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**HOUSE BILL 1077**

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**State of Washington 64th Legislature 2015 Regular Session**

**By** Representatives Kirby, Ryu, McBride, and Stanford; by request of Insurance Commissioner

AN ACT Relating to credit for reinsurance; adding new sections to chapter 48.12 RCW; recodifing RCW 48.12.164 and 48.12.166; and repealing RCW 48.12.154, 48.12.156, 48.12.158, 48.12.160, 48.12.162, and 48.12.168.

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF WASHINGTON:

NEW SECTION. **Sec.**  The purpose of this subchapter is to protect the interest of insureds, claimants, ceding insurers, assuming insurers, and the public generally. The legislature intends to ensure adequate regulation of insurers and reinsurers and adequate protection for those to whom they owe obligations. Therefore, the legislature provides a mandate that upon the insolvency of a non-United States insurer or reinsurer that provides security to fund its United States obligations in accordance with this subchapter, the assets representing the security must be maintained in the United States and claims must be filed with and valued by the state insurance commissioner with regulatory oversight, and the assets distributed, in accordance with the insurance laws of the state in which the trust is domiciled that are applicable to the liquidation of domestic United States insurance companies. The legislature declares that the matters contained in this subchapter are fundamental to the business of insurance in accordance with 15 U.S.C. Secs. 1011-1012.

NEW SECTION. **Sec.**  Credit for reinsurance is allowed a domestic ceding insurer as either an asset or a reduction from liability on account of reinsurance ceded only when the reinsurer meets the requirements of section 3, 4, 5, 6, 7, or 8 of this act. Credit is allowed under section 3, 4, or 5 of this act only as respects cessions of those kinds or classes of business which the assuming insurer is licensed or otherwise permitted to write or assume in its state of domicile or, in the case of a United States branch of an alien assuming insurer, in the state through which it is entered and licensed to transact insurance or reinsurance. Credit is allowed under section 5 or 6 of this act only if the applicable requirements of section 9 of this act have been satisfied.

NEW SECTION. **Sec.**  Credit is allowed when the reinsurance is ceded to an assuming insurer that is licensed to transact insurance or reinsurance in this state.

NEW SECTION. **Sec.**  Credit is allowed when the reinsurance is ceded to an assuming insurer that is accredited by the commissioner as a reinsurer in this state. In order to be eligible for accreditation, a reinsurer must:

(1) File with the commissioner evidence of its submission to this state's jurisdiction;

(2) Submit to this state's authority to examine its books and records;

(3) 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;

(4) File annually with the commissioner 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; and

(5) 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 meets this requirement as of the time of its application if it maintains a surplus as regards policyholders in an amount not less than twenty million dollars and its accreditation has not been denied by the commissioner within ninety days after submission of its application.

NEW SECTION. **Sec.**  (1) Credit is allowed when the reinsurance is ceded to an assuming insurer that is domiciled in, or in the case of a United States branch of an alien assuming insurer is entered through, a state that employs standards regarding credit for reinsurance substantially similar to those applicable under this statute and the assuming insurer or United States branch of an alien assuming insurer:

(a) Maintains a surplus as regards policyholders in an amount not less than twenty million dollars; and

(b) Submits to the authority of this state to examine its books and records.

(2) Subsection (1)(a) of this section does not apply to reinsurance ceded and assumed pursuant to pooling arrangements among insurers in the same holding company system.

NEW SECTION. **Sec.**  (1) Credit is allowed when the reinsurance is ceded to an assuming insurer that maintains a trust fund in a qualified United States financial institution, as defined in section 14(2) of this act, for the payment of the valid claims of its United States ceding insurers, their assigns, and successors in interest. To enable the commissioner to determine the sufficiency of the trust fund, the assuming insurer must report annually to the commissioner information substantially the same as that required to be reported on the national association of insurance commissioners annual statement form by licensed insurers. The assuming insurer must submit to examination of its books and records by the commissioner and bear the expense of examination.

(2)(a) Credit for reinsurance shall not be granted under this section unless the form of the trust and any amendments to the trust have been approved by:

(i) The commissioner of the state where the trust is domiciled; or

(ii) The commissioner of another state who, pursuant to the terms of the trust instrument, has accepted principal regulatory oversight of the trust.

(b) The form of the trust and any trust amendments also must be filed with the commissioner of every state in which the ceding insurer beneficiaries of the trust are domiciled. The trust instrument must provide that contested claims are valid and enforceable upon the final order of any court of competent jurisdiction in the United States. The trust must vest legal title to its assets in its trustees for the benefit of the assuming insurer's United States ceding insurers, their assigns, and successors in interest. The trust and the assuming insurer are subject to examination as determined by the commissioner.

(c) The trust remains in effect for as long as the assuming insurer has outstanding obligations due under the reinsurance agreements subject to the trust. By February 28th of each year the trustee of the trust must report to the commissioner in writing the balance of the trust and listing the trust's investments at the preceding year-end and certify the date of termination of the trust, if so planned, or certify that the trust will not expire prior to the following December 31st.

(3) The following requirements apply to the following categories of assuming insurer:

(a) The trust fund for a single assuming insurer consists of funds in trust in an amount not less than the assuming insurer's liabilities attributable to reinsurance ceded by United States ceding insurers, and, in addition, the assuming insurer must maintain a trusteed surplus of not less than twenty million dollars, except as provided in (b) of this subsection.

(b) At any time after the assuming insurer has permanently discontinued underwriting new business secured by the trust for at least three full years, the commissioner with principal regulatory oversight of the trust may authorize a reduction in the required trusteed 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 United States 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 must 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 trusteed surplus may not be reduced to an amount less than thirty percent of the assuming insurer's liabilities attributable to reinsurance ceded by United States ceding insurers covered by the trust.

(c)(i) In the case of a group including incorporated and individual unincorporated underwriters:

(A) For reinsurance ceded under reinsurance agreements with an inception, amendment, or renewal date on or after January 1, 1993, the trust must consist of a trusteed account in an amount not less than the respective underwriters' several liabilities attributable to business ceded by United States domiciled ceding insurers to any underwriter of the group;

(B) For reinsurance ceded under reinsurance agreements with an inception date on or before December 31, 1992, and not amended or renewed after that date, notwithstanding the other provisions of this subchapter, the trust must consist of a trusteed account in an amount not less than the respective underwriters' several insurance and reinsurance liabilities attributable to business written in the United States; and

(C) In addition to these trusts, the group must maintain in trust a trusteed surplus of which one hundred million dollars is held jointly for the benefit of the United States domiciled ceding insurers of any member of the group for all years of account.

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

(iii) Within ninety days after its financial statements are due to be filed with the group's domiciliary regulator, the group must provide to the commissioner an annual certification by the group's domiciliary regulator of the solvency of each underwriter member; or if a certification is unavailable, financial statements, prepared by independent public accountants, of each underwriter member of the group.

(d) In the case of a group of incorporated underwriters under common administration, the group must:

(i) Have continuously transacted an insurance business outside the United States for at least three years immediately prior to making application for accreditation;

(ii) Maintain aggregate policyholders' surplus of at least ten billion dollars;

(iii) Maintain a trust fund in an amount not less than the group's several liabilities attributable to business ceded by United States domiciled ceding insurers to any member of the group pursuant to reinsurance contracts issued in the name of the group;

(iv) In addition, maintain a joint trusteed surplus of which one hundred million dollars is held jointly for the benefit of United States domiciled ceding insurers of any member of the group as additional security for these liabilities; and

(v) Within ninety days after its financial statements are due to be filed with the group's domiciliary regulator, make available to the commissioner an annual certification of each underwriter member's solvency by the member's domiciliary regulator and financial statements of each underwriter member of the group prepared by its independent public accountant.

NEW SECTION. **Sec.**  Credit is allowed when the reinsurance is ceded to an assuming insurer that has been certified by the commissioner as a reinsurer in this state and secures its obligations in accordance with the requirements of this section.

(1) In order to be eligible for certification, the assuming insurer must meet the following requirements:

(a) The assuming insurer must be domiciled and licensed to transact insurance or reinsurance in a qualified jurisdiction, as determined by the commissioner pursuant to subsection (3) of this section;

(b) The assuming insurer must maintain minimum capital and surplus, or its equivalent, in an amount to be determined by the commissioner by rule;

(c) The assuming insurer must maintain financial strength ratings from two or more rating agencies deemed acceptable by the commissioner by rule;

(d) The assuming insurer must agree to submit to the jurisdiction of this state, appoint the commissioner as its agent for service of process in this state, and agree to provide security for one hundred percent of the assuming insurer's liabilities attributable to reinsurance ceded by United States ceding insurers if it resists enforcement of a final United States judgment;

(e) The assuming insurer must agree to meet applicable information filing requirements as determined by the commissioner, both with respect to an initial application for certification and on an ongoing basis; and

(f) The assuming insurer must satisfy any other requirements for certification deemed relevant by the commissioner.

(2) An association including incorporated and individual unincorporated underwriters may be a certified reinsurer. In order to be eligible for certification, in addition to satisfying the requirements of subsection (1) of this section:

(a) The association must satisfy its minimum capital and surplus requirements through the capital and surplus equivalents (net of liabilities) of the association and its members, which includes 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;

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

(c) Within ninety days after its financial statements are due to be filed with the association's domiciliary regulator, the association must provide to the commissioner an annual certification by the association's domiciliary regulator of the solvency of each underwriter member; or if a certification is unavailable, financial statements, prepared by independent public accountants, of each underwriter member of the association.

(3) The commissioner must create and publish a list of qualified jurisdictions, under which an assuming insurer licensed and domiciled in such a jurisdiction is eligible to be considered for certification by the commissioner as a certified reinsurer.

(a) In order to determine whether the domiciliary jurisdiction of a non-United States assuming insurer is eligible to be recognized as a qualified jurisdiction, the commissioner must evaluate the appropriateness and effectiveness of the reinsurance supervisory system of the jurisdiction, both initially and on an ongoing basis, and consider the rights, benefits, and the extent of reciprocal recognition afforded by the non-United States jurisdiction to reinsurers licensed and domiciled in the United States. A qualified jurisdiction must agree to share information and cooperate with the commissioner with respect to all certified reinsurers domiciled within that jurisdiction. A jurisdiction may not be recognized as a qualified jurisdiction if the commissioner has determined that the jurisdiction does not adequately and promptly enforce final United States judgments and arbitration awards. Additional factors may be considered in the discretion of the commissioner.

(b) A list of qualified jurisdictions shall be published through the national association of insurance commissioners' committee process. The commissioner must consider this list in determining qualified jurisdictions. If the commissioner approves a jurisdiction as qualified that does not appear on the list of qualified jurisdictions, the commissioner must provide thoroughly documented justification in accordance with criteria to be developed by rule.

(c) United States jurisdictions that meet the requirement for accreditation under the national association of insurance commissioners' financial standards and accreditation program must be recognized as qualified jurisdictions.

(d) If a certified reinsurer's domiciliary jurisdiction ceases to be a qualified jurisdiction, the commissioner has the discretion to suspend the reinsurer's certification indefinitely in lieu of revocation.

(4) The commissioner must assign a rating to each certified reinsurer, giving due consideration to the financial strength ratings that have been assigned by rating agencies deemed acceptable to the commissioner by rule. The commissioner must publish a list of all certified reinsurers and their ratings.

(5) A certified reinsurer must secure obligations assumed from United States ceding insurers under this section at a level consistent with its rating, as specified in rules adopted by the commissioner.

(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 section 13 of this act, or in a multibeneficiary trust in accordance with section 6 of this act, except as otherwise provided in this section.

(b) If a certified reinsurer maintains a trust to fully secure its obligations under section 6 of this act, and chooses to secure its obligations incurred as a certified reinsurer in the form of a multibeneficiary trust, the certified reinsurer must 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 section or comparable laws of other United States jurisdictions and for its obligations under section 6 of this act. It is a condition to the grant of certification under this section that the certified reinsurer must have bound itself, by the language of the trust and agreement with the commissioner with principal regulatory oversight of each such trust account, to fund, upon termination of any trust account, out of the remaining surplus of the trust any deficiency of any other trust account.

(c) The minimum trusteed surplus requirements provided in section 6 of this act are not applicable with respect to a multibeneficiary trust maintained by a certified reinsurer for the purpose of securing obligations incurred under this section, except that the trust must maintain a minimum trusteed surplus of ten million dollars.

(d) With respect to obligations incurred by a certified reinsurer under this section, if the security is insufficient, the commissioner must 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.

(e) For purposes of this section, a certified reinsurer whose certification has been terminated for any reason must be treated as a certified reinsurer required to secure one hundred percent of its obligations.

(i) As used in this section, "terminated" means revocation, suspension, voluntary surrender, and inactive status.

(ii) If the commissioner continues to assign a higher rating as permitted by this section, this subsection (5)(e) does not apply to a certified reinsurer in inactive status or to a reinsurer whose certification has been suspended.

(6) If an applicant for certification has been certified as a reinsurer in a national association of insurance commissioners 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 the assuming insurer must be considered to be a certified reinsurer in this state.

(7) A certified reinsurer that ceases to assume new business in this state 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 must continue to comply with all applicable requirements of this section, and the commissioner must assign a rating that takes into account, if relevant, the reasons why the reinsurer is not assuming new business.

NEW SECTION. **Sec.**  Credit is allowed when the reinsurance is ceded to an assuming insurer not meeting the requirements of section 3, 4, 5, 6, or 7 of this act, but only as to the insurance of risks located in jurisdictions where the reinsurance is required by applicable law or regulation of that jurisdiction.

NEW SECTION. **Sec.**  If the assuming insurer is not licensed, accredited, or certified to transact insurance or reinsurance in this state, the credit permitted by sections 5 and 6 of this act must not be allowed unless the assuming insurer agrees in the reinsurance agreements:

(1)(a) That in the event of the failure of the assuming insurer to perform its obligations under the terms of the reinsurance agreement, the assuming insurer, at the request of the ceding insurer, must submit to the jurisdiction of any court of competent jurisdiction in any state of the United States, will comply with all requirements necessary to give the court jurisdiction, and will abide by the final decision of the court or of any appellate court in the event of an appeal; and

(b) To designate the commissioner or a designated attorney as its true and lawful attorney upon whom may be served any lawful process in any action, suit, or proceeding instituted by or on behalf of the ceding insurer.

(2) This section is not intended to conflict with or override the obligation of the parties to a reinsurance agreement to arbitrate their disputes, if this obligation is created in the agreement.

NEW SECTION. **Sec.**  If the assuming insurer does not meet the requirements of section 3, 4, or 5 of this act, the credit permitted by section 6 or 7 of this act must not be allowed unless the assuming insurer agrees in the trust agreements to the following conditions:

(1) Notwithstanding any other provisions in the trust instrument, if the trust fund is inadequate because it contains an amount less than the amount required by section 6(3) of this act, or if the grantor of the trust has been declared insolvent or placed into receivership, rehabilitation, liquidation, or similar proceedings under the laws of its state or country of domicile, the trustee must comply with an order of the commissioner with regulatory oversight over the trust or with an order of a court of competent jurisdiction directing the trustee to transfer to the commissioner with regulatory oversight all of the assets of the trust fund.

(2) The assets must be distributed by and claims must be filed with and valued by the commissioner with regulatory oversight in accordance with the laws of the state in which the trust is domiciled that are applicable to the liquidation of domestic insurance companies.

(3) If the commissioner with regulatory oversight determines that the assets of the trust fund or any part thereof are not necessary to satisfy the claims of the United States ceding insurers of the grantor of the trust, the assets or part thereof must be returned by the commissioner with regulatory oversight to the trustee for distribution in accordance with the trust agreement.

(4) The grantor must waive any right otherwise available to it under United States law that is inconsistent with this provision.

NEW SECTION. **Sec.**  If an accredited or certified reinsurer ceases to meet the requirements for accreditation or certification, the commissioner may suspend or revoke the reinsurer's accreditation or certification.

(1) The commissioner must give the reinsurer notice and opportunity for hearing. The suspension or revocation may not take effect until after the commissioner's order on hearing, unless:

(a) The reinsurer waives its right to hearing;

(b) The commissioner's order is based on regulatory action by the reinsurer's domiciliary jurisdiction or the voluntary surrender or termination of the reinsurer's eligibility to transact insurance or reinsurance business in its domiciliary jurisdiction or in the primary certifying state of the reinsurer under section 7(6) of this act; or

(c) The commissioner finds that an emergency requires immediate action and a court of competent jurisdiction has not stayed the commissioner's action.

(2) While a reinsurer's accreditation or certification is suspended, no reinsurance contract issued or renewed after the effective date of the suspension qualifies for credit except to the extent that the reinsurer's obligations under the contract are secured in accordance with section 13 of this act. If a reinsurer's accreditation or certification is revoked, no credit for reinsurance may be granted after the effective date of the revocation except to the extent that the reinsurer's obligations under the contract are secured in accordance with section 7(5) or 13 of this act.

NEW SECTION. **Sec.**  (1) A ceding insurer must take steps to manage its reinsurance recoverable proportionate to its own book of business. A domestic ceding insurer must notify the commissioner within thirty days after reinsurance recoverables from any single assuming insurer, or group of affiliated assuming insurers, exceeds fifty percent 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.

(2) A ceding insurer must take steps to diversify its reinsurance program. A domestic ceding insurer must notify the commissioner within thirty days after ceding to any single assuming insurer, or group of affiliated assuming insurers, more than twenty percent 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.

NEW SECTION. **Sec.**  An asset or a reduction from liability for the reinsurance ceded by a domestic insurer to an assuming insurer not meeting the requirements of sections 2 through 12 of this act must be allowed in an amount not exceeding the liabilities carried by the ceding insurer. The reduction must be in the amount of funds held by or on behalf of the ceding insurer, including funds held in trust for the ceding insurer, under a reinsurance contract with the assuming insurer as security for the payment of obligations thereunder, if the security is held in the United States subject to withdrawal solely by, and under the exclusive control of, the ceding insurer; or, in the case of a trust, held in a qualified United States financial institution, as defined in section 14(2) of this act. This security may be in the form of:

(1) Cash;

(2) Securities listed by the securities valuation office of the national association of insurance commissioners, including those deemed exempt from filing as defined by the purposes and procedures manual of the securities valuation office, and qualifying as admitted assets;

(3)(a) Clean, irrevocable, unconditional letters of credit, issued or confirmed by a qualified United States financial institution, as defined in section 14(1) of this act, effective no later than December 31st of the year for which the filing is being made, and in the possession of, or in trust for, the ceding insurer on or before the filing date of its annual statement;

(b) Letters of credit meeting applicable standards of issuer acceptability as of the dates of their issuance (or confirmation) must, notwithstanding the issuing (or confirming) institution's subsequent failure to meet applicable standards of issuer acceptability, continue to be acceptable as security until their expiration, extension, renewal, modification, or amendment, whichever first occurs; or

(4) Any other form of security acceptable to the commissioner.

NEW SECTION. **Sec.**  (1) For the purposes of section 13(3) of this act, a "qualified United States financial institution" means an institution that:

(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 any state thereof;

(b) Is regulated, supervised, and examined by United States federal or state authorities having regulatory authority over banks and trust companies; and

(c) Has been determined by either the commissioner or the securities valuation office of the national association of insurance commissioners to meet the standards of financial condition and standing as are considered necessary and appropriate to regulate the quality of financial institutions whose letters of credit will be acceptable to the commissioner.

(2) A "qualified United States financial institution" means, for the purposes of those provisions of this subchapter specifying those institutions that are eligible to act as a fiduciary of a trust, an institution that:

(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 any state thereof and has been granted authority to operate with fiduciary powers; and

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

NEW SECTION. **Sec.**  The commissioner may adopt rules and regulations implementing the provisions of this subchapter.

NEW SECTION. **Sec.**  This act applies to all cessions after the effective date of this act under reinsurance agreements that have an inception, anniversary, or renewal date not less than six months after the effective date of this act.

NEW SECTION. **Sec.**  RCW 48.12.164 and 48.12.166 are each recodified as new sections in chapter 48.12 RCW under the subchapter heading “credit for reinsurance” created in section 18 of this act.

NEW SECTION. **Sec.**  Sections 1 through 16 of this act are each added to chapter 48.12 RCW and codified with the subchapter heading "credit for reinsurance."

NEW SECTION. **Sec.**  The following acts or parts of acts are each repealed:

(1) RCW 48.12.154 (Rules) and 1997 c 379 s 9;

(2) RCW 48.12.156 (Qualified United States financial institution—Definition) and 1997 c 379 s 2;

(3) RCW 48.12.158 (Insolvency of non-United States insurer or reinsurer—Maintenance of assets—Claims) and 1997 c 379 s 3;

(4) RCW 48.12.160 (Credit for reinsurance—Trust fund—Regulatory oversight) and 1997 c 379 s 6, 1996 c 297 s 1, 1994 c 86 s 1, 1993 c 91 s 2, 1977 ex.s. c 180 s 3, & 1947 c 79 s .12.16;

(5) RCW 48.12.162 (Credit for reinsurance—Contract provisions—After December 31, 1996—Payment—Rights of original insured or policyholder) and 1997 c 379 s 4; and

(6) RCW 48.12.168 (Credit for reinsurance—Foreign ceding insurer) and 1997 c 379 s 8.

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