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New York Releases Proposed Amendment to Regulation No. 20 Relaxing Collateral Requirements for Unauthorized Reinsurers and Prohibiting Arbitration

On December 24, 2008, the New York State Insurance Department (“NYSID”) released Proposed Tenth Amendment to Regulation No. 20 (11 NYCRR 125) Credit for Reinsurance from Unauthorized Reinsurers (the “Proposal”). The Proposal is similar to the NAIC reinsurance regulatory modernization proposal, and, if adopted, would significantly reform existing reinsurance regulation.



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one of these conditions is that the parties to the reinsurance contract must agree to resolve any disputes relating to or arising out of the transaction in court, thereby precluding arbitration.

Under the Proposal, an unauthorized reinsurer may reduce its collateral posting requirement if it receives quality ratings on a stand-alone basis separate from its parent from at least two of the following five rating agencies: (1) Standard & Poor’s (“S&P”), (2) Moody’s Investors Service (“Moody’s”), (3) Fitch Ratings (“Fitch”), (4) A.M. Best Company (“Best”), or (5) any other rating agency recognized by the Securities Valuation Office of the NAIC. An unauthorized reinsurer with the highest rating would be granted 100% credit, whereas one with a lower rating would be granted a lesser a credit determined on a sliding scale as specified in the chart below.

Credit Allowed	Best	S&P	Moody’s	Fitch
100%	A++	AAA	Aaa	AAA
90%	A+	AA+, AA, AA-	Aa1, Aa2, Aa3	AA+, AA, AA-
80%	A, A-	A+, A, A-	A1, A2, A3	A+, A, A-
25%	B++, B+	BBB+, BBB, BBB-	Baa1, Baa2, Baa3	BBB+, BBB, BBB-
0%	B, B-, C++, C+, C, C-, D, E, F	BB+, BB, BB-, B+, B, B-, CCC, CC, C, D, R, NR	Ba1, Ba2, Ba3, B1, B2, B3, Caa, Ca, C	BB+, BB, BB-, B+, B, B-, CCC+, CCC, CCC-, DD

Each reinsurer would be required to post the difference between the collateral required and the credit allowed in order for the ceding insurer to get financial statement credit. For example, a reinsurer that receives a 90% credit would need to post sufficient collateral to secure 10% of its liabilities. Note that if the rating of the assuming reinsurer drops, the credit to the ceding insurer will be adjusted accordingly, provided, however, that in the interest of market stability and solvency of the ceding insurer, the New York Superintendent of Insurance may authorize a higher level of continued credit for reinsurance for a specified period unless it is determined that the reinsurance recoverables are uncollectible.

Each unauthorized reinsurer must also maintain evidence that it satisfies the following requirements in order for the ceding insurer to get credit for reinsurance:

- it meets the standards of solvency, including standards for capital adequacy, established by its domiciliary regulator;
- it is authorized in its domiciliary jurisdiction to assume the kind or kinds of reinsurance ceded by the ceding insurer; and
- it maintains a policyholders' surplus or equivalent in excess of \$250 million, calculated using U.S. GAAP or U.S. Statutory Accounting Principles.

With respect to an unauthorized alien reinsurer, such reinsurer must be domiciled in a country which has executed a Memorandum of Understanding ("MoU") with the NYSID and which allows U.S. reinsurers access to its market on terms and conditions that are at least as favorable as those provided in New York. The NYSID has executed MoUs with regulators in a number of countries including France and Bermuda.

Finally, in addition to imposing requirements on the unauthorized reinsurer, the Proposal sets forth conditions that the ceding insurer must satisfy in order to take financial statement credit, including a requirement that it maintains in its records audited financial statements, prepared in accordance with GAAP or SAP or reconcilable to GAAP or SAP of the unauthorized reinsurer from inception or for the previous three years, whichever is less. Furthermore, the reinsurance contract between the ceding insurer and the unauthorized reinsurer must contain certain provisions as specified below:

- a requirement that the reinsurer provide the ceding insurer with written notice of any change in its license status within 30 days;

- a requirement that the reinsurer provide the ceding insurer with written notice of any change in its rating status within 30 days;
- an insolvency clause as specified under the New York Insurance Law;
- a requirement that the reinsurer designate an agent in New York or in the ceding insurer's domiciliary state for service of process;
- a jurisdiction clause subjecting the reinsurer to the jurisdiction of the courts of the United States or any state thereof, and apparently prohibiting arbitration of disputes; and
- a choice of law clause requiring that actions arising from performance of the contract be governed by the laws of New York or the ceding insurer's domiciliary state.

If adopted, the Proposal would significantly liberalize current reinsurance regulation in New York. However, the language requiring disputes to be resolved in court is controversial, as arbitration is overwhelmingly the preferred forum for dispute resolution in reinsurance disputes.

The NYSID will accept comments regarding the Proposal until February 6, 2009. Please contact Nick Pearson or Mohana Terry for further discussion or information about this Proposal.

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