in the change in net assets in the accompanying financial statements.

Investments may be exposed to various risks, such as interest rate, market and credit risks. As a result, it is at least reasonably possible that changes in risks in the near term could affect investment balances, and those effects could be significant.

Fair value of financial instruments: The following methods and assumptions were used to estimate the fair value of each class of the NAIC's financial instruments at December 31, 2016 and 2015:

Cash and cash equivalents: The carrying amount approximates fair value because of the short maturity of these instruments.

Investment securities, except alternative investments: The fair values of fixed income, and domestic and international equity investments are based on quoted market prices at the reporting date for those or similar investments. A portion of the fixed income investments are valued based on quoted prices for similar instruments in active markets.

Alternative investments: The NAIC reports the fair value of market alternative investments using the practical expedient. The practical expedient allows for the use of net asset value (NAV), either as reported by the investee fund or as adjusted by the NAIC based on various factors.

Note 1. Nature of Operations and Summary of Significant Accounting Policies (Continued)

Fair value measurements: Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date in its principal market, or in the absence of a principal market, the most advantageous market for the investment or liability. The NAIC accounts for its investments at fair value. In accordance with the guidance, the NAIC has categorized its investments based on the priority of the inputs to the valuation technique, which gives the highest priority to unadjusted quoted prices in active markets for identical assets (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are described below:

Level 1: Quoted prices for identical instruments traded in active markets

Level 2: Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in inactive markets; or derived from inputs that are observable

Level 3: Valuations for assets and liabilities that are derived from other valuation methodologies, including option pricing models, discounted cash flow models and similar techniques, and not based on market exchange, dealer or broker trade transactions. Level 3 valuations incorporate certain assumptions and projections in determining the fair value assigned to such assets or liabilities

Investments and concentrations of credit risk: Financial instruments that potentially subject the NAIC to significant concentrations of credit risk consist principally of cash and investments. The NAIC maintains deposits in financial institutions in excess of federally insured limits. Management monitors the soundness of these financial institutions and believes the NAIC's risk is negligible.

Alternative investments are redeemable with the fund at net asset value under the original terms of the partnership and/or subscription agreements. However, it is possible that these redemption rights may be restricted or eliminated by the funds in the future, in accordance with the fund agreements. Due to the nature of the investments held by the funds, changes in market conditions and the economic environment may significantly impact the net asset value of the funds and, consequently, the fair value of the NAIC's interests in the funds. Although a secondary market exists for these investments, it is not active and individual transactions are typically not observable. When transactions do occur in this limited secondary market, they may occur at discounts to the reported net asset value. It is therefore reasonably possible that if the NAIC were to sell these investments in the secondary market, a buyer may require a discount to the reported net asset value, and the discount could be significant.

Property and equipment: Property and equipment are stated at cost. Depreciation is computed using the straight-line method over the estimated useful life of each asset. Leasehold improvements are depreciated over the shorter of the lease term or their respective estimated useful lives.

The cost of internally developed software is expensed until the technological feasibility of the software has been established. Thereafter, all software development costs are capitalized until such time as the product is available for general release to customers. The development costs of enhancements that extend the life or improve the marketability of the original product are capitalized. The establishment of technological feasibility and the ongoing assessment of recoverability of capitalized software development costs require considerable judgment by management with respect to certain external factors, including, but not limited to, anticipated future revenues, estimated economic life and changes in software and hardware technologies. The cost of capitalized software is amortized on the straight-line method over the products' estimated useful lives.

Note 1. Nature of Operations and Summary of Significant Accounting Policies (Continued)

	Estimated Useful Lives
Furniture and equipment	5-13 years
Computer and related equipment	3 years
Computer software	3-10 years
Leasehold improvements	10-13 years

Uses of estimates: The preparation of financial statements in conformity with accounting principles generally accepted in the United State of America (U.S. GAAP) requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Basis of accounting for revenues: Revenue is recognized as follows:

- Database fee revenue is recognized upon the filing of insurance companies' annual statements.

- Publications and insurance data products revenue is recognized when the product is shipped to the customer.

- Valuation services and transaction filing fee revenue is recognized when the service or filing has been performed.

- License fees consist of revenue earned from a related party for the use of the NAIC's producer data. Administrative services consist of revenues earned from related parties for administrative services and the use of the NAIC's facilities and equipment. Revenue from administrative services/license fees is recognized as revenue when the services are performed and when the use of the NAIC's assets occurs, in accordance with the terms contained in written agreements in effect with related parties.

- Revenue from fees for member assessments apply to an assessment fiscal year ended April 30, and are recorded in the calendar year assessed as receivables and deferred revenue. At December 31 of each year, 1/3 of the assessments are accounted for as deferred revenue.

Income taxes: The NAIC has been granted exemption from income taxes by the Internal Revenue Service under the provisions of section 501(c)(3) of the Internal Revenue Code and a similar provision of state law. However, the NAIC is subject to federal income tax on any unrelated business taxable income.

Uncertain tax positions, if any, are recorded in accordance with *FASB Accounting Standards Codification* (ASC) 740, Income Taxes. ASC 740 requires the recognition of a liability for tax positions taken that do not meet the more-likely-than-not standard that the position will be sustained upon examination by the taxing authorities. There is no liability for uncertain tax positions recorded at December 31, 2016 or 2015.

Note 1. Nature of Operations and Summary of Significant Accounting Policies (Continued)

Net assets: The NAIC operating reserve is based on a liquid reserve, defined as total net assets, less net property and equipment, as a percentage of the future year's budgeted operating expenses. On July 7, 2015, following a comprehensive review by an outside consultant to reflect the NAIC's current operating environment, the NAIC adopted a target liquid reserve range of 83.4 percent to 108.2 percent. Net assets are allocated by the Executive (EX) Committee and Internal Administration (EX1) Subcommittee as a function of the budgeting process. As of December 31, 2016 and 2015, net assets were fully allocated, with the exception of an amount maintained as unallocated equal to 1.5 percent of the next year's projected net assets. The unallocated balance will be used to fund priority initiatives that may arise in the next year.

Pension plan: The Compensation-Retirement Benefits topic of the ASC requires employers to recognize on their statements of financial position a liability and/or an asset equal to the under-funded or over-funded status of their defined benefit pension and other postretirement benefit plans. The funded status that the NAIC has reported on the statements of financial position under the topic is measured as the difference between the fair value of plan assets and the benefit obligation.

Functional expenses: The Not-for-Profit Entities topic of the ASC requires nonprofit organizations to disclose expenses by functional classification. The NAIC presents expenses only by their natural classification in the December 31, 2016 and 2015, statements of activities. Management believes that disclosing expenses by function is insignificant to the financial statements taken as a whole, and therefore does not apply the provision of the topic as it relates to the disclosure of expenses by functional classification.

Recent accounting pronouncements: In May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2014-09, *Revenue from Contracts with Customers (Topic 606)*. This guidance is intended to improve comparability of accounting treatment for revenue recognition across geographies and industries, and to provide more useful information to financial statement readers through enhanced disclosure requirements. It replaces industry-specific guidance with a principles-based approach for revenue recognition, and is a step toward convergence of accounting principles generally accepted in the United States of America and International Financial Reporting Standards. In general, it requires revenue recognition to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. This ASU, as deferred one year by ASU No. 2015-14, is effective for annual reporting periods beginning after December 15, 2018, and interim periods within annual periods beginning after December 31, 2019. Therefore, this ASU will be effective for the NAIC for the fiscal year ending December 31, 2020. The ASU permits the use of either of two methods: a full retrospective or a retrospective with the cumulative effect and additional disclosures. Management has not yet selected a transition method, as the NAIC is currently evaluating the impact of the new standard on its sources of support and financial statements, and is reviewing its revenue recognition policies and processes for any necessary amendments.

In February 2016, the FASB issued ASU No. 2016-02, *Leases (Topic 842).* The guidance in this ASU supersedes the leasing guidance in ASC Topic 840, Leases*.* Under the new guidance, lessees are required to recognize lease assets and lease liabilities on the balance sheet for all leases with terms longer than 12 months. Leases will be classified as either finance or operating, with classification affecting the pattern of expense recognition in the income statement. The new standard is effective for fiscal year 2020. A modified retrospective transition approach is required for lessees for capital and operating leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements, with certain practical expedients available. The NAIC is currently evaluating the impact of the pending adoption of the new standard on the financial statements.

Note 1. Nature of Operations and Summary of Significant Accounting Policies (Continued)

In August 2016, the FASB issued ASU No. 2016-14, *Not-for-Profit Entities (Topic 958): Presentation of Financial Statements of Not-for-Profit Entities*. The new standard changes presentation and disclosure requirements with the intention of helping nonprofits provide more relevant information about their resources to donors, grantors, creditors and other financial statement users. This pronouncement decreases the number of net assets classes from three to two. The new classes will be “net assets with donor restrictions” and “net assets without donor restrictions.” The standard will take effect for annual financial statements issued for fiscal years beginning after December 15, 2017, and for interim periods within fiscal years beginning after December 15, 2018. Therefore, this ASU will be effective for the NAIC’s fiscal year ending December 31, 2019. Management is in the process of evaluating the impact of this new guidance.

Note 2. Investments and Investment Income

	2016		2015	
	Cost	**Fair Value**	Cost	Fair Value
Government bonds	**$ 5,611,657**	**$ 5,529,053**	$ 5,234,975	$ 5,169,717
Corporate bonds	**6,671,274**	**6,581,898**	8,328,714	8,173,239
Fixed income mutual funds	**23,875,945**	**23,391,204**	19,531,597	19,153,221
Foreign fixed income funds	**5,521,204**	**4,878,069**	6,283,519	5,336,888
Domestic equity mutual funds	**9,473,793**	**9,786,234**	-	-
Common stock:				
Industrials	**1,361,256**	**2,377,115**	2,032,537	2,881,104
Consumer discretionary	**1,868,403**	**2,868,749**	2,407,056	4,365,657
Financials	**2,066,830**	**3,354,443**	2,108,316	2,715,243
Information technology	**3,401,153**	**5,845,457**	5,757,677	8,763,857
Other industries	**15,010,887**	**19,455,443**	18,918,559	23,629,892
Foreign common stock	**142,238**	**669,180**	611,113	1,224,705
American depository receipts	**-**	**-**	99,335	402,901
Foreign equity mutual funds	**6,460,263**	**7,326,880**	6,043,980	6,706,731
Master limited partnerships	**3,579,069**	**2,609,611**	4,531,283	2,976,310
Alternative equity funds	**6,065,000**	**6,932,981**	6,065,000	7,129,883
	$ 91,108,972	**$ 101,606,317**	$ 87,953,662	$ 98,629,348

Total investment income (loss) comprises the following:

	2016	2015
Interest and dividend income	**$ 2,959,313**	$ 2,956,460
Net realized gains	**4,447,938**	2,966,551
Net unrealized losses	**(178,342)**	(8,323,651)
	$ 7,228,909	$ (2,400,640)

Note 2. Investments and Investment Income (Continued)

The following table summarizes the valuation of financial instruments measured at fair value on a recurring basis, segregated by the general classification of such instruments pursuant to the valuation hierarchy:

	December 31, 2016			
	Total Fair Value	Level 1	Level 2	Level 3
Government bonds	$ 5,529,053	$ -	$ 5,529,053	$ -
Corporate bonds	6,581,898	-	6,581,898	-
Fixed income mutual funds	23,391,204	23,391,204	-	-
Foreign fixed income funds	4,878,069	4,878,069	-	-
Domestic equity mutual funds	9,786,234	9,786,234	-	-
Common stock:				
Industrials	2,377,115	2,377,115	-	-
Consumer discretionary	2,868,749	2,868,749	-	-
Financials	3,354,443	3,354,443	-	-
Information technology	5,845,457	5,845,457	-	-
Other industries	19,455,443	19,455,443	-	-
Foreign common stock	669,180	669,180	-	-
Foreign equity mutual funds	7,326,880	7,326,880	-	-
Master limited partnerships	2,609,611	2,609,611	-	-
	94,673,336	$ 82,562,385	$ 12,110,951	$ -
Investments measured at net asset value:				
Alternative equity hedge funds	6,932,981			
Total investments	$ 101,606,317			

Note 2. Investments and Investment Income (Continued)

	December 31, 2015			
	Total Fair Value	Level 1	Level 2	Level 3
Government bonds	$ 5,169,717	$ -	$ 5,169,717	$ -
Corporate bonds	8,173,239	-	8,173,239	-
Fixed income mutual funds	19,153,221	19,153,221	-	-
Foreign fixed income funds	5,336,888	5,336,888	-	-
Common stock				
Industrials	2,881,104	2,881,104	-	-
Consumer discretionary	4,365,657	4,365,657	-	-
Financials	2,715,243	2,715,243	-	-
Information technology	8,763,857	8,763,857	-	-
Other industries	23,629,892	23,629,892	-	-
Foreign common stock	1,224,705	1,224,705	-	-
American depository receipts	402,901	402,901	-	-
Foreign equity mutual funds	6,706,731	6,706,731	-	-
Master limited partnerships	2,976,310	2,976,310	-	-
	91,499,465	$ 78,156,509	$ 13,342,956	$ -
Investments measured at net asset value:				
Alternative equity hedge funds	7,129,883			
Total investments	$ 98,629,348			

	Alternative Equity Funds	
	2016	2015
Total gains (losses), net, included in earnings attributable to the change in unrealized gains (losses), net, relating to financial instruments still held	**$ (196,902)**	$ 116,442

The following table sets forth additional disclosure of the NAIC's investments whose fair value is estimated using NAV per share (or its equivalent) as of December 31, 2016 and 2015:

	Fair Value			
Investment	**December 31, 2016**	December 31, 2015	Unfunded Commitment	Redemption Frequency
Alternative equity funds (A)	**$ 6,932,981**	$ 7,129,883	$ -	Quarterly

(A) This fund aims to generate consistent absolute returns by investing in assets with a diversified group of investment managers through managed account structures (Managed Account Structures) or in the private investment funds sponsored by investment managers (collectively, Hedge Fund Managers or Hedge Funds).

Note 3. Property and Equipment

Property and equipment at December 31 consisted of the following:

	2016	2015
Furniture and equipment	**$ 5,410,732**	$ 5,971,484
Computer and related equipment	**11,289,661**	15,382,275
Computer software	**35,237,705**	32,254,237
Leasehold improvements	**18,293,345**	17,781,277
	70,231,443	71,389,273
Less accumulated depreciation and amortization	**43,237,741**	43,797,723
	$ 26,993,702	$ 27,591,550

Note 4. Operating Leases

The NAIC leases its office space in Kansas City, New York, and Washington, D.C. under noncancellable operating leases. Certain parts of the agreements contain escalation clauses providing increased rentals based on maintenance, utility and tax increases. The NAIC also leases certain office equipment under noncancellable operating leases, which expire at various dates through 2016. The accompanying financial statements reflect rent expense on the straight-line method over the terms of the leases. Total rental expenses under all leases for the years ended December 31, 2016 and 2015, were $2,723,047 and $2,503,132, respectively.

The Kansas City office space lease includes various lease incentives, free rent and scheduled rent increases. The lessor agreed to pay the NAIC base rental differential payments totaling $2,390,571 plus 6 percent interest over the course of the initial lease term. Annual payments of $285,140 are being made to the NAIC through fiscal year 2022. The outstanding noncurrent principal balance of this receivable is reported as an incentive receivable on the statements of financial position and had a balance of $1,201,114 and $1,402,127 as of December 31, 2016 and 2015, respectively. This outstanding receivable is being recognized in the statements of activities on a straight-line basis over the life of the lease and is included in the deferred lease incentive described below.

Deferred lease incentives consist primarily of reimbursements for leasehold improvements, parking costs and moving costs. U.S. GAAP requires that the above items be recognized as a reduction of rental expense over the term of the lease. The unamortized balance in deferred lease incentive was $10,020,665 and $11,373,018 as of December 31, 2016 and 2015, respectively.

Future minimum lease payments at December 31, 2016, are as follows:

Years ending December 31:	
2017	$ 3,711,196
2018	3,730,102
2019	3,750,093
2020	3,769,956
2021	3,780,816
Thereafter	10,222,873
Total future minimum lease payments	$ 28,965,036

Note 5. Employee Retirement Plans

The NAIC has a noncontributory defined benefit plan covering all employees with a hire date prior to January 1, 2000. As of December 31, 2012, accrued benefits for all active participants were frozen. The benefits are based on years of service and the employee's compensation prior to January 1, 2013.

The following table sets forth the plan's funding status, amount recognized in the NAIC's financial statements, and other required disclosures:

	2016	2015
Projected benefit obligation	**$ (48,846,489)**	$ (46,176,278)
Fair value of plan assets	**43,202,452**	41,042,215
Funded status of plan	**$ (5,644,037)**	$ (5,134,063)
Accrued benefit cost recognized in the statements of financial position	**$ (5,644,037)**	$ (5,134,063)
Accumulated benefit obligation	**$ 48,846,489**	$ 46,176,278
Employer contributions	**$ -**	$ -
Plan settlements	**$ -**	$ -
Benefits paid	**$ (1,624,458)**	$ (2,089,846)
Interest cost	**$ 1,863,934**	$ 1,729,456
Return on plan assets	**(2,420,076)**	(2,716,600)
Amortization of net loss	**991,049**	730,952
Net pension (benefit) cost	**$ 434,907**	$ (256,192)

Weighted average assumptions used to determine benefit obligations are as follows:

	2016	2015
Discount rate	**3.95%**	4.25%
Salary rate	**N/A**	N/A
Measurement date	**December 31, 2016**	December 31, 2015

Weighted average assumptions used to determine net pension costs are as follows:

	2016	2015
Discount rate	**4.25%**	3.80%
Salary rate	**N/A**	N/A
Expected return on plan assets	**6.25%**	6.50%
Measurement date	**December 31, 2016**	December 31, 2015

Note 5. Employee Retirement Plans (Continued)

The expected rate of return on plan assets is determined by those assets' historical long-term investment performance, current asset allocation and estimates of future long-term returns by asset class.

The following is the plan's weighted average asset allocation by asset category as of December 31, 2016 and 2015 (the measurement date of the plan assets):

	2016	2015
Equity securities	**51.90%**	48.46%
Debt securities	**48.10%**	51.54%

Plan assets are held by an insurance company, which invests the plan assets in accordance with the provisions of the plan agreement. The plan agreement permits investment in common stocks, corporate bonds, U.S. government securities and other specified investments, based on certain target allocation percentages. Asset allocation is primarily based on a strategy to provide stable earnings while still permitting the plan to recognize potentially higher returns through a limited investment in equity securities. Plan assets are rebalanced as necessary based upon the minimum and maximum restrictions set forth in the plan's investment policy statement. Plan assets are valued using Level 1 inputs and are based on unadjusted quoted market prices within active markets.

The benefits expected to be paid to participants over the next 10 years, as of December 31, 2016, are as follows:

Years ending December 31:	
2017	$ 3,273,902
2018	3,690,213
2019	4,054,101
2020	4,182,903
2021	3,937,732
2022-2026	17,209,974
Total	$ 36,348,825

The annual amount is actuarially calculated by the NAIC's independent consultant firm and represents the amount necessary to fully fund the actuarial accrued liability and normal cost of the plan.

The NAIC provides a defined contribution 401(a) plan (Plan B) that covers substantially all employees with one year or more of service. Each year, the Executive Committee and (EX1) Internal Administration Subcommittee determine the contribution for the next year. The NAIC matched up to 5.5 and 4.5 percent of compensation of employees who contributed to Plan B and contributed 3.0 percent of all employees' compensation in 2016 and 2015, respectively. The pension expense related to Plan B for the years ended December 31, 2016 and 2015, was $3,066,114 and $2,567,998, respectively.

Note 6. Related-Party Transactions

The NAIC and the National Insurance Producer Registry (the NIPR) executed a Licenses and Services Agreement (the Agreement) effective January 1, 2012, for an initial term of five years. The agreement will automatically renew each year thereafter unless either party provides written notice of termination to the other party no later than 180 days prior to the end of the renewal period. The terms of the agreement provide for (1) a 38 percent license fee for the NIPR to use the NAIC's producer data; (2) the reimbursement of the actual cost of services, facilities and equipment provided by the NAIC to the NIPR; and (3) the reimbursement of system usage fees related to ongoing infrastructure costs for the NIPR.

The total amount of revenue recognized during the year and amount owed at year-end from the NIPR are as follows:

	2016	2015
Administrative services provided by the NAIC	**$ 1,242,779**	$ 1,164,013
License fee	**$ 12,733,249**	$ 11,503,594
System usage fee	**$ 222,918**	$ 191,400
Amounts payable to the NAIC	**$ 1,379,931**	$ 1,237,197

Effective June 2007, the NAIC entered into a service agreement with the Interstate Insurance Product Regulation Commission (the IIPRC), whereby the NAIC provides certain administrative services to the IIPRC. The NAIC received an administrative fee of $125,000 for both of the years ended December 31, 2016 and 2015. The IIPRC also pays an annual license and maintenance fee in the amount of $25,000 for the use of the NAIC's System for Electronic Rate and Form Filing. The NAIC also has an operating note receivable due from the IIPRC. Repayment of principal and interest is deferred until certain operating performance measures are met by the IIPRC. Additionally, certain expenses are paid on behalf of, and reimbursed by, the IIPRC.

The total amount of revenue recognized during the year and amounts owed at year-end from the IIPRC are as follows:

	2016	2015
Administrative services provided by the NAIC	**$ 125,000**	$ 125,000
License fee paid to the NAIC	**$ 25,000**	$ 25,000
Amounts payable to the NAIC	**$ 40,032**	$ 25,808
Note payable to the NAIC	**$ 3,227,696**	$ 3,155,950

An additional line of credit in the amount of at least $100,000 to be used by the IIPRC in fiscal year 2017 will be considered by the NAIC at the NAIC 2017 Spring National Meeting.

Note 7. Contingencies

The NAIC is, from time to time, subject to claims and lawsuits arising in the ordinary course of business. Although the ultimate disposition of such proceedings is not presently determinable, management does not currently believe the ultimate resolution of these matters will have a material adverse effect on the financial condition, results of operations or cash flows of the NAIC.

Note 8. Subsequent Events

Management has performed an evaluation of events that have occurred subsequent to December 31, 2016, through February 16, 2017, which is the date the financial statements were available to be issued. No significant matters were identified for disclosure during this evaluation.