

CSI - Ohio
The Common Sense Initiative

Business Impact Analysis

Agency Name: **Ohio Department of Insurance**

Regulation/Package Title: **Special Purpose Financial Captives**

Rule Number(s): **3901-11-05 and 3901-11-06**

Date: **February 27, 2015**

Rule Type:

- ☒ New
 ☐ 5-Year Review
☐ Amended
 ☐ No Change
☐ Rescinded

The Common Sense Initiative was established by Executive Order 2011-01K and placed within the Office of the Lieutenant Governor. Under the CSI Initiative, agencies should balance the critical objectives of all regulations with the costs of compliance by the regulated parties. Agencies should promote transparency, consistency, predictability, and flexibility in regulatory activities. Agencies should prioritize compliance over punishment, and to that end, should utilize plain language in the development of regulations.

Regulatory Intent

1. Please briefly describe the draft regulation in plain language.

Please include the key provisions of the regulation as well as any proposed amendments.

The two rules submitted in this packet provide guidelines for determinations that are to be made by the superintendent in respect to Special Purpose Financial Captives (SPFC).

SPFC's are authorized under Chapter 3964. of the Revised Code, and may only provide reinsurance of life insurance risks to an Ohio domiciled parent or an affiliated company that is authorized to sell life insurance in Ohio. SPFCs must meet reserving requirements set forth both in the ORC and the rules included in this packet.

77 SOUTH HIGH STREET | 30TH FLOOR | COLUMBUS, OHIO 43215-6117
CSIOhio@governor.ohio.gov

Specifically, rule 3901-11-05 establishes a process and method for a SPFC to request the use of an alternative reserve basis other than that found in the national association of insurance commissioner's accounting practices and procedures manual.

Rule 3901-11-06 establishes a method for determining an acceptable total capital and surplus requirement for an insurance company that will place its own risks and obligations into a SPFC. The rule also provides guidance regarding the submission of the actuarial report.

2. Please list the Ohio statute authorizing the Agency to adopt this regulation.

Sections 3901.041, 3964.03, and 3964.21 of the Revised Code.

3. Does the regulation implement a federal requirement? ☐ Yes ☒ No

Is the proposed regulation being adopted or amended to enable the state to obtain or maintain approval to administer and enforce a federal law or to participate in a federal program?

☐ Yes ☒ No

If yes, please briefly explain the source and substance of the federal requirement.

Not applicable.

4. If the regulation includes provisions not specifically required by the federal government, please explain the rationale for exceeding the federal requirement.

Not applicable.

5. What is the public purpose for this regulation (i.e., why does the Agency feel that there needs to be any regulation in this area at all)?

Chapter 3964. provides for the formation of domestic SPFCs in Ohio. The rules included in this packet establish regulations to help ensure that proper capital is maintained within the SPFC. Compliance with these rules assists the SPFC and the parent life insurance company to remain financially solvent.

6. How will the Agency measure the success of this regulation in terms of outputs and/or outcomes?

Both rules define requirements and "methodology" (guidelines) to maintain sufficient capital and surplus requirements and the ability to apply for an alternative reserve standard. Thus, success will be evident based on the ease of use for both SPFCs and the department as eligible entities come into compliance with these rules as well as the SPFC maintaining proper capitalization.

Given that this is a new insurance entity operating in Ohio, department staff will closely monitor these outcomes for potential areas of improvement.

Development of the Regulation

7. Please list the stakeholders included by the Agency in the development or initial review of the draft regulation. If applicable, please include the date and medium by which the stakeholders were initially contacted.

In late August 2014, the department began outreach with the Association of Ohio Life Insurance Companies (AOLIC) regarding the drafting of these rules. AOLIC remained in communication with member companies regarding the drafts and stayed in frequent contact with the department. Over the course of the following months, the department emailed the proposed rules to a group of entities that were engaged during the drafting of the enabling legislation. The group included trade organizations, interested insurance companies and professional organizations. The department maintained ongoing communication both via phone and email with the interested companies addressing concerns and comments. As the drafts were edited to address concerns, stakeholders were again notified. On January 28, 2015, the final draft was sent to the stakeholders and to date, the department has not received any additional written feedback.

8. What input was provided by the stakeholders, and how did that input affect the draft regulation being proposed by the Agency?

The department worked in collaboration with the industry to ensure these regulations represent a balance of appropriate regulation and industry buy in. Following stakeholder comment, portions of rule 3901-11-05 regarding contract reserves were determined to be repetitive. As a result, the department consolidated this section during final drafting to reduce any redundancies. Stakeholders also identified technical edits to rule 3901-11-06 that were included in the rule's final draft.

9. What scientific data was used to develop the rule or the measurable outcomes of the rule? How does this data support the regulation being proposed?

These rules were based on extensive review of captive and SPFC programs and laws currently operating in other states. In addition, the department worked extensively with stakeholders to develop reasonable standards.

10. What alternative regulations (or specific provisions within the regulation) did the Agency consider, and why did it determine that these alternatives were not appropriate? If none, why didn't the Agency consider regulatory alternatives?

These rules are driven by the language of the statute which requires the superintendent to establish a prescriptive process for SPFC's regarding alternative reserves methodologies

and capital and surplus requirements. By creating such processes, SPFC managers and entities will be able to predict what is required to maintain compliance.

11. Did the Agency specifically consider a performance-based regulation? Please explain.

Performance-based regulations define the required outcome, but don't *dictate the process* the regulated stakeholders must use to achieve compliance.

The corresponding statute, section 3964.21 of the Revised Code, requires that the superintendent establish processes to approve alternative reserve methodologies and acceptable capital and surplus requirements. Therefore, the rules must dictate the process to determine eligibility rendering performance based regulations not workable.

12. What measures did the Agency take to ensure that this regulation does not duplicate an existing Ohio regulation?

The authority to domicile a SPFC in the state of Ohio was established under Chapter 3964. of the Revised Code which became effective on September 17, 2014. The rules included in the packet are established under a new Ohio Revised Code section and do not duplicate any existing Ohio regulation. There are no other agencies that regulate captive insurance companies.

13. Please describe the Agency's plan for implementation of the regulation, including any measures to ensure that the regulation is applied consistently and predictably for the regulated community.

The department will utilize existing resources within the office of Risk Assessment to oversee the application process and ongoing oversight of SPFCs. The amount of staff dedicated to these entities will be determined on the applications the department receives. The staff involved in this division will remain in communications with other captive jurisdictions operating SPFCs and associations, as well as the NAIC to remain current on best practices.

Adverse Impact to Business

14. Provide a summary of the estimated cost of compliance with the rule. Specifically, please do the following:

- a. Identify the scope of the impacted business community;
- b. Identify the nature of the adverse impact (e.g., license fees, fines, employer time for compliance); and
- c. Quantify the expected adverse impact from the regulation.

The adverse impact can be quantified in terms of dollars, hours to comply, or other factors; and may be estimated for the entire regulated population or for a

“representative business.” Please include the source for your information/estimated impact.

a. These rules impact any entity applying to form a SPFC. Only Ohio domiciled parent or affiliated company authorized to transact life insurance business in this state are eligible to apply. There is no requirement to apply and establishing a SPFC is purely elective.

b. Every SPFC applicant is required to provide reports produced by a qualified independent actuary. The SPFC applicant is thus required to hire a qualified actuary, as defined in paragraph (C)(2) of rule 3901-11-06 of the Administrative Code. In addition, the rules require that the SPFC applicant make financial records and other information available as the superintendent may request to adequately determine all SPFC requirements are met.

c. The cost to secure a qualified actuary is dependent upon the complexity of the review and current industry standards. Most of the information that may be requested during the review, the entity should already have for general and ongoing business operations. Therefore, the exact time will depend on how the entity maintains financial records and information. The actual dollar cost of the review will vary depending on the actuarial firm that is hired to perform the review. Billing rates for actuaries vary similarly to legal billing rates, with average hourly rates ranging from \$250 to \$500 or more. It is reasonable to expect this review to take at least two weeks and potentially a couple of months. Since the rule deals with establishing a new entity, the variance could potentially be wider.

15. Why did the Agency determine that the regulatory intent justifies the adverse impact to the regulated business community?

The guidance established within these rules was developed in consultation with interested stakeholders with the dual objective of ease of use and promoting solvency of both the SPFC and the parent life insurance company. The scope of these regulations is narrow and specific to those entities that elect to apply for licensure as a SPFC.

Regulatory Flexibility

16. Does the regulation provide any exemptions or alternative means of compliance for small businesses? Please explain.

SPFC entities must meet the reporting requirements established within these rules to ensure solvency. These requirements are designed to assist in providing the proper oversight and determinations that will affect the well-being of the entity. Therefore regardless of size, these guidelines must necessarily be applied to all SPFC entities consistently.

17. How will the agency apply Ohio Revised Code section 119.14 (waiver of fines and penalties for paperwork violations and first-time offenders) into implementation of the regulation?

Paperwork violations and/or first time offender issues would be handled on a case by case basis to determine whether the violation could have a serious impact on the overall soundness of the SPFC entity. Minor errors would be handled by advising the entity and providing them an opportunity to cure the omission in compliance with the Ohio Revised Code.

18. What resources are available to assist small businesses with compliance of the regulation?

Department staff is available to assist any SPFC applicant and licensed entity regardless of size. Given that the regulation of such entities is new to Ohio, department staff will maintain specific contact points and update information that will be located in a dedicated area of the department's web page. Staff will also be available during normal business hours to answer any questions.