

HOUSE OF REPRESENTATIVES STAFF ANALYSIS

BILL #: HB 733 Credit for Reinsurance
SPONSOR(S): Fetterhoff
TIED BILLS: **IDEN./SIM. BILLS:** SB 728

REFERENCE	ACTION	ANALYST	STAFF DIRECTOR or BUDGET/POLICY CHIEF
1) Insurance & Banking Subcommittee	16 Y, 0 N	Fortenberry	Luczynski
2) State Administration & Technology Appropriations Subcommittee			
3) Commerce Committee			

SUMMARY ANALYSIS

Reinsurance is a transaction between a primary insurer (ceding insurer) and a reinsurer (assuming insurer) whereby the assuming insurer agrees to cover all or part of the ceding insurer's losses or loss adjustment expenses in exchange for a premium. Because of the impact of hurricanes in Florida, the catastrophe protection provided by reinsurance is a significant reason for ceding insurers' purchase of reinsurance within the state. Most reinsurance that United States (U.S.) ceding insurers acquire is placed with non-U.S. assuming insurers. Because state insurance regulators do not regulate non-U.S. insurers or assuming insurers, the purchase of reinsurance by Florida insurers from such non-U.S. companies provides concern and challenges for state insurance regulators. Depending on their status within Florida, assuming insurers may be authorized or unauthorized. When an assuming insurer is an unauthorized assuming insurer within Florida, the Florida Office of Insurance Regulation (OIR) does not have direct regulatory authority over that assuming insurer. In order to exercise some indirect regulatory authority over these assuming insurers, OIR limits the ceding insurer's credit for reinsurance unless the assuming insurer meets certain criteria. Credit for reinsurance means that a ceding insurer is permitted under statutory accounting rules to recognize the reinsurance as an asset or as a reduction from liability for the amount of the ceded liability or risk transferred.

The bill amends the reinsurance law to add criteria that an assuming insurer must meet in order for a ceding insurer to be given credit for reinsurance. These criteria include having its head office or its domicile, and being licensed in, a reciprocal jurisdiction, maintaining minimum capital and surplus, meeting minimum solvency or capital ratios, providing prompt notice to OIR if it falls below minimum requirements or has legal action taken against it, responding to OIR's document requests, and maintaining a practice of prompt payment of claims. The bill also specifies certain elements that an assuming insurer must include in its reinsurance agreements in order for the ceding insurer to take credit for reinsurance. The bill requires that an assuming insurer's regulatory authority confirm to OIR that the assuming insurer has complied with the capital and surplus requirements and solvency or capital ratio requirements in the bill. It also establishes that a ceding insurer may only take credit for reinsurance agreements entered into, amended, or renewed on or after the date at which the assuming insurer has met the criteria in the bill. Additionally, OIR may suspend or revoke the assuming insurer's eligibility if the assuming insurer does not continue to meet the mandatory criteria.

If insurers are able to take credit for reinsurance for additional reinsurance transactions, they will be able to recognize additional assets or reductions in liability. The greater an insurer's assets or lower its liabilities, the higher the insurer's surplus. The insurer's surplus provides a measure of financial stability and provides a source of funds in the event that reserves are inadequate.

The bill has no impact on state or local government revenues or expenditures. It has no known direct economic impact on the private sector.

The bill has an effective date of July 1, 2021.

FULL ANALYSIS

I. SUBSTANTIVE ANALYSIS

A. EFFECT OF PROPOSED CHANGES:

Reinsurance

Reinsurance is a transaction between a ceding insurer¹ and an assuming insurer whereby the assuming insurer agrees to cover all or part of the ceding insurer's losses or loss adjustment expenses in exchange for a premium. The purposes of reinsurance include increasing capacity, stabilizing underwriting results, financing, providing catastrophe protection, withdrawing from a line or class of business, spreading risk, and obtaining expertise.² Because of the impact of hurricanes in Florida, the catastrophe protection provided by reinsurance is a significant reason for ceding insurers' purchase of reinsurance within the state. While the purchase of reinsurance creates a contractual relationship between the ceding insurer and the assuming insurer, it does not modify the relationship between the ceding insurer and its policyholders.³ Therefore, the ceding insurer remains obligated to pay policyholder claims and only the ceding insurer may recover from the assuming insurer unless an applicable reinsurance contract specifies otherwise.⁴

Most reinsurance that United States (U.S.) ceding insurers acquire is placed with non-U.S. assuming insurers. In fact, in 2018, offshore and non-U.S.-owned⁵ assuming insurers assumed 88.9 percent of insurance premiums ceded by U.S. insurers.⁶ The availability of non-U.S. reinsurance contributes to global diversification of risk, provides claims relief to U.S. insurers, and mitigates the financial impact of catastrophes.⁷ Even though reinsurance provides benefits, because the U.S. state insurance regulators do not regulate non-U.S. insurers or assuming insurers, the purchase of reinsurance by U.S. insurers from such non-U.S. companies provides concern and challenges for state insurance regulators.

Regulation of Reinsurance

Direct Regulation of Authorized Assuming Insurers and Credit for Reinsurance

Regulations and requirements for reinsurance transactions in Florida are provided in s. 624.610, F.S., and ch. 690-144, F.A.C. The Florida Office of Insurance Regulation (OIR)⁸, directly regulates authorized assuming insurers⁹ who are domiciled and licensed in Florida and assuming insurers licensed in Florida who are domiciled in other states.¹⁰ Under current law, if a Florida insurer cedes reinsurance to an assuming insurer who is authorized to transact insurance or reinsurance in Florida

¹ National Association of Insurance Commissioners, https://content.naic.org/consumer_glossary.htm#R (last visited Feb. 22, 2021). A ceding insurer is an insurer that transfers risk assumed from policyholders to an assuming insurer. The ceding insurer and assuming insurer may also be referred to as the primary insurer and the reinsurer, respectively. Reinsurance is also colloquially referred to as "insurance for insurers" because of the risk transfer from one insurer to another.

² National Association of Insurance Commissioners, https://content.naic.org/cipr_topics/topic_reinsurance.htm (last visited Feb. 22, 2021).

³ See IRMI, *In Defense of Reinsurance*, <https://www.irmi.com/articles/expert-commentary/in-defense-of-reinsurance> (last visited Feb. 22, 2021).

⁴ *Id.*

⁵ In the insurance context, a company formed under laws other than those of a U.S. jurisdiction is known as an alien insurer. See s. 624.06, F.S.

⁶ Reinsurance Association of America, *Offshore Reinsurance in the US Market: 2018 Data*, https://www.reinsurance.org/RAA/Industry_Data_Center/Offshore_Report/Offshore_Report_2018_Data.html (last visited Feb. 22, 2021).

⁷ International Association of Insurance Supervisors, *Reinsurance and Financial Stability*, <https://www.iaisweb.org/file/34046/reinsurance-and-financial-stability> (last visited Feb. 22, 2021).

⁸ Statutes also refer to OIR as the office.

⁹ Authorized assuming insurers are licensed or accredited to provide reinsurance in a particular state. See s. 624.610, F.S.

¹⁰ S. 624.610, F.S.

and meets other specified requirements, the ceding insurer is permitted to take credit for that reinsurance on its books.¹¹

Indirect Regulation of Unauthorized Assuming Insurers and Credit for Reinsurance

When an assuming insurer is not an authorized assuming insurer within Florida, OIR does not have direct regulatory authority over that assuming insurer. Pursuant to s. 624.610, F.S., and in order to exercise some indirect regulatory authority over these assuming insurers, OIR limits the ceding insurer's credit for reinsurance unless the assuming insurer posts acceptable collateral or security in the amount of the assuming insurer's obligations under the reinsurance agreement.¹²

National Association of Insurance Commissioners

National Association of Insurance Commissioners Authority, Accreditation, and Model Laws

The National Association of Insurance Commissioners (NAIC) is a "standard-setting and regulatory support organization created and governed by the chief insurance regulators from the 50 states, the District of Columbia, and five U.S. territories."¹³ While the NAIC does not have actual regulatory authority, it allows state regulators to establish standards and best practices, to engage in peer review, and to coordinate regulatory oversight.

The NAIC also maintains an accreditation program that considers key financial authorities and responsibilities of state insurance regulators that warrant national consistency among jurisdictions in order to improve oversight of multi-state insurers and reduce the cost of inefficiencies that is passed on to policyholders.¹⁴ As of November 2019, all 50 states, the District of Columbia and Puerto Rico were accredited by the NAIC.¹⁵

The NAIC develops model laws and regulations to promote uniformity among jurisdictions and to balance the needs of insurers operating in multiple jurisdiction with those of the applicable regulatory frameworks.¹⁶ The model laws are considered best practices for insurance regulation and the accreditation program requires compliance with certain model laws, including those that are solvency related.¹⁷

Credit for Reinsurance Model Law and Regulation and the Covered Agreement

Among the NAIC model laws and regulations that have become part of the accreditation standards are the Credit for Reinsurance Model Law #785 and Credit for Reinsurance Model Regulation #786 (MLMR), amendments to which are designed to modernize reinsurance regulation in the U.S..¹⁸ In 2017, the U.S. entered the Bilateral Agreement Between the United States of America and the European Union on Prudential Measures Regarding Insurance and Reinsurance (Covered Agreement).¹⁹ In 2019, the NAIC made revisions to MLMR in response to the Covered Agreement. In

¹¹ Credit for reinsurance means that a ceding insurer is permitted under statutory accounting rules to recognize the reinsurance as an asset or as a reduction from liability for the amount of the ceded liability or risk transferred. IRMI, <https://www.irmi.com/term/insurance-definitions/credit-for-reinsurance> (last visited Feb. 26, 2021). See also s. 624.610(3), F.S.

¹² See s. 624.610(4), F.S.

¹³ National Association of Insurance Commissioners, https://content.naic.org/index_about.htm (last visited Feb. 26, 2021).

¹⁴ National Association of Insurance Commissioners, *State Legislative Brief The NAIC Accreditation Program*, https://www.naic.org/documents/cmte_legislative_liaison_brief_accreditation.pdf (last visited Feb. 26, 2021).

¹⁵ *Id.*

¹⁶ National Association of Insurance Commissioners, *NAIC Model Laws*, https://content.naic.org/cipr_topics/topic_naic_model_laws.htm (last visited Feb. 26, 2021).

¹⁷ National Association of Insurance Commissioners, *Accreditation*, https://content.naic.org/cipr_topics/topic_accreditation.htm (last visited Feb. 26, 2021).

¹⁸ National Association of Insurance Commissioners, *Revisions to the Credit for Reinsurance Model Law*, https://www.naic.org/documents/committees_e_reinsurance_related_reinsurance_model_law_160108.pdf (last visited Feb. 26, 2021).

¹⁹ U.S. Department of the Treasury, *U.S. – EU Covered Agreement*, <https://home.treasury.gov/policy-issues/financial-markets-financial-institutions-and-fiscal-service/federal-insurance-office/covered-agreements/us-eu-covered-agreement> (last visited Feb. 26, 2021). Covered agreements are authorized under 31 U.S.C. §§ 313–314, and are written bilateral or multilateral agreements regarding

part, the Covered Agreement commits the U.S. to phasing-out collateral requirements for European Union assuming insurers by 2022.²⁰ The Covered Agreement also exempts European Union assuming insurers from current U.S. domiciliary requirements by creating a classification known as a reciprocal jurisdiction.²¹

Effect of the Bill

The changes to MLMR as a result of the Covered Agreement, necessitate that existing Florida law regarding credit for reinsurance be amended. The bill creates a new subsections within the reinsurance statute regarding the circumstances under which ceding insurers can take credit for reinsurance. The bill establishes that a ceding insurer will *not* be permitted to take credit for reinsurance when an assuming insurer is not authorized or accredited to transact insurance or reinsurance in Florida *unless* the assuming insurer agrees to the following in its reinsurance agreements:

- If the assuming insurer fails to perform its obligations under the reinsurance agreement, and at the request of the ceding insurer, the assuming insurer shall submit to the jurisdiction of any U.S. court of competent jurisdiction, comply with the requirements necessary to give that court jurisdiction, and abide by the final decision of that court or any appellate court in the event of an appeal.
- Designate the Florida Chief Financial Officer as its agent to for service of process in a suit by a ceding insurer.

The bill also provides that credit for reinsurance must be allowed when reinsurance is ceded to an assuming insurer that meets all of the following criteria:

- The assuming insurer must be licensed in, and have its head office in or be domiciled in, a reciprocal jurisdiction.
- The assuming insurer must have minimum capital and surplus as calculated by the methodology of its domiciliary jurisdiction in the amount of \$250 million or in a greater amount specified by commission²² rule.
- The assuming insurer must have a minimum solvency or capital ratio as specified by the commission.
- The assuming insurer must agree to provide prompt written notice to OIR if it falls below the minimum requirements specified in the bill or if any regulatory action is taken against it for serious noncompliance with applicable law.
- The assuming insurer must consent in writing to:
 - submit to the jurisdiction of Florida courts;
 - designate the Florida Chief Financial Officer as its agent for service or process or an attorney to accept lawful process;
 - pay all final judgments declared enforceable in the jurisdiction where the judgments were obtained;
 - include a provision in each reinsurance agreement that, where necessary, the assuming insurer will provide security in the amount equal to 100 percent of the assuming insurer's liabilities attributable to reinsurance ceded pursuant to the agreement; and

insurance or reinsurance entered into between the U.S. and one or more foreign authorities to provide protections for insurance and reinsurance consumers similar to those provided by state insurance regulators within U.S. jurisdictions.

²⁰ U.S. Department of the Treasury, *Statement of the United States on the Covered Agreement with the European Union*, <https://ustr.gov/sites/default/files/files/US%20Covered%20Agreement.pdf> (last visited Feb. 26, 2021).

²¹ *Id.* Model Law #785 defines a reciprocal jurisdiction as:

- A non-U.S. jurisdiction that is subject to an in-force covered agreement with the U.S., each within its legal authority, or in the case of a covered agreement between the U.S. and the European Union, is a member state of the European Union;
- A U.S. jurisdiction that meets the requirements for accreditation under the NAIC financial standards and accreditation program;
- A qualified jurisdiction, as determined by an insurance commissioner.

National Association of Insurance Commissioners, *Credit for Reinsurance Model Law-785*, <https://www.naic.org/store/free/MDL-785.pdf> (last visited Feb. 26, 2021).

²² The commission referred to is the Financial Services Commission. Section 20.121(3), F.S., establishes that the Financial Services Commission consists of the Governor, the Attorney General, the Chief Financial Officer, and the Commissioner of Agriculture.

- confirm that the assuming insurer is not presently participating in any solvent scheme of arrangement²³ that involves Florida’s ceding insurers, and should the assuming insurer enter into such arrangement, it will notify OIR and the ceding insurer and will provide appropriate security.
- The assuming insurer must provide documentation to OIR upon request under criteria specified by the commission.
- The assuming insurer must maintain a practice of prompt payment of claims under reinsurance agreements pursuant to criteria specified by the commission.

The bill requires that an assuming insurer’s regulatory authority²⁴ confirm to OIR on an annual basis that the assuming insurer has complied with the capital and surplus requirements and solvency or capital ratio requirements set forth in the bill. It also establishes that a ceding insurer may only take credit for reinsurance agreements entered into, amended, or renewed on or after the date at which the assuming insurer has met the mandatory criteria set forth within the bill. Additionally, credit may only be taken for losses incurred and reserves reported on or after the later of the date upon which the assuming insurer has met these requirements or has entered into a new reinsurance agreement, amendment, or renewal with the ceding insurer.

Pursuant to the bill, if the ceding insurer is subject to rehabilitation, liquidation, or conservation, the ceding insurer may obtain a court order requiring that the assuming insurer post security for all outstanding ceded liabilities. If OIR determines that the assuming insurer no longer meets one or more of the requirements under the bill, OIR may revoke or suspend the assuming insurer’s eligibility under s. 624.610, F.S. While the eligibility is suspended, any reinsurance agreement issued, amended, or renewed after the effective date of the suspension does not qualify for credit for reinsurance. If the eligibility is revoked, credit for reinsurance may not be granted after the effective date of the revocation for any reinsurance agreements entered into by the assuming insurer, including those entered into before the date of the revocation.

The bill provides that the subsection created within s. 624.610, F.S., does not:

- preclude an assuming insurer from volunteering information to OIR;
- limit or alter the capacity of parties to a reinsurance agreement to agree on requirements for security or other terms of the reinsurance agreement, except where otherwise prohibited, or to renegotiate the reinsurance agreement; or
- authorize an assuming insurer to withdraw or reduce the security provided under any reinsurance agreement, except as authorized within the agreement.

The bill makes other technical changes to s. 624.610, F.S., including the deletion of an obsolete subsection and the replacement of the word “commissioner” with “office” in several places.

By allowing insurers to take credit for reinsurance for additional reinsurance transactions, the bill allows insurers to recognize additional assets or reductions in liability. The greater an insurer’s assets or lower its liabilities, the higher the insurer’s surplus. The insurer’s surplus provides a measure of financial stability and provides a source of funds in the event that reserves are inadequate.

B. SECTION DIRECTORY:

Section 1. Amends s. 624.610, F.S., relating to reinsurance.

Section 2. Provides an effective date of July 1, 2021.

²³ A solvent scheme of arrangement is an English statutory procedure that is used by a solvent company to bring finality to some or all of their insurance business, and by insolvent companies, as an alternative to liquidation. They involve running-off business and making distributions to creditors. Michelle Kierce, et al., *Schemes of arrangement and their ongoing currency*, Insurance and Reinsurance 2010, https://www.sidley.com/~media/files/publications/2010/01/schemes-of-arrangement-and-their-ongoing-currency/files/view-article/fileattachment/schemes-of-arrangement-and-their-ongoing-currenc_.pdf (last visited Feb. 27, 2021).

²⁴ The assuming insurer’s regulatory authority is the entity that regulates the conduct of insurance companies in the assuming insurer’s country of domicile.

II. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT

A. FISCAL IMPACT ON STATE GOVERNMENT:

1. Revenues:

None.

2. Expenditures:

None.

B. FISCAL IMPACT ON LOCAL GOVERNMENTS:

1. Revenues:

None.

2. Expenditures:

None.

C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

None known.

D. FISCAL COMMENTS:

None.

III. COMMENTS

A. CONSTITUTIONAL ISSUES:

1. Applicability of Municipality/County Mandates Provision:

Not applicable. This bill does not appear to affect county or municipal governments.

2. Other:

None.

B. RULE-MAKING AUTHORITY:

Section 624.610(14), F.S., provides that the commission may adopt rules necessary to implement the provisions of that section and “protect the interests of insureds, claimants, ceding insurers, assuming insurers, and the public.” The rules must be in “substantial compliance” with the NAIC model regulations relating to credit for reinsurance, the NAIC Accounting Practices and Procedures Manual as of March 2002 and subsequent consistent amendments to it; and the NAIC model regulation for Credit for Reinsurance and Life and Health Reinsurance Agreements.²⁵ The bill requires the exercise of this authority and the adoption of certain forms. Therefore, the bill will likely result in the changes to the rules in ch. 690-144, F.A.C.

C. DRAFTING ISSUES OR OTHER COMMENTS:

None.

²⁵ S. 624.610(14), F.S.

IV. AMENDMENTS/ COMMITTEE SUBSTITUTE CHANGES