

CREDIT FOR REINSURANCE MODEL LAW

Preface to Credit for Reinsurance Models

~~The amendments to the NAIC Credit for Reinsurance Model Law (#785) & Regulation (#786) are part of a larger effort to modernize reinsurance regulation in the United States. The NAIC initially adopted the Reinsurance Regulatory Modernization Framework Proposal during its 2008 Winter National Meeting. The NAIC recommended that this framework be implemented through federal legislation in order to best preserve and improve state based regulation of reinsurance, ensure timely and uniform implementation throughout all NAIC member jurisdictions, and as a more comprehensive alternative to related federal legislation. In addition to this proposed federal legislation, the framework also provided that changes to state insurance laws should be considered. For example, state laws to establish requirements under which states would regulate qualified reinsurers, and also to consider reinsurance risk diversification and notice requirements for ceding insurers.~~

~~On July 21, 2010, Congress passed and the President signed related federal legislation, the Nonadmitted and Reinsurance Reform Act, which became effective July 21, 2011. While this act does not implement the NAIC framework, it does preempt the extraterritorial application of state credit for reinsurance law and permits states of domicile to proceed forward with reinsurance collateral reforms on an individual basis if they are accredited. This federal legislation also does not prohibit the states from acting together, through the NAIC, to achieve the reinsurance modernization framework goals. In addition to the current work on the credit for reinsurance models, the NAIC will continue its efforts to implement other aspects of the framework. These efforts will continue both through work conducted by the Reinsurance Task Force and through referrals to the appropriate groups within the NAIC. In addition, the NAIC will consider a proposal to form a new group to provide advisory support and assistance to states in the review of reinsurance collateral reduction applications. Such a process with respect to the review of applications for reinsurance collateral reduction and qualified jurisdictions should strengthen state regulation and prevent regulatory arbitrage. Such an effort would be supported by NAIC staff with substantial expertise to support the functions of such a group.~~

~~Finally, the NAIC will continue to work on requirements for NAIC review and approval of qualified jurisdictions, and will undertake a re-examination of the collateral amounts within two years from the effective date of the revisions to the models.~~

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Section 2. Credit Allowed a Domestic Ceding Insurer

Credit for reinsurance shall be allowed a domestic ceding insurer as either an asset or a reduction from liability on account of reinsurance ceded only when the reinsurer meets the requirements of Subsections A, B, C, D, E, ~~or F~~ or G of this section; provided further, that the commissioner may adopt by regulation pursuant to Section 5B specific additional requirements relating to or setting forth: (1) the valuation of assets or reserve credits; (2) the amount and forms of security supporting reinsurance arrangements described in Section 5B; and/or (3) the circumstances pursuant to which credit will be reduced or eliminated.

Drafting Note: This new regulatory authority is being added in response to reinsurance arrangements entered into, directly or indirectly, with life/health insurer-affiliated captives, special purpose vehicles or similar entities that may not have the same statutory accounting requirements or solvency requirements as US-based multi-state life/health insurers. To assist in achieving national uniformity, commissioners are asked to strongly consider adopting regulations that are substantially similar in all material respects to NAIC adopted model regulations in the handling and treatment of such reinsurance arrangements.

Credit shall be allowed under Subsections A, B or C of this section only as respects cessions of those kinds or classes of business which the assuming insurer is licensed or otherwise permitted to write or assume in its state of domicile or, in the case of a U.S. branch of an alien assuming insurer, in the state through which it is entered and licensed to transact insurance or reinsurance. Credit shall be allowed under Subsections C or D of this section only if the applicable requirements of Subsection ~~GH~~ have been satisfied.

F. (1) Credit shall be allowed when the reinsurance is ceded to an assuming insurer meeting each of the conditions set forth below.

(a) The assuming insurer must have its head office or be domiciled in, as applicable, and be licensed in a Reciprocal Jurisdiction. A “Reciprocal Jurisdiction” is a jurisdiction that meets one of the following:

(i) A non-U.S. jurisdiction that has entered into a covered agreement with the United States, each within its legal authority, or, in the case of a covered agreement between the United States and European Union, is a member state of the European Union, and is in compliance with all material terms of the covered agreement, including the reciprocal treatment of United States insurers and reinsurers. For purposes of this subsection, a “covered agreement” is an agreement entered into pursuant to Dodd-Frank Wall Street Reform and Consumer Protection Act, 31 U.S.C. §§ 313 and 314, that is currently in effect or in a period of provisional application and addresses the elimination, under specified conditions, of collateral requirements as a condition for entering into any reinsurance agreement with a ceding insurer domiciled in this state or for allowing the ceding insurer to recognize credit for reinsurance;

(ii) A U.S. jurisdiction that meets the requirements for accreditation under the NAIC financial standards and accreditation program; or

(iii) A qualified jurisdiction, as determined by the commissioner pursuant to [Subsection 2E(3) of Credit for Reinsurance Model Law], which is not otherwise described in subparagraph (i) or (ii) above and which meets certain additional requirements as specified by the commissioner in regulation.

(b) The assuming insurer must have and maintain on an ongoing basis minimum capital and surplus, or its equivalent, calculated according to the methodology of its domiciliary jurisdiction, in an amount to be set forth in regulation. If the assuming insurer is an association, including incorporated and individual unincorporated underwriters, it must have and maintain on an ongoing basis minimum capital and surplus equivalents (net of liabilities), calculated according to the methodology applicable in its domiciliary jurisdiction, and a central fund containing a balance in amounts to be set forth in regulation.

(c) The assuming insurer must have and maintain on an ongoing basis a minimum solvency or capital ratio, as applicable, which will be set forth in regulation. If the

assuming insurer is an association, including incorporated and individual unincorporated underwriters, it must have and maintain on an ongoing basis a minimum solvency or capital ratio in the Reciprocal Jurisdiction where the assuming insurer has its head office or is domiciled, as applicable, and is also licensed.

(d) The assuming insurer must agree and provide adequate assurance to the commissioner, in a form specified by the commissioner pursuant to regulation, as follows:

(i) The assuming insurer must provide prompt written notice and explanation to the commissioner if it falls below the minimum requirements set forth in subparagraphs (b) or (c), or if any regulatory action is taken against it for serious noncompliance with applicable law;

(ii) The assuming insurer must consent in writing to the jurisdiction of the courts of this state and to the appointment of the commissioner as agent for service of process. The commissioner may require that consent for service of process be provided to the commissioner and included in each reinsurance agreement. Nothing in this provision shall limit or in any way alter the capacity of parties to a reinsurance agreement to agree to alternative dispute resolution mechanisms, except to the extent such agreements are unenforceable under applicable insolvency or delinquency laws;

(iii) The assuming insurer must consent in writing to pay all final judgments, wherever enforcement is sought, obtained by a ceding insurer or its legal successor, that have been declared enforceable in the jurisdiction where the judgment was obtained;

(iv) Each reinsurance agreement must include a provision requiring the assuming insurer to provide security in an amount equal to one hundred percent (100%) of the assuming insurer's liabilities attributable to reinsurance ceded pursuant to that agreement if the assuming insurer resists enforcement of a final judgment that is enforceable under the law of the jurisdiction in which it was obtained or a properly enforceable arbitration award, whether obtained by the ceding insurer or by its legal successor on behalf of its resolution estate; and

(v) The assuming insurer must confirm that it is not presently participating in any solvent scheme of arrangement which involves this state's ceding insurers, and agrees to notify the ceding insurer and the commissioner and to provide security in an amount equal to one hundred percent (100%) of the assuming insurer's liabilities to the ceding insurer should the assuming insurer enter into such a solvent scheme of arrangement. Such security shall be in a form consistent with the provisions of Section 2E and Section 3 and as specified by the commissioner in regulation.

Drafting Note: Section 9C(4)(e) of the *Credit for Reinsurance Model Regulation (#786)* sets forth the acceptable forms of security under this subparagraph by specifically referencing Sections 12, 13 and 14 of Model #786.

(e) The assuming insurer or its legal successor must provide, if requested by the commissioner, on behalf of itself and any legal predecessors, certain documentation to the commissioner as specified by the commissioner in regulation.

- (f) The assuming insurer must maintain a practice of prompt payment of claims under reinsurance agreements, pursuant to criteria set forth in regulation.
 - (g) The assuming insurer’s supervisory authority must confirm to the commissioner on an annual basis, as of the preceding December 31 or at the annual date otherwise statutorily reported to the Reciprocal Jurisdiction, that the assuming insurer complies with the requirements set forth in subparagraphs (b) and (c).
 - (h) The assuming insurer must satisfy any other requirements deemed relevant by the commissioner, except to the extent they conflict with an applicable covered agreement. Nothing in this provision precludes an assuming insurer from providing the commissioner with information on a voluntary basis.
- (2) The commissioner shall timely create and publish a list of Reciprocal Jurisdictions.
- (a) A list of Reciprocal Jurisdictions is published through the NAIC Committee Process. The commissioner’s list shall include any Reciprocal Jurisdiction as defined under Section 2F(1)(a)(i) and (ii), and shall consider any other Reciprocal Jurisdiction included on the NAIC list. The commissioner may approve a jurisdiction that does not appear on the NAIC list of Reciprocal Jurisdictions in accordance with criteria to be developed under regulations issued by the commissioner.
 - (b) The commissioner may remove a jurisdiction from the list of Reciprocal Jurisdictions upon a determination that the jurisdiction no longer meets the requirements of a Reciprocal Jurisdiction in accordance with a process set forth in regulations issued by the commissioner, except that the commissioner shall not remove from the list a Reciprocal Jurisdiction as defined under Section 2F(1)(a)(i) and (ii). Upon removal of a Reciprocal Jurisdiction from this list credit for reinsurance ceded to an assuming insurer which has its home office or is domiciled in that jurisdiction shall be allowed, if otherwise allowed pursuant to [cite to state law equivalent to Credit for Reinsurance Model Law].
- (3) The commissioner shall timely create and publish a list of assuming insurers that have satisfied the conditions set forth in this subsection and to which cessions shall be granted credit in accordance with this subsection. The commissioner may add an assuming insurer to such list if an NAIC accredited jurisdiction has added such assuming insurer to a list of such assuming insurers or if, upon initial eligibility, the assuming insurer submits the information to the commissioner as required under Paragraph (1)(d) of this subsection and complies with any additional requirements that the commissioner may impose by regulation, except to the extent that they conflict with an applicable covered agreement.
- (4) If the commissioner determines that an assuming insurer no longer meets one or more of the requirements under this subsection, the commissioner may revoke or suspend the eligibility of the assuming insurer for recognition under this subsection in accordance with procedures set forth in regulation.
- (a) While an assuming insurer’s eligibility is suspended, no reinsurance agreement issued, amended or renewed after the effective date of the suspension qualifies for credit except to the extent that the assuming insurer’s obligations under the contract are secured in accordance with Section 3.
 - (b) If an assuming insurer’s eligibility is revoked, no credit for reinsurance may be granted after the effective date of the revocation with respect to any reinsurance agreements entered into by the assuming insurer, including reinsurance agreements entered into prior to the date of revocation, except to the extent that

the assuming insurer's obligations under the contract are secured in a form acceptable to the commissioner and consistent with the provisions of Section 3.

- (5) If subject to a legal process of rehabilitation, liquidation or conservation, as applicable, the ceding insurer, or its representative, may seek and, if determined appropriate by the court in which the proceedings are pending, may obtain an order requiring that the assuming insurer post security for all outstanding liabilities.
- (6) Nothing in this subsection shall limit or in any way alter the capacity of parties to a reinsurance agreement to agree on requirements for security or other terms in that reinsurance agreement consistent herewith.
- (7) Credit may be taken under this subsection only for reinsurance agreements entered into, amended, or renewed on or after the date on which the assuming insurer has satisfied the requirements to assume reinsurance under this subsection, and only with respect to losses incurred and reserves reported on or after the later of (i) the date on which the assuming insurer has met all eligibility requirements pursuant to Section 2F(1) herein, or (ii) the effective date of the new reinsurance agreement, amendment, or renewal.
 - (a) This paragraph does not alter or impair a ceding insurer's right to take credit for reinsurance, to the extent that credit is not available under this subsection, as long as the reinsurance qualifies for credit under any other applicable provision of [cite to state law equivalent to Credit for Reinsurance Model Law].
 - (b) Nothing in this subsection shall authorize an assuming insurer to withdraw or reduce the security provided under any reinsurance agreement except as permitted by the terms of the agreement.
 - (c) Nothing in this subsection shall limit or in any way alter the capacity of parties to any reinsurance agreement to renegotiate the agreement.

Section 5. Rules and Regulations

- A. The commissioner may adopt rules and regulations implementing the provisions of this law.

Drafting Note: It is recognized that credit for reinsurance also can be affected by other sections of the enacting state's code, e.g., a statutory insolvency clause or an intermediary clause. It is recommended that states that do not have a statutory insolvency clause or an intermediary clause consider incorporating such clauses in their legislation.

- B. The commissioner is further authorized to adopt rules and regulations applicable to reinsurance arrangements described in Paragraph (1) of this Section 5B.

Drafting Note: This new regulatory authority is being added in response to reinsurance arrangements entered into, directly or indirectly, with life/health insurer-affiliated captives, special purpose vehicles or similar entities that may not have the same statutory accounting requirements or solvency requirements as US-based multi-state life/health insurers. To assist in achieving national uniformity, commissioners are asked to strongly consider adopting regulations that are substantially similar in all material respects to NAIC adopted model regulations in the handling and treatment of such policies and reinsurance arrangements.

- (1) A regulation adopted pursuant to this Section 5B, may apply only to reinsurance relating to:
 - (a) Life insurance policies with guaranteed nonlevel gross premiums or guaranteed nonlevel benefits;
 - (b) Universal life insurance policies with provisions resulting in the ability of a policyholder to keep a policy in force over a secondary guarantee period;

- (c) Variable annuities with guaranteed death or living benefits;
 - (d) Long-term care insurance policies; or
 - (e) Such other life and health insurance and annuity products as to which the NAIC adopts model regulatory requirements with respect to credit for reinsurance.
- (2) A regulation adopted pursuant to Paragraph 1(a) or 1(b) of this Section 5B, may apply to any treaty containing (i) policies issued on or after January 1, 2015, and/or (ii) policies issued prior to January 1, 2015, if risk pertaining to such pre-2015 policies is ceded in connection with the treaty, in whole or in part, on or after January 1, 2015.

Drafting Note: The NAIC's Actuarial Guideline XLVIII (AG 48) became effective January 1, 2015, and covers policies ceded on or after this date unless they were ceded as part of a reserve financing arrangement as of December 31, 2014. One regulation contemplated by this revision to the NAIC Credit for Reinsurance Model Law is intended to substantially replicate the requirements for the amounts and forms of security held under the rules provided in AG 48. AG 48 was written to sunset upon a state's adoption (pursuant to the enabling authority of the preceding paragraph) of a regulation with terms substantially similar to AG 48. The preceding paragraph is intended to provide continuity of rules applicable to those policies and reinsurance arrangements, including continuity as to the policies covered by such rules. The preceding paragraph is not intended to change the scope of, or collateral requirements for policies and treaties covered under AG 48.

- (3) A regulation adopted pursuant to this Section 5B may require the ceding insurer, in calculating the amounts or forms of security required to be held under regulations promulgated under this authority, to use the Valuation Manual adopted by the NAIC under Section 11B(1) of the NAIC Standard Valuation Law, including all amendments adopted by the NAIC and in effect on the date as of which the calculation is made, to the extent applicable.
- (4) A regulation adopted pursuant to this Section 5B shall not apply to cessions to an assuming insurer that:
- (a) Meets the conditions set forth in Section 2F of the Credit for Reinsurance Model Law in this state or, if this state has not adopted provisions substantially equivalent to Section 2F of the Credit for Reinsurance Model Law, the assuming insurer is operating in accordance with provisions substantially equivalent to Section 2F of the Credit for Reinsurance Model Law in a minimum of five (5) other states; or
 - ~~(a)~~(b) Is certified in this state or, if this state has not adopted provisions substantially equivalent to Section 2E of the Credit for Reinsurance Model Law, certified in a minimum of five (5) other states; or
 - ~~(b)~~(c) Maintains at least \$250 million in capital and surplus when determined in accordance with the NAIC *Accounting Practices and Procedures Manual*, including all amendments thereto adopted by the NAIC, excluding the impact of any permitted or prescribed practices; and is
 - (i) licensed in at least 26 states; or
 - (ii) licensed in at least 10 states, and licensed or accredited in a total of at least 35 states.
- (5) The authority to adopt regulations pursuant to this Section 5B does not limit the commissioner's general authority to adopt regulations pursuant to Section 5A of this law.