

# MCINTYRE & LEMON, PLLC

ATTORNEYS AND COUNSELORS AT LAW

MADISON OFFICE BUILDING

1155 15<sup>TH</sup> STREET, N.W.

SUITE 1101

WASHINGTON, D.C. 20005

TELEPHONE (202) 659-3900

FAX (202) 659-5763

To: Richard Smith, President  
Vermont Captive Insurance Association (VCIA)

From: Jim McIntyre

Re: Report on the NAIC Spring 2014 National Meeting, March 29-April 1, 2014,  
Orlando, FL

Date: April 4, 2014

The National Association of Insurance Commissioners (NAIC) held its spring 2014 meeting in Orlando, Florida, March 29-April 1. Following are actions taken on items of interest to VCIA.

**Captive Insurance.** The Captive SPV issue continued to be a hot issue at the NAIC meeting. It was discussed at length at several meetings and mentioned in many more.

In the Financial Regulation Standards and Accreditation (F) Committee meeting, there was a discussion about the definition of “multistate reinsurer.” The issue is whether the definition of “multistate reinsurer” in the preambles to Part A and Part B accreditation standards includes reinsurers organized under captive laws and reinsuring business written in other states. Are they considered multistate insurers under the accreditation program and, therefore, subject to the laws and regulations covered by the accreditation program? There was a lot of hyperbole about the importance of this issue. For example, Director Huff from Missouri stated, “This is an important issue for state-based regulation. We will move forward on it because of the need for uniformity.” Superintendent Leonardi from Connecticut said, “The captive issue is one of the most important issues that we need to resolve as a regulatory body.” Superintendent Torti stated, “This is an extremely important issue. Solving this issue is critical to the survival of state-based regulation.” He stated that the NAIC decided years ago that reinsurers are multistate companies. Superintendent Lawsky agreed with Superintendent Torti’s comments and stated further, “The stakes on this are as high as any for the NAIC.”

Dan Schelp of NAIC’s legal staff reviewed the proposed definition of a multistate reinsurer (copy of which is attached). He said that the proposal has a broader effect than just reaching the XXX and A XXX arrangements. Reinsurance is a multistate insurance business. He stated that because of the state preemption provisions for reinsurers in the

Dodd-Frank Act, it is important that this issue be resolved. In the case of multistate reinsurers, all accreditation standards would be applicable. It is the committee's intent to bypass the three-year seasoning requirement for accreditation standards and adopt this definition as soon as possible.

The proposed definition of "multistate reinsurer" for accreditation purposes was exposed for a 45-day public comment period, with comments due by May 19.

In the Principle-Based Reserving Implementation (EX) Task Force meeting, there was a discussion about life insurer-owned captive insurers and the report from Rector and Associates. The Rector report addressed solvency implications of life insurer-owned captive insurers and alternative mechanisms. Nineteen comment letters were received from regulators and interested parties commenting on the Rector report. Concerns were expressed about adopting VM 20 as the actuarial method for establishing the "correct" amount of reserves. Other commenters stated the time line was too aggressive and that the report was vague in many of its recommendations.

Nine states have enacted laws adopting the Principle-Based Reserving Model, constituting 9.2 percent of the premium. Four additional states have passed laws which are waiting for their governors' signatures. At least 42 states need to adopt the model, representing 75 percent of premium, for principle-based reserving to become effective. Some commissioners believe that when principle-based reserving is effective, there will not be a need for these types of captive arrangements.

Several people spoke out in favor of putting a moratorium on the establishment of new life insurer-owned captives; those included Superintendent Lawsby from New York and a representative from USAA. The task force will be holding future teleconferences to continue to discuss the report.

The Financial Analysis (E) Working Group developed recommendations on how states should look at SPV transactions for solvency purposes. The working group presented its recommendations to the committee, which are designed to provide recommendations to the domiciliary state regulator to address companies' specific concerns and to the PBR Implementation (EX) Task Force to address issues and concerns regarding the solvency regulatory system.

The Mortgage Guaranty Insurance (E) Working Group is considering revisions to the Mortgage Guaranty Insurance Model Act (Number 630), which would prohibit the use of captives owned by insureds. In Section 8, the revised language states, "No mortgage guaranty insurance company shall enter into captive reinsurance arrangements which involve the direct or indirect ceding of any portion of its risks or obligations to a reinsurer owned or controlled by an insured; any subsidiary or affiliate of an insured . . . ; or any other entity in which an insured . . . has a financial interest . . ." The insurance companies apparently are not fighting this provision because of recent CFPB regulatory actions and fines with respect to such captive reinsurance arrangements.

**Risk Retention Groups.** The attention given to risk retention groups (RRGs) has diminished. There were three items considered at the meeting affecting RRGs, two of

which were considered in earlier deliberations about subjecting regulation of captive RRGs to the accreditation standards.

The Financial Regulation Standards and Accreditation (F) Committee over a year ago proposed that the corporate governance standards, which are part of the Model Risk Retention Act (Number 705), be required as a Part A accreditation requirement for risk retention groups. The comment period on the proposal ended on December 31, 2013, and the proposal to make the corporate governance standards an accreditation requirement will be considered at the 2014 summer national meeting in Louisville. If it is adopted, which I anticipate since there has been no objection to it, the corporate governance standards will be effective January 1, 2017. Only the domiciliary state of a captive RRG would be required to adopt the corporate governance standards.

Another issue before the (F) Committee affecting RRGs was a proposal to clarify the grandfather provisions applicable to reinsurance. The proposal clarifies that the reinsurance guidelines for risk retention groups apply to new reinsurers with which business is placed after January 1, 2011, as opposed to reinsurance contract renewals with grandfathered reinsurers. This item has been exposed for a 30-day comment period that ends May 2.

A question from the (F) Committee was referred to the Financial Condition (E) Committee, requesting guidance on whether and under what circumstances a captive manager would be considered to exert “control” over an RRG for the purposes of the Insurance Holding Company System Regulatory Act and the Model Regulation. Since many of the business functions of captives are outsourced to, and performed by, a captive manager, the question has arisen as to under what circumstances would captive managers be deemed to “control” RRGs for the purposes of the provisions in the Holding Company Act and regulation. This issue was referred to the RRG Task Force for consideration and recommendations back to the (E) Committee.

**Reinsurance.** Nineteen states have passed legislation to adopt the Credit for Reinsurance Model Law, representing more than 50 percent of the reinsurance premium. Nine more states plan to pass legislation later this year or in 2015. If the model is adopted in these additional states, over 80 percent of reinsurance premiums in the U.S. would be covered.

The NAIC has put a priority on states adopting the Credit for Reinsurance Model Law and to approve certified reinsurers for passporting purposes under the law.

**Terrorism Insurance.** The NAIC continues to urge members of Congress to extend the Federal Terrorism Risk Insurance Act (TRIA) before its expiration on December 31, 2014. There were several presentations to the Terrorism Insurance Implementation (C) Working Group regarding the impact of TRIA on the economy and on commercial insureds if the federal act were not reauthorized. NAIC supports the reauthorization of TRIA and has sent a letter to Senators Johnson and Crapo, urging their support for TRIA reauthorization and for prompt Congressional action.

JTM:tm  
Attachment