MEMORANDUM

TO:	SENATE COMMITTEE ON FINANCE, HOUSE COMMITTEE ON COMMERCE AND ECONOMIC DEVELOPMENT
FROM:	DAVID PROVOST, DEPUTY COMMISSIONER, DEPARTMENT OF FINANCIAL REGULATION
SUBJECT:	2020 CAPTIVE BILL
DATE:	JANUARY 17, 2020
CC:	Richard Smith, Vermont Captive Insurance Association; Ian Davis, Vermont Department of Economic Development

Following is an outline of proposed changes to Vermont's captive statute:

Section 1. – Agency Captive Disclosure Requirements

Background: When agency captives were added to the list of available captive types, statute required disclosure of the agency captive to the original policyholders. VCIA received feedback that potential agency captives were concerned that they needed to rework all their policy forms to outline the ownership of the captive to policyholders, which would require re-filing policy forms in other domiciles. DFR has been working with captive managers and others to develop a straightforward sample disclosure, based on disclosures required in captives that reinsured mortgage insurance.

Proposal: Amend statute to simplify the agency captive owner's disclosure requirement.

Section 2. –Dormant Captives

Background: Vermont adopted the concept of the dormant captive in 2013. The dormant captive is relieved of most reporting requirements and pays no tax while it remains dormant. The concept allowed captive owners to keep their captive intact at minimal cost, for future reactivation in Vermont.

One of the requirements of a dormant captive is to maintain minimum capital of $25,000. The original purpose of this requirement was to keep some of the capital that was in the captive available for regulatory costs in the event the dormant captive did not meet even it's minimal responsibilities. But some captives that have applied for dormancy were never capitalized or became operational in the first place, and at least one captive has been licensed to start out in a dormant status pending the death of the owner of the parent company – it make little sense to set aside funds to do nothing when there is so little risk for the regulator.

Proposal: Allow regulatory discretion in setting the capital of a dormant captive.

<u>Section 3. – Sponsored Captive Capitalization</u>
<u>Background</u>: The current minimum capital – referred to as the core capital - for a sponsored cell captive is $250,000. Since the core cannot be accessed by the cells, which have their own capital commensurate with their risk, $250,000 is not really needed for regulatory purposes.

<u>Proposal</u>: Reduce the minimum capital for a sponsored cell captive to $100,000.

<u>Section 4. – Unaffiliated Business in Protected Cells of Sponsored Captives</u>
<u>Background</u>: Protected cells are a popular alternative risk transfer mechanism worldwide and are a growth area for Vermont. Cells are more and more often operating like stand-alone captives, addressing similar issues and opportunities. Allowing some unaffiliated business within a cell will help keep the captive option open.

<u>Proposal</u>: Allow flexibility to insure unaffiliated business in a cell under the same circumstances as might be allowed in a stand-alone captive.

<u>Sections 5 & 6. – Separate Accounts in Protected Cells</u>
<u>Background</u>: One feature that is allowed in the captive law is the ability to establish separate accounts within a captive. Separate accounts allow the segregation of assets and liabilities within a company. Such segregation has been used by companies to apportion business for eventual sale (as might be appropriate in the divestiture of a subsidiary), or for business purposes such as to manage separate divisions or segments without the formality and costs associated with a separate subsidiary corporation. In keeping with the desire to allow cells to conduct business as any captive would, this section proposes to explicitly allow cells to form separate accounts within a given cell. The provisions mirror those applicable to standalone captives, and extends the protections of statutory clarity.

<u>Proposal</u>: Explicitly allow cells to form separate accounts within a given cell.

<u>Sections 7 & 8. – Legal Investments in Cells</u>
<u>Background:</u> Certain captives are required to follow strict, prescriptive, investment statutes. Those statutes are from an old model law, developed for commercial insurance companies and don't always fit well with the captive insurance concept. Last year the legislature gave most companies the option to follow the old model, or to develop their own investment policy, subject to Commissioner approval. That option was not extended to sponsored cell companies but DFR considers it appropriate to do so now.

<u>Proposal</u>: Provide flexibility in investments by giving sponsored captive companies, and the cells within said companies, the option to follow the old rules, or develop a plan for DFR approval.

<u>Sections 9 & 10 – Erroneous Statutory References</u>
<u>Proposal</u>: Correct 2 erroneous statutory references.

Section 11. – Accreditation Standard for RRG Examinations

Background: Examinations of risk retention groups are conducted in accordance with NAIC accreditation standards which require among other things that DFR conduct the examination following the NAIC examiners handbook and file the report within 60 days of its completion. DFR has followed these standards for years but recently discovered that the statutory directive to do so, as required for accreditation, was missing.

Proposal: Incorporate sections 3573 and 3574 into Chapter 142