1. Chapter 16-187, Hawaii Administrative Rules, entitled, "Term and Universal Life Insurance Reserve Financing", is adopted to read as follows:

"HAWAII ADMINISTRATIVE RULES

TITLE 16

DEPARTMENT OF COMMERCE AND CONSUMER AFFAIRS

CHAPTER 187

TERM AND UNIVERSAL LIFE INSURANCE RESERVE FINANCING

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§16-187-107 Requirements applicable to covered policies to obtain credit for reinsurance; opportunity for remediation
§16-187-101  Purpose. The purpose of this chapter is to conform to national standards governing reserve financing arrangements pertaining to life insurance policies containing guaranteed nonlevel gross premiums, guaranteed nonlevel benefits and universal life insurance policies with secondary guarantees; and to ensure that, with respect to each such financing arrangement, funds consisting of primary security and other security, as defined in section 16-187-104, are held by or on behalf of ceding insurers in the forms and amounts required herein. In general, reinsurance ceded for reserve financing purposes has one or more of the following characteristics: some or all of the assets used to secure the reinsurance treaty or to capitalize the reinsurer (1) are issued by the ceding insurer or its affiliates; or (2) are not unconditionally available to satisfy the general account obligations of the ceding insurer; or (3) create a reimbursement, indemnification or other similar obligation on the part of the ceding insurer or any if its affiliates (other than a payment obligation under a derivative contract acquired in the normal course and used to support and hedge liabilities pertaining to the actual risks in the policies ceded pursuant to the reinsurance treaty).  [Eff ]  (Auth: HRS §§431:2-201, 431:4A-104) (Imp: HRS §§431:4A-101 through 431:4A-104)

§16-187-102  Applicability. This chapter shall apply to reinsurance treaties that cede liabilities pertaining to covered policies, as that term is defined in section 16-187-104, issued by any life insurance company domiciled in this state. This
chapter and chapter 168, shall both apply to such
reinsurance treaties; provided, that in the event of a
direct conflict between the provisions of this chapter
and chapter 168, the provisions of this chapter shall
apply, but only to the extent of the conflict.
[Eff ] (Auth: HRS §§431:2-201,
431:4A-104) (Imp: HRS §§431:4A-101 through 431:4A-
104)

§16-187-103 Exemptions. This chapter shall not
apply to the following:

(1) Reinsurance of:
   (A) Policies that satisfy the criteria for
   exemption set forth in section 16-171-
   905(f) or (g); and which are issued
   before the later of:
      (i) The effective date of this
          chapter, and
      (ii) The date on which the ceding
           insurer begins to apply the
           provisions of VM-20 to establish
           the ceded policies’ statutory
           reserves, but in no event later
           than January 1, 2020;
   (B) Portions of policies that satisfy the
       criteria for exemption set forth in
       section 16-171-905(e) and which are
       issued before the later of:
       (i) The effective date of this
           chapter, and
       (ii) The date on which the ceding
           insurer begins to apply the
           provisions of VM-20 to establish
           the ceded policies’ statutory
           reserves, but in no event later
           than January 1, 2020;
   (C) Any universal life policy that meets
       all of the following requirements:
      (i) Secondary guarantee period, if
          any, is five (5) years or less;
(ii) Specified premium for the secondary guarantee period is not less than the net level reserve premium for the secondary guarantee period based on the Commissioners Standard Ordinary valuation tables and valuation interest rate applicable to the issue year of the policy; and

(iii) The initial surrender charge is not less than one hundred percent (100%) of the first-year annualized specified premium for the secondary guarantee period;

(D) Credit life insurance;

(E) Any variable life insurance policy that provides for life insurance, the amount or duration of which varies according to the investment experience of any separate account or accounts; or

(F) Any group life insurance certificate unless the certificate provides for a stated or implied schedule of maximum gross premiums required in order to continue coverage in force for a period in excess of one year;

(2) Reinsurance ceded to an assuming insurer that meets the applicable requirements of section 431:4A-101(d), HRS;

(3) Reinsurance ceded to an assuming insurer that meets the applicable requirements of section 431:4A-101(b) or (c), HRS, and that, in addition:

(A) Prepares statutory financial statements in compliance with the National Association of Insurance Commissioners Accounting Practices and Procedures Manual, without any departures from the National Association of Insurance Commissioners’ statutory accounting practices and procedures pertaining to the admissibility or valuation of
assets or liabilities that increase the assuming insurer’s reported surplus and are material enough that they need to be disclosed in the financial statement of the assuming insurer pursuant to Statement of Statutory Accounting Principles No. 1; and

(B) Is not in a company action level event, regulatory action level event, authorized control level event, or mandatory control level event as those terms are defined in chapter 431, article 3, part IV, HRS, when its risk-based capital is calculated in accordance with the life risk-based capital report including overview and instructions for companies, as the same may be amended by the National Association of Insurance Commissioners from time to time, without deviation;

(4) Reinsurance ceded to an assuming insurer that meets the applicable requirements of section 431:4A-101(b) or (c), HRS, and that, in addition:

(A) Is not an affiliate, as that term is defined in section 431:11-102, HRS, of:

(i) The insurer ceding the business to the assuming insurer; or

(ii) Any insurer that directly or indirectly ceded the business to that ceding insurer;

(B) Prepares statutory financial statements in compliance with the National Association of Insurance Commissioners Accounting Practices and Procedures Manual;

(C) Is both:

(i) Licensed or accredited in at least 10 states (including its state of domicile), and

(ii) Not licensed in any state as a captive, special purpose vehicle,
special purpose financial captive, special purpose life reinsurance company, limited purpose subsidiary, or any other similar licensing regime; and

(D) Is not, or would not be, below five hundred percent (500%) of the authorized control level risk-based capital as that term is defined in chapter 431, article 3, part IV, HRS, when its risk-based capital is calculated in accordance with the life risk-based capital report including overview and instructions for companies, as the same may be amended by the National Association of Insurance Commissioners from time to time, without deviation, and without recognition of any departures from National Association of Insurance Commissioners’ statutory accounting practices and procedures pertaining to the admission or valuation of assets or liabilities that increase the assuming insurer’s reported surplus;

(5) Reinsurance ceded to an assuming insurer that meets the requirements of either section 431:4A-104(b)(4)(A) or (B), HRS; or

(6) Reinsurance not otherwise exempt under subsections (a) through (e) if the insurance commissioner ("commissioner"), after consulting with the National Association of Insurance Commissioners’ Financial Analysis Working Group or other group of regulators designated by the National Association of Insurance Commissioners, as applicable, determines under all the facts and circumstances that all of the following apply:

(A) The risks are clearly outside of the intent and purpose of this chapter (as described in section 16-187-101);
(B) The risks are included within the scope of this chapter only as a technicality; and

(C) The application of this chapter to those risks is not necessary to provide appropriate protection to policyholders. The commissioner shall publicly disclose any decision made pursuant to subsection (f) to exempt a reinsurance treaty from this chapter, as well as the general basis therefor (including a summary description of the treaty). [Eff ] (Auth: HRS §§431:2-201, 431:4A-104) (Imp: HRS §§431:4A-101 through 431:4A-104)

§16-187-104 Definitions. For the purposes of this chapter:
"Actuarial method" means the methodology used to determine the required level of primary security, as described in section 16-187-105.
"Covered policies" means the following: subject to the exemptions described in section 16-187-103, covered policies are those policies, other than grandfathered policies, of the following policy types:
(1) Life insurance policies with guaranteed nonlevel gross premiums and/or guaranteed nonlevel benefits, except for flexible premium universal life insurance policies; or,
(2) Flexible premium universal life insurance policies with provisions resulting in the ability of a policyholder to keep a policy in force over a secondary guarantee period.
"Grandfathered policies" means covered policies that were:
(1) Issued prior to January 1, 2015; and
(2) Ceded, as of December 31, 2014, as part of a reinsurance treaty that would not have met one of the exemptions set forth in section
"Non-covered policies" means any policy that does not meet the definition of covered policies, including grandfathered policies.

"Required level of primary security" means the dollar amount determined by applying the actuarial method to the risks ceded with respect to covered policies, but not more than the total reserve ceded.

"Primary security" means the following forms of security:

(1) Cash meeting the requirements of section 431:4A-102(1), HRS;

(2) Securities listed by the Securities Valuation Office meeting the requirements of section 431:4A-102(2), HRS, but excluding any synthetic letter of credit, contingent note, credit-linked note or other similar security that operates in a manner similar to a letter of credit, and excluding any securities issued by the ceding insurer or any of its affiliates; and

(3) For security held in connection with funds-withheld and modified coinsurance reinsurance treaties:
   (A) Commercial loans in good standing of CM3 quality and higher;
   (B) Policy loans; and
   (C) Derivatives acquired in the normal course and used to support and hedge liabilities pertaining to the actual risks in the policies ceded pursuant to the reinsurance treaty.

"Other security" means any security acceptable to the commissioner other than security meeting the definition of primary security.

"Valuation manual" means the valuation manual adopted by the National Association of Insurance Commissioners as described in section 431:5-307(o)(2)(A), HRS, with all amendments adopted by the National Association of Insurance Commissioners that
are effective for the financial statement date on which credit for reinsurance is claimed.


§16-187-105 The actuarial method. (a) The actuarial method to establish the required level of primary security for each reinsurance treaty subject to this chapter shall be VM-20, applied on a treaty-by-treaty basis, including all relevant definitions, from the valuation manual as then in effect, applied as follows:

(1) For covered policies described in section 16-187-104, "Covered policies," subsection (1), the actuarial method is the greater of the deterministic reserve or the net premium reserve regardless of whether the criteria for exemption testing can be met. However, if the covered policies do not meet the requirements of the stochastic reserve exclusion test in the valuation manual, then the actuarial method is the greatest of the deterministic reserve, the stochastic reserve, or the net premium reserve. In addition, if such covered policies are reinsured in a reinsurance treaty that also contains covered policies described in section 16-187-104, "Covered policies," subsection (2), the ceding insurer may elect to instead use subsection (a)(2) as the actuarial method for the entire reinsurance agreement. Whether subsection (a)(1) or (a)(2) are used, the actuarial method must comply with any requirements or restrictions that the valuation manual imposes when aggregating these policy types for purposes of principle-based reserve calculations.
(2) For covered policies described in section 16-187-104, "Covered policies," subsection (2), the actuarial method is the greatest of the deterministic reserve, the stochastic reserve, or the net premium reserve regardless of whether the criteria for exemption testing can be met.

(3) Except as provided in subsection (a)(4), the actuarial method is to be applied on a gross basis to all risks with respect to the covered policies as originally issued or assumed by the ceding insurer.

(4) If the reinsurance treaty cedes less than one hundred percent (100%) of the risk with respect to the covered policies, then the required level of primary security may be reduced as follows:

(A) If a reinsurance treaty cedes only a quota share of some or all of the risks pertaining to the covered policies, the required level of primary security, as well as any adjustment under subparagraph (C), may be reduced to a pro rata portion in accordance with the percentage of the risk ceded;

(B) If the reinsurance treaty in a non-exempt arrangement cedes only the risks pertaining to a secondary guarantee, the required level of primary security may be reduced by an amount determined by applying the actuarial method on a gross basis to all risks, other than risks related to the secondary guarantee, pertaining to the covered policies, except that for covered policies for which the ceding insurer did not elect to apply the provisions of VM-20 to establish statutory reserves, the required level of primary security may be reduced by the statutory reserve retained by the ceding insurer on those covered policies.
policies, where the retained reserve of those covered policies should be reflective of any reduction pursuant to the cession of mortality risk on a yearly renewable term basis in an exempt arrangement;

(C) If a portion of the covered policy risk is ceded to another reinsurer on a yearly renewable term basis in an exempt arrangement, the required level of primary security may be reduced by the amount resulting by applying the actuarial method including the reinsurance section of VM-20 to the portion of the covered policy risks ceded in the exempt arrangement, except that for covered policies issued prior to January 1, 2017, this adjustment is not to exceed \( \frac{cx}{(2 \times \text{number of reinsurance premiums per year})} \) where \( cx \) is calculated using the same mortality table used in calculating the net premium reserve; and

(D) For any other treaty ceding a portion of risk to a different reinsurer, including but not limited to stop loss, excess of loss and other non-proportional reinsurance treaties, there will be no reduction in the required level of primary security.

(b) It is possible for any combination of subsections (a)(4)(A), (a)(4)(B), (a)(4)(C), and (a)(4)(D) to apply. Such adjustments to the required level of primary security will be done in the sequence that accurately reflects the portion of the risk ceded via the treaty. The ceding insurer should document the rationale and steps taken to accomplish the adjustments to the required level of primary security due to the cession of less than one hundred percent (100%) of the risk.

(c) The adjustments for other reinsurance will be made only with respect to reinsurance treaties
entered into directly by the ceding insurer. The ceding insurer will make no adjustment as a result of a retrocession treaty entered into by the assuming insurers.

(d) In no event will the required level of primary security resulting from application of the actuarial method exceed the amount of statutory reserves ceded.

(e) If the ceding insurer cedes risks with respect to covered policies, including any riders, in more than one reinsurance treaty subject to this chapter, in no event will the aggregate required level of primary security for those reinsurance treaties be less than the required level of primary security calculated using the actuarial method as if all risks ceded in those treaties were ceded in a single treaty subject to this chapter.

(f) If a reinsurance treaty subject to this chapter cedes risk on both covered and non-covered policies, credit for the ceded reserves shall be determined as follows:

(1) The actuarial method shall be used to determine the required level of primary security for the covered policies, and section 16-187-107 shall be used to determine the reinsurance credit for the covered policy reserves; and

(2) Credit for the non-covered policy reserves shall be granted only to the extent that security, in addition to the security held to satisfy the requirements of paragraph (1), is held by or on behalf of the ceding insurer in accordance with section 431:4A-101 and 431:4A-102, HRS. Any primary security used to meet the requirements of this paragraph may not be used to satisfy the required level of primary security for the covered policies. [Eff ]

§16-187-106 Valuation used for purposes of calculations. For the purposes of both calculating the required level of primary security pursuant to the actuarial method and determining the amount of primary security and other security, as applicable, held by or on behalf of the ceding insurer, the following shall apply:

(1) For assets, including any such assets held in trust, that would be admitted under the National Association of Insurance Commissioners Accounting Practices and Procedures Manual if they were held by the ceding insurer, the valuations are to be determined according to statutory accounting procedures as if such assets were held in the ceding insurer’s general account and without taking into consideration the effect of any prescribed or permitted practices; and

(2) For all other assets, the valuations are to be those that were assigned to the assets for the purpose of determining the amount of reserve credit taken. In addition, the asset spread tables and asset default cost tables required by VM-20 shall be included in the actuarial method if adopted by the National Association of Insurance Commissioners’ Life Actuarial (A) Task Force no later than the December 31st on or immediately preceding the valuation date for which the required level of primary security is being calculated. The tables of asset spreads and asset default costs shall be incorporated into the actuarial method in the manner specified in VM-20. [Eff ] (Auth:  HRS §§431:2-201, 431:4A-104) (Imp:  HRS §§431:4A-101 through 431:4A-104)
§16-187-107  Requirements applicable to covered policies to obtain credit for reinsurance; opportunity for remediation. (a) Subject to the exemptions described in section 16-187-103 and the provisions of subsection (b), credit for reinsurance shall be allowed with respect to ceded liabilities pertaining to covered policies pursuant to sections 431:4A-101 and 431:4A-102, HRS, if, and only if, in addition to all other requirements imposed by law or regulation, the following requirements are met on a treaty-by-treaty basis:

(1) The ceding insurer’s statutory policy reserves with respect to the covered policies are established in full and in accordance with the applicable requirements of section 431:5-307, HRS, and related regulations and actuarial guidelines, and credit claimed for any reinsurance treaty subject to this regulation does not exceed the proportionate share of those reserves ceded under the contract;

(2) The ceding insurer determines the required level of primary security with respect to each reinsurance treaty subject to this chapter and provides support for its calculation as determined to be acceptable to the commissioner;

(3) Funds consisting of primary security, in an amount at least equal to the required level of primary security, are held by or on behalf of the ceding insurer, as security under the reinsurance treaty within the meaning of section 431:4A-102, HRS, on a funds withheld, trust, or modified coinsurance basis;

(4) Funds consisting of other security, in an amount at least equal to any portion of the statutory reserves as to which primary security is not held pursuant to paragraph (3), are held by or on behalf of the ceding insurer as security under the reinsurance
treaty within the meaning of section 431:4A-102, HRS;

(5) Any trust used to satisfy the requirements of this section shall comply with all of the conditions and qualifications of section 16-168-11, except that:

(A) Funds consisting of primary security or other security held in trust, shall for the purposes identified in section 16-187-106, be valued according to the valuation rules set forth in section 16-187-106, as applicable; and

(B) There are no affiliate investment limitations with respect to any security held in such trust if such security is not needed to satisfy the requirements of subsection (a)(3);

(C) The reinsurance treaty must prohibit withdrawals or substitutions of trust assets that would leave the fair market value of the primary security within the trust (when aggregated with primary security outside the trust that is held by or on behalf of the ceding insurer in the manner required by subsection (a)(3)) below one hundred two percent (102%) of the level required by subsection (a)(3) at the time of the withdrawal or substitution; and

(D) The determination of reserve credit under section 16-168-11(d)(3) shall be determined according to the valuation rules set forth in section 16-187-106, as applicable; and

(6) The reinsurance treaty has been approved by the commissioner.

(b) The requirements of subsection (a) must be satisfied as of the date that risks under covered policies are ceded (if such date is on or after the effective date of this regulation) and on an ongoing basis thereafter. Under no circumstances shall a ceding insurer take or consent to any action or series
of actions that would result in a deficiency under subsection (a)(3) or (a)(4) with respect to any reinsurance treaty under which covered policies have been ceded, and in the event that a ceding insurer becomes aware at any time that such a deficiency exists, it shall use its best efforts to arrange for the deficiency to be eliminated as expeditiously as possible.

(c) Prior to the due date of each quarterly or annual statement, each life insurance company that has ceded reinsurance within the scope of section 16-187-102 shall perform an analysis, on a treaty-by-treaty basis, to determine, as to each reinsurance treaty under which covered policies have been ceded, whether as of the end of the immediately preceding calendar quarter (the valuation date) the requirements of subsections (a)(3) and (a)(4) were satisfied. The ceding insurer shall establish a liability equal to the excess of the credit for reinsurance taken over the amount of primary security actually held pursuant to subsection (a)(3), unless either:

(1) The requirements of subsections (a)(3) and (a)(4) were fully satisfied as of the valuation date as to such reinsurance treaty; or

(2) Any deficiency has been eliminated before the due date of the quarterly or annual statement to which the valuation date relates through the addition of primary security and/or other security, as the case may be, in such amount and in such form as would have caused the requirements of subsections (a)(3) and (a)(4) to be fully satisfied as of the valuation date.

(d) Nothing in subsection (c) shall be construed to allow a ceding company to maintain any deficiency under subsection (a)(3) or (a)(4) for any period of time longer than is reasonably necessary to eliminate it. [Eff ] (Auth: HRS §§431:2-201, 431:4A-104) (Imp: HRS §§431:4A-101 through 431:4A-104)

§16-187-109  Prohibition against avoidance.  No insurer that has covered policies as to which this chapter applies (as set forth in section 16-187-102) shall take any action or series of actions, or enter into any transaction or arrangement or series of transactions or arrangements if the purpose of such action, transaction or arrangement or series thereof is to avoid the requirements of this chapter, or to circumvent its purpose and intent, as set forth in section 16-187-101.  [Eff ] (Auth:  HRS §§431:2-201, 431:4A-104)  (Imp:  HRS §§431:4A-101 through 431:4A-104)

2.  The adoption of chapter 16-187, Hawaii Administrative Rules, shall take effect ten days after filing with the Office of the Lieutenant Governor.

I certify that the foregoing are copies of the rules, drafted in the Ramseyer format pursuant to the requirements of section 91-4.1, Hawaii Revised Statutes, which were adopted on M DD, YYYY, and filed with the Office of the Lieutenant Governor.

CATHERINE P. AWAKUNI COLÓN  
Director of Commerce and Consumer Affairs
APPROVED AS TO FORM:

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Deputy Attorney General