

Senate Bill No. 1216

CHAPTER 277

An act to amend Sections 922.2, 922.4, 922.5, 922.8, and 12121 of, to add Sections 717.5, 922.31, 922.42, 922.43, and 922.85 to, to add and repeal Section 922.41 of, and to repeal and add Section 922.6 of, the Insurance Code, relating to reinsurance.

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LEGISLATIVE COUNSEL'S DIGEST

SB 1216, Lowenthal. Reinsurance: professional reinsurers.

(1) Existing law prohibits the transaction of any class of insurance in this state without first being admitted for that class of insurance, and admission is secured by procuring a certificate of authority from the Insurance Commissioner. Before granting a certificate of authority to any applicant, the commissioner is required to consider the qualifications of the applicant, including, but not limited to, capital and surplus and lawfulness and quality of investments.

This bill would authorize the commissioner to designate an insurer as a professional reinsurer when an insurer admitted and domiciled in this state, or an insurer applying to become admitted and domiciled in this state, is determined by the commissioner to be qualified, as specified, which includes, but is not limited to, the commissioner determining that the insurer is principally engaged in the business of reinsurance, that the insurer does not conduct significant amounts of direct insurance as a percentage of its net premiums, and is not engaged, on an ongoing basis, in the business of soliciting direct insurance.

(2) Existing law requires insurers doing business in this state to annually make and file with the commissioner financial statements.

Existing law requires that credit for reinsurance as an asset or deduction from liability be allowed a domestic ceding insurer only if the reinsurance contract includes certain provisions, including, in the event of insolvency and the appointment of a conservator, liquidator, or statutory successor of the ceding company, that the reinsurance will be payable, as specified, without diminution because of the insolvency.

This bill would revise that requirement to additionally apply in the event of a change in status of the ceding company, as specified, including when the commissioner finds that the conditions for the appointment of a conservator, liquidator, or statutory successor has occurred with respect to the ceding company.

The bill would also require a ceding insurer to take steps to manage its reinsurance recoverables proportionate to its own book of business and to

diversify its reinsurance program. The bill would also require a domestic ceding insurer to 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 the reinsurance recoverables are likely to exceed that limit, as specified. The bill would also require a domestic ceding insurer to 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 is likely to exceed this limit, as specified.

(3) Existing law also allows credit for reinsurance when the reinsurance is ceded to an assuming insurer that is accredited as a reinsurer in this state, except as specified. Existing law describes an accredited reinsurer for purposes of this provision as one that, among other criteria, maintains a surplus as regards to policyholders in an amount that is either not less than \$20,000,000, and whose accreditation has not been denied by the commissioner within the last 90 days, or maintains a surplus that is less than \$20,000,000 and whose accreditation has been approved by the commissioner.

This bill would instead require that the reinsurer 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, and would delete the provision authorizing a reinsurer whose accreditation has been approved to maintain a surplus of less than \$20,000,000. The bill would instead provide that an assuming insurer who maintains a surplus of not less than \$20,000,000 and whose accreditation has not been denied by the commissioner within the last 90 days shall be deemed to meet that requirement and would require that an assuming insurer who is not deemed to meet this requirement obtain the affirmative approval of the commissioner. The bill would require that the approval of the commissioner be based upon a finding that the assuming insurer has adequate financial capacity to meet its reinsurance obligations and is otherwise qualified to assume reinsurance from domestic insurers.

(4) Existing law also provides that credit is allowed when reinsurance is ceded to an assuming insurer that maintains a trust fund, as specified.

This bill would authorize the commissioner to authorize a reduction in the required trustee surplus after an assuming insurer has permanently discontinued underwriting new business secured by the trust for at least 3 full years, as specified.

The bill would also enact, only until January 1, 2016, provisions governing the certification and rating of assuming insurers by the commissioner and specify additional circumstances under which credit shall be allowed to a domestic insurer when the reinsurance is ceded to an assuming insurer that has been certified. The bill would require, among other things, that the assuming insurer be domiciled and licensed to transact insurance or reinsurance in a qualified jurisdiction and would require the commissioner

to create and publish a list of qualified jurisdictions, as specified. The bill would also require the assuming insurer to maintain minimum capital and surplus, or its equivalent, in an amount determined by the commissioner, and to maintain financial strength ratings from 2 or more rating agencies, as specified. The bill would impose various filing requirements on certified reinsurers, including notification within 10 days of any regulatory actions taken against the certified reinsurer and annual audited financial statements. The bill would also require the commissioner to assign a rating to each certified reinsurer based on specified criteria, such as the certified insurer's financial strength rating from an acceptable rating agency and the certified insurer's reputation for prompt payment of claims. The bill would also authorize the commissioner to suspend or revoke an accredited or certified reinsurer's accreditation or certification after notice and opportunity for hearing, as specified.

The bill would make other related changes.

(5) Existing law provides that credit for reinsurance as an asset or a deduction from liability is allowed a foreign ceding insurer, with exceptions, to the extent the credit has been allowed by the ceding insurer's state of domicile if the state of domicile is accredited by the National Association of Insurance Commissioners (NAIC), or the credit or deduction from liability would be allowed if the foreign ceding insurer were domiciled in this state. Credit for reinsurance as an asset or a deduction from liability may be disallowed if the commissioner finds that the financial condition of the reinsurer, or the collateral or other security provided by the reinsurer, does not satisfy the credit for reinsurance requirements applicable to a ceding insurer domiciled in this state.

This bill would instead require that credit for reinsurance not be denied a foreign ceding insurer to the extent that credit is recognized by the ceding insurer's domestic state regulator, provided that the domestic state is accredited by the NAIC, or the domestic state regulator has financial solvency requirements similar to the requirements necessary for NAIC accreditation.

The people of the State of California do enact as follows:

SECTION 1. Section 717.5 is added to the Insurance Code, to read:

717.5. (a) For purposes of Sections 700 and 717, the commissioner may determine that an insurer admitted and domiciled in this state, or an insurer applying to become admitted and domiciled in this state, including an applicant pursuant to subdivision (a) of Section 709.5, is qualified to be designated as a professional reinsurer, if the commissioner determines that the insurer is all of the following:

- (1) Principally engaged in the business of reinsurance.
- (2) Does not conduct significant amounts of direct insurance as percentage of its net premiums.

(3) Is not engaged, on an ongoing basis, in the business of soliciting direct insurance.

(b) The commissioner may consider any information relevant to this determination. An insurer that holds, or is applying for qualification as, a professional reinsurer, shall provide the commissioner with information or documentation regarding the determinations under this section, upon request. The commissioner may prescribe terms and conditions applicable to the certificate of authority, as appropriate under this section.

(c) A domestic, professional reinsurer shall continue to be qualified as long as it continues to meet the requirements set forth in this section.

(d) The commissioner may, after notice and an opportunity to be heard, revoke a reinsurer's qualification, if the reinsurer no longer qualifies under this section.

(e) A domestic insurer that is qualified as a professional reinsurer may include that designation in its name, solicitations, and advertisements.

(f) An insurer seeking qualification under this section shall pay a filing fee of two thousand five hundred dollars (\$2,500), in advance, to the commissioner.

(g) The commissioner may adopt regulations in accordance with the procedure provided in Chapter 3.5 (commencing with Section 11340) of Part 1 of Division 3 of Title 2 of the Government Code or otherwise prescribe requirements consistent with this section.

(h) The commissioner may post prescribed requirements, consistent with this section, on the department's Internet Web site.

SEC. 2. Section 922.2 of the Insurance Code is amended to read:

922.2. (a) Credit for reinsurance shall be allowed a domestic ceding insurer as either an asset or a deduction from liability in accordance with Sections 922.4 and 922.5 only if the reinsurance contract contains provisions that provide, in substance, as follows:

(1) The reinsurer shall indemnify the ceding insurer for the risk it has assumed according to the terms and conditions contained in the reinsurance contract.

(2) In the event of insolvency, or a change in the status of the ceding company as defined in this section, and the appointment of a conservator, liquidator, or statutory successor of the ceding company, the reinsurance shall be payable to the conservator, liquidator, or statutory successor on the basis of claims allowed against the insolvent company by any court of competent jurisdiction or by any conservator, liquidator, or statutory successor of the company having authority to allow those claims, without diminution because of that insolvency or change in status, or because the conservator, liquidator, or statutory successor has failed to pay all or a portion of any claims. Payments by the reinsurer as set forth in this subdivision shall be made directly to the ceding insurer or to its conservator, liquidator, or statutory successor, except where the contract of insurance or reinsurance specifically provides another payee of such reinsurance in the event of the insolvency or change in status of the ceding insurer.

The reinsurance contract may provide that the conservator, liquidator, or statutory successor of a ceding insurer shall give written notice of the pendency of a claim against the ceding insurer indicating the policy or bond reinsured, within a reasonable time after such claim is filed and the reinsurer may interpose, at its own expense, in the proceeding in which the claim is to be adjudicated, any defense or defenses which it may deem available to the ceding insurer or its conservator, liquidator, or statutory successor. The expense thus incurred by the reinsurer shall be payable subject to court approval out of the estate of the insolvent ceding insurer as part of the expense of conservation or liquidation to the extent of a proportionate share of the benefit which may accrue to the ceding insurer in conservation or liquidation, solely as a result of the defense undertaken by the reinsurer.

(b) Payment pursuant to a reinsurance contract shall be made within a reasonable time with reasonable provision for verification in accordance with the terms of the reinsurance agreement. However, in no event shall the payments be beyond the period required by the National Association of Insurance Commissioners (NAIC) Accounting Practices and Procedures Manual.

(c) The original insured or policyholder shall not have any rights against the reinsurer which are not specifically set forth in the contract of reinsurance, or in a specific agreement between the reinsurer and the original insured or policyholder.

(d) For purposes of this section, the phrase “change in the status of the ceding company” means a finding by the commissioner that conditions set forth in subdivision (d) or (i) of Section 1011, a Regulatory Action Level Event as defined in Section 739.4, or any other event which permits the appointment of a conservator, liquidator, or statutory successor has occurred with respect to the ceding company.

SEC. 3. Section 922.31 is added to the Insurance Code, to read:

922.31. (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, exceeds 50 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 shall 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 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 shall demonstrate that the exposure is safely managed by the domestic ceding insurer.

SEC. 4. Section 922.4 of the Insurance Code is amended to read:

922.4. Credit for reinsurance shall be allowed a domestic ceding insurer as either an asset or a deduction from liability on account of reinsurance ceded only when the reinsurer meets the requirements of subdivision (a), (b), (c), (d), or (e). Credit shall be allowed under subdivision (a), (b), or (c) only for cessions of those kinds or classes of business that 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.

(a) Credit shall be allowed when the reinsurance is ceded to an assuming insurer that is licensed to transact insurance or reinsurance in this state unless the assuming insurer is the subject of a regulatory order or regulatory oversight by any state in which it is licensed based upon a commissioner's determination that the assuming insurer is in a hazardous financial condition.

(b) (1) Credit shall be allowed when the reinsurance is ceded to an assuming insurer that is accredited as a reinsurer in this state unless the assuming insurer is the subject of a regulatory order or regulatory oversight by any state in which it is licensed based upon a commissioner's determination that the assuming insurer is in a hazardous financial condition. An accredited reinsurer is one that does all of the following:

(A) Files with the commissioner evidence of its submission to this state's jurisdiction.

(B) Submits to this state's authority to examine its books and records.

(C) Designates the commissioner or a designated attorney in this state 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.

(D) Is 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, is entered through and licensed to transact insurance or reinsurance in at least one state.

(E) Files 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 other financial information requested by the commissioner.

(F) Submits a statement, signed and verified by an officer of the assuming insurer to be true and correct, that discloses whether the assuming insurer or any affiliated person who owns or has a controlling interest in the assuming insurer is currently known to be the subject of any of the following:

(i) Any order or proceeding regarding conservation, liquidation, or receivership.

(ii) Any order or proceeding regarding the revocation or suspension of a license or accreditation to transact insurance or reinsurance in any jurisdiction.

(iii) Any order or proceeding brought by an insurance regulator in any jurisdiction seeking to restrict or stop the assuming insurer from transacting insurance or reinsurance based upon a hazardous financial condition.

The assuming insurer shall provide the commissioner with copies of any orders or other documents initiating proceedings subject to disclosure under this paragraph. The statement shall affirm that no actions, proceedings, or orders subject to this subparagraph are outstanding against the assuming insurer or any affiliated person who owns or has a controlling interest in the assuming insurer, except as disclosed in the statement.

(G) Demonstrates 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 if it maintains a surplus as regards policyholders in an amount that is not less than twenty million dollars (\$20,000,000) and whose accreditation has not been denied by the commissioner within 90 days of its submission. An assuming insurer who is not deemed to meet this requirement shall obtain the affirmative approval of the commissioner. The approval of the commissioner shall be based upon a finding that the assuming insurer has adequate financial capacity to meet its reinsurance obligations and is otherwise qualified to assume reinsurance from domestic insurers.

(2) The commissioner may deny or revoke an assuming insurer's accreditation if the assuming insurer does not meet all of the standards required of an accredited reinsurer, or if its accreditation would be hazardous to the policyholders of this state. In determining whether to deny or revoke accreditation, the commissioner may consider the qualifications of the assuming insurer with respect to all the following subjects:

- (A) Its financial stability.
- (B) The lawfulness and quality of its investments.
- (C) The competency, character, and integrity of its management.
- (D) The competency, character, and integrity of persons who own or have a controlling interest in the assuming insurer.
- (E) Whether claims under its contracts are promptly and fairly adjusted and are promptly and fully paid in accordance with the law and the terms of the contracts.

(3) Credit shall not be allowed a domestic ceding insurer if the assuming insurer's accreditation has been revoked by the commissioner after notice and hearing.

(c) Credit shall be allowed when the reinsurance is ceded to an assuming insurer that has been certified by the commissioner pursuant to Section 922.41.

(d) (1) Credit shall be 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 subdivision (b) of Section 922.7 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 shall report annually to

the commissioner information substantially the same as that required to be reported on the NAIC Annual Statement form by licensed insurers or any other form required by the NAIC.

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

(A) The commissioner of the state where the trust is domiciled.

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

The trust and any trust amendments shall also be filed with the commissioner of every state in which the ceding insurer beneficiaries of the trust are domiciled. Notwithstanding the foregoing, nothing in this paragraph shall prevent the commissioner from disapproving the form of the trust if it is not in compliance with this state's laws and regulations.

(3) Credit for reinsurance shall not be granted under this subdivision unless the following requirements are met:

(A) The trust instrument shall provide that contested claims shall be valid, enforceable, and payable out of funds in trust to the extent remaining unsatisfied 30 days after entry of the final order of any court of competent jurisdiction in the United States.

(B) The trust shall vest legal title to its assets in the trustees of the trust for the benefit of the grantor's United States ceding insurers, their assigns, and successors in interest.

(C) The trust and the assuming insurer shall be subject to examination as determined by the commissioner.

(D) The trust shall remain in effect for as long as the assuming insurer, or any member or former member of a group of insurers, shall have outstanding obligations due under the reinsurance agreements subject to the trust.

(E) No later than February 28 of each year, the trustees of the trust shall report to the commissioner in writing setting forth the balance of the trust and listing the trust's investments at the preceding yearend and shall certify the date of termination of the trust, if so planned, or certify that the trust shall not expire within the next 18 months.

(F) The assuming insurer shall do both of the following:

(i) Submit to the jurisdiction of any court of competent jurisdiction in any state of the United States, comply with all requirements necessary to give the court jurisdiction, and abide by the final decision of the court or of any appellate court in the event of an appeal.

(ii) Designate the commissioner or an attorney in this state as its true and lawful agent upon whom may be served any lawful process in any action, suit, or proceeding instituted by or on behalf of the ceding insurer.

This subparagraph 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.

(G) The assuming insurer shall agree in the trust agreement that notwithstanding any other provision in the trust instrument, if the trust fund

is inadequate because it contains an amount less than the amount required by paragraph (4), 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:

(i) The trustee shall 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.

(ii) The assets shall be distributed by, and insurance claims shall 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.

(iii) 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 shall be returned by the commissioner with regulatory oversight to the trustee for distribution in accordance with the trust agreement.

(iv) The grantor hereby waives any right otherwise available to it under United States law that is inconsistent with this provision.

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

(A) The trust fund for a single assuming insurer shall consist of funds in trust in an amount not less than the assuming insurer's liabilities attributable to reinsurance ceded by United States domiciled ceding insurers, and, in addition, the assuming insurer shall maintain a trustee surplus of not less than twenty million dollars (\$20,000,000), except as provided in subparagraph (B), (C), or (D).

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

(i) For reinsurance ceded under reinsurance agreements with an inception, amendment, or renewal date on or after January 1, 1993, the trust shall consist of a trustee 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.

(ii) 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 article, the trust shall consist of a trustee account in an amount not less than the respective underwriters' several insurance and reinsurance liabilities attributable to business written in the United States.

(iii) In addition to the trusts required in clauses (i) and (ii), the group shall maintain in trust a trustee surplus of which one hundred million dollars (\$100,000,000) shall be held jointly for the benefit of the United States domiciled ceding insurers of any member of the group for all years of account.

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

(v) The group shall, within 90 days after its financial statements are due to be filed with the group's domiciliary regulator, 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.

(C) In the case of a group of incorporated insurers under common administration, the group shall meet all of the following requirements:

(i) Have continuously transacted an insurance business outside the United States for at least three years immediately prior to making application for accreditation and be in good standing with its domiciliary regulator.

(ii) Demonstrate that individual insurer members maintain standards and financial conditions reasonably comparable to admitted insurers.

(iii) Maintain aggregate policyholders' surplus of at least ten billion dollars (\$10,000,000,000).

(iv) 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 such group.

(v) In addition, maintain a joint trustee surplus of which one hundred million dollars (\$100,000,000) shall be held jointly for the benefit of United States ceding insurers of any member of the group as additional security for these liabilities. The commissioner shall have the authority to require additional amounts to be held in the trust as a condition for initial or continued accreditation if the commissioner determines that these additional amounts are required for the protection of ceding insurers.

(vi) Within 90 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 for each underwriter member of the group prepared by its independent public accountant.

(D) 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 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 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 cashflows, and shall 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 50 percent of the assuming insurer's liabilities attributable to reinsurance ceded by United States ceding insurers covered by the trust.

(e) Credit shall be allowed when the reinsurance ceded to an assuming insurer not meeting the requirements of subdivision (a), (b), (c), or (d), but only as to the insurance of risks located in jurisdictions where the reinsurance is required by applicable law or regulation of that jurisdiction. As used in this section, "jurisdiction" means state, district, or territory of the United States and any lawful national government.

SEC. 5. Section 922.41 is added to the Insurance Code, to read:

922.41. (a) Credit shall be allowed a domestic insurer 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. Credit shall be allowed at all times for which statutory financial statement credit for reinsurance is claimed under this section. The credit allowed shall be based upon the security held by or on behalf of the ceding insurer in accordance with a rating assigned to the certified reinsurer by the commissioner. The security shall be in a form consistent with the provisions of this section, any regulations promulgated by the commissioner and Section 922.5.

(b) In order to be eligible for certification, 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, as determined by the commissioner pursuant to subdivisions (f) and (g).

(2) The assuming insurer shall maintain minimum capital and surplus, or its equivalent, in an amount to be determined by the commissioner, but no less than two hundred fifty million dollars (\$250,000,000) calculated in accordance with paragraph (4) of subdivision (f) of this section or Section 922.5. 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 two hundred fifty million dollars (\$250,000,000) and a central fund containing a balance of at least two hundred fifty million dollars (\$250,000,000).

(3) The assuming insurer shall maintain financial strength ratings from two or more rating agencies deemed acceptable by the commissioner. These ratings shall be based on interactive communication between the rating agency and the assuming insurer and shall not be based solely on publicly available information. These financial strength ratings will be one factor used by the commissioner in determining the rating that is assigned to the assuming insurer. Acceptable rating agencies include the following:

- (A) Standard & Poor's.
- (B) Moody's Investors Service.
- (C) Fitch Ratings.
- (D) A.M. Best Company.
- (E) Any other nationally recognized statistical rating organization.

(4) The assuming insurer shall agree to submit to the jurisdiction of this state, appoint the commissioner or a designated attorney in this state as its agent for service of process in this state, and agree to provide security for 100 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.

(5) The assuming insurer shall 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.

(6) The certified reinsurer shall comply with any other requirements deemed relevant by the commissioner.

(c) (1) If an applicant for certification has been certified as a reinsurer in an NAIC accredited jurisdiction, the commissioner may defer to that jurisdiction's certification, and has the discretion to defer to the rating assigned by that jurisdiction if the assuming insurer submits a properly executed Form CR-1 (as published on the department's Internet Web site), and such additional information as the commissioner requires. The commissioner, however, may perform an independent review and determination of any applicant. The assuming insurer shall then be considered to be a certified reinsurer in this state.

(2) If the commissioner defers to a certification determination by another state, any change in the certified reinsurer's status or rating in the other jurisdiction shall apply automatically in this state as of the date it takes effect in the other jurisdiction unless the commissioner otherwise determines. The certified reinsurer shall notify the commissioner of any change in its status or rating within 10 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 subdivision (h).

(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 suspends or revokes the certified reinsurer's certification in accordance with this section and Section 922.42, 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) An association, including incorporated and individual unincorporated underwriters, may be a certified reinsurer. In order to be eligible for certification, in addition to satisfying requirements of subdivision (b) the reinsurer shall meet all of the following 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 shall 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 underwriter member; or if a certification is unavailable, financial statements, prepared by independent public accountants, of each underwriter member of the association.

(e) (1) The commissioner shall post notice on the department's Internet Web site promptly upon receipt of any application for certification, including 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 90 days after posting the notice required by this subdivision.

(2) The commissioner shall issue written notice to an assuming insurer that has made application and has been approved as a certified reinsurer. Included in such notice shall be the rating assigned the certified reinsurer in accordance with subdivision (h). The commissioner shall publish a list of all certified reinsurers and their ratings.

(f) The certified reinsurer shall 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. All information submitted by certified reinsurers that is not otherwise public information subject to disclosure shall be exempted from disclosure under Chapter 3.5 (commencing with Section 6250) of Division 7 of Title 1 of the Government Code, and shall be withheld from public disclosure. The applicable information filing requirements are as follows:

(1) Notification within 10 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 those changes and the reasons for those changes.

(2) Annually, Form CR-F or CR-S, as applicable pursuant to the instructions as published on the department's Internet Web site.

(3) Annually, the report of the independent auditor on the financial statements of the insurance enterprise, on the basis described in paragraph (4).

(4) Annually, audited financial statements, (audited United States Generally Accepted Accounting Principles basis, if available, audited International Financial Reporting Standards basis statements are allowed, but must include an audited footnote reconciling equity and net income to a United States Generally Accepted Accounting Principles basis, or, with the written permission of the commissioner, audited International Financial Reporting Standards statements with reconciliation to United States Generally Accepted Accounting Principles 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 three years filed with the certified reinsurer's supervisor.

(5) At least annually, an updated list of all disputed and overdue reinsurance claims regarding reinsurance assumed from United States domestic ceding insurers.

(6) 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.

(7) Any other information that the commissioner may reasonably require.

(g) If the commissioner certifies a non-United States domiciled insurer, the commissioner shall create and publish a list of qualified jurisdictions, under which an assuming insurer licensed and domiciled in such jurisdiction is eligible to be considered for certification by the commissioner as a certified reinsurer.

(1) 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 shall 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. The commissioner shall determine the appropriate process for evaluating the qualifications of those jurisdictions. Prior to its listing, a qualified jurisdiction shall agree in writing 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, including, but not limited to, the following:

(A) The framework under which the assuming insurer is regulated.

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

(C) The substance of financial and operating standards for assuming insurers in the domiciliary jurisdiction.

(D) 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.

(E) The domiciliary regulator's willingness to cooperate with United States regulators in general and the commissioner in particular.

(F) The history of performance by assuming insurers in the domiciliary jurisdiction.

(G) Any documented evidence of substantial problems with the enforcement of final United States judgments in the domiciliary jurisdiction.

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

(1) Any other matters deemed relevant by the commissioner.

(2) The commissioner shall consider the list of qualified jurisdictions published through the National Association of Insurance Commissioners (NAIC) committee process in determining qualified jurisdictions. The commissioner may include on the list published pursuant to this section, any jurisdiction on the NAIC list of qualified jurisdictions, or on any equivalent list of the United States Treasury.

(3) If the commissioner approves a jurisdiction as qualified that does not appear on either the NAIC list of qualified jurisdictions, or the United States Treasury list, the commissioner shall provide thoroughly documented justification in accordance with criteria to be developed under this section.

(4) United States jurisdictions that meet the requirements for accreditation under the NAIC financial standards and accreditation program shall be recognized as qualified jurisdictions.

(5) 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.

(h) The commissioner shall 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 pursuant to this section. The commissioner shall publish a list of all certified reinsurers and their ratings.

(1) 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 underwriters that has been approved to do business as a single certified reinsurer may be evaluated on the basis of its group rating. Factors that may be considered as part of the evaluation process include, but are not limited to, the following:

(A) 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 set forth in clauses (i) to (vi), inclusive. The commissioner shall 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.

(i) Ratings category "Secure - 1" corresponds to A.M. Best Company rating A++; Standard & Poor's rating AAA; Moody's Investors Service rating Aaa; and Fitch Ratings rating AAA.

(ii) Ratings category "Secure - 2" corresponds to A.M. Best Company rating A+; Standard & Poor's rating AA+, AA, or AA-; Moody's Investors Service rating Aa1, Aa2, or Aa3; and Fitch Ratings rating AA+, AA, or AA-.

(iii) Ratings category "Secure - 3" corresponds to A.M. Best Company rating A; Standard & Poor's rating A+ or A; Moody's Investors Service rating A1 or A2; and Fitch Ratings rating A+ or A.

(iv) Ratings category “Secure - 4” corresponds to A.M. Best Company rating A-; Standard & Poor’s rating A-; Moody’s Investors Service rating A3; and Fitch Ratings rating A-.

(v) Ratings category “Secure - 5” corresponds to A.M. Best Company rating B++ or B+; Standard & Poor’s rating BBB+, BBB, or BBB-; Moody’s Investors Service rating Baa1, Baa2, or Baa3; and Fitch Ratings rating BBB+, BBB, or BBB-.

(vi) Ratings category “Vulnerable - 6” corresponds to A.M. Best Company rating B, B-, C++, C+, C, C-, D, E, or F; Standard & Poor’s rating BB+, BB, BB-, B+, B, B-, CCC, CC, C, D, or R; Moody’s Investors Service rating Ba1, Ba2, Ba3, B1, B2, B3, Caa, Ca, or C; and Fitch Ratings rating BB+, BB, BB-, B+, B, B-, CCC+, CC, CCC-, or DD.

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

(C) For certified reinsurers domiciled in the United States, 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).

(D) For certified reinsurers not domiciled in the United States, a review annually of Form CR-F (for property/casualty reinsurers) or Form CR-S (for life and health reinsurers) (as published on the department’s Internet Web site).

(E) 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.

(F) Regulatory actions against the certified reinsurer.

(G) The report of the independent auditor on the financial statements of the insurance enterprise, on the basis described in subparagraph (H).

(H) For certified reinsurers not domiciled in the United States, audited financial statements, (audited United States Generally Accepted Accounting Principles basis, if available, audited International Financial Reporting Standards basis statements are allowed, but must include an audited footnote reconciling equity and net income to a United States Generally Accepted Accounting Principles basis, or, with the written permission of the commissioner, audited International Financial Reporting Standards statements with reconciliation to United States Generally Accepted Accounting Principles certified by an officer of the company), regulatory filings, and actuarial opinion (as filed with the non-United States jurisdiction supervisor). Upon the initial application for certification, the commissioner shall consider audited financial statements for the last three years filed with its non-United States jurisdiction supervisor.

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

(J) A certified reinsurer's participation in any solvent scheme of arrangement, or similar procedure, which involves United States 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.

(K) Any other information deemed relevant by the commissioner.

(2) Based on the analysis conducted under subparagraph (E) of paragraph (1) 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 United States ceding insurers, provided that the commissioner shall, at a minimum, increase the security the certified reinsurer is required to post by one rating level under regulations promulgated by the commissioner, if the commissioner finds either of the following:

(A) More than 15 percent 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 one hundred thousand dollars (\$100,000) for each ceding insurer.

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

(3) The assuming insurer shall submit a properly executed Form CR-1 (as published on the department's Internet Web site) as evidence of its submission to the jurisdiction of this state, appointment of the commissioner as an agent for service of process in this state, and agreement to provide security for 100 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. The commissioner shall not certify any assuming insurer that is domiciled in a jurisdiction that the commissioner has determined does not adequately and promptly enforce final United States judgments or arbitration awards.

(4) (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 subdivision (h).

(B) The commissioner shall have the authority to suspend, revoke, or otherwise modify a certified reinsurer's certification 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.

(D) Upon revocation of the certification of a certified reinsurer by the commissioner, the assuming insurer shall be required to post security in accordance with Section 922.5 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 subdivision (d) of Section 922.4, the commissioner may allow additional credit equal to the ceding insurer's pro rata share of those funds, discounted to reflect the risk of uncollectibility 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 uncollectibility.

(i) A certified reinsurer shall secure obligations assumed from United States ceding insurers under this subdivision at a level consistent with its rating. The amount of security required in order for full credit to be allowed shall correspond with the following requirements:

Ratings security required

Secure - 1: 0%

Secure - 2: 10%

Secure - 3: 20%

Secure - 4: 50%

Secure - 5: 75%

Vulnerable - 6: 100%

(1) In order for a domestic ceding insurer to qualify for full financial statement credit for reinsurance ceded to a certified reinsurer, the certified reinsurer shall maintain security in a form acceptable to the commissioner and consistent with the provisions of Section 922.5, or in a multibeneficiary trust in accordance with subdivision (d) of Section 922.4, except as otherwise provided in this subdivision. In order for a domestic insurer to qualify for full financial statement credit, reinsurance contracts entered into or renewed under this section shall include a proper funding clause that requires 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 under this section for reinsurance ceded to the certified reinsurer.

(2) If a certified reinsurer maintains a trust to fully secure its obligations subject to subdivision (d) of Section 922.4, 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 subdivision or comparable laws of other United States jurisdictions and for its obligations subject to subdivision (d) of Section 922.4. It shall be a condition to the grant of certification under this section that the certified reinsurer shall have bound itself, by the language of the trust and agreement with the commissioner with principal regulatory oversight of each of those trust accounts, to fund, upon termination of any of those trust accounts, out of the remaining surplus of those trusts any deficiency of any other of those trust accounts.

(3) The minimum trustee surplus requirements provided in subdivision (d) of Section 922.4 are not applicable with respect to a multibeneficiary trust maintained by a certified reinsurer for the purpose of securing obligations incurred under this subdivision, except that the trust shall maintain a minimum trustee surplus of ten million dollars (\$10,000,000).

(4) With respect to obligations incurred by a certified reinsurer under this subdivision, if the security is insufficient, the commissioner shall reduce the allowable credit by an amount proportionate to the deficiency, and have 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.

(5) For purposes of this subdivision, a certified reinsurer whose certification has been terminated for any reason shall be treated as a certified reinsurer required to secure 100 percent of its obligations.

(A) As used in this subdivision, the term "terminated" means revocation, suspension, voluntary surrender, and inactive status.

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

(6) The commissioner shall require the certified reinsurer to post 100-percent security in accordance with Section 922.5, for the benefit of the ceding insurer or its estate, upon the entry of an order of rehabilitation, liquidation, or conservation against the ceding insurer.

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

(8) In order to facilitate the prompt payment of claims, a certified reinsurer shall 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 that is likely to result in significant insured losses, as recognized by the commissioner. The one-year deferral period is contingent upon the certified reinsurer continuing to pay claims in a timely manner, as determined by the commissioner, in writing. 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:

(A) Line 1: Fire.

- (B) Line 2: Allied lines.
- (C) Line 3: Farmowners multiple peril.
- (D) Line 4: Homeowners multiple peril.
- (E) Line 5: Commercial multiple peril.
- (F) Line 9: Inland marine.
- (G) Line 12: Earthquake.
- (H) Line 21: Auto physical damage.

(9) Credit for reinsurance under this section shall apply only to reinsurance contracts entered into or renewed on or after the effective date of the certification of the assuming insurer. Any reinsurance contract entered into prior to the effective date of the certification of the assuming insurer that is subsequently amended by mutual agreement of the parties to the reinsurance contract after the effective date of the certification of the assuming insurer, or a new reinsurance contract, covering any risk for which collateral was provided previously, shall only be subject to this section with respect to losses incurred and reserves reported from and after the effective date of the amendment or new contract.

(10) Nothing in this section shall be construed to prohibit the parties to a reinsurance agreement from agreeing to provisions establishing security requirements that exceed the minimum security requirements established for certified reinsurers under this section.

(j) 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 shall continue to comply with all applicable requirements of this section, and the commissioner shall assign a rating that takes into account, if relevant, the reasons why the reinsurer is not assuming new business.

(k) Notwithstanding this section, credit for reinsurance or deduction from liability by a domestic ceding insurer for cessions to a certified reinsurer may be disallowed upon a finding by the commissioner that the application of the literal provisions of this section does not accomplish its intent, or either the financial condition of the reinsurer or the collateral or other security provided by the reinsurer does not, in substance, satisfy the credit for reinsurance requirements in Section 922.4.

(l) This section shall remain in effect only until January 1, 2016, and as of that date is repealed, unless a later enacted statute, that is enacted before January 1, 2016, deletes or extends that date.

SEC. 6. Section 922.42 is added to the Insurance Code, to read:

922.42. (a) 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.

(b) The commissioner shall give the reinsurer notice and opportunity for hearing. The suspension or revocation shall not take effect until after the commissioner's order on hearing, unless any of the following applies:

- (1) The reinsurer waives its right to hearing.

(2) 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 subdivision (b) of Section 922.41.

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

(c) 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 922.5. 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 subdivision (i) of Section 922.41 or Section 922.5.

SEC. 7. Section 922.43 is added to the Insurance Code, to read:

922.43. The actual costs and expenses incurred by the department in reviewing requests for accreditation or certification, trusts, and subsequent amendments established or maintained pursuant to Sections 922.1 to 922.7, inclusive, and subsequent reviews, shall be charged to and collected from the requesting reinsurer. If the reinsurer fails to pay the actual costs and expenses promptly when due, then the commissioner may deny the requests, may refuse to allow credit for reinsurance ceded to that reinsurer or group, or may revoke the reinsurer's accreditation or certification.

SEC. 8. Section 922.5 of the Insurance Code is amended to read:

922.5. (a) An asset or a deduction from liability for reinsurance ceded by a domestic insurer to an assuming insurer not meeting the requirements of Section 922.4 shall be allowed in an amount not exceeding the liabilities carried by the ceding insurer to the extent of either of the following:

(1) The asset or deduction is not greater than the amount of funds held by the ceding insurer under a reinsurance contract with that assuming insurer as security for the payment of obligations thereunder and such funds are held in the United States under the exclusive control of the ceding insurer.

(2) The asset or deduction is not greater than the amount of funds held in a trust, satisfactory to the commissioner, on behalf of the ceding insurer under a reinsurance contract with such assuming insurer as security for the payment of obligations thereunder and is held in a qualified United States financial institution, as defined in subdivision (b) of Section 922.7, subject to withdrawal solely by the ceding insurer.

The security under this subdivision may be in the form of cash or securities authorized as general investments under Article 3 (commencing with Section 1170) of Chapter 2, or securities listed by the Securities Valuation Office of the NAIC, including those deemed exempt from filing, as defined by the Purposes and Procedures Manual of the National Association of Insurance Commissioners Securities Valuation Office, qualifying as admitted assets

under this code and with liquidity meeting the requirements of Section 706.5, and not otherwise disallowed in the commissioner's discretion.

(b) An asset or a deduction from liability for reinsurance ceded by a domestic insurer to an assuming insurer not meeting the requirements of Section 922.4 shall be allowed in an amount not exceeding the liabilities carried by the ceding insurer to the extent that security is provided in the form of letters of credit, satisfactory to the commissioner, which shall be:

(1) Clean, irrevocable, unconditional letters of credit, issued or confirmed by qualified United States financial institutions, as defined in subdivision (a) of Section 922.7, effective no later than December 31st in respect of the year for which filing is being made, and in the possession of the ceding insurer on or before the filing date of its annual statement.

(2) Letters of credit meeting applicable standards of issuer acceptability as of the dates of their issuance or confirmation and shall, notwithstanding the issuing or confirming institutions' 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.

(c) For purposes of this section, the phrase "deemed exempt from filing as defined by the Purposes and Procedures Manual of the National Association of Insurance Commissioners Securities Valuation Office" shall mean all United States government securities, and all other securities or bonds with a rating of SVO 1 or FE 1 listed by the National Association of Insurance Commissioners Securities Valuation Office as exempt.

SEC. 9. Section 922.6 of the Insurance Code is repealed.

SEC. 10. Section 922.6 is added to the Insurance Code, to read:

922.6. Credit for reinsurance shall not be denied a foreign ceding insurer to the extent that credit is recognized by the ceding insurer's domestic state regulator, provided that the domestic state is accredited by the National Association of Insurance Commissioners (NAIC), or the domestic state regulator has financial solvency requirements substantially similar to the requirements necessary for NAIC accreditation.

SEC. 11. Section 922.8 of the Insurance Code is amended to read:

922.8. (a) The commissioner, after notice, comment period, and a hearing if requested by more than 10 affected insurers, may issue a bulletin setting forth reasonable requirements for the allowance of reinsurance as an asset or deduction from liability consistent with Sections 922.4 to 922.6, inclusive, including the following:

- (1) Filing requirements for an accredited assuming insurer.
- (2) Accreditation requirements for an assuming insurer with less than a twenty million dollar (\$20,000,000) surplus as regards policyholders.
- (3) The definition of "liabilities" as used in Sections 922.4 and 922.5.
- (4) Investment guidelines for trust funds established and maintained pursuant to subdivision (d) of Section 922.4.
- (5) Definitions and required or permitted conditions for trust funds established and maintained pursuant to Section 922.5.

(6) Requirements of letters of credit established and maintained pursuant to Section 922.5.

(b) On or before January 1, 1998, the commissioner shall notify the Legislature that the bulletin has been promulgated so that the Legislature is able to ensure the commissioner's compliance with the requirements of this subdivision.

(c) The bulletin authorized by this section shall have the same force and effect, and may be enforced by the commissioner to the same extent and degree, as regulations issued by the commissioner until the time that the commissioner issues additional or amended regulations pursuant to subdivision (d).

(d) The commissioner shall adopt regulations implementing the provisions of this law, that shall supersede the bulletin authorized by this section, no later than December 31, 2001.

SEC. 12. Section 922.85 is added to the Insurance Code, to read:

922.85. The commissioner may adopt regulations in accordance with the procedures provided in Chapter 3.5 (commencing with Section 11340) of Part 1 of Division 3 of Title 2 of the Government Code or otherwise prescribe requirements consistent with Sections 922.4, 922.41, 922.42, 922.43, and 922.5, provided the commissioner may update subparagraph (A) of paragraph (1) of subdivision (h) and subdivision (i) of Section 922.41 to add other nationally recognized statistical rating agencies, or to modify the rating categories, the corresponding financial ratings, or the percentage of security required to conform to changes in these factors adopted by the National Association of Insurance Commissioners.

SEC. 13. Section 12121 of the Insurance Code is amended to read:

12121. (a) For financial guaranty insurance that takes effect on or after January 1, 1991, an insurer authorized to transact financial guaranty insurance shall receive credit for reinsurance as an asset or as a reduction from liabilities only if the reinsurance is placed with a reinsurer as provided in subdivision (b), and if the reinsurance agreement may be terminated or amended only if one or more of the following applies:

(1) At the option of the reinsurer or the ceding insurer if the reinsurance agreement provides that the liability of the reinsurer with respect to policies in effect at the date of termination shall continue until the expiration or cancellation of each such policy.

(2) With the consent of the ceding company, if the reinsurance agreement provides for a cutoff of the reinsurance in force as of the date of termination.

(3) At the discretion of the commissioner acting as rehabilitator, liquidator, or receiver of the ceding or assuming insurer.

(b) Reinsurance may be placed with one of the following:

(1) Another financial guaranty insurance corporation admitted pursuant to this article to transact financial guaranty insurance which may be under common control with the ceding financial guaranty insurer or financial guaranty corporation, but which does not own, and is not owned by, in whole or in part, directly or indirectly, the ceding financial guaranty insurer or financial guaranty insurance corporation.

(2) Another financial guaranty insurance corporation admitted pursuant to this article which does own, or is owned by, in whole or in part, directly or indirectly, the ceding financial guaranty insurer or financial guaranty insurance corporation provided that (A) the value of the ownership interest in either case does not exceed the greater of (i) 35 percent of its combined capital and surplus or (ii) 50 percent of the excess of its surplus over its liabilities and capital, and (B) the financial guaranty insurance corporation providing the reinsurance is rated at the time of cession and thereafter in one of the two top generic rating classifications by a securities rating agency acceptable to the commissioner.

(3) An insurer admitted to transact surety insurance but not financial guaranty insurance pursuant to this article, if the insurer meets all of the following criteria:

(A) Has and maintains combined capital and surplus of at least fifty million dollars (\$50,000,000).

(B) Establishes and maintains the reserves required in Sections 12108, 12109, and 12110, except that if the reinsurance agreement is not pro rata the contribution to the contingency reserve shall be equal to 50 percent of the quarterly earned insurance premium.

(C) Complies with the provisions of subdivision (b) of Section 12114, except that its maximum aggregate assumed total net liability shall be one-half that permitted for a financial guaranty insurance corporation. For the purpose of determining compliance with this clause, the assuming reinsurer, unless at the time of cession and thereafter it is rated in one of the two top generic rating classifications by a securities rating agency acceptable to the commissioner, shall be limited to using 10 percent of its capital and surplus in making this calculation.

(D) Complies with the provisions of Section 12115.

(E) If the insurer is an affiliate, parent, or subsidiary of the financial guaranty insurance corporation, the affiliate, parent, or subsidiary shall not assume a percentage of the corporation's total liability in excess of its percentage of equity interest in the corporation.

(F) Assumes from the financial guaranty insurance corporation and any affiliate, parent, or subsidiary that is a financial guaranty insurance corporation or an insurer writing only financial guaranty insurance as is or would be permitted by this article, and any other kinds of insurance that a financial guaranty insurance corporation may write in this state, together with all other reinsurers subject to this paragraph, less than 50 percent of the total exposures insured by the financial guaranty insurance corporation and such affiliates, parent, or subsidiaries after deducting any reinsurance placed with another financial guaranty insurance corporation that is not an affiliate, parent, or subsidiary or an insurer writing only financial guaranty insurance as is or would be permitted by this article that is not an affiliate, parent, or subsidiary.

(4) A nonadmitted insurer transacting only financial guaranty insurance as is or would be permitted by this article and that otherwise complies with the provisions of subparagraphs (A), (E), and (F) of paragraph (3), and

otherwise complies with paragraph (1) or (2), and in compliance with the requirements of subdivision (b) or (c) of Section 922.4 or subdivision (a) of Section 922.5, as applicable.

(5) A nonadmitted insurer not transacting only financial guaranty insurance as is or would be permitted by this article and that complies with the provisions of subparagraphs (A), (C), (E), and (F) of paragraph (3) in an amount not exceeding the liabilities carried by the ceding financial guaranty insurance corporation and in compliance with the requirements of subdivision (b), (c), or (d) of Section 922.4 or subdivision (a) or (b) of Section 922.5, as applicable.

(c) In determining whether the financial guaranty insurance corporation meets the limitations imposed by Section 12115, in addition to credit for other types of qualifying reinsurance, the financial guaranty insurance corporation's aggregate risk may be reduced to the extent of the limit for aggregate reinsurance but, in no event, in an amount greater than the amount of the aggregate risk that will become due during the unexpired term of the reinsurance agreement in excess of the financial guaranty insurance corporation's retention pursuant to the reinsurance agreement.