

US Reinsurance Rules Set for Change

By Richard Liskov*



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is uncertain, but there is a gathering consensus as to what should be done to bring reinsurance regulation into the realities of a global marketplace.

The Two Proposals

The Nonadmitted and Reinsurance Reform Act of 2009 passed the U.S. House of Representatives in September, but awaits action in the Senate. It would streamline regulations of reinsurers by requiring that all states allow a ceding insurer to take credit on its financial statements for reinsurance ceded, if (i) the domiciliary state of the ceding insurer does so, and (ii) the domiciliary state is either accredited by the National Association of Insurance Commissioners (NAIC) or prescribes equivalent financial solvency standards.

The Reinsurance Regulatory Modernization Act of 2009, recently backed by the NAIC, would limit regulation of reinsurers to a single state like the Reform Act, but would go further by prescribing specific solvency standards for U.S. and foreign reinsurers, although those standards will favor U.S. reinsurers. It also would tie the requirement of collateral for securing recoverables to the reinsurer's status in one of five rating tiers based on the reinsurer's ratings from recognized rating agencies, the reinsurer's audited financials and actuarial opinions, and even reputation for prompt claims paying, among other criteria.

Last year it seemed that prospects were bright for achieving significant change in reinsurance rules in the U.S., and that those proposals would equalize the treatment of U.S. and foreign reinsurers. Although they face formidable obstacles, now two possible vehicles for

change have emerged. How soon Congress will enact them

The Proposed Reform Act

The proposed Reform Act would streamline regulations of reinsurers by requiring that all states allow a ceding insurer to take credit on its financial statements for reinsurance ceded, if (i) the domiciliary state of the ceding insurer does so, and (ii) the domiciliary state is either accredited by the NAIC or prescribes equivalent financial solvency standards.. Since states do not regulate reinsurers for market conduct, that would mean only one state will oversee a reinsurer, unless that company also engages in direct business.

The Reform Act does not address collateral requirements on unlicensed reinsurers. Changing the collateral requirements is the most significant feature of the Modernization Act proposal.

The Proposed Modernization Act

The Modernization Act would create a new federal agency to certify state insurance departments eligible to act as the "Home State" regulator for U.S. reinsurers or the "Port of Entry" regulator for foreign reinsurers. As with the proposed Reform Act, only one state would have authority over reinsurers.

The most significant aspect of the proposal is that it will impose specific federal standards for reinsurers, both U.S. and foreign. Reinsurers that desire to avoid the current restrictive rules will need a minimum of \$250 million in capital.. The percentage of liabilities that must be secured, however, would differ between U.S. and foreign reinsurers. U.S. insurers which meet any of the first three rating tiers would be able to avoid any collateral requirement, while only those foreign reinsurers receiving the highest ratings could do so. Unlicensed foreign reinsurers in the second and third tiers would have to secure 10% and 20% of their liabilities, but U.S. reinsurers in those same tiers would be exempt from posting any security for their liabilities.

The Prognosis

The proposed Reform Act already approved by the U.S. House stands a far better chance of actually becoming law in the coming year than the proposed Modernization Act. As of now, the most likely scenario in the near term is incremental, not significant, change in the way reinsurance is regulated in the U.S..

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