

# Foundational Principles

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Restructuring Mechanisms (E) Subgroup  
Exposure Draft 5-4-22

### Background

An **insurance business transfer** (IBT) represents a transaction designed to transfer existing insurance obligations of one insurer (transferor) to a second insurer (transferee) without policyholder consent, subject to regulatory approval and, subject to court approval. While policyholder consent is not required, notice to policyholders and to the general public is required, and concerns regarding the transaction will be considered in the regulatory and/or court approval process. Pursuant to an IBT, the transferee becomes directly liable to policyholders and the transferring insurer's obligations under the contracts are extinguished thereby achieving legal finality for the transferring insurer.

A **corporate division** is a division of one insurer into two or more resulting insurers. The dividing insurer's assets and liabilities are allocated between or among the resulting insurers without requiring policyholder consent.

This document is foundational principles for state insurance regulators to use in reviewing IBT and corporate division transactions. While this guidance recommends minimum review standards, it does not rise to the level of a model law or regulation.

The exact laws under which both transactions are implemented can differ from one jurisdiction to the next and are not detailed herein. This guidance is not intended to address the legality of these transaction in various states but rather to provide a baseline of foundational principles to be used by all jurisdictions to address the primary risks associated with such transactions. Note that some jurisdictions have noted concerns that their laws do not permit nondomiciliary jurisdictions to sever policyholder rights without policyholder consent.

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### Foundational Principles to Guide in Reviewing IBT and Corporate Divisions

1. **Policyholders and Other Key Stakeholders Should Never Be Left Worse Off** - Policyholders should be left in the same or a better position after completion of the transaction. The transaction should not be approved unless the effect on policyholders and other key stakeholders is neutral or there is some expected policyholder benefit(s). It is preferable that they are left in better position, but at a minimum the policyholders should be in a neutral position. Policyholders and other key stakeholders include those related to both the transferred policies and the remaining policies which are not transferred. Consideration should include the following: (Sources: 1, 3)
  - a. How the security of policyholders' and claimants' (who include persons with certain rights and contingent rights under the policies) contractual rights are affected.
  - b. How policyholders' rights and reasonable expectations appear to be affected.
  - c. The compensation offered to policyholders for any loss of rights or expectations.
  - d. That policyholders will receive the same or better level of service regarding claims settlement, and access to support and capital as they received prior to the IBT or corporate division.
  - e. Continuity of guaranty fund coverage and other secondary market coverage.

#### **Drafting Note:**

Comments are requested on both the term no worse off and how it is measured. The terms of the insurance policy or reinsurance contract do not typically change. Does the term no worse off include more measures than financial strength / financial ability and operational measures such as service to policyholders?

Comments are requested on the definition of policyholders and key stakeholders: regulators noted that policyholders on both sides of the transaction (those transferred and those not transferred) should both be protected. However, in cases of secondary transfers of assumed reinsurance obligations, more input is requested.

2. **Robust Regulatory Review Process** - Reviewing authorities should undertake efforts to establish, at a high level of confidence, that policyholders and other key stakeholders will experience no adverse effects. At a high level, the following key elements need to be embedded in law (along with existing *Insurance Holding Company System Regulatory Act* (#440) Form A requirements):
  - a. The regulatory review must be robust, including evaluations of legal implications such as anti-innovation laws for policyholders in other states, financial projections, actuarial analysis and capital projections. The review should identify key risks to the transaction, and should, at a minimum, include the following: (Sources: 1)
    - i. A prospective solvency assessment. (Source: 4)
    - ii. A finding that the assets to be transferred to insurers (or surviving entities) involved in the transaction are adequate to cover the insurer's liabilities being transferred.

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- iii. A conclusion that the transaction does not have any adverse impact on policyholders and other key stakeholders, including services, benefits from reinsurers, guaranty associations or other secondary market mechanisms.
  - iv. A consideration of the plans of any insurer involved in the transaction to liquidate another involved insurer, sell or dividend assets, consolidate, merge, or make other changes, and the resulting impact on capital, policyholders, reinsurers, and guaranty associations.
  - v. An analysis of any relevant contracts, including claims management and reinsurance and recordkeeping. (Source: 4)
- b. Require Strong Financial Standards and Stress Testing
- i. Prescribed conservative assumptions should be included in capital calculations to avoid the manipulation of capital thresholds.
  - ii. Actuarial reserve and capital calculations should be performed by an expert that is independent of the insurance companies involved. (Source: 1, 7) Resulting projected RBC ratios and projected capital ratings should be reviewed. Policyholders and other key stakeholders should have the same economic protections which existed prior to the IBT or corporate division.
  - iii. The final decision should outline the purpose of the transaction and impacts to policyholders and other key stakeholders and the opinion of the independent expert(s), and reviewing regulators, including other impacted regulators, and the input from policyholders and other key stakeholders.
- c. Ultimate authority
- i. IBTs will require review by:
    - 1. Domestic regulators of both the assuming company and transferring company,
    - 2. Notice to other affected regulators,
    - 3. Report of Independent expert(s), and
    - 4. Court approval as the final authority
  - ii. Corporate Divisions will require review by
    - 1. Domestic regulator(s),
    - 2. Notice to other affected regulators,
    - 3. Report of Independent expert(s),etc. and
    - 4. Domestic regulators as the final authority.

### **Drafting Note:**

Comments are requested on the use of an independent expert for corporate divisions. If commenters believe that an independent expert is not needed for a corporate division; should the department be required to show that they have adequate resources and expertise such as, actuarial experienced in the book of business being transferred, examiners with appropriate credentials and experience, etc. to review and approve a corporate division?

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### 3. Guaranty Fund Coverage - No impacted policyholder should lose guaranty fund protection as a result of a transaction. (Sources: 1, 2)

- a. If there was guaranty fund coverage before the division or IBT, state regulators should ensure that there is coverage after the division or IBT. A division or IBT should not reduce, eliminate or in any way impact guaranty fund coverage. Guaranty fund representatives, National Conference of Insurance Guaranty Funds (NCIGF) and National Organization of Life and Health Insurance Guaranty Associations (NOLHGA) are useful resources for any guaranty fund coverage issues that arise in evaluating these transactions.

#### **Drafting Note:**

*National Conference of Insurance Guaranty Funds (NCIGF) commented that changes to existing Guaranty Fund models may be needed and will appoint a subcommittee to assist. The Restructuring Mechanisms (E) Working Group has made a referral to the Receivership and Insolvency (E) Task Force.*

### 4. Secondary Market Mechanisms (Source: 6)

- a. If there were any secondary market or similar mechanisms which benefited the policyholders and other key stakeholders or otherwise accrued to the claims of policies, before the division or IBT, state regulators should ensure that the benefits remain after the division or IBT. A division or IBT should not reduce, eliminate or in any way impact coverage benefits.
- b. Other organizations such as the National Workers Compensation Reinsurance Association should be contacted, when relevant.

### 5. Use Uniform NAIC Valuation and Accounting Standards (Source: 7)

- a. When evaluating the solvency impact of a proposed transaction, the accounting utilized should be in conformance with the NAIC's uniform statutory accounting principles valuation and accounting rules in the Accounting Practices and Procedures Manual (AP&P Manual). Regulators are discouraged from allowing any permitted practices. If permitted practices are utilized, the impact of the deviations from the AP&P Manual at the time of the transaction, and in any subsequent projections, should be thoroughly analyzed and quantified and should be disclosed as part of the information shared with other affected regulators. In addition, statutory filings shall continue to provide disclosures of the impacts of prescribed and permitted practices in accordance with the Accounting Practices and Procedures Manual.

### 6. Independent Expert (Sources: 1, 3, 7, 8)

- b. The ability of a Commissioner to hire independent experts for specialized transaction review and financial testing, to be paid for by the applicant is essential;
- c. The regulatory review process for IBTs and corporate divisions will utilize an independent expert to advise and assist the ultimate reviewing authority (regulator and or the court) in reviewing proposed transactions (including advising on any adverse impact on policyholders, reinsurers, or guaranty associations) and to provide any other assistance or advice the regulator may require.

*Drafting Note: See request for comments on independent expert for corporate divisions.*

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- d. The independent expert evaluation should be undertaken by an expert to establish, at a high level of confidence, that policyholders and other key stakeholders will experience no adverse effects. The independent expert must provide a detailed report regarding the prospective solvency of the resulting entity.
- e. Other independent experts will also provide reports to be reviewed by the regulator and the ultimate approving authority. This will include an independent actuarial review of the reserves and capital (e.g. RBC and financial strength) before and after the transaction. The review is to ensure that all of the policyholders and other key stakeholders are a neutral or better condition after the proposed transaction. Note that the actuarial review is one of several experts that will likely be included and taken into consideration. While the independent expert can provide comments and evaluation of the reports of the other experts, the overall expert cannot change the reports of the other employed experts. For example, the reviewing expert cannot change the consulting actuarial opinion.
- f. The experts should be independent of any influence from the companies involved and subject to the approval of the domestic regulators.

### 7. Due Process (Sources: 1,3)

- a. Robust due process must be afforded to stakeholders (policyholders, claimants, reinsurers, guaranty associations including other regulators, etc.) impacted by a transaction in advance of any public hearing along with access to information concerning the transaction. This should include:
  - i. Notice to stakeholders in a form to be approved by the regulator;
  - ii. Public hearing;
  - iii. Adequate time to assess the impact as determined by the domestic regulator, but no less than 30 days; and
  - iv. Opportunity to submit written comments and or attend public hearings.

### Table of Sources

Reference	Source
1	American Property Casualty Insurance Association (APCIA) suggested concepts
2	National Conference of Insurance Guaranty Funds (NCIGF)
3	Prudential Regulation Authority (PRA)/Financial Conduct Authority (FCA) – UK part 7
4	Laws or procedures in Rhode Island
5	Corporate Division comment letter 7-24-29, (Athene, John Hancock TransAmerica Venerable) referencing Michigan Corporate Division law
6	Illinois Corporate Division example
7	Comment letter New York Life and Northwestern Mutual on restructuring charges
8	IBT Coalition comment letter

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