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Understanding Reinsurance Collateral Modernization

- Reinsurance, insurance for insurance companies, is one of the major tools that insurers use to pay claims.
- Through global reinsurance markets, the risk of a hurricane hitting Texas might be grouped together with the risks of an industrial accident in Japan, flooding in the United Kingdom, and a cyclone in Australia. Because all of these events are very unlikely to happen at the same time, reinsurers can make profits off of one type of coverage even as they pay massive claims on another.
- The overwhelming majority of reinsurance sold in the United States—and an even larger percentage of reinsurance used to back hurricane risk in Texas—comes from companies with headquarters outside of the United States.
- Under current Texas law, international reinsurers that don't have a subsidiary in the United States need to provide collateral (money pledged to secure an obligation) that's equal to the amount of reinsurance they write.
- This need to provide collateral discourages more capital from entering the market and makes reinsurance more expensive for everyone.
- The requirements to provide collateral apply even to reinsurers based in places like Switzerland, Germany, Japan, and the United Kingdom that have reinsurance regulations that are every bit as tough as America's.
- The National Association of Insurance Commissioners has proposed changes in laws that let state regulators decide that strong reinsurers based in well-known, tightly regulated jurisdictions *don't* have to provide such collateral.

- Customers—primary insurance companies—that still want to demand collateral still can. And regulators can also demand it if they have concerns about a foreign country’s regulatory system.
- Modernizing reinsurance collateral requirements simply bring Texas’ laws into compliance with those that exist elsewhere in the world and in many other states.
- Already, New York, Florida, New Jersey, Indiana, Virginia, Georgia, Louisiana, Connecticut, Pennsylvania, Delaware, and California have passed similar laws modernizing collateral requirements.
- Other states will do so in the near future.
- The proposals will make reinsurance less expensive for everyone while still maintaining strong standards that assure that reinsurance claims will get paid.

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