

Vermont Department of Financial Regulation

Captive Insurance Division

Bulletin No. C-2014-01

Guidance for Special Purpose Financial Insurers

Purpose:

The purpose of this bulletin is to provide guidance regarding licensing standards and regulatory requirements for Special Purpose Financial Insurance Companies. For specific requirements under Vermont law, please refer to 8 V.S.A. Chapter 141. Other information, including specific filing requirements can be found at <http://www.dfr.vermont.gov/captives/home>.

Special Purpose Financial Insurance Companies are valuable tools that allow the insurance industry to address unique risks or to provide an efficient source of capital. They benefit the consumer by enabling traditional insurers to offer necessary products at affordable rates. However, concerns about their use have been raised by numerous state and federal regulators.

Special Purpose Financial Insurance Companies are not captives in the self-insurance sense, since they are ultimately funding the risk of unrelated policyholders; they behave as commercial reinsurers with a single customer.

Therefore, we believe they should be regulated more like traditional companies in order to preserve the confidence of policyholders in the traditional insurers that sell policies, and in the state-based regulatory system.

Applicability:

The following standards will apply to Special Purpose Financial Insurance Companies and certain insurer-owned captive insurance companies licensed after January 1, 2014, unless otherwise exempted by the commissioner:



Qualified transactions

Vermont considers the following standards as representative best practice alternatives for treatment as permitted assets or as a reduction in liabilities to support underlying reserves, subject to a detailed review of each application submitted:

- Prioritized letters of credit in favor of the ceding company;
- Securitizations, i.e. sale of bonds;
- Surplus notes issued in accordance with SSAP41;
- Reinsurance agreements with traditional insurance/reinsurance companies with acceptable financial strength ratings.

Other financing arrangements will be considered on a case-by-case basis.

Review of transactions

- Vermont will obtain an independent actuarial review of each application by an actuary of the Department's choosing;
- Vermont will continue to work directly with the cedant's regulator to review each transaction;
- Vermont will continue to require documentation of approval or non-disapproval of each transaction from the cedant's regulator;

Reporting

- Companies shall obtain a company and group code number from the National Association of Insurance Commissioners (NAIC). This will improve interested regulators' ability to ascertain the extent of captive activity by using the NAIC database and reviewing ceding companies' reinsurance schedules. Modifications to the blanks have been adopted that specifically report amounts ceded to captive subsidiaries in the cedants' reinsurance schedules and notes to the financial statements;
- Annual and quarterly statements, including management discussion and analysis, actuarial opinion, audited financial statements, and all other required supplemental filings and information specified by the Department, shall be prepared on appropriate NAIC blanks, in accordance with instructions;
- Annual and quarterly statements shall be filed with the State of Vermont and the NAIC.

Disclosure

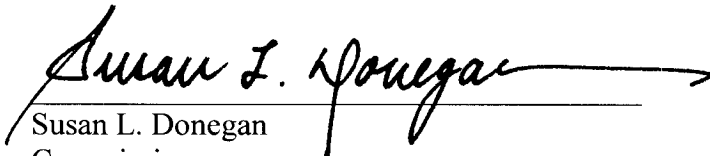
- Vermont law provides the Commissioner with discretion to disclose confidential information to other commissioners whose laws allow them to maintain equivalent confidentiality of information received. We intend to exercise that discretion. Please refer to 8 V.S.A. Chapter 141, §6002(c)(3);
- Vermont also intends to participate in NAIC Supervisory Colleges, which provide a forum for discussion among regulators and an opportunity to discuss a Special Purpose Financial Insurance Company's plan of operation in a confidential setting.

Summary:

Vermont's goal is to support the use of appropriate uniform standards for regulation of insurer-owned captives and Special Purpose Financial Insurance Companies and to establish best practices and high standards for their continued use. Vermont will continue to strive to maintain and enhance confidence in the state system of regulation, which will provide necessary assurance that each Special Purpose Financial Insurance Company will have the ability to meet its obligations to the cedant. Properly constructed and regulated Special Purpose Financial Insurance Companies have a place in the insurance marketplace, helping insurers to continue to offer affordable insurance products.

This applies prospectively to Special Purpose Financial Insurance Companies as defined in subchapter 4 of 8 V.S.A., chapter 141, and to certain insurer-owned captives, licensed after January 1, 2014. Voluntary compliance by companies licensed prior to that date is encouraged, and will be considered best practice.

Dated at Montpelier, Vermont this 27th day of January, 2014.



Susan L. Donegan
Commissioner