Willkie Farr & Gallagher LLP

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Recent Developments and Current Trends in

Insurance Transactions and Regulation

YEAR IN REVIEW 2013

January 2014

To Our Clients and Friends:

We are pleased to present our annual Insurance Transactions and Regulation **Year in Review** for 2013. In it we cover the year's most important developments, from M&A and traditional capital markets, to insurance-linked securities and alternative capital, to developments in regulation, both in the US and internationally.

The past year was an exciting one for the industry, as this review demonstrates. It was also an exciting year for our firm. For the year, Willkie was ranked Band 1 for corporate insurance matters by *Chambers*, was ranked Number 1 for insurance M&A deal value by *SNL*, and was a leading firm for ILS, including cat bonds, sidecars and other alternative capital solutions.

We hope that you find this **Year in Review** informative. If you would like further information about any of the topics covered here, please do not hesitate to contact us. A list of the partners and counsel in the group appears at the back of the publication.

The **Willkie Farr & Gallagher LLP** Corporate Insurance and Regulatory Group.

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I. M&A Recap

A. Not a Vintage Year for Insurance M&A

A total of 62 life and property-casualty ("P&C") insurance M&A transactions were announced in 2013, representing approximately $7.0 billion of aggregate announced deal value.[1] Announced life insurance deal volume was on pace with 2012, while aggregate deal value lagged considerably. Sixteen life insurance M&A transactions ($2.9 billion of deal value) were announced in 2013, compared to 15 life insurance M&A transactions ($4.5 billion of deal value) in 2012. Announced P&C insurance deal volume and value in 2013 both declined precipitously from 2012. Forty-six P&C insurance M&A transactions ($4.14 billion of deal value) were announced in 2013, compared to 77 P&C insurance M&A transactions ($22.2 billion of deal value) in 2012.

The most significant life insurance M&A transactions announced in 2013 were: (i) Protective Life's acquisition of MONY Life Insurance Company from AXA ($1.1 billion);[2] (ii) SCOR's acquisition of Generali's U.S. life reinsurance operations ($750 million); (iii) Resolution Life Holdings' acquisition of Lincoln Benefit Life from Allstate ($600 million);[2] and (iv) Global Atlantic's acquisitions of Aviva USA's life insurance operations and Forethought Financial Group for undisclosed sums. Protective has been an active consolidator of U.S. life insurance properties for a number of years, including Liberty Life (2010), United Investors (2010) and J.P. Morgan Chase Life (2006).[2] The acquisition of MONY was consistent with Protective's long-term acquisition strategy, providing a large block of seasoned policies with limited exposure to product and equity market guarantees, at a price that is immediately accretive to earnings. Meanwhile, the disposition of MONY permitted AXA to redeploy capital to other group members and to finance acquisitions in higher growth markets. SCOR's acquisition of Generali's U.S. operations followed its 2011 acquisition of Transamerica Re,[2] furthering its strategy of becoming a major participant in the U.S. life reinsurance sector. Resolution's acquisition of Lincoln Benefit, which has not yet closed, represents the company's first step in implementing a novel run-off strategy that it previously employed in the U.K. Finally, entering 2014, Global Atlantic has positioned itself as a significant force in life insurance M&A by announcing the Aviva and Forethought deals in relatively quick succession.

Also, Berkshire Hathaway announced two notable annuity transactions in 2013. In one transaction, Berkshire Hathaway reinsured $4.0 billion of guaranteed minimum death benefit and guaranteed minimum income benefit exposures under annuities issued by a subsidiary of CIGNA.[2] In the other, Berkshire acquired Hartford's U.K. variable annuity business for $285 million, in a deal that brought $1.75 billion of assets to Berkshire. The transactions were significant to the larger life insurance M&A market because they involved variable products that recently have been viewed as problematic risks by many potential buyers of life insurance properties. For Berkshire Hathaway, however, these transactions represented an opportunity to use its sizable balance sheet to take on difficult exposures at favorable prices.

Turning to the P&C insurance sector, several significant M&A transactions were announced in 2013. The largest was Travelers' $1.1 billion acquisition of Dominion of Canada General Insurance Co. This transaction, which was Travelers' first acquisition since 2010, furthered its strategy of using M&A to expand its international operations. The acquisition of Dominion, a personal and commercial lines insurer, significantly expands Travelers' exposure to risks in Canada.

Also of note, Enstar Group, one of the most active buyers of P&C insurance properties in recent years, announced two acquisitions in 2013. In June, Enstar agreed to acquire Atrium Underwriting Group and Arden Reinsurance Company for an aggregate price of $263 million.[2] Atrium is a Lloyd's managing agency and syndicate with third party names' capital, and Arden is a Bermuda reinsurer. In July, Enstar announced that it and private equity firm Stone Point would acquire Torus Insurance from an investor group including private equity funds First Reserve and Corsair

[1] Deal volume and value amounts in this report are from SNL's database.
[2] Willkie Farr & Gallagher LLP advised on this transaction.

Capital for cash and stock equal to $692 million.[2] Torus has U.S., Bermuda and U.K. insurance subsidiaries and a Lloyd's managing agency and syndicate. Historically, Enstar has focused on acquiring run-off insurance and reinsurance companies. These transactions, however, represent an expansion into "live" underwriting. In addition, both involve Lloyd's properties. As discussed in Section I.D below, a key driver of London market P&C insurance M&A in 2013 has been the desire on the part of both industry and private equity buyers to gain entrance to the Lloyd's market.

In September 2013, American Family Insurance, a mutual insurer that focuses on property, casualty and auto insurance, announced it had agreed to buy Homesite Group, Inc. for $616 million from a group of shareholders including Alleghany Corporation.[2] Homesite sells homeowners, renters and condominium insurance direct-to-homeowners. This acquisition was American Family's second acquisition in the past 12 months, and its largest to date.

Finally, in December 2013, Bermuda reinsurer SAC Re announced that it had agreed to be acquired by an investor group led by hedge fund Two Sigma for $625 million.[2] This transaction evidences the continuing allure of off-shore reinsurance vehicles to hedge funds that are eager to invest in reinsurance company assets.

A large number of insurance broker transactions were announced in 2013. Most of these deals were small, private transactions, but two are worth noting. First, on April 15, 2013, private equity firm Madison Dearborn announced that it had entered into a merger agreement to acquire National Financial Partners, a provider of benefits, wealth management and insurance services, in a deal valued at $1.3 billion. Second, on August 5, 2013, private equity firm Hellman & Friedman agreed to acquire Hub International for $4.4 billion. The sellers, Apax Partners and an affiliate of Morgan Stanley, had taken the company private in 2007 for approximately $2.0 billion.

B. Private Equity Acquisitions of Life Insurance Companies – Recent Developments

Over the past few years, private equity-backed entities have been increasingly frequent bidders for life insurers. Private equity-backed bidders have often focused on issuers of annuities, a line of business where investment risks tend to predominate over other risks, although many other types of insurers have also been targeted. An attraction of these deals to private equity-backed bidders is that these deals often are viewed as an opportunity for the bidders to create value by applying their sophisticated investment management expertise to the large pools of assets backing insurance reserves. Many private equity-backed bidders perceive these assets to have been undermanaged, or managed too conservatively.

In response to this trend, some state insurance regulators, led by the New York Department of Financial Services (the "NYDFS"), have begun to re-examine the conditions under which they will approve the purchase of a domestic insurer by private equity or hedge funds and other private investors. The regulators have expressed concern that these buyers may manage insurer investment portfolios too aggressively in pursuit of short-term returns, resulting in insolvencies and the failure of the insurers to meet their long-term obligations to policyholders.

Two recent transactions have clarified to some extent how the NYDFS and other regulators view these transactions: the purchase of the U.S. life insurance and annuity business of Aviva plc[2] by Athene Holdings Ltd., an insurance holding company backed in part by Apollo Management, which closed on October 2, 2013, and Guggenheim's purchase of the U.S. operations of Sun Life of Canada, which closed on August 2, 2013. On August 14, 2013, the NYDFS issued a press release announcing that it had reached an agreement with Athene Holding Ltd. on a set of heightened policyholder protections in connection with the former's acquisition of Aviva Life and Annuity of New York, the NY-domiciled subsidiary of Aviva USA.

[2] Willkie Farr & Gallagher LLP advised on this transaction.

The principal policyholder protections noted in the press release are:

- Athene will maintain Aviva New York's RBC at an amount not less than 450% (the NYDFS did not specify whether the 450% was based on the Company Action Level);
- Athene will establish a "backstop" trust account totaling $35 million to be used to replenish Aviva New York's capital in the event its RBC falls below 450%. The trust account will be held for seven years;
- Athene must obtain prior regulatory approval for any material change in Aviva New York's plan of operations, including in respect of investments, dividends or reinsurance; and
- Aviva New York will file quarterly RBC reports (rather than only the annual reports required under New York law), and will disclose "necessary information" concerning corporate structures, control persons "and other information regarding the operations of the company."

The NYDFS press release in the Aviva deal largely tracked the conditions set forth a few weeks earlier in a similar NYDFS press release with respect to the Sun Life deal, although the dollar amount of the trust fund was smaller. The NYDFS release relating to Aviva New York was quickly followed by a press release from the Iowa Insurance Department ("IID"), the primary regulator of Aviva's principal U.S. life insurance subsidiary, announcing that it had approved the Athene-Aviva deal. In its release, the IID stated that its approval was subject to the implementation of a capital maintenance agreement, a five-year moratorium on the payment of dividends by Aviva's Iowa domestic insurer and a special provision eliminating the minimum-size exemption from approval of affiliate agreements with respect to Athene, among other things. Notably, none of the regulatory announcements included any special limits on permitted investments, the initial source of the regulators' concern.

Other states have not imposed similar protections, welcoming investment by private equity in the life insurance business. These states may recognize that a planned short-term holding period for an investment in a life insurer is not necessarily inconsistent with prudent investment risk, given the substantial sums of their investors' (and their own) money that private equity managers put at risk in making these purchases.

The NYDFS has very recently announced that it is developing new regulations for life insurer acquisitions by private equity-backed buyers, to formalize the guardrails it imposed, on an *ad hoc* basis, in the Aviva and Sun Life deals. We expect these regulations to largely mirror the conditions imposed in those transactions. A working group of the National Association of Insurance Commissioners (the "NAIC") also is considering these issues, although the positions of the NAIC's members differ by state. To date, none of these heightened concerns have affected acquisitions of non-life insurers. We continue to believe there is value for private equity-backed buyers in insurer acquisitions (both life and non-life), whether within or outside of New York.

C. Thoughts on the State of Insurance M&A

1. Life Insurance

Overall, we expect 2014 to look much like 2013 in life insurance M&A. We anticipate the large U.S. carriers will continue to focus their activities on overseas markets and overseas distribution, with Asia and South America being the most popular targets. As a result, consolidators, such as Protective and Resolution, as well as private equity should enjoy a relatively open field in U.S. life insurance M&A.

We are optimistic that improving securities markets and rising interest rates will stimulate M&A deal flow involving issuers of variable annuities. Notwithstanding the Berkshire and Guggenheim deals, variable annuity writers have been difficult to sell since the financial crisis. Buyers have shunned risks resulting from benefit guarantees that the financial crisis exposed to be problematic and, in certain cases, unhedgeable. A rising stock market and higher interest rates may mitigate some of the concerns, which may enhance valuations and encourage buyers and sellers to pursue these transactions.

Finally, on the subject of private equity, we believe private equity-led M&A has been a positive for the insurance industry, providing significant competition in recent sales processes and enhancing transaction valuations at a time when industry buyers largely have been absent. With prominence, of course, has come increased regulatory scrutiny: as noted above, the NYDFS and the NAIC are considering whether and how to regulate private equity acquisitions of life insurers. We have some concern that heavy-handed regulation could suppress the appetite of private equity firms for M&A in the life sector. On the whole, however, we do not regard the commitments required of Athene and Guggenheim as preclusive of further deal-making, and are optimistic that new regulations will not drive private equity from the market.

2. P&C Insurance

For many years we and other commentators have been predicting an increased tempo of P&C insurance M&A activity—particularly among the Bermuda companies with significant reinsurance operations. Our prediction may be proved correct in 2014. The influence of ILS investors—including dedicated ILS funds, hedge and pension funds and endowments—on the traditional reinsurance and retrocessional natural catastrophe markets has increased capacity and affected pricing. This segment of the reinsurance market historically has been a key contributor to the profits of many of the Bermuda companies. We will be watching carefully to see if the competitive pressures of non-traditional sources of reinsurance capacity provide a catalyst to deal-making in Bermuda and elsewhere as those companies seek to adapt to a changing competitive landscape.

More generally, we believe that the next 12-18 months will look very much the same as the past few years, in terms of the number and types of transactions involving P&C insurers. We do not anticipate there will be significant M&A activity at the holding company level. That being said, we do anticipate a continuation of the trend toward transactions involving renewal rights, loss portfolio transfers, Lloyd's and London market entities and specialty and small commercial insurers. Recent reserving and rating-agency issues encountered by a number of these insurers have accelerated deal processes, if not resulted in actual deals. We also believe that run-off P&C insurer consolidators such as Enstar and Catalina will remain a formidable presence in P&C insurance M&A.

D. London Market Developments

Last year was marked by significant M&A activity within the London market generally and, in particular, at Lloyd's of London. A key driver of M&A activity in the London market in 2013 remained the desire of trade buyers to seek consolidation, private equity firms to gain entrance to the Lloyd's market and some existing market participants to sell their stakes at increasingly attractive multiples.

The perception remains that M&A activity, as compared to a syndicate start-up, assures a more straightforward entry into the Lloyd's market, although we note below a recent upturn in syndicate start-up activity. Several trade buyers have sought to expand and diversify their portfolios and businesses through Lloyd's acquisitions and were able to agree on deals in auctions involving non-trade buyers. Trade buyers continue to value the access to international markets, licensing advantages and favorable credit rating and security that participation in the Lloyd's market brings. Although we have seen the Lloyd's Franchise Board recently approve start-up syndicates at Lloyd's in compelling cases with differentiated business plans, it currently is generally easier for anyone interested in a Lloyd's platform to acquire one, rather than to establish one.

In the first half of 2013, formal auctions were conducted for both Atrium Underwriting Group and Torus Insurance.[3] Both deals attracted significant interest in the London market by potential buyers, and the sellers in both deals included private equity firms. While the successful bidder in both deals was Enstar, a reinsurance and run-off group located in Bermuda, Enstar partnered with private equity firm Stone Point Capital, which publicly supported Enstar's acquisition of both Atrium and Torus.

[3] Willkie Farr & Gallagher (UK) LLP advised on this transaction.

I. M&A Recap

In July 2013, New York-based AmTrust Financial Services entered into an agreement to purchase the loss-making Lloyd's vehicle, Sagicor Europe, which included its Lloyd's managing agent Sagicor at Lloyd's. This agreement followed the collapse of the proposed sale of Sagicor Europe to European private equity firm AnaCap in June 2013, following an extensive auction process. AmTrust was reported to have been eager to secure a Lloyd's platform for a number of years and turned to M&A after it was unable to secure approval for a start-up. AmTrust is thought to have paid £55 million for Sagicor Europe, representing a multiple of 1.35x book value.

In August 2013, London-listed (re)insurer Lancashire Holdings Limited announced its agreement to acquire the Cathedral Group, an integrated Lloyd's vehicle.[3] At the time, Cathedral was majority-owned by private equity firm Alchemy Partners, and was put up for sale in April 2013 in an auction process. The consideration represented 1.6x Cathedral's net tangible assets at the end of March 2013, which is in line with the multiples achieved by other sellers of Lloyd's franchises (e.g., Atrium, Kiln, Hardy, Talbot). The transaction was valued at £266 million, of which £131 million was raised through a private placement of new shares in Lancashire. The transaction was a Class 1 transaction requiring approval by Lancashire shareholders, who approved the deal in September 2013. Completion took place in November 2013, upon the granting of regulatory approval by the U.K.'s new PRA and Lloyd's.

Another trend in the U.K. insurance market in 2013 was activity involving stakes in motor and other personal lines insurers. In April 2013, private equity firm Aquiline completed its acquisition of Equity Red Star, a motor insurer which is the largest personal lines insurer at Lloyd's, from Insurance Australia Group. In August 2013, the U.K. personal lines insurer Esure floated its shares on the London Stock Exchange, which followed the listing on the London Stock Exchange of another U.K. personal lines insurer, Direct Line, and sales of stakes by Royal Bank of Scotland in a £2.6 billion IPO in 2012. Also in August 2013, private equity firm CVC Capital Partners agreed to purchase specialist appliance insurer Domestic & General from Advent International for £524 million. Finally, in October 2013, Goldman Sachs entered into a transaction to acquire a 50% stake in U.K. motor insurer Hastings Insurance Group. Goldman Sachs is reported to have paid £150 million for Hastings with the transaction completing in January 2014.

The most significant M&A deal of the year in the Lloyd's market was Sompo's acquisition of Canopius in December 2013. Sompo, a subsidiary of the Japanese insurer NKSJ, agreed to pay £594 million for Canopius, which is the highest nominal price for a Lloyd's vehicle since Apollo and CVC paid £880 million for Brit Insurance in 2011, valuing Canopius at 1.5x book value. It is understood that NKSJ views the acquisition as part of its long-term strategy to grow its overseas insurance business. Viewed by size, Canopius represented an attractive target for NKSJ, having a combined stamp capacity across all of its syndicates of just over £1 billion in 2014, making it one of the top ten Lloyd's carriers.

At year end, Sompo's acquisition of Canopius marked the seventh significant M&A transaction in the Lloyd's market in 2013, following on from the management buy-out of Ark Syndicate Management, ANV's acquisition of the Jubilee Managing Agency, Lancashire's purchase of Cathedral, AmTrust's acquisition of Sagicor Europe, Enstar and Stone Point's acquisition of Atrium and Aquiline's acquisition of Equity Redstar.

Another trend in 2013 involved Lloyd's approving new syndicates to be managed by both established and new managing agencies. Established for the 2013 underwriting year were Nephila's Syndicate 2357,[3] Randall & Quilter's Syndicate 1991 and White Mountain's Syndicate 1945.

This start-up activity contrasts with the 2012 underwriting year, when no start-up syndicates were approved by Lloyd's. The hiatus in syndicate approvals at that time led many prospective market participants either to resort to acquisitions as a means of entry into the Lloyd's market or, in the case of existing participants such as Ark, Beazley, Canopius and Catlin, to use special purpose syndicates as

[3] Willkie Farr & Gallagher (UK) LLP advised on this transaction.

a way of extending their participation at Lloyd's. Special purpose syndicates can be used to underwrite quota share reinsurance of another syndicate's business for a year of account, typically to take advantage of specific market circumstances, for example in the wake of major catastrophe losses.

Looking ahead in 2014, we can expect further consolidation in the market, with speculation centered around the prospect of further M&A activity involving the remaining independent players. We also anticipate a continuation of the recent increase in Lloyd's syndicate start-ups, with at least three new fully fledged syndicates entering the market with an aggregate stamp capacity of £269 million for the upcoming 2014 underwriting year: Axis's Syndicate 1686,[3] Duncan Dale's Syndicate 1729, and Acappella Syndicate 2014, the last of which changed its special-purpose syndicate status to become a full member. Illustrating this recurrence of start-up activity, 35% of Lloyd's £1.5 additional capacity for the 2014 underwriting year derives from syndicates that have entered the market since 2010. Of that 35% figure, half derives from syndicates that started underwriting in the 2014 underwriting year. We await to see what further M&A and syndicate start-up developments will arise in the course of 2014 at Lloyd's and the U.K. market generally.

[3] Willkie Farr & Gallagher (UK) LLP advised on this transaction.

II. Capital Markets Update

A. Insurer Initial Public Offerings

The year 2013 also witnessed the return of initial public offering ("IPO") activity to the insurance sector, with several significant transactions occurring after a dearth of activity in 2012. Third Point Re,[2] Essent,[2] ING's U.S. life insurance business (to be renamed Voya Financial) and Fidelity & Guaranty Life each made its public debut as a listed company. Each of these offerings was made for unique reasons, but some general themes and predictions for 2014 emerge when they are considered as a whole.

1. Life Insurers

The ING US offering was made pursuant to the restructuring plan submitted by ING Group to the European Commission. In order to receive state aid from the Netherlands during the financial crisis, in 2009 ING Group agreed to divest its insurance and asset management businesses, including ING US, over a period of years. ING Group ultimately elected to commence the sale process for ING US through an IPO in which all the shares sold were owned by ING Group. The offering raised approximately $1.3 billion for ING. ING Group is required to divest the remainder of ING US in stages through 2016 (although a faster disposition is possible), so further secondary offerings of shares seem likely.

Following the trail blazed by ING US, in December 2013 Fidelity & Guaranty Life raised over $150 million in its IPO. The proceeds were used in part to invest in F&G's business, and in part to pay a sizable dividend to its owner, Harbinger Group Inc. The IPO followed the well-publicized troubles of Philip Falcone, the CEO of Harbinger's ultimate parent. In mid-2013, Mr. Falcone reached a settlement with the Securities and Exchange Commission ("SEC") that, among other things, barred him from the securities industry for a multi-year period, and shortly thereafter the NYDFS imposed a similar bar prohibiting him from serving as an officer or director or exercising control over any New York-licensed insurer. While the sale may have been motivated in part by a desire to reduce Mr. Falcone's ownership interest in Fidelity & Guaranty, it also enabled Harbinger and its investors to realize some of the substantial increase in Fidelity & Guaranty's value since its acquisition by Harbinger. Harbinger acquired Fidelity & Guaranty in 2011 from Old Mutual for approximately $350 million, while the IPO valued the company at slightly under $1 billion.

2. Mortgage Insurers

Taking advantage of the improving fundamentals of the U.S. housing market, two mortgage insurers went public in the early part of November 2013. The first, Essent Group, raised $335 million, followed by NMI Holdings, Inc., which raised approximately $30 million. Essent's IPO built upon several years of strong growth in its business and standing within the mortgage insurance segment. The bulk of the proceeds went to support its operations. Showing confidence in the company, one of its principal stockholders made an investment at the IPO price, which was disclosed on the cover of the prospectus. NMI's IPO, though much smaller, was motivated in part by similar reasons, although NMI also faced a deadline under an agreement with its initial investors requiring it to list its shares on NASDAQ within a relatively tight time period or face the replacement of all of its directors. As of early January 2014, NMI was trading below its IPO price, while Essent was trading significantly higher than its IPO price.

3. Reinsurers

Third Point Re's successful IPO had been anticipated for some time. The shareholders of this reinsurer took advantage of favorable market conditions to list the company and raise money for its operations. Another reinsurer, Blue Capital Reinsurance Holdings, also made its U.S. listing debut in 2013 (discussed in Section III.B below). Blue Capital's business plan relies on Montpelier Re's underwriting expertise and infrastructure; Blue Capital may perhaps be thought of as a public sidecar to Montpelier.

[2] Willkie Farr & Gallagher LLP advised on this transaction.

Looking forward, 2014 may see further offerings by similar companies. On the life side, in the past few years a fair amount of M&A activity has involved private equity-backed buyers; one or more of these companies may go public. PE-backed insurers in other businesses may also take the opportunity to raise funds on the public markets, especially if the stock market remains strong. Although the market for capital for P&C insurers has been fundamentally and permanently changed by the availability of sidecars and other alternatives, a listing and public float remain important goals of early stage investors in insurers.

B. General Overview and Update on Liability Management Transactions

Last year saw a number of liability management transactions in the insurance industry, as insurance companies looked to take advantage of low spreads and investor interest to repurchase outstanding debt securities with a high coupon and replace it with newly-issued debt or hybrid securities with a lower coupon.

Issuers who took advantage of the favorable climate to repurchase some of their outstanding debt or hybrid securities included: Pacific Life, which completed a modified Dutch auction tender offer to purchase a series of surplus notes in January 2013; The Hartford, which purchased senior notes through a Dutch auction and waterfall tender offers in March 2013 to reduce its debt as part of its capital management plan, before issuing lower coupon senior notes in April 2013; Allstate, which implemented an ambitious capital management plan using preferred stock and subordinated debt to fund the retirement, through waterfall tenders, of higher cost debt securities;[2] Liberty Mutual, which, following on from their Dutch auction and waterfall tender offers in 2012, continued to purchase a significant amount of their outstanding junior subordinated debentures in the open market; CNO Financial, which completed an any-and-all tender offer to purchase a series of its outstanding convertible senior notes as part of its securities repurchase program; and ING Group, which conducted a cross-border tender offer for any-and-all of its senior notes guaranteed by The Netherlands. To the extent that interest rates remain low and investor appetite for highly rated debt remains strong, we expect this trend to continue in 2014.

Another notable transaction was Prudential Financial's redemption of all of its NYSE-listed junior subordinated notes at par in June 2013. These notes had been issued by Prudential Financial in 2008 as hybrid capital accompanied by a replacement capital covenant ("RCC"). Taking a slightly different approach in comparison to some other insurers, Prudential conducted a consent solicitation in 2012, asking holders of the relevant covered debt to agree to the termination of the original RCC; Prudential then entered into a more flexible, issuer-friendly version of the RCC in line with the latest S&P requirements, which permitted Prudential ultimately to redeem its junior subordinated notes in 2013.

Taking advantage of the continuing investor appetite for the new range of hybrid securities issued by insurance holding companies that started to hit the market in 2012, W. R. Berkley in April 2013 issued a series of subordinated debentures, the proceeds of which it used in part to redeem its outstanding trust preferred securities—the new generation of hybrid securities replacing the old.[2] Like the Aflac and Hannover subordinated debenture offerings in 2012, the W. R. Berkley securities had the "non-call 5" structure, in which, during the first five years, optional redemption at par is permitted following a tax event, or optional redemption at the greater of par and a make-whole amount is permitted following a rating agency event. These terms seem to have become the market standard for this type of hybrid security.

Also in 2013, Aspen Insurance executed several liability management transactions. In May 2013, it issued $275 million of fixed-to-floating rate perpetual preference shares intended to qualify for Tier 1 capital treatment under rules of the BMA.[2] The securities included a provision entitling Aspen Insurance to vary the terms of the preference shares, exchange them in the event the desired Tier 1 regulatory capital treatment is not recognized, or redeem the preference shares if they qualify for neither Tier 1 nor Tier 2

[2] Willkie Farr & Gallagher LLP advised on this transaction.

capital treatment under the BMA capital rules. Aspen used the proceeds to settle the cash portion of the settlement of its hybrid PIERS issued in 2005, following its decision to trigger mandatory conversion. Later in November 2013, Aspen Insurance also issued a new series of senior notes to take advantage of low interest rates and similarly used the proceeds to redeem a series of higher yielding outstanding notes.[2]

Finally, Allstate also introduced an innovative product to the retail market in December 2013, with two issuances of NYSE-listed depositary shares representing preferred stock from a new program developed with Incapital.[2] These depositary share offerings typically have a one-week marketing period, similar to traditional retail notes, and have the flexibility to reopen multiple times to allow Allstate to concentrate on the retail segment.

C. Funding Agreement-Backed Notes

Funding agreement-backed notes are designed to generate regular cash flows to service the debt on short- or medium-term notes issued through a securitization vehicle, and to transfer the credit quality of a policyholder claim at the insurance company to the notes of that vehicle.

In 2013, issuances remained below pre-financial crisis levels, but the funding agreement-backed notes market continued to recover, following the significant decrease in activity observed in 2009. In recent years issuances have been confined to a three- to four-issuer-market led by MetLife and New York Life and, to a lesser degree, Mass Mutual and Principal Financial. MetLife has been the leading issuer of funding agreements in each of the last five years, and New York Life is the next largest of the three remaining consistent issuers. 2013 also saw a return to the market by two issuers that were mainstays of the market prior to the financial crisis, Prudential and Jackson National. Capacity may now exist for additional issuances by the industry based on a stronger balance sheet position, a reduction in operating leverage and a strengthening of statutory capital.

Most of the activity was concentrated in the first nine months of 2013, with a mix of domestic issuances, foreign-denominated issuances (Euro, Sterling, Norwegian krone, Canadian dollars and Australian dollars) and a welcome return to the Swiss market where MetLife issued funding agreement-backed notes in the first offering of these notes since 2007 – perhaps a portent for the future.

D. Selected SEC Comment Letter Developments

1. Management's discussion and analysis (MD&A)

Continuing a trend, the SEC staff remained critical regarding the adequacy of registrants' MD&A disclosures, including the results of operations, critical accounting estimates and liquidity and capital resources. Staff comments have concentrated on requiring registrants to provide additional disclosure on the reasons for changes, especially significant changes relating to results of operations. In addition, SEC staff frequently asked registrants to quantify key metrics in MD&A, discuss how metrics are calculated, including any limitations thereon, provide metrics on a disaggregated basis (such as segment by segment or geography) and ensure that key metrics used to explain periodic fluctuation are linked to financial statements.

2. Captive Reinsurance

In addition to the investigation and June 2013 report of the NYDFS into the use of captive reinsurance by the life insurance industry in connection with insurance reserve financing transactions and the July 2013 publication of the *NAIC White Paper on Captives and Special Purpose Vehicles* (see Section V.B.2.a below), the SEC staff has also focused on this aspect of registrants' disclosures in 2013 periodic reports. Given the uncertainties associated with the continued use of captive reinsurers and registrants' existing disclosure in their Risk Factors, the staff has asked that registrants not only expand their disclosure to better explain the nature and types of coverage written by, and the business purposes of, captive reinsurers, but also to provide additional disclosures to be included in their MD&A detailing the reasonably likely effects on their financial position and results of operations and financial position if the practice were discontinued. The SEC staff

[2] Willkie Farr & Gallagher LLP advised on this transaction.

has also noted that if registrants do not believe that such additional disclosures are required, they should provide their analysis of Section 501.02 of the Financial Reporting Codification, regarding prospective information that supports such a conclusion, including, specifically, the two assessments management must make regarding a known trend, demand, commitment, event or uncertainty. As the NYDFS and the NAIC continue to study the use of captives and special purpose financial vehicles and consider whether financial statements of insurance companies should disclose information about transactions involving these arrangements, we expect this to be a continued point of focus of the SEC staff.

3. Loss Contingencies

The SEC has focused on the processes for estimation and disclosure of loss contingencies and has challenged whether disclosures evolve appropriately as matters progress. The SEC staff has requested that registrants "tell their whole story" in disclosures, including how matters have developed over time and how key developments have affected disclosures or amounts recognized in financial statements. The SEC staff has also focused on the process by which registrants develop an estimated loss or range of losses for each reporting period, especially where registrants have legal cases that remain open for a number of years.

4. Statutory Disclosure and Dividend Restrictions

The SEC staff has recently focused on the long-standing requirements for disclosures relating to regulatory required statutory capital and surplus, under ASC 944-505-50 and restrictions on the payment of dividends, under Rule 4-08(e) of Regulation S-X. Statutory capital and surplus amounts are required to be audited in the annual financial statements, and the SEC staff has reminded registrants that all minimum capital requirements, including those for non-regulated subsidiaries and foreign operations, should be disclosed. However, the SEC staff has acknowledged that for entities operating in many jurisdictions, only those jurisdictions in which the registrants conduct significant operations need be included. The SEC staff has requested that insurance registrants disclose the nature of any dividend restrictions at the parent and subsidiary levels and the amount of retained earnings or net income restricted or unrestricted for payment of dividends.

5. Low Interest Rates and Investments

With a particular sensitivity to low interest rates, the SEC staff has requested that insurance companies provide more expansive disclosures detailing how continued low interest rates are expected to affect future financial position, cash flow and profitability of certain products. The SEC staff has requested disclosure of information on how cash flows will be reinvested as investments mature or are called and information on cash flows that are committed to pay guaranteed features that are due. The SEC staff has also asked that registrants disclose information such as the amount of maturing or callable investments, their weighted average yields and insurance liabilities with minimum interest rate guarantees by product type.

In addition, the SEC staff continues to scrutinize disclosures about investments and financial instruments, including management determinations about the credit quality of investments, and has requested that insurance company registrants summarize the procedures that management performed to make such determinations.

6. Reinsurance Receivables

The SEC staff has also commented on disclosures concerning the credit quality of financing receivables and allowances for credit losses associated with insurance-specific balances, such as reinsurance receivables. ASU 2010-20 amended ASC 310 to require insurance company registrants to improve their disclosures about the credit quality of financing receivables and the related allowance for credit losses. According to the FASB, reinsurance receivables on paid claims fall under the ASU. Unpaid claims, while not falling under ASC 310, may fall within the scope of ASC 450 and therefore require disclosure.

7. Loss Adjustment Expense

Another area of concentration for the SEC staff has been loss adjustment expense. Insurance company registrants have been asked by the SEC staff to explain in disclosures the key methods and assumptions used in deriving the registrants' loss adjustment expense and the related reserves, with a particular emphasis on reserve disclosure related to catastrophes. Disclosures should comply with the requirements of Industry Guide 6, and the critical accounting policy section of registrants' MD&A should discuss the drivers of changes in estimates, including any assumptions that have changed or are reasonably likely to change.

III. Insurance-Linked Securities

A. Insurance-Linked Securities and Alternative Risk Transfers

"Insurance-Linked Securities" or "ILS" is the name given to a group of structurally related alternative risk transfer products. This group includes catastrophe bonds ("cat bonds"), sidecars, industry loss warranties, collateralized reinsurance facilities, extreme mortality and longevity derivatives and bonds, Triple X excess reserve financing facilities and dedicated fund and asset management vehicles. Increasingly favorable pricing (particularly in the cat bond market) for sponsoring ceding companies relative to more traditional reinsurance and retrocessional products and increasing and broadening investor appetite for higher yielding non-correlated asset classes resulted in a substantial increase in transaction activity in 2013 in most segments of this increasingly important market. The over-arching trend of convergence between traditional reinsurance and ILS seemed to pick up speed in 2013. Some commentators noted a significant downward pull of the alternative risk transfer market on the pricing of traditional reinsurance. Nowhere was this trend more in evidence than the significant downward pressure on rates on line for traditional natural catastrophe reinsurance resulting from "inexpensive" cat bond alternatives. We discuss these trends in more detail below.

1. Catastrophe Bonds

According to industry publication *Trading Risk*, over $7 billion of cat bonds were offered in 2013—the best year in terms of deal activity since 2007. Perhaps more importantly, the aggregate principal amount of cat bonds outstanding at year-end exceeded $20 billion, a record for the asset class. The amount of cat bonds outstanding is significant because most cat bonds are issued through so-called "shelf programs," with sponsors typically issuing new bonds on maturity of previously issued bonds. With over $20 billion of cat bonds outstanding, the pump is well primed for future issuances.

Over 30 sponsors brought cat bonds to market in 2013, including first-time sponsors Axis (Northshore Re) and QBE (VenTerra Re). The year also saw sponsors such as Allstate (Sanders Re) and Catlin (Galileo Re) return to the cat bond market for the first time since the financial crisis. Large direct writers continued to support the market with U.S. sponsors AIG (Tradewynd Re), Nationwide (Caelus Re), State Farm (Merna Re), Travelers (Long Point Re) and USAA (Residential Re) and European insurers Allianz (Blue Danube Re) and Axa (Calypso Capital) each sponsoring significant transactions. Reinsurers Munich Re (Queen Street), Scor (Atlas) and Swiss Re (Mythen) continued to access the ILS market for retrocessional capacity. Particularly noteworthy in this regard were Scor's Atlas IX[2] extreme mortality bond, its first such offering, and Swiss Re's Mythen Re combined P&C and mortality shelf.

The majority of the year's cat bonds used indemnity triggers and the balance primarily used industry loss or weighted industry loss triggers. Of particular interest was the market's receptivity to annual aggregate bonds, with sponsors taking advantage of investor flexibility with respect to terms as well as price. In this regard, one of the most innovative structures this year was Argo's Loma Re which combined indemnity and industry loss components in a single bond.

Continuing a trend that began in the financial crisis, collateral continued to be invested conservatively in U.S. Treasury money market funds or, for European sponsors, EBRD and similar quasi-sovereign instruments. Bermuda continued to be a popular domicile for issuers. More than half of sponsors elected to domicile their special purpose reinsurance vehicles in that jurisdiction. According to industry publication *Trading Risk*, 42 new cat bond vehicles listed on the Bermuda Stock Exchange in 2013, with a market cap of $4.6 billion (60% of the volume of total cat bonds issued for the year), compared with 15 new ILS vehicles listed with a market cap of $2.6 billion in 2012. The Cayman Islands remain a popular destination as well, with most of the deals that do not use a Bermuda SPRV using a Cayman vehicle. Ireland remained the destination of

[2] Willkie Farr & Gallagher LLP advised on this transaction.

choice for French sponsors. Also of interest to EU sponsors are reports that Malta is in the process of implementing a regulatory and tax framework designed specifically to facilitate ILS transactions for EU sponsors. We are following this development closely and will provide updates as the year progresses.

2. Sidecars

Notwithstanding choppy traditional market conditions, sidecar formation continued to be active. Long-standing and new sponsors continued to make use of the flexibility that these quota share facilities provide. Sidecar formation in 2013 primarily involved retrocessional facilities, although some market facing facilities were also formed.

Ace, Argo, Markel, Renaissance Re, Validus, Hannover Re and Swiss Re reloaded existing facilities or brought new facilities to market this year. In April 2013 Ace launched a second Altair Re sidecar with the same $95 million capacity as its predecessor. Argo Group renewed its Harambee Re[2] sidecar for 2014 at a larger size than in 2013, and Markel had $215 million for its retro-focused New Point Re VI. Renaissance Re saw the first renewal of its Upsilon Re retro sidecar in January 2013, increasing its size to $137 million from $74 million of capital when it was launched in January 2012. Hannover Re raised $330 million for its K vehicle in 2013. Swiss Re significantly expanded its Sector Re sidecar over the year, according to industry publication *Trading Risk*, with sources suggesting that it has roughly doubled in size to $500 million-$700 million. By contrast, Validus shrank its AlphaCat 2014 sidecar, cutting the vehicle back to $160 million from $230 million last year.

In addition, new participants Aspen, Everest Re, Partner Re, Munich Re and Scor all formed sidecars as well. In March 2013, PartnerRe became the latest reinsurer to launch a strategic sidecar-style vehicle, with $75 million Lorenz Re,[2] and Aspen raised $65 million for Silverton Re[2] in December 2013. New launches continued in January 2014, with Scor raising $55.5 million for Atlas X, its first sidecar since the 2001 hard market, and Everest Re raising $370 million for its special purpose reinsurer Mt Logan Re, making Mt Logan Re one of the largest collateralized reinsurer sidecars behind Swiss Re's Sector Re and Hannover Re's K vehicle.

One of the more interesting developments in the use of sidecars in 2013 was the continued evolution of the traditional structure to take on more of the characteristics of cat bonds. Investors in sidecars have traditionally invested in privately placed equity or debt securities offered by a special purpose reinsurance company—the sidecar. Historically, the securities offered have not been 144A eligible, contained transfer restrictions and provided more limited disclosure to investors than is provided with 144A eligible securities. They also tend to have fewer investors than do cat bonds.

In contrast, until relatively recently, cat bonds have been offered primarily on a 144A basis in traditional "book build" offerings. The disclosure documents used in these offerings tend to be more similar to those used in registered offerings, containing extensive disclosures with respect to structure and risks and requiring extensive participation by the sponsor, bankers, modeling firms and legal counsel. This year a number of the sidecar transactions were structured as 144A eligible transactions in order to expand the pool of potential investors and to facilitate liquidity for existing investors. We view this as a positive for the market, but note that, as is always the case with innovation, it may take a while for prior expectations with respect to timing and execution to catch up to the enhanced disclosure and opinion requirements and the incremental work involved in bringing a 144A offering to market.

B. ILS Fund Formation and Management

Perhaps adopting an attitude of "if you can't beat them join them," several reinsurers, continuing to adapt to the impact of ILS on the traditional natural catastrophe reinsurance market, leveraged their industry expertise to sponsor ILS-dedicated asset managers and funds. A number of insurers and reinsurers for several years through seed investments in ILS-dedicated fund managers or direct fund management through capital markets affiliates have sought and attracted third party capital for ILS investment. In 2013 this trend accelerated, with a number of reinsurers

[2] Willkie Farr & Gallagher LLP advised on this transaction.

launching new capital markets divisions in order to attract investors keen on accessing direct or tailored insurance risk. A flurry of deals were announced as the year was coming to a close and several of these funds are in the capital-raising stage in anticipation of being active in 2014. This includes Lancashire with its Kinesis[2] brand taking over from the previous Saltire structure, Montpelier's Blue Capital and XL Group-backed New Ocean,[2] which announced it has secured capital from private equity firm Stone Point.

We are seeing both open-end and closed-end fund structures, with many closed-end structures in particular utilizing segregated accounts of Bermuda SAC companies to isolate portfolios of reinsurance risks as between different classes of investors or risk periods. Another trend has been to enhance the traditional sidecar with a holding company structure, or fund, designed to facilitate the redeployment of investor capital from one underwriting period to the next. In addition, a number of open-end ILS funds have been organized, which generally allow for more frequent subscription and redemption activity into an existing portfolio of risks, subject to side pockets, slow-pay redemption shares (redeemable based on portfolio runoff rather than at NAV) and other restrictions principally designed to maintain liquidity and protect new investors from pre-existing events affecting the portfolio.

Another noteworthy development was Montpelier Re's sponsorship this Fall of a NYSE-listed ILS investment vehicle, Blue Capital Reinsurance Holdings. Montpelier had previously sponsored the London listing of a similar ILS investment vehicle. These publicly traded vehicles have the advantage over traditional fund structures of providing more permanent dedicated investment funding. That being said, it remains to be seen whether there will be more follow-on offerings by other ILS fund sponsors.

C. Excess Reserve Financing

Over the past year we saw a noticeable slowdown in the number of new excess reserve financing transactions. The likely cause was caution from both regulators and insurance companies in the life insurance reserve financing market as a result of the NAIC Captives and Special Purpose Vehicle Use (E) Subgroup activities, as well as the NYDFS's release of its own report on captives and special purpose vehicles ("SPVs"), which describes excess reserve financing transactions unaffectionately as "shadow insurance." The exceptions to this trend were transactions that occurred in connection with M&A activity in the life insurance industry. Buyers of life companies with large term life and universal life reserves on their books often require that existing deals be either amended to their liking or replaced by new structures. Even with the slowdown, several life companies continued to complete new transactions in 2013, and several other existing transactions were restructured to take advantage of lower lending rates and the continued interest by reinsurance companies to act as credit providers.

1. Summary of Deal Activity

a) AXXX Market Remains Open

As was the case in 2012, many of the transactions for which we acted as deal counsel were designed to provide reserve financing for universal life policies subject to Regulation AXXX. The expansion of lenders willing to provide financing to fund AXXX reserves, which started in 2012, continued in 2013. The size of the transactions ranged from a low of $100 million to $2 billion, as life insurance companies continued to take advantage of increased lender interest in financing redundant reserves. In most transactions in both the XXX and AXXX markets, commitments were for 10-20 years, although several transactions involved shorter terms intended to act as a financing bridge until other expected sources of funding would become available.

b) Continuance of Non-Recourse Transactions as the Structure of Choice

Although one or two XXX transactions in 2013 utilized traditional letters of credit, the vast majority of deals were secured by non-recourse letters of credit or contingent notes, as those transactions have essentially replaced traditional letters of credit among lenders and reinsurance companies active in the AXXX market. In the past, the obligation to reimburse the bank for any draw on the letter of credit was guaranteed by a parent holding company, thus

[2] Willkie Farr & Gallagher LLP advised on this transaction.

being known as a "recourse" transaction. In a non-recourse transaction, no such guaranty is required. Rather, the ability to draw on the letter of credit or contingent note is subject to certain conditions precedent. These conditions usually include the reduction of the funds backing economic reserves to zero and a reduction in a prescribed amount of the captive's capital, and a draw limited to an amount necessary for the captive to pay claims then due. Because of these conditions, lenders and other funding sources have become more comfortable assuming the risk of relying for repayment on the long-term cash flows from a block of universal life policies.

c) Choice of Domicile for Captives and Limited Purpose Subsidiaries

Vermont remained the preferred domiciliary jurisdiction for captive life insurers in 2013. With several states having adopted captive insurer laws or amending and expanded existing captive insurer laws over the past few years to facilitate reserve funding transactions, 2013 saw several other states – including Arizona, Delaware, Nebraska and Iowa – being utilized as captive insurer domiciles. 2013 also saw the continued, although limited, use of the recently enacted "limited purpose subsidiary" statutes in several states, as discussed in the next section.

2. Utilized Structures

a) Limited Purpose Subsidiaries

After the first use of an LPS in 2012, 2013 saw the continued, but limited, use of the LPS laws in AXXX transactions. Over the past few years, several states have enacted Limited Purpose Subsidiary statutes, which are meant to encourage their respective domiciliary life insurance companies to organize their captive insurers in the domiciliary state. Georgia, Indiana, Iowa and Texas have each promulgated an LPS statute. The advantage of an LPS over a captive insurer is that an LPS, once licensed, may provide its ceding company parent with full credit for reinsurance without posting any security in the form of a letter of credit or a credit for reinsurance trust. Under the LPS statutes, an LPS is permitted to take statutory financial statement credit for the face amount of letters of credit as well as parental guaranties by statutory authority; the LPS need not seek regulatory approval for a permitted practice or other dispensation to use this accounting treatment. Also, because the LPS is domiciled in the same state as the ceding insurer, the signatory approval process is streamlined. Although this was a major development in the ability to finance Regulation XXX/AXXX reserves, we have not seen the use of the LPS statutes take off as expected, likely as a result of the general lackluster market activity in 2013 brought on by insurer and regulator caution in general.

b) Credit-Linked Notes vs. Letters of Credit

Following on the heels of the 2012 boom, the use of contingent credit-linked notes in a role that may be analogous to a "synthetic letter of credit" continued to be the structure of choice. In these non-recourse transactions, an SPV issues a puttable note to a captive insurer. The captive insurer's right to "put" a portion of the note back to the SPV in exchange for cash is contingent on the same types of conditions that would otherwise apply in a non-recourse contingent letter of credit transaction. The use of these notes, rather than letters of credit, has provided a means for reinsurance companies, which contractually agree to provide the funds to the SPV to satisfy the put, to enter a market that was once only available to banks.

c) Funding Sources Beyond Banks

With the emergence over the past few years of the contingent credit-linked note transactions, the market for funding sources in AXXX transactions has expanded beyond banks. Large reinsurance companies have shown a keen interest in participating in these transactions through support of the SPVs that issue the contingent notes. With the expansion of the group of potential funding sources for these transactions, life insurance companies can seek more competitive pricing and terms. 2013 saw reinsurance companies surpass banks as the primary "risk taker" in these transactions, with banks for the most part sitting on the sidelines.

D. Longevity

While the U.S. pension risk market was very quiet in 2013, the U.K. market had a record-breaking year, with more than £16 billion in longevity and buy-out deal volume, easily exceeding the prior record of £12 billion in 2011. Since 2008, the size of the U.K. market averaged approximately £8 billion annually, though many expect the 2013 levels to become the new normal in light of the rapidly growing demand. In addition to the improving solvency levels, Aon Hewitt cited an increase in M&A activity as one of the principal reasons for the increased number of pension risk transfers, as companies seek to resolve pension issues in order to facilitate a sale.

The longevity market in the U.K. continues to be characterized by the large size of the relatively small number of transactions. In December 2013 alone, three transactions accounted for £5.3 billion of the £8.9 billion in longevity-only deals total for 2013. First, the pharmaceutical company AstraZeneca, whose pension fund has approximately £6.9 billion in assets, entered into a £2.5 billion swap with Deutsche Bank, covering approximately 40% of AstraZeneca's pension liabilities with respect to some 10,000 of its retirees. In addition, Carillion plc, a construction services firm, hedged £1 billion of the pension risk related to its five defined benefit pension plans through a longevity swap with Deutsche Bank. Finally, BAE Systems entered into £1.8 billion of longevity insurance contracts with Legal & General ("L&G"), covering two of BAE's pension funds. This was BAE's second foray into the longevity market in 2013. In February 2013, it transferred approximately £3.2 billion of this risk to L&G.

German reinsurer Hannover Re also completed three longevity reinsurance deals in the U.K. market in 2013. In February 2013, it entered into a £2 billion longevity reinsurance contract with L&G. In April 2013, in two separate reinsurance transactions, Hannover Re assumed some £490 million in longevity risk from Abbey Life, a U.K. insurance company owned by Deutsche Bank, and another £460 million from Rothesay Life, at the time an insurance subsidiary of Goldman Sachs. These three transactions alone generated approximately £150 million of Hannover Re's 2013 premium income.

As in 2012, the U.K. longevity market in 2013 was dominated by a few insurance companies, with L&G, Pension Insurance Corporation and Rothesay Life covering approximately 93% of the longevity business. In October 2013, however, Goldman Sachs sold a majority stake in Rothesay to a group of funds including Blackstone Group. This transaction significantly increased the number of players in the U.K. longevity market and signaled an increased level of interest by hedge funds in this marketplace. Funds managed by Blackstone and GIC Pte, Singapore's sovereign wealth fund, each acquired 28.5 percent of the Rothesay shares, while MassMutual obtained a 7 percent stake. Goldman retained a 36 percent interest.

The most innovative longevity transaction of 2013 was executed in the Netherlands. In December 2013, Aegon announced a longevity risk transfer transaction pursuant to which it transferred the risk associated with €1.4 billion of its longevity reserves to capital markets investors and reinsurers, with the assistance of Société Générale as the intermediary. The transaction used a medically based model of longevity risk developed by Risk Management Solutions ("RMS"). In addition, scenario-based modeling results were provided by RMS to investors in order to enable them to better assess the investment risk. Under the terms of the transaction, the final payment will be based on 50-year modeled scenarios. This structure is intended to allow Aegon to hedge 70 years of projected longevity risk under a 20-year instrument. SCOR Global Life reinsured 50% of the residual trend risk for this deal.

The Aegon transaction prompted a number of commentators to suggest that the development of longevity models will quickly pave the way for a longevity bond market, estimated to have a potential size five times greater than the market for natural catastrophe risks. In addition, it has been suggested that at some point reinsurance companies will also look at the capital markets to transfer a portion of longevity risk off their books. However, according to Hannover Re, pricing for longevity capital markets products is not yet attractive and, at least for now, major reinsurers will continue to be the principal ultimate holders of longevity risk.

IV. Developments in Corporate Governance and Shareholder Activism

The most noteworthy trends in corporate governance and shareholder activism in 2013, in our view, are: a continued reduction in the number of companies failing say-on-pay votes; a continued decrease in the total number of shareholder proposals coming to a vote; the continued inability of the proxy advisory firms to develop new governance proposals (beyond their familiar stand-bys of declassifying boards, majority voting for directors and eliminating supermajority provisions) that shareholders will consistently approve; and a possible slow decline in the influence of the proxy advisory firms. Although it is too soon to say that we are now living in a "post-ISS" world, corporations large and not-so-large have adapted to the modern shareholder and a new sense of business-as-usual has emerged. The improved economy has undoubtedly helped as well.

A. Say-on-Pay

In 2013, voting results at U.S. public companies once again were overwhelmingly in favor of approval of companies' executive compensation and related proxy statement disclosures. According to Georgeson Inc., only 22 companies in the S&P 1500 received less than a majority of votes cast in favor of their say-on-pay resolutions during the 2013 proxy season, as compared to 39 companies in 2012. Opposition to say-on-pay resolutions declined in the broader market as well, although less dramatically, from 51 companies in the Russell 3000 that failed this vote in 2012 to 47 Russell 3000 companies in 2013.

Shareholder disapproval of say-on-pay resolutions declined despite continued unfavorable coverage of executive compensation in the media and continued pressure from the Obama Administration, most recently its mid-2013 proposal to cap top pay at military contractors at $400,000. Disapprovals declined notwithstanding that, once again, many more companies received adverse recommendations from Institutional Shareholder Services Inc. ("ISS") and Glass, Lewis & Co., LLC ("Glass Lewis") than actually failed their votes. Passing votes were most common at the largest companies; for example, less than 1% of the S&P 500 companies failed their votes.

Improved communications between issuers and major shareholders about compensation issues undoubtedly played a part in the continued improvement in say-on-pay votes. This "engagement" with shareholders is strongest among the largest companies, which have the resources to invest the considerable time required. At the same time, many large institutional investors have developed their capacities to engage with issuers, as well as their own independent points of view about acceptable pay practices. Institutions in 2013 are more often using ISS and Glass Lewis as sources of data about company practices, rather than unthinkingly following their recommendations. Although some institutional shareholders have been alert to pay issues for years, the "new normal" is a heightened awareness across the large shareholder groups.

Finally, we continue to watch the development of so-called "mandatory say-on-pay" in the U.K. Under legislation enacted in 2013 that came into force on October 1, 2013, U.K. "quoted companies" (*i.e.*, companies whose equity share capital has either been included in the U.K.'s Official List, or is officially listed in a European Economic Area state, or is admitted to trading on either the New York Stock Exchange or NASDAQ) are now required to hold a binding vote at least every three years on their remuneration policy. In addition, quoted companies are also now required on an annual basis to produce a remuneration report, which will be subject to an annual advisory vote.

The requirements for the remuneration policy are broad: for example, a future policy table must be included, which must set out how each component of pay supports the company's short- and long-term objectives, the maximum that may be paid under each component and a description of the applicable framework to assess performance. The policy must also contain a statement of principles that will apply to officer recruitment, which must include the maximum level of variable pay that may be granted, although

this does not need to be expressed in monetary terms. Furthermore, the policy must also describe any obligation contained in the officers' employment agreements that could give rise to remuneration payments or "loss of office" payments. As to loss of office payments, the policy must set out the company's criteria for setting notice periods and the principles that will apply to the calculation of these payments. Payments under agreements made before June 27, 2012 will not fall within the scope of these principles, provided that the relevant agreement is not subsequently modified or renewed. Finally, the policy must state the extent to which shareholders' views on remuneration have been considered when drafting the policy.

Once a company's policy is approved, the company may not make compensation payments outside the scope of the policy without reapproval. If a policy is not approved by the company's shareholders, the company will have to convene a separate general meeting to vote on the policy again, presumably as amended to be more palatable to its shareholders. If a previous policy is already in place, the company may continue to follow the most recently approved policy, but it will need shareholder approval for any non-compliant payments. In general, any obligation to make a payment that contravenes the policy will have no effect, and the directors and officers involved may be subject to a fine.

Most quoted companies will present their remuneration policies and reports at their respective annual meetings ("AGMs") in the next few months. Therefore, heading into the AGM season, it will be interesting to see how shareholders react to their new powers of approval and whether any remuneration policies are not approved. Successful experience in the U.K. with mandatory votes on executive compensation could lead shareholder advocates to push for their implementation in some form in the U.S.

B. Shareholder Proposals

In the 2013 proxy season, according to Georgeson, 263 corporate governance shareholder proposals were voted on at the S&P 1500 companies, compared to 269 in 2012. Of these proposals, it continues to be that only proposals to declassify the board of directors, eliminate supermajority shareholder vote requirements, and institute majority voting for directors (at companies with no majority vote policy) obtain on average a majority of votes cast in favor. Interestingly, these majority voting proposals continue to receive strong support (72% of votes cast in favor, according to Georgeson), notwithstanding that only a small number of directors actually fail to receive a majority vote each year. In 2013, of the 8,700 directors up for election tracked by Georgeson, only 25 failed to obtain a majority of votes cast. All other governance proposals on average failed to receive a majority of votes cast. Of these, proxy access proposals deserve special note.

In mid-2011 the D.C. Circuit Court of Appeals vacated the SEC's proposed proxy access rule (Rule 14a-11), which was never reproposed by the SEC. However, in 2012 nearly 30 stockholder proposals for some form of proxy access were submitted to issuers, of which approximately ten came to a vote. Consistent with our prediction last year, proxy access did not take off as an issue in 2013; instead, of companies tracked by Georgeson, only 11 received a proposal for proxy access, and only nine of these proposals came to a vote. (A small number of companies adopted proxy access as a management proposal or simple by-law amendment.) The shareholder proposals set forth a range of ownership thresholds and other requirements for the right to proxy access, and on average failed to obtain a majority vote. It is worth noting, however, that the proxy access proposals structured to provide access only to shareholders that have held at least 3% of the outstanding stock for at least three years (consistent with the requirements of the SEC's vacated Rule 14a-11) obtained majority support at 75% of the companies holding a vote on them. Notwithstanding this record of success, we still doubt proxy access proposals will ramp up in 2014.

In addition to corporate governance proposals, shareholder activists also continued to present social issues for consideration in 2013. Following the Supreme Court's *Citizens United* decision, political contributions and lobbying by issuers have become subjects of great interest to a variety of constituencies. Shareholder proposals on this topic came to a vote at 78 companies in the S&P 1500

in 2013; only one of them received a majority vote. Another approximately dozen companies held a vote on whether to produce a sustainability or similar report. For example, shareholders of one insurer were asked to vote on whether the board should issue an annual report on environmental, social and governance issues, to enable shareholders to evaluate the company's "impact on society." None of these proposals received a majority vote in favor.

C. Proxy Fights

In 2013, no public proxy fights affected a significant insurance holding company. These proxy fights are unique in their complexity, because of the interplay of insurance regulation (with its strict limits on obtaining "control" of an insurer, as defined for insurance law purposes), and the federal securities and state corporate laws that govern proxy fights. This complexity likely holds down the number of such contests.

Nevertheless, in several current instances, investors who sometimes take an activist approach have filed Schedule 13Ds or otherwise are reported to have amassed a meaningful stake in a public insurance holding company. There may be more to report at this time next year.

V. Principal Regulatory Developments Affecting Insurance Companies

A. Overview

In 2013, regulatory developments and announcements of new regulatory priorities affecting insurance companies were made by state regulators and the NAIC, as well as federal and international regulators.

The federal government's presence in insurance regulation increased throughout 2013. One of the most significant federal developments was the release by the Federal Insurance Office (the "FIO") of its long-awaited report on the state of U.S. insurance regulation. The report's suggestions and tone demonstrate the FIO's support for an increased role of the federal government in the regulation of insurance. In 2013, the Financial Stability Oversight Council ("FSOC") made its first designations of systemically important nonbank financial companies ("SIFIs") that will be subject to consolidated federal supervision and enhanced regulatory standards. The first three entities to be designated as SIFIs are American International Group, Inc., General Electric Capital Corporation, Inc., and, controversially, Prudential Financial, Inc. The designation of Prudential Financial, Inc. was made over the objection of Roy Woodall, the insurance industry member of FSOC, who suggested that FSOC should rely on the recommendations of individuals with insurance expertise when determining whether an insurance company should be designated as a SIFI.

Internationally, the Financial Stability Board ("FSB") designated a list of nine Global Systemically Important Insurers ("G-SIIs"): Allianz SE American International Group, Inc.; Assicurazioni Generali S.p.A.; Aviva plc; Axa S.A.; MetLife, Inc.; Ping An Insurance (Group) Company of China, Ltd.; Prudential Financial, Inc.; and Prudential plc. At the same time, the International Association of Insurance Supervisors ("IAIS") released proposed regulatory measures that will apply to G-SIIs, including enhanced supervision and required financial distress planning. G-SIIs will also be the first insurance entities to be subject to the IAIS's group-wide capital measures, with certain capital requirements proposed to become effective in 2015. Additionally, the IAIS moved into the final planning phases for its framework for the supervision of internationally active insurance groups known as ComFrame.

For the past few years, the NAIC has focused on its solvency modernization initiative ("SMI"), which resulted in major initiatives that include the adoption of the Risk Management and Own Risk and Solvency Assessment Model Act (the "ORSA Model Act"), the amendments to the NAIC Model Insurance Holding Company Systems Regulatory Act, revisions to the Credit for Reinsurance Model Act, and the adoption of principle-based reserving ("PBR"). In recognition of the approaching end of the developmental phase of SMI and the shift of the NAIC's focus to implementation of SMI going forward, the NAIC disbanded its SMI Task Force. It is expected that SMI initiatives will continue to be addressed by other NAIC committees and state legislatures during 2014.

On the life insurance side, both the NAIC and the NYDFS turned their attention to private equity and hedge fund investment in life insurance companies. At the same time as the NAIC developed a new working group to consider risks associated with private equity and hedge fund investment in life insurers, the NYDFS began to impose conditions on the acquisition of life insurers by private equity and hedge fund buyers.

B. Insurance Topics of General Interest

1. Federal Insurance Office Update

On December 12, 2013, the FIO released its long-awaited report on how to modernize and improve U.S. insurance regulation. Noting the long-term debate over state-based versus federal insurance regulation, the FIO suggests a reframing of the debate to identify those areas where federal involvement is warranted, not whether federal regulation should completely displace state-based regulation. In the FIO's view, appropriate areas for federal involvement could include direct regulation, setting standards to be implemented by the states, or operating

a program that supports or replaces a failed insurance market. While noting that by its very nature a system of 56 independent jurisdictions is limited in its ability to regulate uniformly, resulting in unnecessary costs and inefficiencies, the FIO expressed the belief that, in the short term, U.S. insurance regulation can be modernized and improved by a combination of targeted and broad steps by the states and certain federal actions. However, the report also warns that if the states do not act in the near term to effectively regulate matters on a consistent and cooperative basis, in the FIO's view there will be a greater role for federal regulation of insurance.

a) The FIO Report

The report's principal findings are divided between matters of prudential (*i.e.*, solvency) regulation and matters of marketplace regulation. With respect to solvency, the report in general terms looks for greater consistency and transparency across the states, while maintaining a high level of protection for policyholders. With respect to direct areas for federal involvement in insurance regulation, the report makes several key recommendations. First, the report recommended that mortgage insurers should be federally regulated and overseen from a solvency and business practices perspective. The report bases this recommendation on the strong national interest in housing market conditions and the U.S. government's role in that market. Second, the report recommends that the U.S. Treasury and the U.S. Trade Representative pursue "covered agreements" for reinsurance collateral requirements affecting non-U.S. reinsurers. These agreements would streamline the process of reducing collateral requirements for reinsurance credit for reinsurers in specified jurisdictions, a process state regulators have been somewhat slow to implement on their own. Further, in an echo of its observations about group supervision described above, the FIO proposes to itself participate in supervisory colleges to monitor financial stability and identify issues or gaps in the regulation of large national and internationally active insurers.

The FIO report contains a number of other ideas and recommendations. It is required reading for anyone with an interest in the future of insurance regulation. It does not set a prescriptive timetable for any of the measures it proposes, but clearly looks to the near term as the time frame for moving forward.

b) Implications of FIO Report for State-Based Regulation

Over the past several years, the debate at NAIC meetings has reflected the increasing involvement of federal and international regulators and standard setters. Today, the goals and standards of the NAIC and state regulators are commonly set by federal and international forces – and state regulators are fighting to explain and maintain the U.S. state system of insurance regulation. During the NAIC's tri-annual national meetings, growing tensions within and among these groups regarding governance and jurisdiction have increasingly been publicly aired, most notably at the NAIC's year-end fall national meeting in Washington, D.C. in December 2013.

The FIO report concluded that the state-based system of insurance regulation is inherently limited in its ability to regulate uniformly and efficiently, and that this lack of uniformity is acutely felt in both financial matters and marketplace oversight.

Not surprisingly, citing the threat of federal intervention, a common theme of the NAIC's fall national meeting was uniform state insurance regulation. The chairs of various committees stressed that the states' ability to ward off federal intervention depends on state adoption of NAIC models, including state legislative deferral to NAIC-developed standards as drafted and amended over time. Examples cited by regulators included the incorporation in state law of NAIC-governed rules such as statutory accounting practices and procedures, risk-based capital instructions, the financial examiners handbook and other such standards. In addition, in response to the FIO report, Senator Ben Nelson, CEO of the NAIC, noted in his welcome letter to the fall national meeting that the NAIC "remain[s] focused on ensuring that FIO does the job it was created to do, and not [the NAIC's] job, while recognizing that the FIO can supplement and enhance existing efforts of the NAIC and state insurance regulators to strengthen the position of the United States in international discussions relative to insurance issues."

2. Special Purpose Vehicles / Captives

a) NAIC

Captives and SPV White Paper. The Captives and SPV Use (E) Subgroup of the Financial Condition (E) Committee of the NAIC (the "Captives/SPV Subgroup") finalized its much anticipated Captives and Special Purpose Vehicles White Paper ("Captives White Paper") on June 6, 2013. The formation of the Captives/SPV Subgroup was prompted, in part, by perceived inconsistencies in state regulatory requirements for insurers' use of captive insurers and SPVs.

The Captives White Paper outlines the findings of the Captives/SPV Subgroup's study of the use of captives and SPVs by life insurance companies or insurance company holding companies to transfer insurance risks, and offers a variety of recommendations, including the following:

- *Access to Alternative Markets*: That the NAIC consider updating the Special Purpose Reinsurance Vehicle Model Act (Model 789) to reflect alternative market solutions designed to shift risk to the capital markets or provide other forms of business financing that would be acceptable to state insurance regulators, in order to ensure uniformity in this area.

- *Credit for Reinsurance Model Law Enhancements*: That the use of conditional letters of credit or other forms of collateral in Captives/SPV transactions to satisfy credit for reinsurance under the Credit for Reinsurance Model Law (Model 785) be studied further to determine whether they are providing the protections intended by this model law.

- *Accounting Considerations*: That possible solutions be developed for addressing any remaining XXX and AXXX perceived redundancies prior to the effective date of PBR, such that perceived redundancies should be "addressed directly as opposed to through the use of captives and SPVs."

- *Financial Analysis Handbook*: That guidance be developed in the *Financial Analysis Handbook* for the states' review and ongoing analysis of transactions involving captives and SPVs.

- *Confidentiality, Disclosure and Transparency*: That the issue of confidentiality related to commercially owned captives and SPVs be studied more closely, with the aim of providing "greater clarity regarding the specific reasons for and against the use of confidentiality for such entities;" and that consideration be given to enhanced disclosure in ceding company statements regarding the impact of captive/SPV transactions on the financial position of the ceding insurer.

The committees of the NAIC that received these and other referrals from the Captives/SPV Subgroup have begun considering whether to accept in whole, or in part, any of the recommendations.

New Charges of the Financial Analysis (E) Working Group (FAWG). In a July 2013 conference call, the Financial Analysis (E) Working Group (the "FAWG") unanimously adopted the following new charges relating to the use of captives/SPVs:

- Perform analytical reviews of transactions (occurring on or after a date as determined by the NAIC membership) by nationally significant U.S. life insurers to reinsure XXX and/or AXXX reserves with affiliated captives, SPVs, or any other U.S. entities that are subject to different solvency regulatory requirements than the ceding life insurers, to preserve the effectiveness and uniformity of the solvency regulatory system;

- For transactions entered into and approved prior to this date and still in place, collect specified data in order to provide regulatory insight into the prevalence and significance of these transactions throughout the industry; and

- Provide recommendations to the domiciliary state regulator to address company-specific concerns and to the Principle-Based Reserving Implementation (EX) Task Force ("PBR Task Force") to address issues and concerns regarding the solvency regulatory system.

These new charges have been much discussed, primarily with respect to whether they might prevent a state from approving a captive/SPV transaction unless it has been

approved by the FAWG. It was clarified, however, that these charges are only intended to subject these transactions to a peer review, not to prevent their approval by the relevant state.

On November 20, 2013, the NAIC Financial Condition (E) Committee (the "(E) Committee") disclosed in its Proposed 2014 Charges that the NAIC has decided that July 23, 2013 was the cutoff date after which regulators are now encouraged to confidentially submit XXX/AXXX captive transactions for companies in their jurisdictions to the FAWG. As of late 2013, we were not aware of any transactions, existing or prospective, that had yet been presented to, or reviewed by, the FAWG.

Treatment of Special Purpose Captives under NAIC Accreditation Standards. The NAIC Financial Regulation and Accreditation Program is a process by which accreditation is given to a state insurance department if it meets certain legal, financial and organizational standards as determined by peer regulators. These standards include adopting certain model laws and regulations developed by the NAIC.

During its December meeting, the Financial Regulation Standards and Accreditation (F) Committee (the "Accreditation Committee") agreed to draft and expose language intended to clarify that single-state licensed special purpose captives that assume reinsurance from cedants operating in multiple states are "multi-state insurers" and as such should be subject to all the accreditation standards applicable to other insurers.

The impact of this change in the application of the NAIC's Accreditation Standards could disrupt the captive/SPV marketplace. If a captive was treated as a multi-state insurer under the Accreditation Standards, it likely also would be subject to, among other items, the capital and surplus requirements, risk-based capital requirements, investment laws and credit for reinsurance laws that apply to traditional multi-state insurers. In addition, numerous changes to laws and regulations would likely be required in each of the states where different capitalization, reinsurance and related standards are applied to captives. In this respect, the Accreditation Committee noted that flexibility would be incorporated into the Accreditation Standards to allow for some seasoning and time for states to make appropriate changes to their laws and regulations.

Principle-Based Reserving and Life-Insurer Owned Captives Transactions. The meeting of the PBR Task Force at the NAIC's fall national meeting focused on the debate over life insurer reserve relief effected through captive transactions and whether the current reserve relief achieved through such transactions should continue, or be subject to a moratorium, and whether such reserve relief should be granted once PBR is fully implemented.

A consensus appeared to be emerging among the PBR Task Force that insurer-owned captive reserve relief reinsurance transactions should not continue once PBR is implemented, noting that once PBR becomes effective the need for alternative reserve relief arrangements should largely be obviated. Complete agreement was not reached, however, on whether until then new life insurer-owned captive transactions should continue to be approved. Superintendent Torti of Rhode Island clarified that reserve relief granted for already approved life insurer-owned captive transactions would continue, while also expressing his view that he would not want any new business added to open-ended existing captive arrangements. The SEC staff's disclosure requirements regarding the risks to life insurers of the possible discontinuation of captive life reinsurance transactions is discussed in Section II.D.2 above.

The PBR Task Force was not able to reach a definitive agreement on these matters, which will no doubt continue to be hotly debated in 2014.

b) New York

The NYDFS released its own report on captives/SPVs entitled "Shining a Light on Shadow Insurance – A Little-Known Loophole That Puts Insurance Policyholders and Taxpayers at Greater Risk." In the report, the NYDFS expressed concerns about insurance companies' use of captives/SPVs in transactions that may "not actually transfer risk" off of the books of the ceding insurance company, potentially leaving insurance companies unable

to handle losses and "put[ting] the stability of the broader financial system at greater risk."

In early August 2013, the NYDFS released a draft Captives Reinsurance Schedule for inclusion in the New York Supplement to the Annual Statement for 2013 reporting. The final version of the Schedule has been incorporated in the 2013 Supplement to Life and Accident and Health Annual Statement, available on the NYDFS web site. All insurance company licensees, both domestic and foreign, as well as accredited reinsurers, are instructed to complete the Schedule. (Initial expectations were that the Schedule would apply only to domestic companies.) The information on captive reinsurance provided by the New York filer must include any captive arrangements within the holding company system, even if the New York licensee is not involved in such captive arrangements. (It should be noted, therefore, that the Captives Reinsurance Schedule to the New York Supplement is meant to capture, on an annual basis, information comparable to that which NYDFS requested in 2012 with its Section 308 request.)

c) Federal

On December 12, 2013, the FIO released its long-awaited report on how to modernize and improve U.S. insurance regulation. The report, several years in the making, reflects a thorough study of the topic and covers a wide range of issues. On the topic of captives and SPVs, the report concludes that states should develop and adopt uniform and robust standards for transparency, uniform capital requirements, nationally consistent standards for oversight that include public disclosure of the finances of captives, and nationally consistent standards for the oversight of captives.

3. NAIC Solvency Modernization Initiative

a) States Begin Adopting the ORSA Model Act

State legislatures began adopting the ORSA Model Act in 2013. The ORSA Model Act includes a provision setting an effective date of January 1, 2015, and will require U.S. insurers that exceed specified premium thresholds to maintain a risk management framework, regularly conduct an own risk and solvency assessment ("ORSA"), and document the results of the ORSA in an annual, confidential summary report (an "ORSA Summary Report"). The ORSA Model Act has been adopted in seven states (California, Iowa, Maine, New Hampshire, Pennsylvania, Rhode Island and Vermont). Implementing legislation was introduced or under consideration in Connecticut, Ohio, Texas and Wyoming. Additionally, legislation was introduced in Virginia and subsequently withdrawn at the request of the Virginia insurance regulator, who wanted to refine the legislation's language. Further, in January 2014, a number of additional states have begun to introduce implementing legislation as their 2014 legislative sessions commence. On January 8, 2014, New York published a proposed regulation that would introduce an ORSA requirement in New York; a summary of the proposed regulation is discussed in Section V.E.2 below.

b) State Adoption of Amended Holding Company Act Continues

During the 2013 legislative sessions, a number of states adopted legislation substantially incorporating the amendments to the Model Insurance Holding Company System Regulatory Act (the "Amended HCA") that were adopted by the NAIC in 2010. As of year-end 2013, 24 states have adopted such legislation, including New York (see discussion in Section V.E.1 below).[4]

The NAIC also made progress with regard to the Amended HCA, as it identified and adopted the "significant elements" that will be required for states to maintain NAIC accreditation, beginning on January 1, 2016. These significant elements include: (i) requiring that the ultimate controlling person of a regulated insurer file an annual enterprise risk report; (ii) authorizing regulator participation in supervisory colleges; (iii) authorizing greater access for regulators to enterprise risk information of insurer affiliates' books and records; (iv) requiring notice of divestiture of controlling interest in a domestic insurer; and (v) expanding

[4] California, Connecticut, Georgia, Idaho, Illinois, Indiana, Kansas, Kentucky, Louisiana, Maine, Maryland, Mississippi, Nebraska, Nevada, New Hampshire, New York, Oklahoma, Oregon, Pennsylvania, Rhode Island, Texas, Vermont, West Virginia and Wyoming.

requirements for notice of affiliate transactions (including reinsurance agreements, tax allocation agreements and modifications of existing agreements).

In response to federal and international expectations regarding group supervision and group solvency, at the NAIC's fall national meeting, the (E) Committee was charged with reviewing the Amended HCA and considering amendments to address issues that have arisen since its adoption by the NAIC, presumably referring to questions raised by the FIO report. Nonetheless, it is understood that this new charge is not intended to delay adoption of the Amended HCA by the various states or the accreditation process as it now stands.

c) Corporate Governance Initiatives

New Corporate Governance Model Takes Shape. Currently, state regulators receive most of their access to corporate governance-related information during the examination of insurers. Recognizing a gap in information between examination cycles, the NAIC spent 2013 continuing its efforts to develop a mechanism for annual filing of corporate governance information. Ultimately, these efforts led to the development of the Corporate Governance Annual Filing Model Act (the "Corporate Governance Model Act").

The Corporate Governance Model Act contains the procedural requirements for a new corporate governance filing, which will be completed in accordance with the NAIC Corporate Governance Annual Filing Guidance Manual (the "Corporate Governance Guidance Manual"). The filing will describe four areas relating to an insurer's corporate governance structure: (i) the corporate governance framework; (ii) board of directors' and committee policies and practices; (iii) management policies and practices; and (iv) management and oversight of critical risk areas. Insurers may select the entity in their corporate structure that would make the annual filing. Thus, the filing could be made by the ultimate controlling entity, an intermediate holding company or one or more individual insurers, depending on the corporate governance structure and procedures within an insurance holding company system. Although regulators and industry members differ on the propriety of using a guidance manual for the corporate governance annual filing, with industry members strongly opposing its use, the Corporate Governance (E) Working Group recently released both the Corporate Governance Model Act and Corporate Governance Guidance Manual for comment, with the comment period ending January 31, 2014. The Corporate Governance (E) Working Group aims for both the Corporate Governance Model Act and the Corporate Governance Guidance Manual to be ready for adoption by the NAIC in the first quarter of 2014.

Proposed Revisions to the Model Audit Rule. In recognition of international insurance governance standards, which generally require an insurer to maintain an internal audit function, the NAIC began the process of implementing such a requirement into its Model Audit Rule. The proposed revisions to the Model Audit Rule would require (a) insurers with annual direct written and unaffiliated premium of at least $500,000 and (b) insurers who are members of a group of insurers with more than $1,000,000 in annual direct written and unaffiliated premium, to maintain an internal audit function. Insurers or insurance groups for whom the internal audit function is not required would nonetheless be encouraged to conduct a self-review to determine whether an internal audit function is warranted. The internal audit function would provide an independent and objective review of an insurer's corporate governance, risk management and internal controls. In order to maintain the internal audit function's independence and objectivity and to enable it to provide reasonable assurance to the insurer's audit committee with respect to internal controls, the chief audit executive should report directly and without restriction to the board of directors, although dual-reporting relationships are permissible. Additionally, the audit committee would receive regular reports on the results of internal audits and any matters relating to the conduct of such audits. As with other recent model law activity at the NAIC, insurers who are part of an insurance holding company system may satisfy this new requirement at the level of individual entities or at the holding company level.

4. Reinsurance

a) Credit for Reinsurance Model Law and Regulations

As 2013 came to a close, the NAIC's amendments to its Credit for Reinsurance Model Law and Regulations (the "Amended Credit for Reinsurance Model Act"), which allow for reduced reinsurance collateral requirements for unauthorized reinsurers, had been adopted by 18 states.[5] The NAIC's Reinsurance (E) Task Force reported that insurers domiciled in these states represent approximately 53% of the primary insurance premium written in the United States. The NAIC reported that at year-end a further six states[6] were considering adopting the Amended Credit for Reinsurance Model Act.

Under the Amended Credit for Reinsurance Model Act, reinsurers domiciled in countries found by the NAIC to have strong systems of domestic insurance regulation (*i.e.*, "qualified jurisdictions") are eligible to apply for "certified reinsurer" status in states that have adopted the amendments. In addition, in order to qualify as a "certified reinsurer," an applicant must also meet certain criteria as to financial strength and reliability as provided in the Amended Credit for Reinsurance Model Act. Certified reinsurers would be permitted to post collateral at reduced levels, and U.S. ceding insurers would be permitted to take full financial statement credit for the reinsurance obligations of such certified reinsurers.

b) Qualified Jurisdictions

At the NAIC's fall national meeting in December 2013, it was announced that the NAIC had completed its expedited review of the international supervisory authorities of Bermuda (Bermuda Monetary Authority), Germany (German Federal Financial Supervisory Authority), Switzerland (Swiss Financial Market Supervisory Authority) and the United Kingdom (Prudential Regulation Authority of the Bank of England), and granted these four jurisdictions "Conditional Qualified Jurisdiction" status for one year. This "Conditional Qualified Jurisdiction" designation may be elevated to a final qualification for each jurisdiction following completion of the full evaluation procedure, which will be conducted for each of these jurisdictions in 2014. Ireland and France are next up for expedited review in 2014.

c) Certified Reinsurers

At the close of 2013, the NAIC's Reinsurance Financial Analysis Working Group (the "Reinsurance-FAWG") had reviewed and "passported" 21 reinsurers that had been approved by Connecticut, Florida and New York as "certified" and eligible for collateral reductions. Other states may now rely on this assessment without having to undertake their own review of these reinsurers. A further two reinsurers are in what has been characterized as the "second round" or "follow-up" stages of review, and one reinsurer is in the initial stage of review.

It was also reported that six reinsurers were not passported, either because the Reinsurance-FAWG disagreed with the approving state's determination or because the reinsurer voluntarily elected to not participate in the process. As a result, if one of those reinsurers should seek to be certified and eligible for collateral reductions in another state (in addition to the original approving state), the reinsurer will need to satisfy that other state's own independent review.

This "passported" status is only good for one year, so as a next step in 2014, the Reinsurance-FAWG will be working to develop a renewal process reflecting a review of the financial condition of the passported reinsurer.

C. Life Insurance Topics

1. Private Equity/Hedge Fund Investments in Life Insurers

Private equity and hedge funds have recently demonstrated increased interest in acquiring life insurance companies. Such buyers have focused on insurers whose principal business is annuities, which present investment risk. The bidders are often interested in applying their sophisticated

[5] Alabama, California, Connecticut, Delaware, Florida, Georgia, Iowa, Louisiana, New Hampshire, New Jersey, New York, Pennsylvania and Virginia have adopted both the Model Law and Model Regulations. Indiana, Maine, Maryland, Missouri and Rhode Island have adopted only the Model Law.

[6] Illinois, Massachusetts, New Mexico, Ohio, Texas and Vermont.

investment management expertise to the assets backing the insurance reserves for these annuities.

Recognizing this trend, insurance regulators have begun to re-examine the insurer acquisition approval standards applicable to private equity or hedge funds or other private investors. Regulatory activity by individual state regulators in this area is discussed in Section I.B above

The NAIC has also taken an interest in private equity funds that are buyers or reinsurers of life insurance companies. In May 2013, the FAWG issued a paper proposing the establishment of a new NAIC working group charged with creating best practices regarding private equity and hedge fund life insurance company acquisitions or reinsurance transactions. In response, the Financial Conditions (E) Committee established the Private Equity Issues (E) Working Group ("PE Working Group"). The first meeting of the PE Working Group was at the NAIC's fall national meeting, at which the group received a presentation from Athene/Apollo regarding its recent acquisition of Aviva's U.S. life and annuities business. The PE Working Group is chaired by Deputy Commissioner Doug Stolte of Virginia and the NYDFS is a member of the working group. The working group indicated that it plans to obtain input from the private equity/hedge fund industry before making any recommendations.

At the end of the NAIC's fall national meeting, the PE Working Group exposed the FAWG issues paper for comment from interested parties by January 30, 2014.

The life insurance industry should carefully monitor the development of potentially new regulations by the PE Working Group and states such as New York, since they may be applied on a broader basis than just those life insurers owned by private equity or hedge funds.

2. Principle-Based Reserving for Life Insurers

For over a decade, the NAIC has been working on developing a principle-based approach for life insurers' reserving methods, in which actuarial judgment and the risks faced by each life insurer would have greater weight on its reserves than the current formulaic approach. PBR is comprised of three principal components: (i) the Model Standard Valuation Law, which was revised by the NAIC in 2009; (ii) the Standard Nonforfeiture Law for Life Insurance, which was amended by the NAIC in August 2012; and (iii) a Valuation Manual, which was adopted by a supermajority of NAIC members in December 2012, although key states such as California and New York objected.

With the major components of PBR finally adopted by the NAIC, 2013 was targeted to be the year that states would begin enacting the amendments to have PBR in place. However, in September 2013, Superintendent Lawsky of New York issued a letter to his fellow insurance regulators again criticizing PBR. In the letter, Superintendent Lawsky states that, in its current form, PBR represents an "unwise move away from reserve requirements that are established by formulas and diligence policed by insurance regulators."

As of the end of 2013, the NAIC has reported that only eight states have adopted laws implementing PBR. Arizona, Indiana, Louisiana, Maine, New Hampshire, Rhode Island and Tennessee have adopted both the amended Standard Nonforfeiture Law for Life Insurance and the amended Standard Valuation Law; Texas has adopted only the Standard Nonforfeiture Law for Life Insurance. Since PBR will become effective only upon legislative adoption of the amended Model Standard Valuation Law by a supermajority of jurisdictions (42) representing at least 75% of the applicable U.S. premium, larger states like New York hold considerable influence over PBR implementation.

In 2013, the NAIC's PBR Task Force and related working groups focused on steps for implementing PBR, including the need for insurance regulators to have adequate resources and the debate over insurer reserve relief through insurer-owned captive transactions and the impact of PBR on such transactions.

As discussed in section V.B.2.a above, the NAIC also has focused on the relationship of the adoption of PBR to insurer-owned captive reserve relief reinsurance transactions. For a discussion of captive-related regulatory activity by the FIO, New York, and the NAIC, please see Section V.B.2 above.

3. Longevity Risks (Joint Forum)

In December 2013 the Joint Forum of the Basel Committee on Banking Supervision, the International Organization of Securities Commissions and the IAIS released its final report on longevity risk transfer transactions entitled "Longevity Risk Transfer Markets: Market Structure, Growth Drivers and Impediments, and Potential Risks" ("Joint Forum Report"). Longevity risk transfer transactions are those in which pension plans or schemes purchase coverage for the risk that pension beneficiaries will live longer than expected. The Joint Forum Report analyzes this emerging longevity risk transfer market and makes several observations and recommendations. In particular, with respect to those jurisdictions in which longevity risks may be assumed by non-insurance companies such as banks, the Joint Forum Report encourages policymakers and regulators to consider which sector is in the best position to bear and manage the risk, and which holders of the risk under their supervision have the appropriate knowledge, skills, expertise and information to manage it. The Joint Forum Report also encourages regulators to cooperate with respect to longevity risk transfer transactions both internationally and cross-sectorally in order to reduce possible regulatory arbitrage.

The NAIC is expected to take up this charge and focus more attention on longevity risk transfer transactions in 2014.

D. Property/Casualty Insurance Topics

1. TRIA Reauthorization Supported by State Insurance Regulators

Following the 9/11 terrorist attacks, the U.S. Congress enacted the Terrorism Risk Insurance Act ("TRIA") in order to provide a federal backstop for insured losses caused by terrorist acts. Following two previous extensions, TRIA is currently set to expire on December 31, 2014. During its summer national meeting in August 2013 in Indianapolis, the NAIC adopted a resolution expressing its support for reauthorization of TRIA. In the resolution, the NAIC noted that TRIA has enabled insurers to offer terrorism coverage and that its existence is required for the insurance marketplace to continue to insure against terrorist acts. Notwithstanding this public support by the NAIC, as of year-end Congress failed to reauthorize TRIA.

Congressional inaction in this regard has resulted in growing concern in the marketplace. It is expected that the property and casualty market will experience temporary disruptions with respect to policies that insure against terrorist acts and that provide coverage beyond December 31, 2013. For example, most banks require terrorism coverage in connection with loans given for large commercial projects. Thus, without a reauthorization of TRIA, banks might start, in the very near term, to start writing down loans that do not have terrorism coverage in place for the entire term of the loan. During its fall national meeting, members of the NAIC's Terrorism Insurance Implementation Working Group noted that states have already begun receiving conditional filings from insurers containing exclusions of terrorism coverage in anticipation of TRIA not being extended.

2. Lender-Placed Insurance

Creditor/lender-placed insurance ("LP Insurance"), which is insurance procured by a lender when its customer fails to carry or renew property hazard insurance on an asset in which the lender has a security interest, continued to garner the attention of state insurance regulators and consumer advocacy groups in 2013.

In 2013, the NYDFS announced its settlement with the country's largest providers of LP Insurance: Assurant, Inc.; QBE Insurance Corporation; Balboa Insurance Company; Meritplan Insurance Company; and American Modern Home Insurance Company. The settlement includes monetary penalties and the insurers' agreement to refund certain premiums to homeowners and to follow certain practices going forward, including a prohibition on issuing LP Insurance on mortgaged property that is serviced by an affiliated bank or servicer.

Following public hearings held during the NAIC's 2012 summer national meeting, in 2013 the NAIC's Property and Casualty Insurance Committee ("P&C Committee")

voted to approve revisiting the NAIC's Creditor-Placed Model Act to determine whether it: (i) currently contains sufficient consumer safeguards; (ii) should be classified as a guideline rather than a model law; and (iii) should be amended or repealed/archived. In carrying out this charge, the P&C Committee worked with the industry, interested parties and consumer advocacy groups to develop a data call to be conducted by NAIC members states. The data call is expected to be limited to the largest participants in the LP Insurance market. It remains to be seen whether the NAIC will amend its Creditor-Placed Model Act.

3. Mortgage Insurance

In 2013, the NAIC's Mortgage Guaranty Insurance (E) Working Group ("MGI WG") worked on updating the regulation of mortgage guaranty insurers ("MGI"). Mortgage insurance transfers a borrower's default risk from the lender to the mortgage insurer. The housing collapse of 2008 and ensuing wave of mortgage defaults resulted in substantial losses for private mortgage insurers. The NAIC formed the MGI WG in late 2012, and it then identified several issues facing the mortgage guaranty industry, including competitive pressures among mortgage insurers resulting in relaxed underwriting standards and generous dividend practices that failed to recognize actual profits of the insurers in the longer term. In mid-2013, the MGI WG published a "concept list" of twelve potential regulatory changes and thereafter drafted amendments to the NAIC Mortgage Guaranty Insurers Model Act (the "MGI Model"), which were exposed for comment on November 25, 2013 through February 15, 2014.

One high-priority issue for the MGI WG has been updating the current MGI Model method for setting the cap on an MGI's total liability, net of reinsurance, at a 25-to-1 ratio for such liability as against the company's capital, surplus and contingency reserves. Regulators and industry both support adding a levels-based approach to the regulatory evaluation of MGIs, like the action levels in RBC analysis. The proposed revisions to the MGI Model principally relate to: (i) capital and reserve standards, including increased minimum capital and surplus requirements, mortgage guaranty-specific risk-based capital standards, dividend restrictions and contingency and premium deficiency reserves; (ii) limitations on the geographic concentration of mortgage guaranty risk, including state-based limitations; (iii) restrictions on mortgage insurers' investments in notes secured by mortgages; (iv) prudent underwriting standards and formal underwriting guidelines to be approved by the insurer's board; (v) the establishment of formal, internal Mortgage Guaranty Quality Control Programs with respect to in-force business; (vi) prohibitions on reinsurance with bank captive reinsurers; and (vii) incorporation of an NAIC Mortgage Guaranty Insurance Standards Manual.

Industry representatives' comments to the proposed revisions reflected a desire for less prescriptive requirements. Furthermore, the FIO report was released after the proposed revisions were prepared, and it not only calls for "robust national solvency and business practice standards, with uniform implementation," but also recommends "federal oversight of federally developed standards applicable to mortgage insurance." Therefore, while the NAIC has proposed substantial revisions to the existing MGI Model, we expect continuing discussion and possible further changes.

E. New York Corner

1. Holding Company Act/Regulations

In 2013, New York incorporated into its insurance holding company laws and regulations many of the amendments made to the NAIC Model Insurance Holding Company System Regulatory Act and Regulation in 2010 (the "Amended HCA"). In the spring of 2013, the NYDFS adopted the Third Amendment to Insurance Regulation 52 and, in July 2013, the legislature enacted a bill amending the insurance holding company law. The amended law and regulation are referred to herein as the NY Holdco Provisions.

Under the NY Holdco Provisions, "a holding company that directly or indirectly controls an insurer" shall file an Enterprise Risk Management ("ERM") Report annually by April 30. In language conforming to the Amended HCA, the NY Holdco Provisions state that the ERM Report should "identify the material risks within the holding company

system that could pose enterprise risk to the insurer." The ERM Report applies to both domestic and foreign insurers licensed in New York.

Some changes to the NY Holdco Provisions are not entirely consistent with the Amended HCA. Under the NY Holdco Provisions, the non-disapproval filing requirement of Section 1505(d) now provides that reinsurance agreements must be filed with the NYDFS 45 days prior to effectiveness (as opposed to the 30 days required for other affiliate agreements), and some changes have also been made to materiality thresholds. The NY Holdco Provisions authorize the NYDFS to participate in supervisory colleges and to pay related expenses. It also incorporates the requirement that a holding company divesting its controlling interest in a New York domestic insurer must file 30 days' prior notice of its cessation of control. Changes have also been made to New York's requirements for the annual registration statement, including that a statement must be submitted regarding the directors' supervision of corporate governance and internal controls.

Because New York law exempts certain insurers (insurance company subsidiaries of New York authorized insurers) from its holding company provisions, in order to comply with the NAIC holding company accreditation provisions, certain changes have also been made to other articles of the New York Insurance Law ("NYIL"): Article 16 regarding such property/casualty insurers ("Article 16 Insurers"); and Article 17 regarding such life insurers ("Article 17 Insurers"). The inclusion of Article 16 and 17 Insurers will result in the application of some of the requirements of the Amended HCA and general holding company regulation to these insurance companies for the first time, as well as explicitly applying the requirement to file an ERM Report and the authorization of New York's participation in supervisory colleges to Article 16 and 17 Insurers. These requirements are not completely uniform.

Certain provisions of the Holdco Provisions may need amendment to harmonize with each other or to correct mistakes, and the NYDFS has recently exposed for public comment a proposed regulation regarding the ERM Report, as discussed in Section V.E.2 below.

2. Proposed Regulations on ERM and ORSA

As expected, on January 8, 2014, the NYDFS released a proposed regulation ("Proposed Regulation 203") that will implement both new reporting requirements regarding ERM and ORSA for certain New York insurers.

a) New York's Proposed ERM Report

The Amended HCA, discussed in Sections V.B.3.b and V.E.1 above, implemented a new required filing to be completed by a controlled insurer's ultimate controlling person; the filing will describe material risks to the holding company system that could pose enterprise risk to controlled insurers. The NYIL requires that an ERM function be adopted by, and an enterprise risk report be filed by, a New York insurer's holding company, the insurer itself, or the insurer's parent corporation; this requirement varies based on whether the requirement is imposed by New York's holding company laws or Article 16 or Article 17 of the NYIL. In addition, Proposed Regulation 203 requires that an enterprise risk filing be submitted by certain New York-domiciled insurers and executed by their chief risk officer or another executive responsible for overseeing the entity's ERM function. If an entity has no enterprise risk-related information to file, it must file a statement affirming that, to its knowledge and belief, no enterprise risk has been identified.

The NYIL already requires insurer members of insurance holding company systems and Article 16 and 17 Insurers to maintain an ERM function and file an enterprise risk report. Proposed Regulation 203 provides additional detail regarding the minimum requirements for an ERM function. Additionally, Proposed Regulation 203 will also require any other domestic insurer not otherwise subject to registration to maintain an ERM function. Furthermore, if such other domestic insurer has annual direct written premium and unaffiliated assumed premium of at least $500 million per year, it will also be required to file an enterprise risk report. New York's ERM filing will be submitted by April 30 of each year.

b) New York's ORSA Requirement

Proposed Regulation 203 generally corresponds to the requirements of the ORSA Model Act, discussed in Section V.B.3.a above. Proposed Regulation 203 will require domestic insurers exceeding certain premium thresholds to regularly conduct an ORSA and file an ORSA Summary Report with the NYDFS each December 1, beginning in 2015. In contrast to the ORSA Model Act, however, Proposed Regulation 203 does not include broad confidentiality protections for the ORSA Summary Report. Instead, the ORSA Summary Report will be protected by already-existing confidentiality provisions, including those in New York's Public Officers Law and Articles 15 and 17 of the NYIL. Additionally, Proposed Regulation 203 does not incorporate the sanctions provisions included in the ORSA Model Act.

F. International Insurance Issues

1. Group Supervision

a) ComFrame and Group Capital Standards

Currently, the IAIS is working on two projects relating to group supervision: (i) the development of a Common Framework for the Supervision of Internationally Active Insurance Groups ("ComFrame"), which has been under development since 2010; and (ii) the development of group-wide capital standards applicable to both G-SIIs and Internationally Active Insurance Groups ("IAIGs").

ComFrame. In July 2010, the IAIS, supported by the G20 and the Financial Stability Board ("FSB"), initiated a three-year process to build the Common Framework for the Supervision of IAIGs, known as ComFrame.

ComFrame is intended to provide a framework of basic standards for IAIGs and a process for supervisors around the world to cooperate in the supervision of IAIGs. The main goals of ComFrame are to develop methods of operating group-wide supervision of IAIGs, establish a comprehensive framework for international regulators, address group-wide activities and risks, and foster a global convergence. Both the requirements and the process of ComFrame touch upon risk management, governance, structure, strategy and financial conditions. It is expected that the ComFrame architecture would regulate anywhere from 50 to 100 IAIGs.

ComFrame continued to be developed in the latter half of 2013. On October 17, 2013, the IAIS published for consultation a third draft of ComFrame. Comments on the draft were open until December 16, 2013. The IAIS intends to group comments into key themes and those themes will then be discussed in sub-committees in early 2014. A revised draft of ComFrame will be developed in March 2014 before field testing of ComFrame begins. Acknowledging that ComFrame will evolve during field testing, further consultations will take place prior to adoption in 2018 and implementation in 2019.

G-SIFIs. Following the 2007-2008 financial crisis, the G20 and FSB identified the need for more effective supervision of global systemically important financial institutions ("G-SIFIs"). The FSB is coordinating an initiative to reduce the moral hazard posed by G-SIFIs and in 2010 developed a general framework, recommendation and timeline for identifying G-SIFIs and determining added loss absorbency measures necessary for risk reduction ("FSB Framework"). While initial G-SIFI-related work focused on the banking sector, the FSB Framework reflected an intent to extend the G-SIFI framework to cover a wider group of institutions, including insurers. Accordingly, the FSB and IAIS have been working to identify insurers whose distress or disorderly failure would cause significant disruption to the global financial system, and a set of policy measures that should be applied to insurers determined to be G-SIIs.

As referenced in Section V.A above, the FSB published a list of the first nine G-SIIs on July 19, 2013. On the same day, the IAIS published an initial assessment methodology for determining G-SIIs and a framework of policy measures for G-SIIs. The policy measures fall into four broad categories:

- Enhanced supervision of G-SIIs by supervisors;
- Effective resolution of G-SIIs that could be significant or critical if they were to fail;
- Loss absorption and the Basic Capital Requirements ("BCR"); and
- Higher Loss Absorption ("HLA") capacity.

The last two categories relate to IAIS's project to develop group-wide capital standards. The IAIS proposes that G-SIIs should face a higher loss absorption capacity, so as to reflect the greater risks that the failure of G-SIIs pose to the global financial system. The IAIS proposes that a cascading approach to achieve HLA capacity should apply, taking into account the extent to which the G-SII has demonstrated effective separation between traditional insurance and non-traditional or non-insurance activities such as financial guaranty insurance, capital markets activities such as credit default swaps, transactions for non-hedging purposes, derivatives trading or leveraging assets.

The development of the BCR is seen as the first of three steps toward developing group-wide global capital standards. The BCR will apply to all group activities, including those of non-insurance subsidiaries of G-SIIs. On December 16, 2013, the IAIS published a consultation paper on proposed options for the development of the BCR. The consultation period will end on February 3, 2014 and field testing of the BCR will commence in March 2014. It is proposed that the G20 will endorse the BCR proposal at its meeting in November 2014.

Following approval of the BCR, the second step will be the development of HLA requirements that build upon the BCR and address additional capital requirements for G-SIIs reflecting their systemic importance in the international financial system. This step is due to be completed by the end of 2015. The final step is to develop a risk-based group-wide global insurance capital standard, which is discussed in the next section.

The Global Insurance Capital Standard. On October 9, 2013, the IAIS published a press release and fact sheet announcing its plan to develop a risk-based group-wide global insurance capital standard ("ICS") by 2016. The IAIS will include the ICS within ComFrame, which itself always included a capital component within its solvency assessment methodology. The IAIS press release indicates that the ComFrame component, which is currently under consultation (as described above), will be used as a starting point for development of the ICS. The IAIS also recognizes that the development and testing of the BCR and HLA will inform development of the ICS. The IAIS plans to test and refine the ICS for two years prior to full implementation in 2019, when it will be implemented alongside ComFrame.

b) The Role of Supervisory Colleges

As discussed above, international insurance regulators continue to formalize the processes for group-level supervision. Domestic support for group-wide supervision was echoed in the FIO report, which noted that "the state of group-wide supervision in the United States has drawn international attention." Although the U.S. regulatory system allows insurance regulators to participate in supervisory colleges, FIO warned that supervisory colleges "are necessary but not sufficient, and do not completely substitute for a consolidated regulator," concluding that "given concerns about the adequacy of solo entity supervision for larger groups ... consolidated supervision for large, internationally-active U.S.-based insurance firms will require continued focus and national attention."

In contrast to the FIO, the NAIC would prefer to delay the implementation of ComFrame and instead allow international sharing of information to be accomplished organically through supervisory colleges. Under this arrangement, supervisory colleges could tailor group oversight for a specific group rather than be forced to follow a prescriptive ComFrame approach. In defense of the state-based system of regulation, the NAIC stated that "[i]nsurance group supervision in the U.S. is a multi-jurisdictional approach that leverages a group-wide perspective on risk with legal entity level application of regulation. Under such an approach, a single all-powerful group regulator is neither advantageous nor necessary." The NAIC has consistently resisted statements from abroad and from within the United States that the state-based system of insurance regulation is not effective. Nonetheless, the NAIC is reviewing the Amended HCA in order to determine whether further group supervision requirements are needed.

2. Solvency II

Solvency II continues to be a major regulatory issue in Europe. The issue has significance beyond Europe for a number of reasons. First, Solvency II affects international groups and the calculation of their group solvency, and therefore affects the assessment of groups that have insurance companies within and outside of the European Union (the "EU"). Second, it affects reinsurers outside of the EU who wish to reinsure European insurance companies. Third, Solvency II has been held up as a new gold standard to which international insurance regulation should aspire. However, the credibility of the latter point has undoubtedly suffered, given the continued delay over the implementation of Solvency II.

Developments in the fourth quarter of 2013 indicate that consensus is being reached at a legislative level on some of the more contentious outstanding issues around the Solvency II regime and that a January 2016 implementation date may be achieved.

a) Key November 2013 Solvency II deal

The original Solvency II Directive was adopted in 2009, with the intention of harmonizing the way insurers allocate capital against risk. However, the full implementation of Solvency II depends on the adoption of the so-called Omnibus II Directive, the purpose of which is to: (i) provide for transitional arrangements for the introduction of the new regime, which had not been adequately dealt with under the original Solvency II Directive; and (ii) facilitate the adoption of subordinate rules that flesh out the higher principles set out in the Solvency II Directive.

In the course of trilogue negotiations among the European Parliament, the European Commission, and the Council of the EU, considerable amendments to the drafting of the Omnibus II Directive were made, leading to numerous delays in finalizing an agreed text. During these negotiations, participants have taken the opportunity to revisit some of the issues that were causing concern in the run-up to the adoption of Solvency II. Of particular concern were two issues: the valuation of so-called long term guarantee ("LTG") products, *i.e.*, life insurance products that are long term, such as annuities, where the insurer has made promises to make certain payment obligations in the future; and the assessment of "equivalency" to Solvency II of regulatory regimes outside of the EU and what transitional arrangements may be made for countries that are not deemed equivalent.

On November 13, 2013, the trilogue negotiations among the European Commission, the European Parliament and the Council of the EU reached a provisional agreement (the "November Agreement") on key elements of Omnibus II. While the revised Omnibus II text has not yet been publicly released, press releases and public statements made by the negotiating parties since the November Agreement provide insight into the issues that have now been agreed. These include agreement with respect to the LTG issue and transitional arrangements for the purposes of equivalency.

The LTG Issue. Life insurers have been concerned that Solvency II could cause long-term guarantee products to be priced out of the market; it could also discourage insurers from investing long term. At the end of 2011, the European insurance industry managed assets worth €7,740 billion, which is about 50% of European GDP. Insurers are major investors in long-term projects and such participation is important not only as providers of protection to policy holders, but also as investors and promoters of economic activity in the real economy. Accordingly, life insurers have advocated that a reduction in long-term investment by insurers could significantly affect the real economy.

One of the key principles of Solvency II is that assets and liabilities should be valued on a market-consistent basis and solvency capital will be calculated by reference to such valuations. Market valuations can cause an increase in volatility and in extreme cases not reflect economic reality. If the present value of future liabilities is out of step with economic reality, then insurers might be required to hold too much capital (or conversely not enough capital). Although this issue applies to all insurers, it particularly concerns life insurers, whose business is to provide protection many years into the future.

The Presidency of the Council of the EU released a press statement on November 14, 2013, shortly after the November Agreement was reached, stating that the agreed new rules contain LTG measures "which adjust current Solvency II framework to cope with 'artificial' volatility and [a] low interest rate environment." Pending release of the Omnibus II text, the hope among insurers is that the revised approach will better reflect the economic reality and will also smooth the transition from the current Solvency I regime.

Equivalence. Equivalence refers to the concept whereby the European Commission assesses, under Solvency II, whether the insurance regulatory regime of a non-EU country is equivalent to Solvency II for three purposes: (i) reinsurance; (ii) group solvency; and (iii) group supervision. The equivalence assessments could affect reinsurance collateral requirements for non-EU reinsurers that reinsure EU cedants, as well as group capital requirements and other compliance requirements generally for non-EU groups with EU subsidiaries and non-EU subsidiaries within EU groups. A finding of non-equivalence could affect the way international groups choose to organize themselves, as well as affect the way international reinsurers consider capital requirements and how they provide security to their EU cedants. A number of countries are in the first "wave" of assessment for equivalence but some others, including the United States and Canada, have chosen not to engage in the formal equivalence assessment process.

The November Agreement offers a solution for the equivalence issue for countries outside of the formal assessment process. It is understood that the revised draft Omnibus II text includes a set of criteria by which the European Commission can unilaterally determine whether the capital adequacy regime of a country is sufficiently equivalent to Solvency II. If it is, the jurisdiction will be granted provisional equivalence, thereby exempting multinational groups from having to operate in accordance with both local and European rules. A country will maintain provisional equivalence status for ten years and this may be extended an unlimited number of times for additional ten year periods. Therefore, even if a regulatory regime fails to achieve equivalence under the formal process, it may still be deemed equivalent for periods of ten years under these transitional provisions.

Other Key Points. In addition to the agreement on the LTG and equivalence issues, it is understood that the revised Omnibus II text will extend the transitional period for full implementation of the Solvency II regime so insurers would now have 16 years to move their existing life insurance book of business to the new regime. Also, agreement has been reached on providing the European Insurance and Occupational Pensions Authority ("EIOPA") with powers to propose rules and issue binding guidance to ensure coherence of national supervision among supervisors of EU member states and to contribute to a single EU rule book on insurance supervision.

b) Next steps

Following the November Agreement, the second "Solvency II Quick Fix Directive" was adopted by the European Parliament and the Council of the EU at first reading on November 21, 2013 and December 5, 2013, respectively. The Second Quick Fix Directive formally extends to January 1, 2016, the deadline for the application of the Solvency II Directive. Despite delays in the past, this deadline is now viewed by regulators as a firm date.

In the context of the drawn-out negotiations and repeated postponements that have affected Omnibus II and Solvency II, the November Agreement is a significant step forward. While the LTG issue and equivalency continue to be a focus of Solvency II discussions, the November Agreement appears to soften the capital requirements for many long-term insurance products and offers a resolution to countries including the U.S. that are not formally assessed as Solvency II-equivalent. The Omnibus II text, once released, will now be subject to a final approval from the European Council, and a vote by the European Parliament that will take place during its March 10-13, 2014 plenary session.

3. The New U.K. Financial Regulatory Structure

Since the Financial Services and Markets Act 2000 ("FSMA") came into force in 2001, the Financial Services Authority ("FSA") had been responsible for both prudential and conduct regulation for all types of financial firms. It was also responsible for the market abuse regime and for the rules relating to public listing of securities. The Bank of England ("BOE") and HM Treasury were the other two bodies making up what was known as the "tripartite system" of U.K. financial services regulation. The BOE had responsibility for payment systems and for overall financial stability, and HM Treasury was responsible for legislation and the overall regulatory framework.

In response to the regulatory weaknesses exposed by the 2007-2008 financial crisis, the U.K. Government passed the Financial Services Act 2012 ("FS Act"). The FS Act came into effect on April 1, 2013, radically overhauling the U.K.'s financial regulatory structure. The FS Act abolished the FSA and launched a new regulatory architecture consisting of the following three bodies:

- *Prudential Regulation Authority ("PRA")*. The PRA is responsible for micro-prudential regulation. It is a subsidiary of the Bank of England ("BOE") and is responsible for the authorisation, regulation and day-to-day supervision of all firms that are subject to significant prudential regulation, including banks, investment banks, building societies and insurance companies. It is accountable to the BOE, HM Treasury, the U.K. Parliament and the National Audit Office.

- *Financial Conduct Authority ("FCA")*. The FCA regulates the conduct of all firms, including firms authorised and subject to prudential supervision by the PRA, in their dealings with retail consumers and on the wholesale financial markets. It is also the prudential regulator for firms that are not regulated by the PRA. The FCA has also taken over the FSA's role relating to LIBOR, including the conduct of a number of ongoing enforcement investigations, and responsibility for the new regime for regulation of LIBOR introduced by the FS Act. Responsibility for the regulation of consumer credit is also due to be transferred from the U.K. Office of Fair Trading to the FCA effective April 1, 2014.

- *Financial Policy Committee ("FPC")*. The FPC is a committee of the Court of Directors of the BOE, responsible for considering macro issues affecting economic and financial stability and for responding to any threats that it identifies. The aim of the body is to address macro-economic weakness, by being the body responsible for maintaining financial stability. It is accountable to the BOE Court of Directors, the U.K. Parliament and HM Treasury. It has powers to direct the PRA and FCA to take certain courses of action to respond to systemic threats to the financial system.

The majority of the FSA's functions were transferred to the PRA and the FCA, although its responsibilities for systemically important infrastructure (*i.e.*, settlement systems and recognized clearing houses) have been transferred to the BOE.

a) FCA, PRA and BOE Powers Over Unregulated Holding Companies

An important new element of regulation introduced by the FS Act that is of interest to insurance groups is that it has created new powers for the FCA, PRA and BOE to impose requirements on U.K. parents of certain regulated firms. The purpose of these powers is to ensure that the regulatory bodies are not prevented from taking appropriate actions regarding a regulated firm due to the legal structure of the regulated firm's corporate group. The powers allow the regulators to: (i) direct "qualifying parent undertakings," as defined in the FSMA, as amended by the FS Act, to comply with specific requirements; (ii) take enforcement action against qualifying parent undertakings if those directions are breached; and (iii) gather information from qualifying parent undertakings. For example, if an authorised firm is in crisis, the new powers may allow a regulator to direct a parent company to provide that firm with capital or liquidity necessary to improve the position of the firm.

How the FCA, PRA and BOE will exercise these powers over unregulated holding companies is currently uncertain. The

FCA, PRA and HM Treasury have indicated that they will be used rarely and only where the regulatory tools available to a regulator are ineffective. Under the FSMA, as amended by the FS Act, the key definition of what is a "qualifying parent undertaking," which determines which entities are subject to these powers, is an entity that satisfies the following conditions:

- The entity must be a parent of a qualifying "authorised person" (*i.e.*, an entity regulated by the FCA and/or the PRA) or of a U.K. recognised investment exchange or of a U.K. recognised clearing house.

- The entity could be any direct or indirect parent of the qualifying authorised person, including an intermediate parent company that is not at the head of the ownership chain.

- The entity must be a body corporate that is incorporated in any part of the U.K. or has a place of business in the U.K. (which means that the qualifying parent undertaking could be a company incorporated anywhere in the world), and it must not itself be an authorised person, a recognised investment exchange or recognised clearing house.

- The entity must be a "financial institution." This term is not defined in the FSMA, the FS Act or subordinate legislation. However, in an October 2012 consultation paper, HM Treasury suggested that, for a parent undertaking to be a financial institution, its main business would need to relate to financial services.

How these new regulatory powers are utilized by the regulators going forward will be something to watch in 2014. Undoubtedly, insurance groups will want to take the scope of these new rules into account when considering where to locate their parent companies.

VI. U.K./EU Tax Developments Affecting Insurance Companies

A. Solvency II-Compliant Insurance Hybrid Debt - U.K. Tax Treatment

1. Introduction

In 2013, investors demonstrated an appetite for insurance hybrid debt. However, some of the features likely to be required of Solvency II-compliant instruments make the tax treatment uncertain or unattractive under general U.K. tax law.

In particular, while issuers of innovative Tier 1 and Tier 2 debt instruments under the existing regulatory regime generally enjoy tax deductions for any coupons paid to investors, instruments reflecting the loss absorbency requirements in accordance with Solvency II may not be tax deductible under current U.K. rules.

2. Solvency II Own Funds Classification

Article 93 of the Solvency II Directive classifies "own funds" (*i.e.*, capital) into three tiers reflecting differences in their quality, based on the extent to which they possess the following loss absorption characteristics:

- The item is available, or can be called up on demand, to fully absorb losses on a going-concern basis, as well as in the case of winding-up ("permanent availability"); and
- In the case of winding-up, the total amount of the item is available to absorb losses and the repayment of the item is refused to its holder until all other obligations, including insurance and reinsurance obligations toward policy holders and beneficiaries of insurance and reinsurance contracts, have been met ("subordination").

The Solvency II Directive sets limits on the proportion of each tier that can be treated as eligible to cover the Solvency Capital Requirement ("SCR") and the Minimum Capital Requirement ("MCR"). These limits require a minimum proportion of eligible own funds to be Tier 1 quality, and permit a maximum proportion to be Tier 3 quality.

Under Article 94 of the Solvency II Directive, capital instruments only qualify as Tier 1 own funds if they substantially possess the characteristics of both permanent availability and subordination. Tier 1 own funds is the highest-quality form of capital, as it allows insurers to absorb losses on a "going concern" basis — in other words, without prompting the winding-up or legal reorganization of the insurer and the consequent disruption and loss of value.

Capital instruments only qualify as Tier 2 own funds if they substantially possess the characteristic of subordination. If the insurer fails, such "gone concern" capital is available to meet liabilities owed to creditors and can also be valuable if an insurance business is being transferred out of an insurer that has entered, or is about to enter, an insolvency proceeding.

When assessing the extent to which an own funds item possesses the characteristics of permanent availability and/or subordination, a firm must consider:

- The duration of the item, in particular whether the item is dated or not and, where it is dated, the relative duration compared with the duration of the firm's insurance and reinsurance obligations;
- Whether the item is free from requirements or incentives to redeem the nominal sum;
- Whether the item is free from mandatory fixed charges; and
- Whether the item is clear of encumbrances.

3. Eligibility Requirements for Hybrid Capital

On this basis, eligibility requirements are being developed for Tier 1 and Tier 2 debt.

Some of the possible features of eligible hybrid debt capital, designed to deliver loss absorption, give rise to U.K. tax problems. These features may include:

- the (re)insurer must have full flexibility over the distributions, meaning that interest may only be paid out of retained earnings, and must be cancellable at the discretion of the issuer on a non-cumulative basis, and non-payment must not constitute an event of default;
- interest payments are mandatorily cancelled (or deferred) during any period of non-compliance with the SCR;
- redemption is mandatorily suspended during any period of non-compliance with the SCR; and
- the right to repayment of the principal and payment of interest, including on a winding-up, must automatically convert to equity or be written down (or be subject to an equivalent mechanism) on the occurrence of a specified trigger event (constituting significant non-compliance with the SCR).

4. U.K. Tax Implications of Certain Loss Absorbency Features

Any "results dependent" aspect of the interest obligation raises various potential U.K. tax problems:

- If interest payments are deemed to be "results dependent," the interest is effectively re-characterized as a dividend and is, therefore, not deductible in computing the issuer's profits for corporation tax purposes, except to the extent that such interest is paid to another company which is subject to U.K. corporation tax. In the past, under the existing solvency regime, it was sufficient for interest payments simply to be deferred, which Her Majesty's Revenue and Customs ("HMRC") accepts does not trigger the "results dependent" rule. However, full discretion over the payment of interest and the cancellation of the obligation to pay interest clearly means that "the consideration given by the company for the use of the principal secured depends (to any extent) on the results of the company's business or any part of the company's business" (Section 1015(4) Corporation Tax Act 2010 ("CTA 2010")). (HMRC has also expressed the view, which is open to technical challenge, that any risk of write-down of the principal makes the interest "results dependent.") In other words, without an amendment to the U.K. tax legislation, it will no longer be possible to issue hybrid capital that is tax deductible for U.K. purposes, but nevertheless qualifies as Tier 1 capital.
- The issuer of the security is de-grouped, and therefore certain group tax relief is not available. Group relationships for certain U.K. tax purposes (including group consolidation of tax profits and losses and tax neutrality for certain intra-group transactions) are determined by reference to the interests of "equity holders." As defined in the relevant tax law, "equity holders" include lenders of loans other than "normal commercial loans," which are defined to exclude loans entitling the creditor to "any amount by way of interest that depends to any extent on the results of the relevant company's business or on the results of any part of that business" (Section 162(4) CTA 2010). So, the issuance of Tier 1 hybrid capital by a subsidiary would forfeit the benefit of certain group tax relief.
- Sales of the security do not qualify for the exemption from stamp taxes for "loan capital." Stamp taxes at 0.5% of the consideration are, in principle, levied on the purchase of securities, subject to an exemption that is available for any loan capital, unless at the time of the transfer or any earlier time it carries "a right to interest the amount of which falls or has fallen to be determined to any extent by reference to the results of, or of any part of, a business" (Section 79(6)(b) Finance Act 1986). Accordingly, securities would be less attractive to potential investors because of the stamp taxes levied on transactions in the securities.

The possibility that the principal of a hybrid security may convert to equity or be written down on the occurrence of a certain trigger event potentially gives rise to volatility in the accounting valuation of the instrument, which in

turn affects the computation of taxable profits under the loan relationships and derivatives tax regimes (Sections 313, 415, 416 and 585 of the Corporation Tax Act 2009 ("CTA 2009")). In addition, under the loan relationships tax regime (Part 5 CTA 2009), any actual write-down of principal would give rise to a deemed taxable profit of the issuer.

The "perpetual" nature of debt may cause U.K. tax problems. HMRC currently accepts that undated debt that is only repayable on a winding-up (so-called contingent perpetual debt) is still a "money debt" under current U.K. tax law, so that the coupon is capable of constituting tax-deductible interest (subject to the results dependency point); however, a recent consultation paper suggests that HMRC is minded to change the general rule in the future.

5. Banking Industry – Taxation of Regulatory Capital Securities Regulations 2013

Parallel issues have already been addressed in the context of banks and the classification of capital under the EU legislative package known as Capital Requirements Directive IV ("CRD IV"), which largely came into effect on January 1, 2014.

New U.K. tax regulations, the Taxation of Regulatory Capital Securities Regulations 2013 (S.I. 2013/3209), were made on December 18, 2013 and became effective on January 1, 2014. They apply to "regulatory capital securities," meaning a security that qualifies as, and forms a component of, Additional Tier 1 capital or Tier 2 capital for a bank. The regulations address the tax issues described above by:

- Confirming that a regulatory capital security represents a loan relationship but excluding any tax charge in respect of a contingent conversion or write-down or on an actual write-down;
- Disapplying the "results dependent" rule and confirming that the coupon on a regulatory capital security is characterised as interest and not a distribution for U.K. tax purposes;
- Treating a regulatory capital security as a "normal commercial loan" for the purposes of the rules determining tax group relationships; and
- Conferring an exemption from all stamp taxes on a transfer of a regulatory capital security.

In addition, interest on a regulatory capital security would in principle be subject to deduction of basic rate income tax (20%) at source. In practice, such a security would typically be listed on a "recognised stock exchange," so as to constitute a "quoted Eurobond," the interest on which is exempt from U.K. withholding tax. However, the regulations helpfully confer a general exemption from withholding tax on regulatory capital securities, whether or not the security is listed.

All the tax reliefs provided by the regulations are subject to an anti-avoidance provision. Relief is denied if there are arrangements of which the main purpose, or one of the main purposes, is to obtain a U.K. tax advantage for any person as result of the application of the regulations in respect of that security.

6. HMRC Consultation with the U.K. Insurance Industry

More attention is being paid to the corresponding tax issues facing insurers, now that there is agreement to implement Solvency II effective January 1, 2016, coupled with the announcement by the PRA in April 2013, in a paper entitled *The Prudential Regulation Authority's Approach to Insurance Supervision*, that, pending full implementation of Solvency II, insurers should "anticipate the enhanced quality of capital that will be needed when issuing or amending capital instruments." If insurers follow the PRA's guidance and construct the terms of their hybrid instruments to reflect the currently anticipated Solvency II requirements, it is already impossible to issue Tier 1 securities that carry deductible interest.

HMRC is working with the insurance industry on this issue, so as to create certainty of tax treatment and support the ability of the industry to raise capital. The U.K. Government announced in the Chancellor's Autumn Statement, on

December 5, 2013, that the Finance Act 2014 will include legislation to allow regulations to be made to set out the tax treatment of Solvency II-compliant capital instruments in advance of agreement to Solvency II.

It is hoped that this will result in similar tax relief being provided to insurers as have been provided to the banking industry in response to CRD IV.

B. EU Financial Transaction Tax

On February 14, 2013, the EU Commission published a proposal for a directive (COM/2013/71) for a common financial transaction tax ("FTT") in EU Member States that choose to participate (the "FTT Zone").

To date, 11 countries (but excluding, in particular, the U.K., Ireland and Luxembourg) have indicated an intention to participate: France; Germany; Italy; Spain; Austria; Belgium; Estonia; Greece; Portugal; Slovakia; and Slovenia.

The proposed FTT has wide scope and would apply to financial transactions where at least one party to the transaction is established in the FTT Zone and either that party or another party is a financial institution established in the FTT Zone:

- "Financial institution" covers a wide range of entities, including insurance and re-insurance companies as well as banks, pension funds and securitization SPVs. It is irrelevant whether the financial institution is acting as principal or agent;
- "Financial transaction" includes the sale and purchase of a financial instrument, a transfer of risk associated with a financial instrument and the conclusion or modification of a derivative. Primary market transactions are excluded, such as the issuance of shares or bonds; and transactions not involving a security, such as entry into an insurance contract or the making of a syndicated loan, are outside the scope. However, the provision of collateral in the form of securities, the transfer of legal title to securities to a custodian, the redemption of shares, repos and stocklending are apparently included; and the effects cascade where a single commercial transaction involves multiple legs — for example, via brokers and members of a clearing system;
- The proposed minimum rate of tax is 0.1% of the consideration (or market value, if higher), or 0.01% of the notional amount in relation to a derivative.

The draft FTT regime published in 2013 contained an important widening of the geographical reach of the proposed tax, with regard to the meaning of the term "established" in the FTT Zone. This definition includes, as might be expected, entities which are actually regulated or formed in a participating Member State or which are carrying on business through a branch in a participating Member State. So, for example, if the French branch of an Irish insurer sells Japanese corporate bonds, the transaction is within the scope of FTT.

However, a financial institution which has no business presence in the FTT Zone at all, but which is party to a transaction where the counterparty is "established" (by reason of authorisation, formation or branch business) in the FTT Zone, or where the underlying financial instrument was issued in the FTT Zone, is deemed to be "established" in the FTT Zone. Accordingly, if a U.K. insurer sells shares in a Dutch company to an Italian buyer, the U.K. insurer will be deemed to be established in Italy and, therefore, within the FTT Zone. Even more controversially, if a Bermudian insurer transfers shares in a German company by way of collateral to a U.S. bank, both the Bermudian insurer and the U.S. bank will be deemed to be established in Germany, and therefore within the FTT Zone.

The breadth of scope is intended to preempt efforts by financial institutions that wish to service the FTT Zone, to avoid FTT by relocating transactions outside the FTT Zone. However, it raises difficult enforcement questions.

The broad theoretical scope is tempered by a rule that, where the person liable for payment of FTT proves that no link exists between the economic substance of the transaction and the FTT Zone, a party will not be deemed to be established in the FTT Zone. However, it is very unclear

at the moment how generously this exception would be interpreted nor what supporting evidence would be needed.

As currently formulated, the introduction of an FTT could impose material costs on both life and general insurers.

In addition, the terms of financial transactions will need to allocate responsibility for the tax contractually, given that the legislation is likely to impose primary liability on any financial institution which is party to the transaction (on both the buy and sell side) and, in the event of default, joint and several secondary liability on all participants.

It is currently unclear whether and, if so, in what form, an FTT may be introduced. This issue is still subject to negotiation between those Member States which choose to participate. Moreover, it is the subject of criticism and legal challenge, principally by reason of the proposed "extra-territorial" reach.

Nevertheless, the proposal was included in the EU Commission's work programme for 2014 published on October 22, 2013 and is identified as one of the priority items for attention over the next few months. So, political momentum still exists for the introduction of an FTT in the EU in some form in the near future.

Willkie's Corporate Insurance and Regulatory Group

Willkie's Corporate Insurance and Regulatory Group is one of the preeminent practices in the industry, representing insurance companies, investment banks, sponsors and other financial institutions in M&A, capital markets and regulatory matters in the U.S., London, Europe, Asia and Bermuda.

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