GOVERNMENT OF PUERTO RICO
OFFICE OF THE COMMISIONER OF INSURANCE

April 11, 2005

RULING LETTER NO. N-AF-4-63-2005

TO ALL DOMESTIC INSURERS

PROCEDURE AND CRITERIA USED BY THE OFFICE OF THE COMMISSIONER OF INSURANCE TO AUTHORIZE DOMESTIC INSURERS TO REINSURE RISK WITH UNAUTHORIZED INSURERS

Dear Sirs and Madams:

Under Section 4.120(1) (b) of the Puerto Rico Insurance Code ("the Code"), domestic insurers may only reinsure with unauthorized insurers if prior authorization is obtained from the Office of the Commissioner of Insurance of Puerto Rico ("the OCI"). Furthermore, Section 5.110 (1) of the Code establishes that insurers may not obtain credit for risk transferred as reinsurance to unauthorized insurers, unless the reinsurance has been transacted pursuant to the aforementioned Section 4.120.

The most recent revision of the procedure and criteria for authorizing domestic insurers to reinsure risk with unauthorized insurers was provided by means of Ruling Letter No. N-E-11-62-93, dated December 2, 1993. With the passage of time, the conditions and circumstances of the reinsurance markets have changed, making it necessary to modify some of the criteria used by the Office to align them with the reality of these markets and the needs of our insurers. Among other modifications, the volume of premiums that may be assumed by an unauthorized insurer without having to comply with authorization requirements is increased and a higher level of solvency is established.

Pursuant to the discretion granted in said Section 4.120, we are hereby revising and establishing the criteria we will use to grant such approval. To this effect we will only allow reinsurance with unauthorized insurers of an amount that is up to 35% of ceded reinsurance, provided that the following conditions are met:

1. The OCI has received satisfactory evidence that the financial condition and practices related to the processing of claims of the unauthorized insurer provide sufficient assurance that the public interest will be adequately protected. To that effect, the unauthorized insurer shall maintain a surplus with respect to policyholders of at least $50,000,000 or, deposits in Puerto Rico as guarantee of the payment of its obligations, if such deposits are subject to withdrawal by the ceding insurer or under such insurer's control, or the insurer holds a clean, unconditional, and irrevocable letter of credit issued by an acceptable financial institution, for an amount agreed to by the ceding insurer and the unauthorized insurer. A "clean, unconditional, and irrevocable" letter of credit is a letter of credit that:

   (i) makes no reference to and is not conditioned by any agreement, document or contract;
   (ii) provides that presenting the letter of credit (sight draft), without any other document, shall be sufficient to draw on the funds established in the letter of credit, and
   (iii) may not be modified or revoked without the consent of the ceding insurer.

Acceptable financial institutions are those that:

   (i) are organized and authorized under the laws of the Commonwealth of Puerto Rico, the United States of America or any of its states;
   (ii) are regulated, supervised, and examined by state authorities of the Commonwealth of Puerto Rico or federal authorities of the United States of America that have regulatory authority over financial institutions; and
   (iii) are not owners, subsidiaries or affiliates of the unauthorized insurer or beneficiaries of the letters of credit.

2. Evidence is provided to the OCI that the unauthorized insurer is a bona-fide insurer, that its operations are reputable, and that the business has been managed competently and reliably. Any two of the following conditions are considered to be evidence of the above:

   a. Maintains an A.M. Best or Standard & Poor's classification of "A" or better.
   b. Appears on the list of the International Insurers Department of the National Association of Insurance Commissioners (NAIC).
   c. Shows evidence of being authorized to do insurance business in one of the states of the United States of America.

3. The unauthorized insurer writes an annual volume of reinsurance premiums in Puerto Rico in an amount not greater than $2,000,000. Notwithstanding the above, if the unauthorized insurer maintains a policyholder surplus (PHS) of no less than $250,000,000, the insurer will be allowed to assume annually the amount of $5,000,000 in premiums. If the unauthorized insurer exceeds the maximum of such reinsurance premiums, the insurer shall file and maintain current an application for authorization at the OCI.

4. Domestic insurers may not cede risk to an unauthorized insurer, whether directly or indirectly if:

    a. A substantial number of the outstanding shares of the unauthorized insurer are owned or controlled, directly or indirectly, by an institution engaged in money lending in Puerto Rico, or if the unauthorized insurer has a substantial financial interest in, directly or indirectly, or as owner, subsidiary or affiliate, or is owned or controlled, directly or indirectly, by any entity engaged in money lending in Puerto Rico that also has a substantial financial interest in such, or relationship as owner, subsidiary or affiliate. It is further provided that the exception in Section 3.041(6)(a) of the Code shall also be applicable to unauthorized insurers.

    b. A substantial part of the outstanding shares of the unauthorized insurer is owned or controlled, directly or indirectly, by a domestic insurer, if such unauthorized insurer has a relationship as owner, subsidiary or affiliate of a domestic insurer.

The aforementioned provisions, except number 4, shall not be applicable to unauthorized insurers who participate in reinsurance treaties or facultative placement, provided that the share of each insurer does not exceed 5% of the treaty or facultative placement, and the aggregate share of such insurers with such limitation does not exceed 25% of the total treaty or placement.

So that we may have sufficient information to exercise our discretion, the ceding insurer shall request in writing authorization to cede risk to an unauthorized insurer at least five (5) days before the reinsurance contract enters into effect. The application shall identify the unauthorized insurer that the ceding insurer proposes to use. No later than sixty (60) days after the reinsurance that is the subject of the application enters into effect, the following information shall be submitted to us:

1. The most recent audited financial statement (or certificate) of the unauthorized insurer, duly sworn by two of the principal officers. If

the unauthorized insurer is organized outside of the United States, the statement should be notarized and authenticated by an Apostille under the Hague Convention of October 5, 1961.

2. An estimate of the amount of premiums to be ceded to the unauthorized insurer.

3. A copy of the cover note or agreement executed with the unauthorized insurer. The agreement shall contain, among the basic requirements of the reinsurance agreement, the insolvency clause required by NAIC. If reinsurance will be placed through a reinsurance broker, the reinsurance contract shall also contain the intermediary clause required by NAIC.

Insurers who reinsure with unauthorized insurers without obtaining authorization from the OCI shall be subject to legal sanctions. In addition, if authorization is not obtained, or authorization is denied for whatever reason, the domestic insurer will not be able to obtain credit for risk ceded to unauthorized insurers.

If authorization is obtained to use an unauthorized insurer, the authorization shall be effective from the date of the reinsurance contract, at the termination of which the ceding insurer shall again apply for our authorization, according to the guidelines set forth in this letter. Contracts that have been executed during that year with unauthorized reinsurers approved by the OCI, shall be valid for the purposes of this Ruling Letter, regardless of their expiration dates, provided that the duration of the reinsurance contract is not longer than one year.

This Ruling Letter is effective immediately and supersedes Ruling Letter Number N-E-11-62-93, dated December 2, 1993.

Strict compliance by all domestic insurers is hereby required with respect to the guidelines set forth in this Ruling Letter. Applications for reinsurance with an unauthorized insurer will only be processed if the application complies with the above requirements.

Very truly yours,

SINGED

Dorelisse Juarbe-Jimenez
Commissioner of Insurance