



Leveraging Legacy Liabilities

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Re: Exposure Drafts issued 5-13-24 Restructuring Mechanisms White Paper and Best Practices Procedures for IBT/Corporate Divisions

To Director Elizabeth Kelleher Dwyer (RI) and Commissioner Glen Mulready (OK),
Co-Chairs of the Restructuring Mechanisms (E) Working Group:

AIRROC is pleased to offer comments in response to NAIC Restructuring Mechanisms (E) Working Group exposure of its drafts of a Restructuring Mechanisms White Paper and Best Practices Procedures for IBT/Corporate Divisions. As a non-profit association AIRROC and its Board do not advocate for any specific position but provide resources and information.

AIRROC is the only US based non-profit association focusing on the legacy sector of the insurance and reinsurance industries. Membership is on a corporate level and given the impact and importance of legacy business to the entire industry, AIRROC has attracted many talented and experienced participants that all have legacy or runoff business in their portfolio. The members include major US and international insurance and reinsurance companies, legacy acquirers, well-known rehabilitations, receiverships and liquidations, brokers, run-off managers and state insurance departments. AIRROC also benefits from its associate members, comprised of law firms and legacy service providers, such as the Big 4 accountancy firms, which support the organization with invaluable knowledge and expertise.

We wish to emphasize that, although AIRROC's legacy agenda can encompass insolvent run-offs, historically and practically, our focus has been the run-off of solvent legacy portfolios. We ask that the Working Group keep this distinction clearly in mind as an overarching drafting issue in the drafts under review.

In addition, although AIRROC's mandate is primarily focused on legacy and run-off insurance, it is important that the drafts make clear that many of the restructuring mechanisms under discussion can be used for both legacy run-off and non-legacy active portfolio transfers.

AIRROC offers the following comments to the above drafts:

1. **Results of UK Part VII Transfers.** Footnote 6 of the draft White Paper requests that commentators indicate whether there have been insurer failures following a UK Part VII Transfer. As outlined in the White Paper, since the legislation was introduced in 2000, there have been over 320 Part VII Transfers approved by the UK Courts. None of these have resulted in an insolvency.

It is important to note that, Part VIIs are often used as a finality mechanism as part of a solvent wind down of a business. As such, following the transfer of liabilities to a new carrier, the original transferor entity is sometimes wound up. An example is the recent transfer by Aetna International LLC to Allianz Partners. This formed part of Aetna's wider exit strategy for its non-core international operations and culminated in the UK entity being deauthorized ahead of a full solvent liquidation.

To answer the specific question raised, we are unaware of any unplanned insolvency following an insurance business transfer in the UK. However, it should be noted that similar mechanisms are available in many other countries throughout Europe.

2. **"Run-off" and RBC Discussion.**

The issues of run-off definition and Risk Based Capital (RBC) calculations for legacy portfolios have been raised before by AIRROC and others and deserves to be re-emphasized.

- a. **Run-Off.** AIRROC offered comments of these issues in response to the NAIC Restructuring Mechanisms (E) Working Group exposure of its 4-4-23 draft Best Practices Procedures for IBT/Corporate Divisions and also comments to the previous Restructuring Mechanisms (E) Subgroup on 4-26-19. In those comments we pointed out that the definitions of run-off vary greatly by company and even change over time due to factors such as changes in underwriting cycle, profitability, reinsurance availability, interest rates and structures to administer.

Runoff and what constitutes runoff have evolved over the years as the industry itself has evolved. In a survey of the market respondents at the time, they were asked "How does your organization define runoff business?"

Sample responses include:

- "All lines of business where premiums are no longer being written."
- "Any discontinued line of business."
- "Business that is being wound down and no longer underwritten."
- "Closed book of business with no more underwriting."
- "2001 and prior."
- "Discontinued companies, affiliates or segments."
- "Non-core to the group."
- "No new written business."

Based on these varied views, AIRROC believes it would be appropriate to define “run-off” with flexibility in the context of restructuring mechanisms (“RMs”). Increasingly, the legacy market has developed to feature many more transactions that incorporate legacy liabilities (back books) where insurers seek capital relief through disposing of prior year liabilities while continuing to underwrite that particular line of business. Most importantly, very large global insurance groups strategically decide to dispose of certain liabilities while continuing to underwrite their core business.

We would caution against assumptions or general statements about “run-off” that may not reflect the complexity of the legacy business and the different ways in which stakeholders use “run-off” as an ongoing business model. As a general matter, AIRROC would encourage the adoption of a broad definition of “run-off” that can be used flexibly to structure RMs when the need arises.

We also urge the Working Group to carefully consider those places in the drafts that discuss the use of RMs in insolvencies. Insolvencies operate in a very different environment, with very specific and well-established statutory and regulatory standards which are distinct from those applicable to IBT and CD transactions under discussion in the drafts. We suggest that the drafts not discuss insolvent RMs except in passing or for contrast to the solvent RMs which should be the focus of discussion.

b. RBC. As stated in our prior comments, the impact of RBC on run-off depends on the definition of run-off, and in many circumstances, RBC may not be suitable for evaluating the risk of run-off. NAIC RBC calculations attempt to summarize several areas of an insurer's risk into a single value with a formula that includes a number of specific factors which may not accurately capture the risk profile of a run-off portfolio, including:

- i. A Reserving Risk Charge which (x) includes 10 years of data (which may not be long enough to accommodate the risks carried in run-off portfolio), and (y) fails to account for possible retroactive reinsurance in the insurer's statutory financials.
- ii. A Premium/Underwriting Risk Charge which reflects premium income which may not be present in a run-off portfolio, specifically, items such as the collection of premium on retrospectively rated policies which may cause distortions in the calculation of Excessive Premium Growth charges and Combined ratio triggers without any change in the risk profile of the company.

Instead of these factors which distort the financial position run-off operations, the most critical issue in run-off is the availability of cash and liquid assets to satisfy policyholder claims and other obligations.

In summary we recommend that questions regarding the definition of “runoff” and applicability of RBC to runoff be directed to other NAIC Working Groups for further development.

3. **Updating the Text.** We note that various statements in the draft White Paper require updating and suggest that the draft White Paper be so updated.

4. **Secondary Issues.** We suggest that the Working Group deemphasize certain issues in the draft that detract from the main subject of restructuring mechanisms. The description of the Virginia statute which discourages novations, for example, is one of a number of different ways that states can interfere with some of these transfers. Although it merits attention, in our view that discussion should be shortened, put in context as one of a number of ways that states can oppose these transfers and moved to a footnote.
5. **Subsequent Steps.** We understand that the Working Group is working to finalize these drafts in a timely manner. When the drafts are finalized, there may still be a need to follow continuing developments within the NAIC and elsewhere which we hope the Working Group could lead. AIRROC would appreciate further information regarding how the Working Group and the NAIC plan to proceed during the implementation and follow-up stages of this process. For example, once the drafts are adopted, referrals may be made to other NAIC committees which, in turn, may require additional changes to the White Paper and the Best Practices Procedures.

Finally, to assist regulators and the market, AIRROC has developed a Restructuring Resource Site <https://www.airroc.org/restructuring-resources> which allows ready access to background, legal and regulatory sources on restructuring mechanisms throughout the country and in the UK.

AIRROC looks forward to a continued dialogue with the NAIC and more specifically the Restructuring Mechanisms (E) Working Group.

Respectfully Submitted,



Executive Director, AIRROC