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INDEPENDENT REGULATORY
REVIEW COMMISSION

2012 AUG 22 AM 11: 30

Regulatory Analysis Form

(Completed by Promulgating Agency)

(All Comments submitted on this regulation will appear on IRRC's website)

(1) Agency:

Insurance Department

(2) Agency Number:

Identification Number: 11-249

IRRC Number: 2970

(3) PA Code Cite:

31 Pa. Code, Chapter 161, §§161.1-161.9

(4) Short Title:

Requirements for Qualified **and Certified** Reinsurers

(5) Agency Contacts (List Telephone Number and Email Address):

Primary Contact:

Peter J. Salvatore, Regulatory Coordinator
1326 Strawberry Square, Harrisburg, PA 17120, (717) 787-4429
psalvatore@pa.gov

Secondary Contact:

(6) Type of Rulemaking (check applicable box):

Proposed Regulation

Final Regulation

Final Omitted Regulation

Emergency Certification Regulation;

Certification by the Governor

Certification by the Attorney General

(7) Briefly explain the regulation in clear and nontechnical language. (100 words or less)

Chapter 161 was initially adopted in 1993 and sets forth requirements to be met for a licensed ceding insurer to receive credit for reinsurance in its financial statements. The purpose of this proposed rulemaking is to update Chapter 161 in accordance with amendments made to 40 P.S. § 442.1 by Act 2012-136 (S.B. 1464), P.L. ___, approved July 5, 2012, ("Act 136") which grants the Insurance Commissioner the authority to "certify" reinsurers so that ceding insurers may receive credit for reinsurance ceded to duly certified reinsurers. The proposed amendments to Chapter 161 are based upon recent amendments to model law and regulation developed by the National Association of Insurance Commissioners (NAIC) entitled "Credit for Reinsurance Model Law" (#785) and "Credit for Reinsurance Model Regulation" (#786) respectively. These amendments are proposed in conjunction with amendments to Chapter 163 (relating to Requirements for Funds Held as Security for the Payment of Obligations of Unlicensed, Unqualified Reinsurers).

(8) State the statutory authority for the regulation. Include specific statutory citation.

The rulemaking is proposed under the authority of sections 206, 506, 1501 and 1502 of The Administrative Code of 1929 (71 P.S. §§ 66, 186, 411 and 412) relating to the general rulemaking authority of the Department and Section 319.1 of the act of May 17, 1921 (P.L. 682, No. 284), known as The Insurance Company Law of 1921 (40 P.S. § 442.1), relating to Credits for Reinsurance.

(9) Is the regulation mandated by any federal or state law or court order, or federal regulation? Are there any relevant state or federal court decisions? If yes, cite the specific law, case or regulation as well as, any deadlines for action.

No. However, these proposed regulations are part of the financial regulation standards the Department must meet in order to maintain its accreditation by the NAIC. Thus, if a jurisdiction opts to certify reinsurers, as Pennsylvania has done with the enactment of Act 136, the standards by which it does so must be substantially similar to NAIC requirements in order for the jurisdiction to maintain NAIC accreditation.

(10) State why the regulation is needed. Explain the compelling public interest that justifies the regulation. Describe who will benefit from the regulation. Quantify the benefits as completely as possible and approximate the number of people who will benefit.

This rulemaking is needed to update Chapter 161 in accordance with amendments made to 40 P.S. § 442.1 by Act 136, which grants the Insurance Commissioner the authority to “certify” reinsurers so that ceding insurers may receive credit for reinsurance ceded to duly certified reinsurers. The general public will benefit to the extent that allowing reduced collateral for reinsurers that are financially solvent and licensed in well-regulated jurisdiction will reduce the cost of reinsurance to ceding insurers in the Commonwealth and reduce trade barriers allowing for more competition in the reinsurance marketplace.

(11) If data is the basis for this regulation, please provide a description of the data, explain in detail how the data was obtained, and how it meets the acceptability standard for empirical, replicable and testable data that is supported by documentation, statistics, reports, studies or research. Please submit data or supporting materials with the regulatory package. If the material exceeds 50 pages, please provide it in a searchable electronic format or provide a list of citations and internet links that, where possible, can be accessed in a searchable format in lieu of the actual material. If other data was considered but not used, please explain why that data was determined not to be acceptable.

N/A

(12) Describe who and how many people will be adversely affected by the regulation. How are they affected?

No adverse effects are anticipated as a result of this rulemaking.

(13) List the persons, groups or entities that will be required to comply with the regulation. Approximate the number of people who will be required to comply.

This proposed rulemaking would apply to all insurance companies domesticated in the Commonwealth and the reinsurers with whom they do business. There are approximately 270 Pennsylvania-domiciled licensed companies.

(14) Provide a specific estimate of the costs and/or savings to the **regulated community** associated with compliance, including any legal, accounting or consulting procedures which may be required. Explain how the dollar estimates were derived.

The amended requirements in Chapter 161 will impose no significant costs upon the regulated community on the transaction of business in this Commonwealth. However, the amended requirements will allow for reduced collateral for reinsurers that are financially solvent and licensed in well-regulated jurisdiction. This reduced collateral will reduce the cost of reinsurance to ceding insurers in the Commonwealth and reduce trade barriers allowing for more competition in the reinsurance marketplace.

(15) Provide a specific estimate of the costs and/or savings to **local governments** associated with compliance, including any legal, accounting or consulting procedures which may be required. Explain how the dollar estimates were derived.

There are no costs or savings to local governments associated with this rulemaking.

(16) Provide a specific estimate of the costs and/or savings to **state government** associated with the implementation of the regulation, including any legal, accounting, or consulting procedures which may be required. Explain how the dollar estimates were derived.

There are no costs or savings to state government associated with this rulemaking

(17) In the table below, provide an estimate of the fiscal savings and costs associated with implementation and compliance for the regulated community, local government, and state government for the current year and five subsequent years.

	Current FY Year	FY +1 Year	FY +2 Year	FY +3 Year	FY +4 Year	FY +5 Year
SAVINGS:	\$	\$	\$	\$	\$	\$
Regulated Community						
Local Government						
State Government						
Total Savings						
COSTS:						
Regulated Community						
Local Government						
State Government						
Total Costs						
REVENUE LOSSES:						
Regulated Community						
Local Government						
State Government						
Total Revenue Losses						

(17a) Provide the past three year expenditure history for programs affected by the regulation.

Program	FY -3	FY -2	FY -1	Current FY

(18) Explain how the benefits of the regulation outweigh any cost and adverse effects.

As noted above, these proposed regulations are part of the financial regulation standards the Department must meet in order to maintain its accreditation by the NAIC. Thus, if a jurisdiction opts to certify reinsurers, as Pennsylvania has done with the enactment of Act 136, the standards by which it does so must be substantially similar to NAIC requirements in order for the jurisdiction to maintain NAIC accreditation.

(19) Describe the communications with and input from the public and any advisory council/group in the development and drafting of the regulation. List the specific persons and/or groups who were involved.

The Department circulated pre-exposure drafts of the regulations to the Insurance Federation of Pennsylvania, Inc. and the Pennsylvania Association of Mutual Insurance Companies.

(20) Include a description of any alternative regulatory provisions which have been considered and rejected and a statement that the least burdensome acceptable alternative has been selected.

No other regulatory schemes were considered. The rulemaking updates Chapter 161 in accordance with the recent amendments to the reinsurance credits law.

(21) Are there any provisions that are more stringent than federal standards? If yes, identify the specific provisions and the compelling Pennsylvania interest that demands stronger regulations.

No.

(22) How does this regulation compare with those of other states? How will this affect Pennsylvania's ability to compete with other states?

The rulemaking has no impact on Pennsylvania's ability to compete with other states. The rulemaking is based upon an NAIC model, the requirements of which are necessary to maintain accredited regulator status. As such, other jurisdictions who elect to "certify" reinsurers must implement substantially regulatory similar requirements. However, if Pennsylvania does not enact standards to certify reinsurers, it may be at a disadvantage to other states that do allow certification.

(23) Will the regulation affect any other regulations of the promulgating agency or other state agencies? If yes, explain and provide specific citations.

No.

(24) Submit a statement of legal, accounting or consulting procedures and additional reporting, recordkeeping or other paperwork, including copies of forms or reports, which will be required for implementation of the regulation and an explanation of measures which have been taken to minimize these requirements.

No additional procedures, reporting, recordkeeping or other paperwork will be required.

(25) Please list any special provisions which have been developed to meet the particular needs of affected groups or persons including, but not limited to, minorities, elderly, small businesses, and farmers.

N/A

(26) Include a schedule for review of the regulation including:

- | | |
|---|-------------------------|
| A. The date by which the agency must receive public comments: | <u>October 8, 2012</u> |
| B. The date or dates on which public meetings or hearings will be held: | <u>NA</u> |
| C. The expected date of promulgation of the proposed regulation as a final-form regulation: | <u>January 29, 2013</u> |
| D. The expected effective date of the final-form regulation: | <u>May 1, 2013</u> |
| E. The date by which compliance with the final-form regulation will be required: | <u>May 1, 2013</u> |
| F. The date by which required permits, licenses or other approvals must be obtained: | <u>NA</u> |

(27) Provide the schedule for continual review of the regulation.

The Department reviews each of its regulations for continued effectiveness on a triennial basis.

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(Pursuant to Commonwealth Documents Law)

DO NOT WRITE IN THIS SPACE

Copy below is hereby approved as to
form and legality. Attorney General

Angela M. Elliott
By _____

(Deputy Attorney General)

AUG 17 2012

Date of Approval

→ Check if applicable.
Copy not approved. Objections
attached.

Copy below is hereby certified to be a true and correct
copy of a document issued, prescribed or promulgated
by:

Insurance Department

(AGENCY)

DOCUMENT/FISCAL NOTE NO. 11-249

DATE OF ADOPTION:

BY:

Michael F. Considine

Michael F Considine
Insurance Commissioner

TITLE:

(EXECUTIVE OFFICER, CHAIRMAN OR
SECRETARY)

Copy below is hereby approved as to form and
legality. Executive or Independent Agencies

Shawn E. Smith

SHAWN E. SMITH

JUL 24 2012

DATE OF APPROVAL

(DEPUTY GENERAL COUNSEL)
(~~CHIEF COUNSEL, INDEPENDENT AGENCY~~)
(STRIKE INAPPLICABLE TITLE)

→ Check if applicable. No Attorney General
approval or objection within 30 days after
submission.

NOTICE OF PROPOSED RULEMAKING

INSURANCE DEPARTMENT

31 Pa. Code, Chapter 161, §§161.1-161.9

REQUIREMENTS FOR QUALIFIED AND CERTIFIED REINSURERS

Preamble

The Insurance Department (Department) proposes to amend Chapter 161 of the Department's regulations (31 Pa. Code Ch. 161) (relating to requirements for qualified reinsurers) to read as set forth in Annex A. The rulemaking is proposed under the authority of sections 206, 506, 1501 and 1502 of The Administrative Code of 1929 (71 P.S. §§ 66, 186, 411 and 412) relating to the general rulemaking authority of the Department and section 319.1 of the act of May 17, 1921 (P.L. 682, No. 284), known as The Insurance Company Law of 1921 (40 P.S. § 442.1), relating to credits for reinsurance.

Purpose

Chapter 161 was initially adopted in 1993 and sets forth requirements to be met for a licensed ceding insurer to receive credit for reinsurance in its financial statements. The purpose of this proposed rulemaking is to update Chapter 161 in accordance with amendments made to 40 P.S. § 442.1 by Act 2012 -136 (S.B.1464), P.L. 1111, approved July 5, 2012 ("Act 136"), which grants the Insurance Commissioner the authority to "certify" reinsurers so that ceding insurers may receive credit for reinsurance ceded to duly certified reinsurers. These amendments are proposed in conjunction with amendments to Chapter 163 (relating to requirements for funds held as security for the payment of obligations of unlicensed, unqualified reinsurers).

The proposed amendments to Chapter 161 are based upon recent amendments to model law and regulation developed by the National Association of Insurance Commissioners (NAIC) entitled "Credit for Reinsurance Model Law" (#785) "Credit for Reinsurance Model Regulation" (#786) respectively. These proposed regulations are part of the financial regulation standards the Department must meet in order to maintain its accreditation by the NAIC. Thus, if a jurisdiction opts to certify reinsurers, as Pennsylvania has done with the enactment of Act 136, the standards by which it does so must be substantially similar to NAIC requirements in order for the jurisdiction to maintain NAIC accreditation.

A copy of the copyrighted NAIC model regulation was provided to the legislative standing committees, the Independent Regulatory Review Commission (IRRC), the Governor's Office of Policy and Planning, the Governor's Office of General Counsel and the Attorney General to assist in their analysis of this proposed rulemaking. Copies of NAIC model regulations are available to the general public by contacting the NAIC

Explanation of Proposed Amendments

The following is a description of the changes contained in the proposed rulemaking:

The heading of Chapter 161 is proposed to be amended to "Requirements for Qualified and Certified Reinsurers" to properly reflect the scope of the regulations.

Section 161.1 (relating to purpose) is proposed to be amended to include a reference to certified insurers, to reflect the deletion of section 161.8, and correct the reference to 40 P. S. § 442.1.

Section 161.2 (relating to definitions) is proposed to be amended to delete the definition of *Unauthorized alien assuming insurer* in accordance with the deletion of section 161.8.

Section 161.3 (relating to credit for reinsurance) is proposed to be amended to: modify the requirements for an assuming foreign insurer to be considered for qualification; authorize a reduction in required trusteed surplus for a qualified alien reinsurer after a risk assessment if an assuming reinsurer has permanently discontinued underwriting new business for at least three calendar years; make editorial changes to clause (3)(vii)(B); add a provision indicating that credit will be allowed when reinsurance is ceded to certified reinsurers; and clarify that credit is allowed pursuant to 40 P.S. § 442.1(b) if it does not exceed the liabilities carried by the ceding insurer.

A new section, § 161.3a (relating to Requirements for Certified Reinsurers), is proposed to be added to: set forth the standards for assuming insurers to be eligible for certification as a certified reinsurer; provide for additional requirements for an association, including incorporated and individual unincorporated insurers to be a certified reinsurer; give the Commissioner discretion to defer to the reinsurer's certification by an NAIC accredited jurisdiction; allow a certified reinsurer to request to maintain its certification in inactive status if it ceases to assume new business; and set forth the Department's procedure for giving notice of and granting certified status to assuming reinsurers.

A new section, § 161.3b (relating to calculation of credit for reinsurance regarding obligations secured with certified reinsurers), is proposed to be added to outline the standards that must be met in order for a domestic ceding insurer to qualify for full financial statement credit for reinsurance ceded to a certified reinsurer. Specifically, as proposed, this section would: provide for the requirements for maintaining security in a form acceptable to the Commissioner and provide additional requirements for security maintained in a multibeneficiary trust; specify the requirements for calculation of the allowable credit; provide that the Commissioner will reduce the allowable credit by an amount proportionate to any deficiency if the security is found to be insufficient and has the discretion to impose further reductions or adjustments upon a finding of material risk or if the Commissioner finds that the reinsurer is not promptly paying claims. Additionally, this section contains a provision that clarifies that parties may agree to provisions establishing security requirements in excess of the minimum requirements required by regulation.

A new section, § 161.3c (relating to concentration risk), is proposed to be added to require domestic ceding insurers to notify the Commissioner within 30 days if reinsurance recoverables from any single assuming insurer, or group of affiliated assuming insurers, exceed 50% of surplus or upon a determination that it is likely to exceed that limit. This section would also require a ceding insurer to take steps to diversify its reinsurance program, requiring notification to the Commissioner within 30 days of ceding more than 20% of the ceding insurer's gross written premium or upon a determination that it is likely to exceed this limit.

Section § 161.6 (relating to revocation of reinsurer qualification or certification), is proposed to be amended to include provisions regarding the procedure for revoking a certified reinsurer's

certification and to require an assuming insurer to post security in order for a ceding insurer to continue to take credit for reinsurance.

Section 161.7 (relating to credit for joint underwriting or pooling arrangements) is proposed to be amended to allow domestic ceding insurers to request specific approval from the Commissioner to take reserve credit for reinsurance ceded in a joint underwriting or joint reinsurance pooling arrangement that involves insurers who are not certified reinsurers.

Section § 161.8. (relating to credit for reinsurance ceded to alien nonaffiliated insurers which write no primary coverages in the United States) is proposed to be deleted in its entirety. This section's requirements, which provide conditions under which partial credit for reinsurance with alien reinsurers may be taken without full collateralization, have been superseded by the enactment of the Act 136 amendments to 40 P.S. § 442.1.

A new section, § 161.8 (relating to reinsurance contracts), is proposed to be added to require that a reinsurance agreement contain a proper insolvency clause, a reinsurance intermediary clause (if applicable), and a mandatory funding clause.

External Comments

The Department circulated pre-exposure drafts of the regulations to the Insurance Federation of Pennsylvania, Inc. and the Pennsylvania Association of Mutual Insurance Companies.

Affected Parties

This proposed rulemaking would apply to all insurance companies domesticated in the Commonwealth and the reinsurers with whom they do business.

Fiscal Impact

State Government

The rulemaking will strengthen and clarify existing regulatory requirements. There will be no material increase in cost to the Department as a result of this rulemaking.

General Public

While the chapter has no immediate fiscal impact on the general public, the general public will benefit to the extent that allowing reduced collateral for reinsurers that are financially solvent and licensed in well-regulated jurisdiction will reduce the cost of reinsurance to ceding insurers in the Commonwealth and reduce trade barriers allowing for more competition in the reinsurance marketplace.

Political Subdivisions

The rulemaking will not impose additional costs on political subdivisions.

Private Sector

The amended requirements in Chapter 161 will impose no significant costs on the transaction of business in this Commonwealth.

Paperwork

The rulemaking would not impose additional paperwork on the Department.

Effectiveness/Sunset Date

The rulemaking will become effective within thirty (30) days after published in final form in the Pennsylvania Bulletin. The Department continues to monitor the effectiveness of regulations on a triennial basis; therefore, no sunset date has been assigned.

Contact Person

Questions or comments regarding the proposed rulemaking may be addressed in writing to Peter J. Salvatore, Regulatory Coordinator, Insurance Department, 1326 Strawberry Square, Harrisburg, PA 17120, within 30 days following the publication of this notice in the *Pennsylvania Bulletin*. Questions and comments may also be e-mailed to psalvatore@pa.gov or faxed to (717) 705-3873.

Under the Regulatory Review Act (71 P. S. §§ 745.1--745.15), the Department is required to write to all commentators requesting whether or not they wish to receive a copy of the final-form rulemaking. To better serve stakeholders, the Department has made a determination that all commentators will receive a copy of the final-form rulemaking when it is made available to the Independent Regulatory Review Commission (IRRC) and the legislative standing committees.

Regulatory Review

Under section 5(a) of the Regulatory Review Act (71 P.S. §745.5(a)), on 8/22/12, the Department submitted a copy of this proposed rulemaking to the Independent Regulatory Review Commission (IRRC) and to the Chairpersons of the Senate Banking and Insurance Committee and the House Insurance Committee. In addition to the submitted proposed rulemaking, the Department has, as required by the Regulatory Review Act, provided IRRC and the Committees with a copy of a detailed Regulatory Analysis Form prepared by the Department. A copy of that material is available to the public upon request.

The IRRC will notify the Department of any objections to any portion of the proposed rulemaking within 30 days of the close of the public comment period. The notification shall specify the regulatory review criteria that have not been met by that portion. The Regulatory

Review Act specifies detailed procedures for the Department, the Governor, and the General Assembly to review these objections before final publication of the regulations.

Michael F. Considine
Insurance Commissioner

Annex A

TITLE 31. INSURANCE

PART VIII. MISCELLANEOUS PROVISIONS

CHAPTER 161. REQUIREMENTS FOR QUALIFIED AND CERTIFIED REINSURERS.

161.1. Purpose.

161.2. Definitions.

161.3. Credit for reinsurance.

161.3a Requirements for Certified Reinsurers

161.3b Requirements for securing obligations of Certified Reinsurers

161.3c Concentration Risk

161.4. Trust fund requirements.

161.5. Determination of reinsurer qualification.

161.6. Revocation of reinsurer qualification.

161.7. Credit for joint underwriting or pooling arrangements.

161.8. [Credit for reinsurance ceded to alien nonaffiliated insurers which write no primary coverages in the United States] **Reserved.**

161.8a Reinsurance contract.

161a.9. Application.

§ 161.1. Purpose.

(a) This chapter sets forth requirements to be met for a licensed ceding insurer to receive credit for reinsurance in its financial statements. This chapter specifies the conditions which shall be met by an unlicensed reinsurer to be considered by the Commissioner for inclusion on a list of qualified **or certified** reinsurers published and periodically reviewed by the Commissioner, as well as, the requirements for receiving reinsurance credit for joint underwriting or joint reinsurance pooling arrangements [and for reinsurance with alien nonaffiliated reinsurers which write no primary coverages in the United States].

(b) This chapter does not apply to reinsurance agreements between or among affiliates which meet the conditions for exemption in section 319.2 of the act (40 P. S. § 442.2) or to the ability of licensed ceding insurers to receive credit for reinsurance by compliance with the conditions specified in 319.1(b) of the act (40 P. S. § 442.1**(b)**).

§ 161.2. Definitions.

The following words and terms, when used in this chapter, have the following meanings, unless the context clearly indicates otherwise:

Accredited state—A state which is accredited by NAIC for compliance with the NAIC

Financial Regulation Standards or successor standards.

Act—The Insurance Company Law of 1921 (40 P. S. §§ 341—991).

Alien insurer—An insurer incorporated or organized under the laws of a foreign nation or of a province or territory other than a state of the United States, the Commonwealth of Puerto Rico or the District of Columbia.

Commissioner—The Insurance Commissioner of the Commonwealth.

Department—The Insurance Department of the Commonwealth.

Foreign insurer—An insurer, other than an alien insurer, not incorporated or organized under the laws of the Commonwealth. For purposes of this chapter, the term also includes a United States branch of an alien assuming insurer which branch is not entered through and licensed to transact insurance or reinsurance in this Commonwealth.

NAIC—National Association of Insurance Commissioners.

Qualified United States financial institution—

(i) An institution which meets the following qualifications. The institution:

(A) Is organized or, in the case of a United States office of a foreign banking organization, licensed, under the laws of the United States or a state thereof.

(B) Is regulated, supervised and examined by Federal or state authorities having regulatory authority over banks and trust companies.

(C) Has been determined by either the Commissioner or the Securities Valuation Office of the NAIC or a successor thereto to meet the standards of financial condition and standing considered necessary and appropriate to regulate the quality of financial institutions whose letters of credit will be acceptable to the Commissioner.

(ii) For purposes of specifying institutions that are eligible to act as a fiduciary of a trust, an institution that meets the following qualifications. The institution:

(A) Is organized, or in the case of a United States branch or agency office of a foreign banking organization, licensed, under the laws of the United States or a state thereof and has been granted authority to operate with fiduciary powers.

(B) Is regulated, supervised and examined by Federal or state authorities having regulatory authority over banks and trust companies.

[*Unauthorized alien assuming insurer*—An insurer which meets the criteria in § 161.8(a)

(relating to credit for reinsurance ceded to alien nonaffiliated insurers which write no primary coverages in the United States).]

§ 161.3. Credit for reinsurance.

A licensed domestic ceding insurer will be allowed credit for reinsurance as either an asset or a deduction from liability on account of reinsurance ceded only when the reinsurer meets the requirements of this section or as otherwise provided in § [§] 161.7 [and 161.8 (relating to credit for joint underwriting or pooling arrangements; and credit for reinsurance ceded to alien nonaffiliated insurers which write no primary coverages in the United States)].

(1) Credit will be allowed when the reinsurance is ceded to an assuming insurer which is licensed to transact insurance or reinsurance in this Commonwealth.

(2) Credit will be allowed when the reinsurance is ceded to an assuming foreign insurer which has met the conditions specified in this paragraph and has been deemed to be a qualified reinsurer by the Commissioner. To be considered for qualification, an assuming foreign insurer shall meet the following conditions. The insurer shall:

(i) File evidence of its submission to the Commonwealth's jurisdiction with the Commissioner.

(ii) Submit to the Commonwealth's authority to examine its books and records.

(iii) Be licensed to transact insurance or reinsurance in at least one state, or in the case of a United States branch of an alien assuming insurer be entered through and licensed to transact insurance or reinsurance in at least one state. After 1994, one of the states in which the insurer is licensed shall be an accredited state.

(iv) File with the application for qualification and annually thereafter a copy of its annual statement filed with the insurance department of its state of domicile and a copy of its most recent audited financial statement.

(v) **[Maintain a surplus as regards policyholders in an amount which is not less than \$20 million] Demonstrate to the satisfaction of the Commissioner that it has adequate financial capacity to meet its reinsurance obligations and is otherwise qualified to assume reinsurance from domestic insurers. An assuming insurer is deemed to meet this requirement as of the time of its application if it maintains a surplus as regards policyholders in an amount not less than \$20 million and its qualification has not been denied by the Commissioner within ninety (90) days after submission of its application.**

[(vi) Cede no more than 50% of its premiums to assuming insurers that are neither licensed nor qualified reinsurers in this Commonwealth.]

(3) Credit will be allowed when the reinsurance is ceded to an assuming alien insurer which has met the conditions specified in this paragraph and has been deemed to be a qualified

reinsurer by the Commissioner. To be considered for qualification, an assuming alien insurer shall meet the following conditions. The insurer shall:

(i) File with the Commissioner evidence of its submission to the Commonwealth's jurisdiction.

(ii) Submit to the Commonwealth's authority to examine its books and records.

(iii) File with the application for qualification and annually thereafter substantially the same information as that required to be reported on the NAIC annual statement blank by licensed insurers.

(iv) Be listed on the Non-Admitted Insurers Listing published by the Non-Admitted Insurers Information Office of the NAIC, or a successor list.

(v) File with the application for qualification and annually thereafter details on the soundness of its ceded reinsurance program, including the identity, domicile and premium volume for each retrocessionaire when the amount of reinsurance premium ceded is greater than or equal to \$50,000. If the insurer demonstrates to the Commissioner's satisfaction its inability to provide the requested detail with respect to individual retrocessionaires because of its method of operation, the Commissioner will consider the acceptability of alternative information pertaining to the soundness of the insurer's ceded reinsurance program.

(vi) Agree to the requirements of this subparagraph in the reinsurance agreements. This subparagraph is not intended to conflict with or override the obligation of the parties to a reinsurance agreement to arbitrate their disputes, if an obligation is created in the agreement.

(A) In the event of the failure of the assuming insurer to perform its obligations under the terms of the reinsurance agreement, the assuming insurer shall at the request of the ceding insurer:

(I) Submit to the jurisdiction of a court of competent jurisdiction in a state of the United States.

(II) Comply with the requirements necessary to give the court jurisdiction.

(III) Abide by the final decision of the court or of an appellate court in the event of an appeal.

(B) The assuming insurer shall designate a person as its true and lawful agent upon whom may be served a lawful process in an action, suit or proceeding instituted by or on behalf of the ceding company.

(vii) Maintain a trust fund in a qualified United States financial institution, for the payment of valid claims of its United States policyholders and ceding insurers, their assigns and successors in interest.

(A) In the case of a single assuming insurer, the trust shall consist of a trustee account in an amount not less than the assuming insurer's liabilities attributable to business directly written or assumed in the United States. In addition, the assuming insurer shall maintain a trustee surplus of at least \$20 million **except as provided in clause A.1.**

(A.1) At any time after the assuming insurer has permanently discontinued underwriting new business secured by the trust for at least three calendar years, the commissioner with principal regulatory oversight of the trust may authorize a reduction in the required trustee surplus, but only after a finding, based on an assessment of the risk, that the new required surplus level is adequate for the protection of U.S. ceding insurers, policyholders and claimants in light of reasonably foreseeable adverse loss development. The risk assessment may involve an actuarial review, including an independent analysis of reserves and cash flows, and will consider all material risk factors, including when applicable the lines of business involved, the stability of the incurred loss estimates and the effect of the surplus requirements on the assuming insurer's liquidity or solvency. The minimum required trustee surplus may not be reduced to an amount less than 30% of the assuming insurer's liabilities attributable to reinsurance ceded by U.S. ceding insurers covered by the trust.

(B) In the case of a group of insurers which includes **incorporated and** unincorporated individual insurers, the trust shall consist of a trustee account not less than the **[group's aggregate] respective insurers' several** liabilities attributable to business directly written or assumed in the United States. In addition, the group shall maintain a trustee surplus of which \$100 million shall be held jointly for the benefit of United States ceding insurers of any **[member] insurer** of the group. The group shall make available to the Commissioner an annual certification of the solvency of each insurer by the group's domiciliary regulator and its independent public accountants.

(4) Credit will be allowed when the reinsurance is ceded to a group of incorporated alien insurers under common administration if the group has met the conditions specified in this subsection and has been deemed to be a qualified reinsurer by the Commissioner. To be considered for qualification the group shall meet the following conditions. The group shall:

(i) Have continuously transacted an insurance business outside the United States for at least 3 years immediately prior to applying for qualification.

(ii) File with the Commissioner evidence of its submission to the Commonwealth's jurisdiction.

(iii) File with the application for qualification and annually thereafter substantially the same information as that required to be reported on the NAIC annual statement blank by licensed insurers.

(iv) Submit to the Commonwealth's authority to examine its books and records and bear the expense of the examination.

(v) File with the application for qualification and annually thereafter details on the soundness of its ceded reinsurance program, including the identity, domicile and premium volume for each retrocessionaire when the amount of reinsurance premium ceded is greater than or equal to \$50,000. If the insurer demonstrates to the Commissioner's satisfaction its inability to provide the requested detail with respect to individual retrocessionaires because of its method of operation, the Commissioner will consider the acceptability of alternative information pertaining to the soundness of the insurer's ceded reinsurance program.

(vi) Maintain an aggregate policyholder's surplus of at least \$10 billion, calculated and reported in substantially the same manner as prescribed by the annual statement instructions and Accounting Practices and Procedures Manual of the NAIC.

(vii) Maintain a trust fund in a qualified United States financial institution for the payment of valid claims of its United States policyholders and ceding insurers, their assigns and successors in interest. The trust shall be in an amount not less than the group's several liabilities attributable to business ceded by United States ceding insurers to any member of the group pursuant to reinsurance contracts issued in the name of the group. The group shall maintain a joint trusteed surplus of which \$100 million shall be held jointly for the benefit of United States ceding insurers of any member of the group as additional security for the liabilities. Each member of the group shall make available to the Commissioner an annual certification of the member's solvency by the member's domiciliary regulator and its independent public accountant.

(viii) Agree to the requirements of this subparagraph in the reinsurance agreements. This subparagraph is not intended to conflict with or override the obligation of the parties to a reinsurance agreement to arbitrate their disputes, if an obligation is created in the agreement.

(A) In the event of the failure of the assuming insurer to perform its obligations under the terms of the reinsurance agreement, at the request of the ceding insurer the assuming insurer shall:

(I) Submit to the jurisdiction of a court of competent jurisdiction in a state of the United States.

(II) Comply with requirements necessary to give the court jurisdiction.

(III) Abide by the final decision of the court or of an appellate court in the event of an appeal.

(B) The assuming insurer shall designate a person as its true and lawful agent upon whom may be served a lawful process in an action, suit or proceeding instituted by or on behalf of the ceding company.

(5) Credit will be allowed when the reinsurance is ceded to an assuming insurer that has been certified by the Commissioner as a reinsurer in this Commonwealth in accordance with the requirements of section 161.3a and secures its obligations in accordance with the requirements of section 161.3b.

(6) Credit will be allowed when the reinsurance is ceded to an assuming insurer that is not a qualified reinsurer in an amount not exceeding the liabilities carried by the ceding insurer in accordance with the requirements of 40 P.S. §442.1(b).

§ 161.3a Requirements for Certified Reinsurers

(a) In order to be eligible for certification as a certified reinsurer, the assuming insurer shall meet the following requirements:

(1) The assuming insurer shall be domiciled and licensed to transact insurance or reinsurance in a qualified jurisdiction.

(i) In accordance with reporting and notification requirements that may be established by the NAIC, the Commissioner will create a list of qualified jurisdictions, which will be published annually in the Pennsylvania Bulletin.

(ii) U.S. jurisdictions that meet the requirement for accreditation under the NAIC financial standards and accreditation program shall be recognized as qualified jurisdictions.

(iii) To determine whether the domiciliary jurisdiction of an alien assuming insurer is eligible to be recognized as a qualified jurisdiction, the Commissioner will evaluate:

A. The appropriateness and effectiveness of the reinsurance supervisory system of the jurisdiction, both initially and on an ongoing basis.

B. The rights, benefits and the extent of reciprocal recognition afforded by the non-U.S. jurisdiction to reinsurers licensed and domiciled in the U.S.

C. Whether the jurisdiction is a qualified jurisdiction as determined by the NAIC through the Committee Process. If the Commissioner approves a jurisdiction as qualified

that does not appear on the NAIC's list of qualified jurisdictions, the Commissioner will provide thoroughly documented justification of reasons therefore.

D. The framework under which the assuming insurer is regulated.

E. The structure and authority of the domiciliary regulator with regard to solvency regulation requirements and financial surveillance.

F. The substance of financial and operating standards for assuming insurers in the domiciliary jurisdiction.

G. The form and substance of financial reports required to be filed or made publicly available by reinsurers in the domiciliary jurisdiction and the accounting principles used.

H. The domiciliary regulator's willingness to cooperate with U.S. regulators in general and the Commissioner in particular.

I. The history of performance by assuming insurers in the domiciliary jurisdiction.

J. Any relevant international standards or guidance with respect to mutual recognition of reinsurance supervision adopted by the International Association of Insurance Supervisors or successor organization.

(iv) A domiciliary jurisdiction of an alien assuming insurer is not eligible to be recognized as a qualified jurisdiction unless:

A. The jurisdiction has agreed to share information and cooperate with the Commissioner with respect to all certified reinsurers domiciled within that jurisdiction.

B. The jurisdiction adequately and promptly enforce final U.S. judgments and arbitration awards.

(v) If a certified reinsurer's domiciliary jurisdiction ceases to be a qualified jurisdiction, the Commissioner may withdraw recognition of that jurisdiction.

(2) The assuming insurer shall maintain minimum capital and surplus, or its equivalent, in an amount to be determined acceptable by the Commissioner in accordance with the following standards:

(i) The assuming insurer must maintain capital and surplus, or its equivalent, of no less than \$250,000,000 calculated in accordance with subparagraph (ii) This requirement

may also be satisfied by an association including incorporated and individual unincorporated underwriters having minimum capital and surplus equivalents (net of liabilities) of at least \$250,000,000 and a central fund containing a balance of at least \$250,000,000.

(ii) Certified reinsurers not domiciled in the U.S., must file with the Commissioner audited financial statements, (audited U.S. GAAP basis if available, audited IFRS basis statements are allowed but must include an audited footnote reconciling equity and net income to a U.S. GAAP basis, or, with the permission of the state insurance commissioner, audited IFRS statements with reconciliation to U.S. GAAP certified by an officer of the company), regulatory filings, and actuarial opinion (as filed with the non-U.S. jurisdiction supervisor). Upon the initial application for certification, the Commissioner will consider audited financial statements for the last three years filed with its non-U.S. jurisdiction supervisor.

(3) The assuming insurer must maintain financial strength ratings from two or more rating agencies deemed acceptable by the Commissioner in accordance with subparagraph (i) and be rated by the Commissioner in accordance with subparagraph (ii).

(i) The financial strength ratings must be based on interactive communication between the rating agency and the assuming insurer and may not be based solely on publicly available information. These ratings will be one factor used by the Commissioner in determining the rating assigned pursuant to subparagraph (ii). Acceptable rating agencies include: Standard & Poor's, Moody's Investors Service, Fitch Ratings A.M. Best Company or any other Nationally Recognized Statistical Rating Organization.

(ii) The Commissioner will assign a rating to each certified reinsurer and shall publish a list of all certified reinsurers and their ratings annually in the Pennsylvania Bulletin in accordance with the following:

A. Each certified reinsurer shall be rated on a legal entity basis, with due consideration being given to the group rating where appropriate, except that an association including incorporated and individual unincorporated insurers that have been approved to do business as a single certified reinsurer may be evaluated on the basis of its group rating.

B. Factors that may be considered as part of the evaluation process include the following:

I. The certified reinsurer's financial strength rating from an acceptable rating agency. The maximum rating that a certified reinsurer may be assigned will correspond to its financial strength rating as outlined in the table below. The Commissioner will use the lowest financial strength rating received from an approved rating agency in establishing the maximum rating of a certified reinsurer. A failure to obtain or maintain at least two

financial strength ratings from acceptable rating agencies will result in loss of eligibility for certification.

<u>Ratings</u>	<u>Best</u>	<u>S&P</u>	<u>Moody's</u>	<u>Fitch</u>
Secure – 1	A++	AAA	Aaa	AAA
Secure – 2	A+	AA+, AA, AA-	Aa1, Aa2, Aa3	AA+, AA, AA-
Secure – 3	A	A+, A	A1, A2	A+, A
Secure – 4	A-	A-	A3	A-
Secure – 5	B++, B+	BBB+, BBB, BBB-	Baa1, Baa2, Baa3	BBB+, BBB, BBB-
Vulnerable – 6	B, B-C++, C+, C, C-, D, E, F	BB+, BB, BB-, B+, B, B-, CCC, CC, C, D, R	Ba1, Ba2, Ba3, B1, B2, B3, Caa, Ca, C	BB+, BB, BB-, B+, B, B-, CCC+, CC, CCC-, DD

II. The business practices of the certified reinsurer in dealing with its ceding insurers, including its record of compliance with reinsurance contractual terms and obligations.

III. For certified reinsurers domiciled in the U.S., a review of the most recent applicable NAIC Annual Statement Blank, either Schedule F (for property/casualty reinsurers) or Schedule S (for life and health reinsurers).

IV. For certified reinsurers not domiciled in the U.S., a review annually of Form CR-F (for property/casualty reinsurers) or Form CR-S (for life and health reinsurers) as developed by the NAIC.

V. The reputation of the certified reinsurer for prompt payment of claims under reinsurance agreements, based on an analysis of ceding insurers' Schedule F reporting of overdue reinsurance recoverables, including the proportion of obligations that are more than 90 days past due or are in dispute, with specific attention given to obligations payable to companies that are in administrative supervision or receivership.

VI. Regulatory actions against the certified reinsurer.

VII. The report of the independent auditor on the financial statements of the insurance enterprise, on the basis described in subclause VIII.

VIII. For certified reinsurers not domiciled in the U.S., audited financial statements, (audited U.S. GAAP basis if available, audited IFRS basis statements are allowed but must include an audited footnote reconciling equity and net income to a U.S. GAAP basis, or, with the permission of the state insurance commissioner, audited IFRS statements with reconciliation to U.S. GAAP certified by an officer of the company), regulatory filings, and actuarial opinion (as filed with the non-U.S. jurisdiction supervisor). Upon the initial application for certification, the Commissioner will consider audited financial statements for the last three years filed with its non-U.S. jurisdiction supervisor.

IX. The liquidation priority of obligations to a ceding insurer in the certified reinsurer's domiciliary jurisdiction in the context of an insolvency proceeding.

X. A certified reinsurer's participation in any solvent scheme of arrangement, or similar procedure, which involves U.S. ceding insurers. The Commissioner shall receive prior notice from a certified reinsurer that proposes participation by the certified reinsurer in a solvent scheme of arrangement.

(iii) Change in Rating or Revocation of Certification.

A. In the case of a downgrade by a rating agency or other disqualifying circumstance, the Commissioner shall upon written notice assign a new rating to the certified reinsurer in accordance with the requirements of clause (a)(3)(ii)(B).

B. The Commissioner shall have the authority to suspend, revoke, or otherwise modify a certified reinsurer's certification in accordance with the procedures set forth in section 161.6 at any time if the certified reinsurer fails to meet its obligations or security requirements under this section, or if other financial or operating results of the certified reinsurer, or documented significant delays in payment by the certified reinsurer, lead the

Commissioner to reconsider the certified reinsurer's ability or willingness to meet its contractual obligations.

C. If the rating of a certified reinsurer is upgraded by the Commissioner, the certified reinsurer may meet the security requirements applicable to its new rating on a prospective basis, but the Commissioner shall require the certified reinsurer to post security under the previously applicable security requirements as to all contracts in force on or before the effective date of the upgraded rating. If the rating of a certified reinsurer is downgraded by the Commissioner, the Commissioner shall require the certified reinsurer to meet the security requirements applicable to its new rating for all business it has assumed as a certified reinsurer.

(4) The assuming insurer must agree to submit to the jurisdiction of this Commonwealth, appoint the Commissioner as its agent for service of process in this state, and agree to provide security for 100% of the assuming insurer's liabilities attributable to reinsurance ceded by U.S. ceding insurers if it resists enforcement of a final U.S. judgment. The assuming insurer must submit a properly executed Form CR-1 as evidence of its submission to the jurisdiction of this Commonwealth, appointment of the Commissioner as an agent for service of process in this state, and agreement to provide security for 100% of the assuming insurer's liabilities attributable to reinsurance ceded by U.S. ceding insurers if it resists enforcement of a final U.S. judgment. The Commissioner may not certify any assuming insurer that is domiciled in a jurisdiction that the Commissioner has determined does not adequately and promptly enforce final U.S. judgments or arbitration awards.

(5) The assuming insurer shall agree to meet applicable information filing requirements both with respect to an initial application for certification and on an ongoing basis. All information submitted by certified reinsurers that is not otherwise public information subject to disclosure shall be confidential and privileged and shall not be subject to subpoena, discovery, the act of February 14, 2008 (P.L. 6, No. 3), known as the "Right-to-Know Law," or admissible in evidence in any private civil action. The applicable information filing requirements are:

(i) Notification within ten days of any regulatory actions taken against the certified reinsurer, any change in the provisions of its domiciliary license or any change in rating by an approved rating agency, including a statement describing such changes and the reasons therefore;

(ii) Annual submission of Form CR-F or CR-S, as applicable as per NAIC instructions.

(iii) Annual submission of the report of the independent auditor on the financial statements of the insurance enterprise, on the basis described in subparagraph (iv) below.

(iv) Annual submission of audited financial statements (audited U.S. GAAP basis if available, audited IFRS basis statements are allowed but must include an audited footnote reconciling equity and net income to a U.S. GAAP basis, or, with the permission of the state insurance commissioner, audited IFRS statements with reconciliation to U.S. GAAP certified by an officer of the company), regulatory filings, and actuarial opinion (as filed with the certified reinsurer's supervisor). Upon the initial certification, audited financial statements for the last 3 years filed with the certified reinsurer's supervisor.

(v) At least annually, filing of an updated list of all disputed and overdue reinsurance claims regarding reinsurance assumed from U.S. domestic ceding insurers;

(vi) A certification from the certified reinsurer's domestic regulator that the certified reinsurer is in good standing and maintains capital in excess of the jurisdiction's highest regulatory action level.

(b) In addition to meeting the requirements of subsection (a), an association, including incorporated and individual unincorporated insurers, may be a certified reinsurer if it satisfies the following additional requirements:

(1) The association shall satisfy its minimum capital and surplus requirements through the capital and surplus equivalents (net of liabilities) of the association and its members, which shall include a joint central fund that may be applied to any unsatisfied obligation of the association or any of its members, in an amount determined by the Commissioner to provide adequate protection.

(2) The incorporated members of the association may not be engaged in any business other than underwriting as a member of the association and shall be subject to the same level of regulation and solvency control by the association's domiciliary regulator as are the unincorporated members.

(3) Within 90 days after its financial statements are due to be filed with the association's domiciliary regulator, the association shall provide to the Commissioner an annual certification by the association's domiciliary regulator of the solvency of each

insurer member; or if a certification is unavailable, financial statements, prepared by independent public accountants, of each insurer member of the association.

(c) If an applicant for certification has been certified as a reinsurer in an NAIC accredited jurisdiction, the Commissioner has the discretion to defer to that jurisdiction's certification, and has the discretion to defer to the rating assigned by that jurisdiction, and such assuming insurer will be considered to be a certified reinsurer in this state in accordance with the following:

(1) The assuming insurer shall submit a properly executed Form CR-1 to the Commissioner.

(2) Any change in the certified reinsurer's status or rating in the other jurisdiction shall apply automatically in this Commonwealth as of the date it takes effect in the other jurisdiction. The certified reinsurer shall notify the Commissioner of any change in its status or rating within ten days after receiving notice of the change.

(3) The Commissioner may withdraw recognition of the other jurisdiction's rating at any time and assign a new rating in accordance with subparagraph (a)(3)(ii).

(4) The Commissioner may withdraw recognition of the other jurisdiction's certification at any time, with written notice to the certified reinsurer. Unless the Commissioner revokes the certified reinsurer's certification in accordance with section 161.6 the certified reinsurer's certification shall remain in good standing in this State for a period of three months, which shall be extended if additional time is necessary to consider the assuming insurer's application for certification in this State.

(d) A certified reinsurer that ceases to assume new business in this Commonwealth may request to maintain its certification in inactive status in order to continue to qualify for a reduction in security for its in-force business. An inactive certified reinsurer shall continue to comply with all applicable requirements of this section and the Commissioner will assign a rating that takes into account, if relevant, the reasons why the reinsurer is not assuming new business.

(e) Certification procedure.

(1) The Department will post notice of any application for certification in the Pennsylvania Bulletin promptly upon receipt and will include instructions on how members of the public may respond to the application. The Commissioner may not take final action on the application until at least 30 days after posting the notice required by this paragraph.

(2) If the Department is satisfied that an assuming insurer has met the conditions for certification and determines to designate the assuming insurer as a certified reinsurer, the Department will issue written notice of the designation to the assuming insurer. Included in such notice shall be the rating assigned the certified reinsurer in accordance with 161.3a(a)(3)(ii).

§161.3b Calculation of credit for reinsurance regarding obligations secured with certified reinsurers

(a) In order for a domestic ceding insurer to qualify for full financial statement credit for reinsurance ceded to a certified reinsurer, the certified reinsurer must maintain security in a form acceptable to the Commissioner and consistent with the provisions of 40 P.S. §442.1(b) or in a multibeneficiary trust in accordance with section 161.3(3)(vii)(B) except that:

(1) If a certified reinsurer maintains a trust to fully secure its obligations subject to section 161.3(3)(vii) and chooses to secure its obligations incurred as a certified reinsurer in the form of a multibeneficiary trust, the certified reinsurer shall maintain separate trust accounts for its obligations incurred under reinsurance agreements issued or renewed as a certified reinsurer with reduced security as permitted by this paragraph or comparable laws of other U.S. jurisdictions and for its obligations subject to 161.3(3)(vii)(B) It shall be a condition to the grant of certification under this subsection that the certified reinsurer shall have bound itself, by the language of the trust and agreement with the chief regulatory official with principal regulatory oversight of each such trust account, to fund, upon termination of any such trust account, out of the remaining surplus of such trust any deficiency of any other such trust account.

(2) The minimum trusted surplus requirements provided in 161.3(3)(vii) are not applicable with respect to a multibeneficiary trust maintained by a certified reinsurer for the purpose of securing obligations incurred under this paragraph, except that such trust shall maintain a minimum trusted surplus of \$10,000,000.

(b) The allowable credit allowed a ceding insurer shall be based upon the security held by or on behalf of the ceding insurer and shall be calculated in accordance with the following requirements:

(1) In order for full credit to be allowed, the amount of security must correspond with the rating assigned by the Commissioner to the certified reinsurer pursuant to section 161.3a(a)(3) as follows:

<u>Rating:</u>	<u>Security required:</u>
<u>Secure – 1</u>	<u>0%</u>

<u>Secure – 2</u>	<u>10%</u>
<u>Secure – 3</u>	<u>20%</u>
<u>Secure – 4</u>	<u>50%</u>
<u>Secure – 5</u>	<u>75%</u>
<u>Vulnerable – 6</u>	<u>100%</u>

(2) Affiliated reinsurance transactions will receive the same opportunity for reduced security requirements as all other reinsurance transactions.

(3) The Commissioner will require the certified reinsurer to post 100% for the benefit of the ceding insurer or its estate, security upon the entry of an order of rehabilitation, liquidation or conservation against the ceding insurer.

(4) In order to facilitate the prompt payment of claims, a certified reinsurer may not be required to post security for catastrophe recoverables for a period of one year from the date of the first instance of a liability reserve entry by the ceding company as a result of a loss from a catastrophic occurrence as recognized by the Commissioner. The one year deferral period is contingent upon the certified reinsurer continuing to pay claims in a timely manner in compliance with its contractual obligations as set forth in the reinsurance agreement under which the claims are ceded. Reinsurance recoverables for only the following lines of business as reported on the NAIC annual financial statement related specifically to the catastrophic occurrence will be included in the deferral:

- Line 1: Fire**
- Line 2: Allied Lines**
- Line 3: Farmowners multiple peril**
- Line 4: Homeowners multiple peril**
- Line 5: Commercial multiple peril**
- Line 9: Inland Marine**
- Line 12: Earthquake**
- Line 21: Auto physical damage**

(c) With respect to obligations incurred by a certified reinsurer, if the security is insufficient, the Commissioner will reduce the allowable credit by an amount proportionate to the deficiency, and has the discretion to impose further reductions in allowable credit upon finding that there is a material risk that the certified reinsurer's obligations will not be paid in full when due.

(d) For purposes of calculating the allowable credit pursuant to this section, a certified reinsurer whose certification has been terminated for any reason shall be treated as a certified reinsurer required to secure 100% of its obligations.

(1) As used in this subsection, the term “terminated” refers to revocation, suspension, voluntary surrender and inactive status.

(2) If the Commissioner continues to assign a higher rating as permitted by other provisions of this section, this requirement does not apply to a certified reinsurer in inactive status or to a reinsurer whose certification has been suspended.

(e) Based on the analysis conducted under section 161.3a(a)(3)(ii)(B)(V) of a certified reinsurer’s reputation for prompt payment of claims, the Commissioner may make appropriate adjustments in the security the certified reinsurer is required to post to protect its liabilities to U.S. ceding insurers, provided that the Commissioner will, at a minimum, increase the security the certified reinsurer is required to post by one rating level under §161.3a(b)(1) if the Commissioner finds either of the following:

A. More than 15% of the certified reinsurer’s ceding insurance clients have overdue reinsurance recoverables on paid losses of 90 days or more which are not in dispute and which exceed \$100,000 for each cedent.

B. The aggregate amount of reinsurance recoverables on paid losses not in dispute that are overdue by 90 days or more exceeds \$50,000,000.

(f) Nothing in this section shall prohibit the parties to a reinsurance agreement from agreeing to provisions establishing security requirements that exceed the minimum security requirements under this section or under section 161.8a.

§161.3c. Concentration Risk.

(a) A ceding insurer shall take steps to manage its reinsurance recoverables proportionate to its own book of business. A domestic ceding insurer shall notify the Commissioner within 30 days after reinsurance recoverables from any single assuming insurer, or group of affiliated assuming insurers, exceed 50% of the domestic ceding insurer’s last reported surplus to policyholders, or after it is determined that reinsurance recoverables from any single assuming insurer or group of affiliated assuming insurers is likely to exceed this limit. The notification must demonstrate that the exposure is safely managed by the domestic ceding insurer.

(b) A ceding insurer shall take steps to diversify its reinsurance program. A domestic ceding insurer shall notify the Commissioner within 30 days after ceding to any single assuming insurer, or group of affiliated assuming insurers, more than 20% of the ceding insurer's gross written premium in the prior calendar year, or after it has determined that the reinsurance ceded to any single assuming insurer, or group of affiliated assuming insurers is likely to exceed this limit. The notification must demonstrate that the exposure is safely managed by the domestic ceding insurer.

§ 161.4. Trust fund requirements.

(a) A trust required under § 161.3(3) or (4) (relating to credit for reinsurance) shall be established and maintained in a form approved by the Commissioner. The trust instrument shall provide that contested claims shall be valid and enforceable out of funds in trust to the extent remaining unsatisfied 30 days after entry of the final order of a court of competent jurisdiction in the United States. The trust shall vest legal title to its assets in the trustees of the trust for the benefit of the grantor's United States policyholders and ceding insurers, their assigns and successors in interest. The trust and the assuming insurer shall be subject to examination as determined by the Commissioner. The trust described in this section shall remain in effect for as long as the assuming insurer or a member or former member of a group of insurers shall have outstanding obligations due under reinsurance agreements subject to the trust.

(b) By February 28 of each year, the trustees of a trust established to comply with § 161.3(3) or (4) shall report to the Commissioner in writing setting forth the balance of the trust and listing the trust's investments at the preceding year's end and shall certify the date of termination of the trust, if so planned, or certify that the trust will not expire prior to the next following December 31. The assuming insurer shall annually submit a financial exhibit which quantifies the liabilities attributable to business directly written or assumed in the United States.

(c) An amendment to the trust will not be effective unless reviewed and approved in advance by the Commissioner.

§ 161.5. Determination of reinsurer qualification.

(a) Applications for designation as a qualified reinsurer shall be submitted by the assuming insurer and shall be accompanied by a properly executed Form QR-1 as provided in Appendix A (relating to Form QR-1 Certificate of Assuming Insurer).

(b) If the Department is satisfied that an assuming insurer has met the conditions for qualification and determines to designate the assuming insurer as a qualified reinsurer, the Department will issue written notice of the designation to the assuming insurer and include the insurer on a list of qualified reinsurers published and periodically reviewed by the Commissioner.

(c) If the Department determines that qualification will be denied, the Department will issue written notice of denial to the assuming insurer. The assuming insurer may request a hearing to review the Department's denial. The hearing will be held in accordance with 2 Pa.C.S. §§ 501—508 and 701—704 (relating to the Administrative Agency Law) and 1 Pa. Code Part II (relating to the general rules of administrative practice and procedure).

§ 161.6. Revocation of reinsurer qualification or certification.

(a) If the Department determines that a [qualified] reinsurer has failed to continue to meet one or more of the conditions for qualification **or certification**, the Commissioner may upon written notice and hearing revoke its qualification **or certification** and remove it from the published list of qualified **or certified** reinsurers.

(b) If an assuming insurer's qualification has been revoked by the Commissioner after notice, a ceding insurer shall be allowed to continue to take credit for reinsurance ceded to the assuming insurer until the end of the contract year or 1 year from the date of the revocation, whichever time is less, but in no event less than 6 months.

(b.1) If an assuming insurer's certification has been revoked by the Commissioner, the assuming insurer shall be required to post security in accordance with 40 P.S. §442.1(b) in order for the ceding insurer to continue to take credit for reinsurance ceded to the assuming insurer. If funds continue to be held in trust in accordance with § 161.4 the Commissioner may allow additional credit equal to the ceding insurer's pro rata share of such funds, discounted to reflect the risk of un-collectability and anticipated expenses of trust administration. Notwithstanding the change of a certified reinsurer's rating or revocation of its certification, a domestic insurer that has ceded reinsurance to that certified reinsurer may not be denied credit for reinsurance for a period of three months for all reinsurance ceded to that certified reinsurer, unless the reinsurance is found by the Commissioner to be at high risk of un-collectability.

(c) If a modification, amendment or revision to an existing reinsurance agreement, which increases the risk reinsured, takes place after an assuming insurer's qualification **or certification** has been revoked, credit will not be allowed a ceding insurer for additional risks ceded after the date and directly resulting from the modification, amendment or revision.

(d) Notwithstanding the provisions of subsections (b) and (c), a ceding insurer may continue to take credit for reinsurance ceded before the date of the revocation of the assuming insurer's qualification with respect to a risk covered by the reinsurance agreement during the time the assuming insurer's qualification was in effect.

§ 161.7. Credit for joint underwriting or pooling arrangements.

(a) Domestic ceding insurers which are participating in a joint underwriting or joint reinsurance pooling arrangement, in which the insurers participating in the arrangement are not qualified **or**

certified reinsurers, may request specific approval by the Commissioner to take reserve credit for reinsurance ceded under those arrangements.

(b) The Commissioner may specify what information is required to be filed with respect to the participants in the arrangement to determine whether credit shall be allowed.

(c) In determining whether credit will be allowed under this section, the Commissioner will consider:

(1) The amount of risk ceded under the arrangement to reinsurers which are either qualified reinsurers under this chapter or which are licensed to transact insurance or reinsurance in this State.

(2) The financial condition and state of domicile of the participants.

(3) The length of time the agreement has been in force and the effect of the agreement on the participants.

(4) The type of risk being reinsured by the pool and the maximum per risk exposure of the pool.

(5) The management and control of the operations of the pool.

(6) Other information the Commissioner may prescribe.

§ 161.8. [Credit for reinsurance ceded to alien nonaffiliated insurers which write no primary coverages in the United States.

(a) This section applies to reinsurance ceded by a domestic ceding insurer to an alien nonaffiliated assuming insurer which:

(1) Writes no primary coverages in the United States and thereby is not eligible for consideration for inclusion on the Non-Admitted Insurers Listing published by the Non-Admitted Insurers Information Office of the NAIC, or a successor list.

(2) Has not provided security in full for the ceded recoverables under section 318.1(b) of the act (40 P. S. § 442.1).

(3) Is authorized in its domiciliary jurisdiction to assume the kinds of insurance ceded thereto.

(b) When a domestic ceding insurer cedes reinsurance to an alien nonaffiliated assuming insurer which meets the criteria in subsection (a), referred to in this section as an “unauthorized alien assuming insurer,” credit will be allowed for the amount of unsecured ceded reinsurance recoverables by a deduction from liability, not to exceed in the aggregate 10% of the ceding insurer’s policyholders surplus, only when the following conditions are met:

(1) The ceding insurer establishes an unauthorized reinsurance reserve which is a percentage of the unsecured ceded reinsurance recoverable from the unauthorized alien assuming insurers for which credit for reinsurance is taken as permitted in this section. The percentage shall be equal to the greatest of one of the following:

(i) The largest percentage of uncollectible ceded unauthorized reinsurance experienced by the ceding insurer during any one of the last 5 full calendar years, as measured by dividing the amount of reinsurance recoverables due and payable to the ceding insurer for that calendar year from the unauthorized alien assuming insurers, over 90 days past due and not in dispute, by the amount of reinsurance recoverables due and payable to the ceding insurer and actually collected by the ceding insurer for that same calendar year from unauthorized alien assuming insurers.

(ii) The largest percentage of unearned premiums ceded by the ceding insurer to any one unauthorized alien assuming insurer as measured at the end of the last previous calendar year by dividing the amount of the calendar year-end unearned premium reserve ceded to each unauthorized alien assuming insurer by the total amount of the unearned premium reserve ceded to unauthorized alien assuming insurers.

(iii) Fifteen percent.

(2) The unauthorized alien assuming insurer provides to and maintains authorized security with the ceding insurer for ceded reinsurance recoverables under section 319.1(b) of the act (40 P. S. § 442.1(b)) in an amount at least equal to 110% of the unearned premium and known case outstanding reserves for loss and allocated loss adjustment expense ceded to the unauthorized alien assuming insurer by the ceding insurer.

(3) The unauthorized alien assuming insurer maintains adjusted shareholder funds of at least \$20 million.

(4) The unauthorized alien assuming insurer maintains an acceptable level of premium writing in relation to its adjusted shareholder funds that does not exceed a net written premium to adjusted shareholder funds ratio of 3:1.

(5) The unauthorized alien assuming insurer is included in the Insurance Solvency International (ISI) classic database and does not fail more than four of the nine ISI tests.

(6) The ceding insurer limits the maximum amount of liability for loss with respect to any one risk ceded to any one unauthorized alien assuming insurer to 10% of the unauthorized alien assuming insurer's adjusted shareholder funds and limits the aggregate premium cession to the assuming insurer to 20% of the unauthorized alien assuming insurer's adjusted shareholder funds.

(7) The reinsurance agreements between the unauthorized alien assuming insurer and the ceding insurer contain:

(i) An agreement by the unauthorized alien assuming insurer that, in the event of the failure of the unauthorized alien assuming insurer to perform its obligations under the terms of the reinsurance agreement, the unauthorized alien assuming insurer, at the request of the ceding insurer, shall submit to the jurisdiction of any court of competent jurisdiction in a state in the United States, comply with requirements necessary to give that court jurisdiction and abide by the final decision of that court or of an appellate court in the event of an appeal. The provision does not override an agreement between the ceding insurer and the unauthorized alien assuming reinsurer to arbitrate.

(ii) An agreement by the unauthorized alien assuming insurer to designate a person as its true and lawful agent upon whom may be served any lawful process in an action, suit or proceeding instituted by or on behalf of the ceding insurer.

(iii) An insolvency clause as provided for in section 319.1(d) of the act.

(8) The unauthorized alien assuming insurer substantially meets other reasonable standards of solvency as may be established from time to time by the Commissioner.

(9) The credit claimed for reinsurance recoverable under this section is supported by proper and appropriate records maintained by the ceding insurer as to:

(i) The solvency of the unauthorized alien assuming insurer, including ISI reports and test results.

(ii) Documentation necessary to demonstrate for purposes of financial examinations conducted by the Department that the conditions of this section have been met for reserve credit taken under this section.

(10) The ceding insurer files with the Department annually within 30 days of the filing by the ceding insurer of its annual statutory financial statement a ceded reinsurance report, as prescribed by the Commissioner, with respect to the credit for reinsurance taken under this section. The report shall include a certification by the chief financial officer of the ceding insurer that the credit for reinsurance meets the requirements of this section.

(11) The ceding insurer promptly provides for the necessary increase in its ceded reserves with respect to applicable reinsurance recoverables—that is, it eliminates the previous credit taken by the ceding insurer under this section for that unauthorized alien assuming insurer—and shall give immediate notice to the Department if:

(i) Obligations of an unauthorized alien assuming insurer for which credit for reinsurance was taken under this section are more than 90 days past due and not in dispute.

(ii) There is material indication or evidence that an unauthorized alien assuming insurer for which credit for reinsurance was taken under this section is failing to meet the standards in this section.

(c) For purposes of subsection (b)(11)(i), a claim in dispute is one in which one of the following applies:

(1) The ceding insurer or unauthorized alien assuming insurer has instituted arbitration or litigation proceedings in good faith over the issue of the recoverability of the loss or allocated loss adjustment expense.

(2) The ceding insurer has received a formal written communication from the unauthorized alien assuming insurer, within a time period specified in the reinsurance agreement, denying the validity of coverage for the loss or allocated loss adjustment expense.

(d) As used in this section, adjusted shareholder funds shall be as reported by ISI or other recognized National rating agency as the Commissioner may, from time to time, approve for purposes of compliance with this section.

(e) Subsection (b)(2)—(5) and (7) do not apply when reinsurance cessions are made by domestic ceding insurers to unauthorized alien assuming insurers of risks located in jurisdictions where the reinsurance is required by applicable law or regulation of that jurisdiction.] **Reserved.**

§161.8a Reinsurance Contracts.

A ceding insurer will not be granted a credit or allowed an asset or reduction from liability for reinsurance effected with assuming insurers meeting the requirements of this Chapter unless the reinsurance agreement includes the following provisions:

(1) A proper insolvency clause as provided for in section 319.1(d) of the act (40 P.S. §442.1(d)), which stipulates that reinsurance is payable directly to the liquidator or successor without diminution regardless of the status of the ceding company.

(2) A reinsurance intermediary clause, if applicable, which stipulates that the credit risk for the intermediary is carried by the assuming insurer.

(3) A mandatory funding clause requiring the certified reinsurer to provide and maintain security in an amount sufficient to avoid the imposition of any financial statement penalty on the ceding insurer for reinsurance ceded to the certified reinsurer.

§ 161.9. Application.

(a) Credit will be allowed when the reinsurance is ceded to an assuming insurer not meeting the requirements of this section or § 161.3 (relating to credit for reinsurance) with respect to the

insurance of risks located in jurisdictions if the reinsurance is required by applicable law or regulation of that jurisdiction. As used in this section, “jurisdiction” means a state, district or territory of the United States and a lawful national government.

(b) An insurer which has been designated as a qualified reinsurer prior to August 28, 1993, will have until August 28, 1995, to achieve compliance with this chapter or have its qualification revoked.

[(c) Credit for reinsurance will be allowed a foreign licensed ceding insurer as permitted by the laws or regulations of that insurer’s state of domicile if the laws or regulations are substantially similar to the NAIC model law relating to credit for reinsurance. In the absence of substantially similar laws or regulations, credit for reinsurance will be allowed under the requirements of this chapter.]



August 22, 2012

Mr. David Sumner
Executive Director
Independent Regulatory Review Comm.
333 Market Street, 14th Floor
Harrisburg, PA 17101

Re: Insurance Department Proposed Regulation No. 11-249

Dear Mr. Sumner:

Pursuant to Section 5(a) of the Regulatory Review Act, enclosed for your information and review is proposed regulation 31 Pa. Code, Chapter 161, Requirements for Qualified and Certified Reinsurers.

The proposed amendments to Chapter 161 are based upon recent amendments to model law and regulation developed by the National Association of Insurance Commissioners (NAIC) entitled "Credit for Reinsurance Model Law" (#785) "Credit for Reinsurance Model Regulation" (#786) respectively. These proposed regulations are part of the financial regulation standards the Department must meet in order to maintain its accreditation by the NAIC.

If you have any questions regarding this matter, please contact me at (717) 787-4429.

Sincerely yours,

A handwritten signature in black ink that reads "Peter J. Salvatore". The signature is written in a cursive style with a prominent initial "P".

Peter J. Salvatore
Regulatory Coordinator

TRANSMITTAL SHEET FOR REGULATIONS SUBJECT TO THE
REGULATORY REVIEW ACT

I.D. NUMBER: 11-249
SUBJECT: REQUIREMENTS FOR QUALIFIED AND CERTIFIED REINSURERS
AGENCY: DEPARTMENT OF INSURANCE


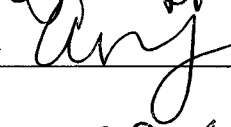
TYPE OF REGULATION

- X Proposed Regulation
Final Regulation
Final Regulation with Notice of Proposed Rulemaking Omitted
120-day Emergency Certification of the Attorney General
120-day Emergency Certification of the Governor
Delivery of Tolled Regulation
a. With Revisions b. Without Revisions

2012 AUG 22 AM 11:30

RECEIVED
IRRC

FILING OF REGULATION

DATE	SIGNATURE	DESIGNATION
8/21/12		HOUSE COMMITTEE ON INSURANCE MAJORITY CHAIRMAN <u>REP. NICHOLAS MICOZZIE</u>
8-22-12		SENATE COMMITTEE ON BANKING & INSURANCE MAJORITY CHAIRMAN <u>SEN. DONALD C. WHITE</u>
8-22-12	C. Schiel	INDEPENDENT REGULATORY REVIEW COMMISSION
8-22-12	C. Kennedy	ATTORNEY GENERAL (for Final Omitted only)
8/24/12	Steph J. Hoff	LEGISLATIVE REFERENCE BUREAU (for Proposed only)
8/22/12	Samuel Hansen	