THE CINCINNATI INSURANCE COMPANIES

The Cincinnati Insurance Company ▪ The Cincinnati Indemnity Company
The Cincinnati Casualty Company ▪ The Cincinnati Specialty Underwriters Insurance Company
The Cincinnati Life Insurance Company

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July 23, 2018

Honorable Maria T. Vullo, Chair
Reinsurance Task Force
National Association of Insurance Commissioners
1100 Walnut Street, Suite 1500
Kansas City, MO 64106-2197

RE: Comments of The Cincinnati Insurance Companies on Proposed Revisions to the Credit for Reinsurance Model Law (785) & Regulation (786)

Dear Superintendent Vullo:

The Cincinnati Insurance Companies ("Cincinnati") offer the following comments on the proposed changes to the Credit for Reinsurance Model Law (785) and Model Regulation (786), as exposed for comment by the Reinsurance Task Force on June 21, 2018.

INTRODUCTION. The proposed changes are being pursued by the NAIC to implement the terms of the covered agreement agreed to by United States and the European Union (EU) relating to reinsurance collateral, and to offer similar relief from reinsurance collateral to qualifying non-EU jurisdictions. The proposed changes would create a new category or foreign jurisdiction to be known as a "Reciprocal Jurisdiction." These jurisdictions would include jurisdictions that have entered into a treaty or other international agreement with the United States governing credit for reinsurance, and to other jurisdictions that have already been designated as a Qualified Jurisdiction and that meet certain other requirements. Reinsurers domiciled or headquartered in Reciprocal Jurisdictions would not be required to post collateral.

KEY PRINCIPLES. When the Reinsurance Task Force held its public hearing on this issue on February 20, 2018 in New York City, we emphasized four key principles in our public testimony:

1. To ensure the primacy of state insurance regulation in the implementation of the covered agreement, and when considering possible approaches to extend the covered agreement's zero reinsurance collateral benefit to non-EU jurisdictions (i.e., no new covered agreements, which erode the primacy of state insurance regulation).
2. To ensure that no jurisdiction gets the benefit of zero reinsurance collateral without granting mutual recognition of the entire U.S. system of insurance regulation.
3. To only grant the benefit of zero reinsurance collateral to non-EU jurisdictions which agree to adhere to all terms and conditions included in the U.S.-EU covered agreement.

4. To require reversion to 100% collateral for any assuming reinsurer domiciled in a jurisdiction which breaches the terms and conditions of the covered agreement, or breaches similar terms and conditions imposed upon non-EU jurisdictions as a condition to obtain the benefit of zero collateral.

Although the revisions to the Credit for Reinsurance Model Law (785) and Model Regulation (786) exposed for comment on June 21 are generally consistent with these key principles, they do fall short in several respects, as more fully explained below.

COMMENTS SUBMITTED BY OUR TRADE ASSOCIATIONS. We are members of three national insurance trade associations (ACLI, PCI and RAA), all of whom are preparing their own comments on the proposed changes to the Credit for Reinsurance Model Law (785) and Model Regulation (786). Having been privy to, and involved in, the preparation of the comment letters to be submitted by ACLI, PCI and RAA, we believe you will find those comment letters to be most helpful as you consider the need for amendments and clarifications to the Model Law & Regulation changes proposed by the Reinsurance Task Force on June 21.

CINCINNATI'S PRIMARY CONCERNS WITH THE PROPOSED CHANGES. Our primary concerns with the proposed changes to the Model Law and Regulation include the following:

1. Law vs. Regulation. Except for the forms included in the Credit for Reinsurance Model Regulation (786),[1] we believe that the **entirety** of the regulation, including the changes proposed on June 21, should be incorporated into the Credit for Reinsurance Model Law (785).

   We have always been concerned that too much of the NAIC's Credit for Reinsurance public policy pronouncement was contained in the model regulation, which is more prone to tinkering and gamesmanship than a legislatively-enacted model law. Some might argue that having a model law and a model regulation made sense in the pre-covered agreement era, when state insurance regulators may have needed more flexibility in the regulation of credit for reinsurance, but that is no longer the case. Regulatory flexibility is no longer compatible with the credit for reinsurance paradigm imposed on the states by the covered agreement, which requires strict adherence by all affected parties to the terms and conditions of the covered agreement. Regulatory flexibility is also incompatible with extension of the zero reinsurance collateral benefit to assuming reinsurers in non-EU jurisdictions since strict adherence to the terms and conditions under which the benefit is granted will be critical to all affected parties.

   In both instances (implementation of the covered agreement and adoption of the NAIC's proposed zero collateral paradigm for non-EU jurisdictions), there can be no room allowed for tinkering. The terms and conditions under which assuming reinsurers in Reciprocal Jurisdictions are exempt from posting reinsurance collateral in the U.S., and the terms and conditions under which Reciprocal Jurisdictions grant mutual recognition of the entire U.S. system of insurance regulation, **must be set in stone**.

   We therefore urge the Reinsurance Task Force to consolidate the Credit for Reinsurance Model Law (785) and the Credit for Reinsurance Model Regulation (786), and all proposed revisions, into the Credit for Reinsurance Model Law (785), with one exception: the forms included in the

[1] The forms promulgated in the Credit for Reinsurance Model Regulation (785) include Form AR-1 (Certificate of Assuming Reinsurer); Form CR-1 (Certificate of Certified Reinsurer); Form RJ-1 (Certificate of Reinsurer Domiciled in Reciprocal Jurisdiction); Form CR-F; and Form CR-S.

current Credit for Reinsurance Model Regulation (786), and the newly proposed form (Form RJ-1; Certificate of Reinsurer Domiciled in Reciprocal Jurisdiction), should remain in the model regulation.

2. The "Catch-All" Provisions. The proposed revisions to the Model Law and the Model Regulation include "catch-all" provisions under which any state regulator can supplement the requirements set forth in the models with additional requirements for qualifying as a Reciprocal Jurisdiction.[2] While we recognize that this is a common feature of NAIC models, we are also concerned that a decision by individual state regulators to add to the requirements of the models could prompt some foreign jurisdictions to seek new covered agreements with the U.S. to avoid varying state requirements. We would prefer to avoid additional covered agreements being negotiated since they conflict with the primacy of state insurance regulation. We would therefore urge the Reinsurance Task Force to consider eliminating these "catch all" provisions.

3. Full Mutual Recognition. When the Reinsurance Task Force held its hearing on this issue on February 20, Cincinnati testified that the NAIC must ensure that no jurisdiction gets the benefit of zero reinsurance collateral without granting mutual recognition of the entire U.S. system of insurance regulation. The proposed changes to the Model Regulation provide that a Reciprocal Jurisdiction may not subject U.S. insurers to global group supervision rules unless those requirements are consistent with those of the state granting credit for reinsurance to a ceding insurer or the ceding insurer's domiciliary state.[3] While this is positive, it falls short of an absolute requirement that the jurisdiction provide full mutual recognition of the entire U.S. system of regulation. Cincinnati urges the Reinsurance Task Force to add broader language clarifying that full mutual recognition is required.

4. Requiring Reversion to 100% Collateral. When the Reinsurance Task Force held its hearing on this issue on February 20, Cincinnati testified that a 100% reinsurance collateral requirement **should** be immediately imposed upon any assuming reinsurer domiciled in a jurisdiction which breaches the terms and conditions of the covered agreement, or breaches similar terms and conditions imposed upon non-EU jurisdictions as a condition to obtain the benefit of zero collateral. Section 9(F) of the proposed revisions to the Model Regulation seems to address this situation, but does not mandate reversion to 100% collateral when a breach occurs.[4] Cincinnati urges the Reinsurance Task Force to add clearer language clarifying that 100% collateral shall be immediately imposed in such cases and the procedures for re-imposing the 100% requirement.

Thank you for consideration of Cincinnati's comments.

Sincerely,

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[2] Proposed Revisions to Model Law (785), Section F(1)(h). Proposed Revisions to Model Regulation (786), Section 9(B)(2)(e).
[3] Proposed Revisions to Model Regulation (786), Section 9(B)(c)(2).
[4] Under Section 9(F), a commissioner "may revoke or suspend the eligibility of an assuming reinsurer" for zero collateral when a breach occurs, or "may require the assuming reinsurer to post security" when a breach occurs.