



REINSURANCE ASSOCIATION OF AMERICA

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September 21, 2007

Via E-mail

Commissioner John Oxendine
Chair, Reinsurance Task Force
Two Martin Luther King Jr. Drive
West Tower, Suite 704
Atlanta, GA 30334

RE: RSRD Proposal/Port of Entry Proposal

Commissioner Oxendine and Members of the Reinsurance Task Force:

The Reinsurance Association of America (RAA) is a national trade association representing property and casualty organizations that specialize in reinsurance. The RAA membership is diverse, including large and small, broker and direct, U.S. companies and subsidiaries of foreign companies. Together, RAA members write nearly 2/3 of the gross reinsurance coverage provided by U.S. property and casualty reinsurers and affiliates.

The RAA applauds the Reinsurance Task Force's effort to address Charge 2, comprehensive reinsurance regulatory reform, rather than just focusing on collateral reduction. The proposal correctly recognizes that reinsurance is a global business that should be regulated in a manner that reflects the way business is conducted. We are pleased to see the NAIC embrace the concept of a single state regulator for reinsurance but, as our comments reflect below, there are several significant issues that must be addressed in order to achieve the necessary uniformity. Uniformity and true enforceable mutual recognition among the states are critical components of successful single state regulation. We also applaud the NAIC's acknowledgment that mutual recognition with non-U.S. jurisdictions is the way to address how non-U.S. reinsurers participate in the U.S. market. We encourage you to create a framework of mutual recognition with other regulatory regimes that is based upon an informed mutual determination that each maintains substantially equivalent regulatory standards and enforcement capabilities so that duplicative regulation can truly be minimized. Finally, we encourage you to include an exception for affiliate transactions in the proposal. Because these transactions are already subject to regulatory reporting and scrutiny before the transaction is even effected, collateral relief for affiliate transactions would seem to be one of the least controversial aspects of comprehensive reform.

We appreciate the amount of work that has occurred in such a short period of time as well as the fact that many critical details are yet to be developed. Although the RAA agrees with many of the technical comments set forth in the IP letter, the primary purpose of our

letter is to provide our preliminary comments regarding the most significant issues that need further clarification and/or development based on our understanding of the current proposal. The RAA has addressed many of these issues and is willing to assist in any way that we can.

RSRD Document

Treatment of U.S. Reinsurers

1. **Brief Summary.** The RSRD document proposes to develop a system to allow for a single state regulator for authorized reinsurers (passport system), “providing for a single point for establishment of laws and regulations governing reinsurance transactions.” “U.S. licensed insurers providing reinsurance” can choose which state will act as their home state regulator. If it complies with its home state’s laws, a U.S. licensed reinsurer can automatically assume reinsurance business in all other (host) states.

2. **Issues.**
 - a. The proposal does not establish mutual recognition among the states. (Paragraph 2). Although the proposal states that there will be a single point for establishing laws and regulations, there is no discussion as to how this system will be implemented (federal enabling legislation, interstate compact, etc.) or enforced. To achieve genuine single state reinsurance regulation, there must be enforceable mutual recognition among all of the states so that the home regulator’s decisions are respected and a patchwork system does not result.

 - b. Need to clarify who is subject to the proposal. (Paragraph 3). It is unclear from the draft which entities are subject to the proposal. The proposal states that “U.S. licensed insurers providing reinsurance” will have a choice as to which state will act as their home regulator. Does this include a primary company writing reinsurance as well as professional reinsurers? This should be clarified as a company that writes both insurance and reinsurance presents numerous complicated regulatory issues. We would also suggest that the use of the terms “insurer” and “reinsurer” throughout both draft documents be reviewed for clarity. (The need to clarify which types of entities are subject to the proposal also arises in the discussion of non-U.S. reinsurers).

 - c. Need to clarify use of the terms “host” and “home”. These are important terms in defining various regulators responsibilities under the proposal. The use of these terms should be clarified throughout the document to make it clear, for example, who the “home” supervisor is in that context (a state, a non-U.S. jurisdiction), etc.

- d. Lack of uniformity and continued extraterritorial application of law. (Paragraph 6, 2nd bullet point). The proposal does not create uniformity nor does it eliminate the extraterritorial application of state law. The first bullet point under paragraph 6 provides that states will be required to grant appropriate credit for reinsurance in compliance with the requirements of the reinsurer’s U.S. domiciliary regulator. The next bullet point, however, eliminates that uniformity by expressly permitting the cedent’s domiciliary regulator “to evaluate the amount of the liabilities ceded and retained, to determine whether the contract qualifies as reinsurance, and to evaluate the transaction’s compliance with diversification requirements, material transactions, hazardous financial condition laws, etc.” This is not a system that reflects deference to a home state regulator or a single point for the regulation of reinsurance transactions but rather, the reinsurer continues to be subject to 50 different sets of laws and regulations established by the cedents’ state of domicile. The U.S. licensed reinsurer’s home regulator should decide all issues relating to that reinsurance and those issues should be respected by, and enforced in, the other states.
- e. Need to clarify how single state regulators are qualified to ensure the system is meaningful and enforceable. (Paragraph 6, 7th and 8th bullet points). It is unclear how an individual state can qualify to be a single state regulator for U.S. reinsurers. The proposal states that to be a port of entry for non-U.S. reinsurers, a state must meet NAIC standards with regard to conducting adequate supervision of its licensed and, where applicable, its certified reinsurers. Is the process the same for being a single state regulator for U.S. reinsurers? What does “accreditation” mean – is it the current NAIC accreditation process or is it some sort of “super accreditation”? The proposal needs to address the “race to the bottom” concern (i.e., that reinsurers will select the jurisdiction with the lightest regulation as its home state regulator) articulated by several regulators so that this new system is respected and more easily enforced.
- f. Need to clarify what U.S. licensed reinsurers can do in host states. The proposal should make clear that a U.S. licensed reinsurer is able to not only provide creditable reinsurance throughout the U.S., but also to conduct business in accordance with the broader “doing business” statutes. This point should be clarified throughout both draft documents.

Treatment of Non-U.S. Reinsurers

1. **Summary.** The RSRD document proposes to establish the NAIC Reinsurance Supervision Review Department (RSRD) to negotiate mutual recognition agreements with jurisdictions that are deemed to be “functionally equivalent.” Non-U.S. reinsurers from those jurisdictions would then select a

port of entry (POE) state where they will undergo a certification process. If certified, the non-U.S. reinsurer would then qualify for credit for reinsurance and be authorized to conduct cross border business of reinsurance. The RSRD would establish principles concerning regulatory equivalence as well as set new minimum guidelines for states that want to be a port of entry for non-U.S. reinsurers. The POE is the primary U.S. regulator of a certified reinsurer; allocation of authority between the U.S. and other regulatory regimes will be determined in accordance with a set of nine principles articulated in the proposal.

2. **Issues.**

- a. Need to clarify what non-U.S. reinsurers can do in the U.S. (Paragraph 6). Are non-U.S. reinsurers being certified to do anything other than qualify for credit for reinsurance in the United States in accordance with the POE's rules and regulations? Does certification result in the ability to do business in the U.S.? These activities have traditionally been reserved for licensed insurers subject to the full panoply of U.S. regulation.
- b. Proposal should consider adding an additional regulatory option for non-US reinsurers. (Paragraph 6). The proposal does not appear to offer a streamlined licensing option to non-U.S. entities to be regulated like U.S. licensed reinsurers (i.e., single state regulator). It seems that a desirable regulatory goal would be to encourage licensing as a viable option for all entities, regardless of domicile in addition to the certification procedure.
- c. Need to clarify who the parties are to the mutual recognition agreement and their authority to enter into the agreement. (Paragraph 6). It is unclear who the parties to the mutual recognition agreement will be (i.e., the RSRD, an individual state, etc.) or what the legal authorization is for that entity to execute a mutual recognition agreement. It is critical that the mutual recognition agreements be constitutional and enforceable.
- d. Need to clarify how mutual recognition agreements should be negotiated, enforced and terminated. The proposal should identify in what areas the parties should determine that the other's jurisdiction maintains and applies legal standards and regulatory requirements that are "functionally equivalent" to those applied by the U.S. regulator. We suggest the areas should include:
 - i. Financial condition, including capitalization, investment and reserving requirements;
 - ii. Licensing, including an assessment of the quality and competence of licensee ownership and management;
 - iii. Periodic examination of the financial condition and operating practices of licensees; and

- iv. Management of insurers within holding company systems.

The proposal should also clearly set out how mutual recognition agreements will be enforced, how they can be terminated and how all affected parties' interests will be protected if they are terminated.

- e. Need to clarify the standards for a state to be a POE for non-U.S. reinsurers. (Paragraph 6, 7th and 8th bullet points). Are there requirements in addition to the existing accreditation requirements? Is it anticipated that all 50 states will qualify to be POE states? These are important issues to address so that the system will be viewed by other regulators as sufficiently rigorous.
- f. Need to address how the POE system will be implemented or enforced. The proposal needs to address how the POE system will be implemented in the 50 states and how decisions by a POE state will be enforced in the other states.

Principles for Regulatory Equivalence

1. **Brief Summary.** Articulates nine principles that are the starting point for developing a framework of mutual recognition.
2. **Issues.**
 - a. The proposal needs to set forth the explicit criteria for recognition that non-U.S. jurisdictions must meet and the various options that are available.
 - b. The RAA applauds the requirement that there must be reciprocal recognition and encourages the NAIC to ensure that this remains a component of the mutual recognition structure.
 - c. The goal of reinsurance regulation should be clarified to state that it is to protect insurer's solvency so that they can perform their obligations to policyholders (rather than to protect policyholders, who are not in privity with reinsurers).

POE/Establishment of Collateral Document

1. **Summary.** Collateral will be set by the POE regulator based on reinsurer's claims-paying ability (considering financial condition and other factors) in accordance with uniform standards established by the NAIC. A state will be required to grant appropriate credit for reinsurance ceded by one of its

licensed insurers in compliance with requirements of the reinsurer's U.S. domiciliary or POE regulator. However, the ceding insurer's domiciliary regulator retains the authority it has under existing law to evaluate the amount of liabilities ceded and retained, to determine whether the contract qualifies as reinsurance and to evaluate the transaction's requirements with diversification requirements, material transaction laws, etc. The ceding insurer's regulator also has discretion to amend the collateral requirements of certified non-U.S. reinsurers.

2. Issues.

- a. Lack of Enforcement Mechanism. What happens if the states do not grant credit for reinsurance? How can they be forced to comply? (Overview section).
- b. Lack of Uniformity. The proposal does not establish uniformity of regulation. For example, the proposal contains language that states that regulators may, but are not required, to use ratings to determine whether to grant credit to ceding companies. This creates uncertainty for the effective operation of the system, as it is unclear under what circumstances regulators may disregard the ratings. This could result in inconsistencies between POE regulators (reinsurers with similar characteristics could end up with different ratings due solely to the POE used). A lack of uniformity also results from the fact that the ceding insurer's regulator retains the authority to change the collateral decision by the reinsurer's domiciliary/POE. Both of these issues should be addressed so that the reinsurer's domiciliary/POE regulator makes the collateral decision based upon clearly articulated criteria and that decision is then enforceable in all the other states. (Overview section).
- c. Clarification of the RSRD's authority. The proposal needs to clearly set forth the RSRD's responsibilities, the basis of its authority for those responsibilities and whether its decisions are binding on the states.
- d. Clarification of process for U.S. reinsurers. By its terms, the proposal only provides for non-U.S. reinsurers to obtain a rating. The proposal then states that U.S. reinsurers rated Class 1 – 4 do not have to provide collateral. The proposal needs to be clarified to either: (1) make clear that U.S. reinsurers do not need to obtain a rating to be relieved from posting collateral; or (2) describe how U.S. reinsurers obtain a rating so that they can achieve the benefit of the Class 1-4 rating. (Pages 3, 8).
- e. Role of mutual recognition process. The purpose of mutual recognition is for jurisdictions to mutually recognize the sufficiency and equivalence of one another's regulatory regimes so that they can determine to what extent they will defer to and rely upon the home jurisdiction's supervision or will

provide reciprocal legal benefits to the licensees of each other's jurisdictions. The proposal attempts to employ a mutual recognition process but ultimately falls short of this goal. For example, the proposal imposes substantial collateral requirements on all highly rated reinsurers, even those from jurisdictions that have been deemed to be "functionally equivalent." We suggest that the proposal should reflect (1) trust in the conclusion that a jurisdiction has been deemed to be functionally equivalent after a rigorous evaluation process; and (2) a consistent philosophy as to the impact of a jurisdiction concluding that another jurisdiction is "functionally equivalent": i.e., non-U.S. companies from "functionally equivalent" jurisdictions should be treated in the same manner that U.S. regulators want U.S. licensed companies to be treated in countries that have deemed the U.S. to be "functionally equivalent." We urge the NAIC to create a mutual recognition system that encourages and supports trust in a jurisdiction's informed determination that another jurisdiction's regulation is "functionally equivalent."

- f. Inclusion of affiliate transaction exception. The dialogue at the RTF over the past year has included the possibility of exempting affiliate transactions from collateral requirements. Given the RTF's broadened approach to regulatory reform, we were surprised that this was not included in the proposal. We urge the Task Force to include affiliate transaction relief since these transactions are already subject to holding company act regulation in the U.S. The domestic regulator has the opportunity to assess the relative financial strength of the affiliated reinsurer, the ultimate holding company and significant persons within the holding company system. (See also rationale for an affiliate exception submitted by the Interested Persons to the Reinsurance Task Force in June 2006). In light of the above, we request that the Task Force reconsider its position on affiliate reinsurance collateral requirements, leaving the determination to the domiciliary regulator's discretion under the holding company system laws and regulations. (Page 8).

Thank you for the opportunity to provide our preliminary comments. The RAA looks forward to working with the Reinsurance Task Force, and the entire NAIC, towards comprehensive reinsurance regulatory reform. Please contact us with any questions or let us know if we can be of assistance.

Sincerely,



Frank Nutter



Tracey Laws

cc: Members of the Reinsurance Task Force
Bryan Fuller