STATE OF TENNESSEE
DEPARTMENT OF COMMERCE AND INSURANCE
500 JAMES ROBERTSON PARKWAY
NASHVILLE, TENNESSEE 37243-5065
615-741-6007

BILL HASLAM
GOVERNOR

JULIE MIX McPEAK
COMMISSIONER

Bulletin No. 15-02

TO: All Tennessee Captive Insurance Companies and Approved Captive Managers

FROM: Julie Mix McPeak, Commissioner Julie Mix McPeak

RE: Credit for Reinsurance Ceded to Unauthorized Reinsurers by Tennessee Captive Insurance Companies

DATE: October 22, 2015

The purpose of this Bulletin is to provide guidance to the Tennessee captive insurance industry on credit for reinsurance obtained by Tennessee captives from unauthorized reinsurers.

Tenn. Code Ann. § 56-13-112(b) states, in part:

> The commissioner shall have the discretion to allow a captive insurance company to take credit for the reinsurance of risks or portions of risks ceded to an unauthorized reinsurer, after review, on a case by case basis. The commissioner may require any documents, financial information or other evidence that such an unauthorized reinsurer will be able to demonstrate adequate security for its financial obligations.

Tenn. Code Ann. § 56-13-112(c) states:

> In addition to reinsurers authorized by this title, a captive insurance company may take credit for the reinsurance of risks or portions of risks ceded to a pool, exchange or association to the extent authorized by the commissioner. The commissioner may require any documents, financial information or other evidence that such a pool, exchange or association will be able to provide adequate security for its financial obligations. The commissioner may deny authorization or impose any limitations on the activities of a reinsurance pool, exchange or association that, in the commissioner's judgment, are necessary and proper to provide adequate security for the ceding captive insurance company and for the protection and consequent

ceding captive insurance company and for the protection and consequent benefit of the public at large.

The Department makes an initial determination whether to allow a Tennessee captive insurance company to take credit for reinsurance at the time the company is formed. Captives who desire to utilize an unauthorized reinsurer will include specific information with their proposed business plan filed with the application. Absent adverse notification from the Department, captive insurance companies may deem their existing unauthorized reinsurance arrangements that were included in the original business plan, or were included in an approved change of business plan, to be allowed on an ongoing basis under Tenn. Code Ann. § 56-13-112. Such reinsurance contracts will be reviewed during the captive insurance company's Tenn. Code Ann. § 56-13-109 examination, or as needed.

Notwithstanding the above, any authorization made by the Department for a captive insurance company to take credit for reinsurance from an unauthorized reinsurer is valid for that captive only in accordance with the terms of its business plan. Other Tennessee captives seeking to enter into a reinsurance contract with the same unauthorized reinsurer should likewise include the details of the proposed reinsurance agreement in its proposed business plan or submit a change of business plan.

In deciding whether to grant a captive insurance company credit for reinsurance purchased from an unauthorized reinsurer, the Department will give the greatest weight to the following criteria:

- The policy issued to the original named insured is issued by a traditional admitted domestic insurance carrier acting as a front.
- The reinsurance agreement is made upon secured collateral. This includes reinsurance agreements made on a funds withheld basis, via a domestic U.S. trust, or via a letter of credit issued by a reputable U.S. based financial institution.
- The reinsurance agreements are obtained from an accredited reinsurer as defined by Tenn. Code Ann. § 56-2-208.
- Reinsurance is obtained from a reinsurer that is highly rated by a reputable rating agency.
- The reinsurer has a paid in unencumbered capital and surplus of at least $20,000,000 and agrees to submit to Tennessee copies of its audited annual financial statements as well as copies of any examination report conducted by its home domicile.

Additionally, the Department will give weight to arrangements where the reinsurer is domiciled in a jurisdiction with a solid reputation for providing accountability and oversight to its insurers. The Department also places weight on the experience and reputation of the captive manager and other service providers selected by the captive owner.

Some captives choose to participate in reinsurance exchange pooling arrangements structured in any number of ways. When such pooling arrangements include scenarios where a Tennessee captive insurance company cedes risk to an unauthorized reinsurer, the Department will give the greatest weight to arrangements where the ceded premium is held in a domestic U.S. trust, or where all pool participants are managed by the same captive manager. Any type of proposed pooling arrangement should include information sufficient to satisfy the Department that adequate controls are present and that the pooling arrangement, and its participants, possesses sufficient liquidity and accountability.

The foregoing is not intended to be an exhaustive list of acceptable reinsurance structures. The Department retains the discretion to grant credit for reinsurance to any unauthorized reinsurer on a case-by-case basis. Captive owners, and prospective captive owners, are encouraged to meet with the Department to discuss their proposed plan of operations to work out an acceptable arrangement where credit for reinsurance can be granted.

Due to the unique nature of the captive insurance industry, this guidance is only applicable to captive insurance companies and is not applicable to other insurance companies licensed by the Department of Commerce and Insurance. This guidance also does not apply to risk retention groups, including risk retention groups organized as captive insurance companies.

Any questions about the intent of this Bulletin should be directed to the Insurance Division, Captive Insurance Section, 7th Floor, Davy Crockett Tower, 500 James Robertson Parkway, Nashville, Tennessee, 37243, and/or telephone number (615) 741-3805.