Ohio Insurance Institute
Representing Ohio's property/casualty insurance industry

Our mission
To act as the Ohio property and casualty insurance industry's voice on matters affecting or involving the industry.

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Proponent Testimony—SB 284 (Hottinger, Peterson)
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Chairman Hackett, Vice Chair Hottinger, Ranking Member Craig and members of the Senate Insurance and Financial Institutions Committee, thank you for allowing me to come before this Committee to discuss the importance and necessity of prompt passage of SB 284. I am Michael Farley and I have the distinct honor to serve as the Vice President, Government Affairs and General Counsel for the Ohio Insurance Institute ("OII"). The OII is a trade and information association of more than 55 Ohio-based property and casualty insurance companies and related affiliate organizations. OII members write approximately 87% of the auto insurance in Ohio. And OII members write about two-thirds of the commercial insurance in the state.

I come to you today to explain the importance of SB 284 and to seek your support. First, I will state what has already been stated: reinsurance is insurance for insurance companies. Reinsurance serves as an integral component of the spreading of risk to promote proper pricing, availability of products, and is a solvency protection tool for insurers in the event of catastrophic risk. There are a variety of technical ways to cede the given risk to a reinsurance policy. For the purposes of SB 284, it is most important to discuss the entities that are reinsurers.

Traditionally, the major reinsurers have been based in Europe. Leading up to and during World War II, regulators and insurers in the United States began to become concerned about the ability to recover on reinsurance policies issued by European companies. Thus began the requirement for "alien" (non-U.S. insurers) to post collateral in the United States equal to the amount of reinsurance written in the United States.

In order for insurers in the United States to receive full credit for the reinsurance they purchased from an alien reinsurer, they must have purchased the reinsurance with a reinsurer that posted one hundred percent collateral in the United States. Very succinctly, the credit received by the insurer allowed the U.S. insurer to receive full credit in their financials for ceding, or giving up that risk, to a reinsurer. The insurer was no longer liable for those risks ceded—as an accounting function. Regulators allowed the grant of credit when they were assured that the reinsurer would pay for the ceded risk. For over fifty years, this was accomplished by simply posting full collateral in the United States.

Receiving credit for reinsurance is important because domestic insurers are limited to how much insurance they may write based on their risk based capital. RBC is a different topic but the most important job of domestic insurance regulators is to ensure solvency of insurers. Simply put, an insurer must have sufficient capital capacity to write additional insurance. The amount of insurance an insurer can write is directly correlated to their capital capacity. Ceding risk to reinsurers is often a tool to gain capital capacity.

This regulatory regime did require additional capital to be held by alien reinsurers. This likely led to higher premiums on U.S. insurers. Eventually, prudential regulators in the United States and Europe developed a system of evaluating reinsurers and the domiciliary regulator of the reinsurer. This led to the current regime that is currently in Ohio law.

Senate Bill 140 (130th General Assembly) was a comprehensive regulatory upgrade bill passed in 2014. SB 140 allowed for a sliding scale of collateral based on the transparency and strength of the foreign regulator and the reinsurer. The stronger regulators entered into agreements with the National Association of Insurance Commissioners ("NAIC") to provide collateral relief for reinsurers.

In September, 2017, the United States government and the European Union entered into a covered agreement. The purpose of the covered agreement was to place European insurers on equal basis of collateral requirements as U.S. insurers. Where differences between the terms of the covered agreement and state law occur, the covered agreement will govern—the covered agreement will preempt state law.

SB 284 implements the response by state insurance regulators. Most notably, SB 284 creates a "reciprocal jurisdiction" that recognizes those jurisdictions that meet sufficient solvency requirements and protections deemed necessary by regulators in the United States. Where a reinsurer is regulated by a reciprocal jurisdiction, the reinsurance collateral requirements are removed.

The members of the Ohio Insurance Institute strongly support adoption of SB 284. We appreciate the diligence of Director Froment and her leadership at the

NAIC in crafting this response to changing international prudential regulation. SB 284 is an appropriate response to an international improvement in transparency and quality of prudential regulation. Perhaps most importantly, SB 284 is a clear statement to maintain the principle of state-based regulation. By passing SB 284, the Ohio General Assembly demonstrates, once again, that the states are best-suited to regulate insurance.

Mr. Chairman, thank you for the opportunity to discuss this very important matter. I am happy to attempt to answer any questions that there may be.