



**KAREN WELDIN STEWART
INSURANCE COMMISSIONER**

December 12, 2013

To: Director John Huff, Chair, Financial Regulation Standards and Accreditation (F) Committee

From: Steve Kinion, Director, Bureau of Captive and Financial Insurance Products

Re: Response to December 2, 2013 Memorandum from Superintendent Torti

On behalf of Commissioner Stewart, I present this memorandum in response to the December 2 memorandum sent to the F Committee by Rhode Island Superintendent Joseph Torti. In his memorandum Superintendent Torti requests that the F Committee consider changing the definition of multi-state insurer for purposes of the NAIC's accreditation program so that it includes captive insurance companies. If this request becomes effective, then any captive insurer that reinsures risks located in a state other than the captive's domiciliary state would be subject to the accreditation standards. While the thrust of Superintendent Torti's request regards life-insurer owned captive insurers which reinsure XXX and AXXX excess reserves, the request would encompass practically all captives which act as reinsurers. Last August Superintendent Torti presented the same memorandum and at that time the Delaware Insurance Department replied that it opposed adopting the accreditation standards for life-insurer owned captive insurers. Delaware's position has not changed. Below are the enumerated reasons why Delaware's position has not changed.

First, the application of the accreditation standards to these captives would directly conflict with not only Delaware law, but very likely the laws of the 30 plus states that are now captive insurance domiciles. Chapter 69 of the Delaware Insurance Code specifically exempts captive insurers from all other provisions of the insurance code unless otherwise stated. For purposes of Superintendent Torti's request this means captive insurers are exempt from Parts A through D of the accreditation standards. When states are required to adopt laws in order to satisfy accreditation requirements, it typically means adding new laws. In order to implement Superintendent Torti's request it would mean changing existing laws, which in states like

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Delaware have been in place for many years. In Delaware's case it would mean asking the Delaware General Assembly to change a public policy it enacted years ago and for which no in-state constituency desires a change. Seeking such change will be a formidable challenge, especially because the facts do not support doing so.

Second, Superintendent Torti's request is premature. The NAIC is only beginning to gather data about life-insurer owned captive insurers that reinsure XXX and AXXX excess reserves. Consider the status quo: (1) only last August did the Financial Analysis Working Group begin to collect information for its survey regarding these types of captives and the FAWG's work continues; (2) the final report prepared by Rector & Associates for these life insurer-owned captives is not complete and less than three months ago the Principle-Based Reserving Implementation Task Force received Rector & Associates' initial report; (3) the initial report did not offer any final recommendations, but instead posed questions for the PBR Task Force's consideration; (4) the initial report does not recommend making the regulation of these captives an accreditation standard – it merely mentions doing so; and, (5) the initial report is clear that if the NAIC intends to develop uniform regulatory standards for life-insurer owned captives, then a monumental amount of work remains to be done.

Third, the monumental amount of work regarding how to regulate life insurer-owned captives is only beginning. There is much work to complete in order to develop guidance for the states in regard to regulating life-insurer owned captives. If the NAIC is to follow its own recommendations, it must first develop guidance, and then consider any accreditation standards. The NAIC's *Captive & Special Purpose Vehicle White Paper* on page 32 is clear when it states that additional guidance must be developed by the NAIC before considering any accreditation questions,

To the extent affiliated captives and SPVs may be created in the future for purposes unseen today, *additional guidance should be developed by the NAIC* to assist the states in a uniform review of transactions, including recommendations for minimum analysis to be performed, as well as ongoing monitoring of the ceding insurer, the captive and the holding company. The guidance should be developed for perspectives of the ceding state, the captive state and the lead state. *Once developed*, the guidance should be considered to be added to the NAIC Financial Regulation Standards and Accreditation Program standards to ensure consistency and uniformity among the states.

The status quo is that life insurer-owned captives and SPVs are being created and will continue to be created. The NAIC has not yet taken some important steps to develop and complete guidance that assists states in reviewing these transactions. One untaken step is selecting the membership of the Captives (EX) Working Group. The Delaware Insurance Department believes it is a critical step to appoint the members of this working group. To support Delaware's position, it refers to the following passage on page 12 of the August 24, 2013 version of the Principles-Based Reserving Implementation Plan,

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The NAIC needs to further assess the solvency implications of life insurer-owned captive insurers and other alternative mechanisms in the context of PBR. The solution for captives and SPVs within the context of PBR will be largely based on Captives and Special Purpose Vehicle (SPV) Use (E) Subgroup's report as adopted by the Financial Condition (E) Committee and referred to the PBR Implementation (EX) Task Force. *The Task Force will create a Working Group to concentrate on this issue and propose the way forward.*

Via the captive white paper and PBR Task Force, the NAIC has created a road map for addressing life insurer-owned captives. It is important to continue down the existing road map and not detour to pursue requests that are premature. Today, a monumental amount of work remains to be done in order to reach some type of resolution for life insurer-owned captives. Only after that work is completed will Superintendent Torti's request to impose accreditation standards on life insurer-owned captives become a topic that is ripe for discussion.

Thank you for your consideration of this memorandum and if necessary, I look forward to any further dialogue on this topic.