

INSURANCE
DEPARTMENT OF BANKING AND INSURANCE
OFFICE OF SOLVENCY REGULATION

Reduction from Liability for Reinsurance
Utilization of Trust Agreements with Letters of Credit to Satisfy the Reduction of Reinsurance
Liability

Proposed Amendments: N.J.A.C. 11:2-28.9, and 28.10

Authorized By: Donald Bryan, Acting Commissioner, Department of Banking and Insurance.

Authority: N.J.S.A. 17:1-8.1, 17:1-15e, and 17:51B.1 et. seq.

Calendar Reference: See Summary below for explanation of exception to calendar requirements.

Proposal Number: PRN 2005-307

Submit comments by November 5, 2005 to:

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The agency proposal follows:

Summary

Companies regulated by the Department of Banking and Insurance (Department), are permitted a reduction in liability for reinsurance ceded by an authorized or licensed insurer and are required to employ standards regarding the placement and holding of the security and the form of the security instruments utilized in the reduction of liabilities by a ceding reinsurer, pursuant to N.J.S.A. 17:51B-3 et seq. That law states: "If such 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 subject to withdrawal solely by, and under the exclusive control of, the ceding insurer, such securities shall be in the form of cash; securities listed by the Securities Valuation Office of the NAIC and qualifying as admitted assets, clean , irrevocable, evergreen, unconditional letters of credit issued or confirmed by a qualified United States financial institution....”

The Department now seeks to amend the Administrative Code to permit the use of qualifying letters of credit within ceded reinsurance trust accounts.

The proposed amendments include amending N.J.A.C. 11:2-28.9(a)3 to permit the use of letters of credit within trust account agreements, as qualified, pursuant to N.J.A.C 11:2-28.8.

The Department will also amend the heading of N.J.A.C 11:2-28.10, **Letters of credit qualified pursuant to N.J.A.C 11:2-28.8**, to include a reference to N.J.A.C. 11:2-28.9

A 60-day comment period is provided for this notice of proposal, and, therefore, pursuant to N.J.A.C 1:30-3.3(a)5, the proposal is not subject to the provisions of N.J.A.C 1:30-3.1 and 3.2, governing rulemaking calendars.

Social Impact

These proposed amendments should have a favorable impact upon insurers, policyholders and the Department. The use of letters of credit within trust agreements would provide insurers an option which is an acceptable investment in today’s financial environment. Letters of credit are acceptable separately as reinsurance offsets. Thus allowing them as security in a trust agreement will foster uniformity and consistency within the Department’s analysis of companies seeking credit for reinsurance within the solvency regulation analysis process. This amendment

will benefit insurers as it comports with the efforts of many states which have permitted the use of letters of credit within trust agreements as a reinsurance offset.

Economic Impact

These proposed amendments should have a favorable economic impact upon insurers, policyholders and the Department. Since letters of credit have very specific conditions that must be met, the allowance of them within trust agreements as a reinsurance offset creates one more instrument for insurers to utilize within their financial business plans to maintain proper capital and surplus requirements. Letters of credit may be readily drawn down for surplus fulfillment as required and, as such, assist in the proper maintenance of reinsurance by insurers on behalf of its policyholders. The Department believes that there will not be a cost impact to insurers who utilize letters of credit in the manner permitted by the proposed amendments and that there should not be any additional cost to the Department.

Federal Standards Statement

The proposed amendments do not contain standards or requirements that are the subject of any Federal requirements or standards.

Jobs Impact

The Department does not anticipate that these proposed amendments will result in the generation or loss of jobs.

Agriculture Industry Impact

The proposed amendments will have no impact on the agriculture industry.

Regulatory Flexibility Analysis

These rules directly impact all authorized and admitted insurers. The Department believes that these proposed amendments will apply to few, if any, “small businesses,” as the term is defined in the Regulatory Flexibility Act, N.J.S.A 52:14B-16 et. seq., because the affected insurers do not employ fewer than 100 full-time employees. The Department does not believe that insurers will be required to hire any consultants or bear the cost of any other professional services to comply with the proposed amendments. Existing staff should be able to make the administrative and other changes necessary for compliance, as they already do in response to evolution in the market. No additional reporting or recordkeeping requirements would be imposed by the proposed amendments.

The Department does not believe that different requirements based upon insurer size would be appropriate or feasible since the proposal does not mandate the use of letters of credit; it merely provides an additional financial option for insurers. Accordingly, the proposal provides no differentiation in compliance requirements based upon company or business size.

Smart Growth Impact

The proposed amendments have no impact on the achievement of smart growth and implementation of the State Development and Redevelopment Plan.

Full text of the proposal follows (additions indicated in boldface **thus**; deletions indicated in brackets [thus]):

11:2-28.9 Trust agreements qualified pursuant to N.J.A.C. 11:2-28.8

(a) An admitted asset or a reduction from liability for reinsurance ceded to an unauthorized assuming insurer pursuant to N.J.A.C. 11:2-28.8 shall be permitted only when the requirements set forth below and in N.J.A.C. 11:2-28.10 and 28.11 are met.

1. – 2. (No change.)

3. All assets in the trust account shall be held by the trustee at the trustee's office in the United States, except that a bank may apply for the Commissioner's permission to use a foreign branch office of such bank as trustee for trust agreements established pursuant to this section. If the Commissioner approves the use of such foreign branch office as trustee, then its use must be approved by the beneficiary in writing and the trust agreement must provide that the written notice described in 4i below must also be presentable, as a matter of legal right, at the trustee's principal office in the United States. The trust assets shall consist of cash (United States legal tender), certificates of deposit (issued by a United States bank and payable in United States legal tender), **letters of credit (issued by a United States financial institution authorized to issue letters of credit and payable in United States legal tender)**, investments of stocks and bonds listed by the NAIC's Securities Valuation Office, or any obligations issued by the State of New Jersey or any of its political subdivisions, or any combination of the above, provided that such investments are issued by an institution that is not the parent, subsidiary or an affiliate of either the grantor or the beneficiary.

4. - 12. (No change.)

(b) – (f) (No change.)

11:2-28.10 Letters of credit qualified pursuant to N.J.A.C 11:2-28.8 **and 28.9**.

(a) - (j) (No change.)

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