



THE GENERAL INSURANCE ASSOCIATION OF JAPAN

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February 6, 2018

Superintendent Maria T. Vullo
New York State Department of Financial Services
Chair, NAIC Reinsurance (E) Task Force
Via email to jstultz@naic.org

Re: NAIC request for comments on reinsurance collateral reform

Dear Superintendent Vullo,

The General Insurance Association of Japan (GIAJ)¹ appreciates the opportunity to comment as the NAIC initiates discussions on how to proceed with collateral elimination under the Covered Agreement.

The GIAJ believes that the NAIC's collateral reform should take due account of the following principles: consistency with existing rules, fair treatment among reinsurers, efficiency of supervision, and removal of duplicative regulations. We believe these principles support the objectives of the NAIC to promote competitive markets and policyholder protection.

Our specific comments on the “approaches to reinsurance collateral reform” build on these principles.

Request for Comments.

- *Amending the Credit for Reinsurance Model Law (#785) and the Credit for Reinsurance Model Regulation (#786) to eliminate reinsurance collateral requirements for EU-based reinsurers meeting the conditions of the Covered Agreement.*
- *Extending similar treatment to reinsurers from other jurisdictions covered by potential future covered agreement(s) that might be negotiated pursuant to the Dodd-Frank Wall Street Reform and Consumer Protection Act.*
- *Providing reinsurers domiciled in NAIC Qualified Jurisdictions with similar reinsurance collateral requirements*

Collateral elimination should be achieved by amending the existing Model Law/Regulation.

We support the NAIC’s moves to achieve collateral elimination by amending the existing Credit for Reinsurance Model Law (#785) and the Credit for Reinsurance Model Regulation (#786). As part of efforts to modernize reinsurance regulation, #785 and #786 were amended in 2011 to allow reinsurance collateral reduction for non-U.S. based reinsurers. Collateral elimination under the Covered Agreement and collateral reduction under

¹ GIAJ is an industry organization whose 26 member companies account for about 95 percent of the total general insurance premiums in Japan which is one of seven jurisdictions listed in the NAIC List of Qualified Jurisdictions. Some of our members or their affiliates are certified reinsurers.

#785 and #786 for Certified Reinsurers in Qualified Jurisdictions are technically similar in that reinsurance regulations of foreign jurisdictions are evaluated to allow credit for reinsurance. Therefore, it is consistent and efficient to achieve reinsurance collateral reform by amending #785 and #786.

EU-based reinsurers, reinsurers from other jurisdictions covered by potential future covered agreement(s) and reinsurers domiciled in NAIC Qualified Jurisdictions should be provided with consistent reinsurance collateral requirements.

Regarding the three approaches to the Model Law/Regulation amendment listed in the Notice, we support “Providing reinsurers domiciled in NAIC Qualified Jurisdictions with similar reinsurance collateral requirements”. We support neither the first approach, “Amending the Credit for Reinsurance Model Law (#785) and the Credit for Reinsurance Model Regulation (#786) to eliminate reinsurance collateral requirements for EU-based reinsurers meeting the conditions of the Covered Agreement”, nor the second approach, “Extending similar treatment to reinsurers from other jurisdictions covered by potential future covered agreement(s) that might be negotiated pursuant to the Dodd-Frank Wall Street Reform and Consumer Protection Act.”

With regard to the first and second approaches in which the effect of collateral elimination is limited to the EU and/or jurisdictions covered by potential future covered agreements, we fear that they could potentially be arbitrary and inconsistent with the existing framework. Theoretically, it is possible that a jurisdiction under the scope of a covered agreement could fail to be recognized as a Qualified Jurisdiction. If this proves to be the case, while reinsurers domiciled in such jurisdictions will still be preferentially treated and granted reinsurance collateral elimination, reinsurers domiciled in Qualified Jurisdictions without a covered agreement will only be granted collateral reduction. The NAIC should avoid such a situation as it goes against the principle of fair treatment for reinsurers.

Moreover, these approaches require #785 and #786 to incorporate additional categories such as “the European Union (EU)” or “jurisdictions under the scope of covered agreement(s)”. This makes the framework unnecessarily complex, and should be avoided.

In addition, according to the Dodd-Frank Act, a covered agreement could potentially deal with a wide range of issues related to prudential measures of insurance or reinsurance. Furthermore, it is far from certain how future covered agreements are to be negotiated with foreign government(s). The NAIC should avoid subjecting the Model Law/Regulation to such externalities and uncertainties.

Contrary to these two approaches, the NAIC can avoid the above-mentioned unfair treatment, regulatory complexities and uncertainties under the third approach, “Providing reinsurers domiciled in NAIC Qualified Jurisdictions with similar reinsurance collateral requirements”. The NAIC can leverage the current framework under #785 and #786 concerning Certified Reinsurers and Qualified Jurisdictions by revising the existing provisions on reinsurance collateral reduction (#785 Section 2E and #786 Section 8) to achieve reinsurance collateral elimination, and also apply them to Certified Reinsurers in every Qualified Jurisdiction regardless of EU membership status.

As for any EU jurisdiction not yet recognized as a Qualified Jurisdiction, a provision could be added, for example, to #785 Section 2E (3) and #786 Section 8C, to allow such jurisdictions to acquire Qualified Jurisdiction status. These revisions would secure efficiency and promote regulatory consistency between EU and non-EU Qualified Jurisdictions by making the best use of the NAIC's existing scheme.

Requirements on individual reinsurers should also be consistent between reinsurers domiciled in EU and non-EU Qualified Jurisdictions.

If the conditions for reinsurance collateral elimination stipulated in Article 3 Paragraph 4 of the Covered Agreement apply to EU reinsurers, the same conditions must apply to reinsurers domiciled in non-EU Qualified Jurisdictions. Otherwise, there exists the risk of arbitrage (i.e. reinsurers domiciled in jurisdictions which could fail to be recognized as a Qualified Jurisdiction enjoy an advantage over reinsurers domiciled in non-EU Qualified Jurisdictions).

We also suggest amending the existing requirements on Certified Reinsurers with regard to (i) minimum capital/surplus and (ii) financial strength ratings as follows, and applying them consistently to reinsurers domiciled in both EU and non-EU Qualified Jurisdictions:

- (i) Allowing the use of audited financial statements submitted to the home supervisor.
- (ii) Replacing the financial strength rating requirements with requirements to maintain on an ongoing basis the domestic (home jurisdiction's) SCR.

These revisions would help reduce the burden on state insurance regulators, the NAIC and relevant reinsurers, while maintaining the existing framework.

Request for Comments.

- *Considering changes to the criteria for evaluating whether a jurisdiction should be a Qualified Jurisdiction.*

Criteria for evaluating whether a jurisdiction should be a Qualified Jurisdiction need no change.

The existing “Process for Developing and Maintaining the NAIC List of Qualified Jurisdictions” is comprehensive and specific enough to provide the information necessary to evaluate reinsurance regulations of foreign jurisdictions, and to determine credit for reinsurance. For both the reinsurance collateral reduction currently allowed and collateral elimination under the Covered Agreement, reinsurance regulations of foreign jurisdictions are evaluated to allow credit for reinsurance. Therefore, it is unnecessary to make the criteria any stricter.

In particular, the re-evaluations that Qualified Jurisdictions are subject to every five years should be conducted in an efficient manner with a focus on material changes to the applicable reinsurance supervisory system that may affect the status of the Qualified Jurisdiction.

Request for Comments.

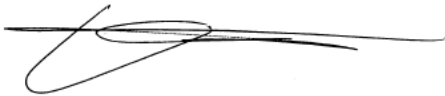
- *Considering additional “guardrails” relative to U.S. ceding companies, such as changes to the risk-based capital (RBC) formula or new regulatory approaches to help address the increased financial solvency risks caused by the elimination of reinsurance collateral.*

No need to consider additional “guardrails”.

We do not believe additional “guardrails” need to be considered. Ceded reinsurance credit risk is appropriately captured, and consistently examined through the NAIC Property/Casualty Risk-Based Capital (RBC). The reliability of the current RBC to provide sufficient guardrails is supported by the fact that no collateral or additional guardrails are required for licensed reinsurers or accredited reinsurers (#785 Section 2AB and Section 3). At the same time, both the Qualified Jurisdictions and the Covered Agreement frameworks evaluate and recognize reinsurance regulations of foreign jurisdictions. These layers of measures provide sufficient policyholder protection. Additional requirements go against facilitation of fair competition and appropriate risk diversification. The credit risk of assuming reinsurers and whether or not to require collateral should ultimately be determined by the individual ceding insurers.

Article 3 Paragraph 1 (b) of the Covered Agreement stipulates that, regarding any new requirements on reinsurers, Home (EU) and Host (US) Party Assuming Reinsurers should be treated equally. From the standpoint of consistency, #785 and #786 should also secure the same treatment of assuming reinsurers domiciled in EU and non-EU Qualified Jurisdictions. Such treatment would also be beneficial in avoiding any risk of arbitrage (i.e. reinsurers domiciled in jurisdictions which could fail to be recognized as a Qualified Jurisdiction enjoy an advantage over reinsurers domiciled in non-EU Qualified Jurisdictions).

Sincerely,

A handwritten signature in black ink, appearing to be 'Mamoru Otsubo', written over a horizontal line.

Mamoru Otsubo
General Manager,
International Policy Planning Department
The General Insurance Association of Japan