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To: Richard Smith, President
Vermont Captive Insurance Association

From: Jim McIntyre

Date: April 17, 2013

Re: Report on the NAIC Spring National Meeting, April 6-9, 2013,
Houston, Texas

The National Association of Insurance Commissioners (NAIC) held its spring 2013 meeting in Houston, Texas, April 6-9, 2013. The following actions were taken on items of interest to VCIA:

Risk Retention Groups. The Risk Retention (C) Working Group adopted the Risk Retention and Purchasing Group Handbook. Prior to adopting the handbook, there was a significant amount of discussion regarding language in Section II A.3. Notice and Registration Forms. The issue in this section was language that would permit a nondomiciliary state to ask for "other reasonable information necessary to verify that the entities qualified as RRGs or PGs. . . ." The issue was whether the nondomiciliary state can investigate whether an RRG or PG is "qualified" once it had been approved by the domiciliary state. After a lot of discussion, the working group decided to leave the language as proposed. The working group did accept an amendment that I proposed--to clarify that the information being required by a nondomiciliary state must be consistent with the LRRA. The recommendation of the working group to adopt the revised Risk Retention Group and Purchasing Group Handbook was approved by the Property and Casualty Insurance (C) Committee and subsequently by the entire NAIC.

The Risk Retention Group (E) Task Force discussed an issue raised by the Annual Financial Reporting Model Regulation (#205) regarding reconciliation from GAAP to SAP accounting in annual audited financial reports. It was noted that complying with this requirement is very expensive and imposes a hardship on RRGs because two sets of financial statements must be prepared. After discussing this issue, the task force agreed to recommend to the Financial Regulation Standards and Accreditation (F) Committee that it remove the requirement in the Part A standards for captive risk retention groups that the reconciliation of surplus from other bases of accounting (e.g., generally accepted accounting principles) to statutory accounting principles be an audited component of the audited financial report. I understand that the result would be that they would keep reconciliation in the yellow book, but reconciliation would not be required to be in the audited financial statements. This recommendation was approved by the Financial Condition (E) Committee.

The task force discussed the draft captive/SPV white paper. Jill Jacobi (CA) stated that based upon the task force's charge to monitor activities of other NAIC committees with respect to effects on RRGs, it was important that the task force review this white paper. She also stated that certain recommendations could have an impact on RRGS; for example, those of monitoring the activities of the IAIS. David Provost (Vermont) stated that he did not see much correlation to RRGs.

The recommendation to adopt the corporate governance provisions of the Risk Retention Group Model Act for accreditation purposes has been exposed for one year, the comment date ending on December 31, 2013. Assuming that the corporate governance standards will become an accreditation requirement, they would be effective January 1, 2017. This is a substantially similar requirement, which means that the standards do not have to be adopted verbatim, as long as the provisions are substantially similar to those in the model act.

The business transacted with the Producer-Controlled Property/Casualty Insurer Act (#235) was exposed by the (F) Committee for a 30-day comment period on whether it should become an accreditation requirement. This amended model would delete the exemption for risk retention groups. This act would apply to RRGs as an accreditation standard.

The risk-based capital accreditation requirements for risk retention groups will become effective January 1, 2014.

In another matter before the task force, it was suggested that the task force review changes to model acts and model regulations, such as the Holding Company Act, to determine if changes to the models are applicable to risk retention groups. It was also suggested that a small-company exemption for risk retention groups should be considered for the Holding Company Act. This issue will be discussed on a later conference call. At the (F) Committee meeting, NAMIC requested a small-company exemption from the Insurance Holding Company System Regulatory Act and model regulation. This request will be considered at the summer 2013 meeting.

Principle-Based Reserving.   The Principle-Based Reserving Implementation (EX) Task Force discussed a draft principle-based reserving (PBR) implementation plan and a draft PBR legislative packet designed to better align life insurance policy reserves to product risks. Both drafts were exposed for a 30-day comment period. These documents form the basis to implement the NAIC's decision to use principle-based reserving for life insurance companies. The PBR Implementation Plan specifically addresses the need to further assess the solvency implications of life insurer owned captive insurers and other alternative mechanisms in the context of PBR. The task force also discussed the captive and special purpose vehicle (SPV) white paper. Superintendent Torti (RI) noted that the white paper was being exposed for a comment period which ends on April 29. Principle-based reserving could reduce the need for insurers to create captive insurers to address "perceived" reserve redundancies. The task force will be working on this issue simultaneously with the Financial Condition (E) Committee.

In response to a question from Dave Provost, Superintendent Torti said that the SPV issue is linked to the PBR Task Force's efforts. The task force plans to address SPV issues identified in the Captive and Special Purpose Vehicle (SPV) Use (E) Subgroup's report in connection with PBR implementation. Doug Stolte (VA) said that he does not think PBR will eliminate use of SPV/captives. Superintendent Torti agreed.

Commissioner White (DC) reported on Federal Insurance Office activities with respect to several insurance issues. He stated that the FIO has expressed an interest in oversight of captives/SPVs and that Director McRaith has appointed a small committee to look at captive/SPV issues. He is concerned about the use of captives as risk transfer mechanisms as well as solvency of these companies. One of the questions being considered is how regulatory standards can be adopted that establish a benchmark to prevent a race to the bottom.

The issues being discussed in the Principle-Based Reserving (EX) Task Force raise significant issues for the captive community. Superintendent Torti can use this forum in addition to the (E) Committee which he chairs, to affect the use of captive insurers. This whole issue of principle-based reserving and solvency could spread beyond life insurer owned captives to captives generally. I note that Commissioner Donegan from Vermont is a member of the task force**.**

Reinsurance. The Reinsurance Task Force discussed the status of adoption of the revised Credit for Reinsurance Model Law and Model Regulation. Eleven states, representing 45 percent of the U.S. reinsurance premiums, have enacted the models. Legislation is pending in 12 more states, and if the legislation is adopted in those states, it would bring the amount of premiums covered to 75 percent. The NAIC at its plenary session adopted the revisions to the Credit for Reinsurance Model Law and Model Regulation for accreditation purposes.

The NIMA states met and decided to offer states a free membership for one year, with a goal of getting 20 states to join. NIMA is a voluntary association of states to collect and distribute among the states, where risks are located, surplus lines premium taxes.

Financial Stability. The Financial Stability (EX) Task Force was established to focus on issues of financial stability from a holistic point of view. While this task force is not focusing specifically on captive insurers, it should be monitored because of the potential to look at all insurers for financial solvency purposes. In a discussion about implementation of its charges, the chair, Thomas Leonardi from Connecticut, stated that there is a potential for a two-tier system of insurers.

TRIA. There was a meeting on insurance for acts of terrorism sponsored by the NAIC's Center for Insurance Policy and Research. A representative from the Congressional Research Service gave an overview of the current federal terrorism insurance program. Others expressed the need for hard data to convince Congress to extend the current program. A representative from Marsh & McLennan said that 2,600 companies had been surveyed for a report on terrorism insurance that will be released toward the end of April.

JTM:tm