

September 15, 1983

SUBJECT: INSURANCE

WITHDRAWN

CIRCULAR LETTER NO. 19 (1983)

September 15, 1983

TO: ALL LICENSED INSURANCE COMPANIES

SUBJECT: LETTERS OF CREDIT

The Department has recently reviewed the various conditions it has required in connection with the use of letters of credit and by means of this Circular Letter advises all licensed insurers that the Department will not find letters of credit to be acceptable unless they meet the following conditions:

- (1) The letter of credit must be "clean", irrevocable and unconditional. By "clean" and unconditional, it is meant that the letter of credit stipulates that the beneficiary need only draw a sight draft under the letter of credit and present it to obtain funds and that no other document need be presented. The letter of credit must also indicate that it is not subject to any conditions or qualifications outside of the letter of credit. In addition, the letter of credit itself cannot contain references to any other agreements, documents or entities.
- (2) The heading of the letter of credit may include a boxed section which contains the name of the applicant and other appropriate notations to provide a reference for such letter of credit. The boxed section must be clearly marked to indicate that such information is for internal identification purposes only and does not affect the terms of the letter of credit or the bank's obligations thereunder.
- (3) The letter of credit must contain a statement to the effect that the obligation of the bank under the letter of credit is in no way contingent upon reimbursement with respect thereto.
- (4) The term of the letter of credit must be for at least one year and must contain an "evergreen clause", which prevents the expiration of the letter of credit without due notice from the issuer. In addition, the "evergreen clause" should allow for a period of no less than 30 days notice prior to expiry date for non-renewal.
- (5) The letter of credit must state whether it is subject to and governed by the Laws of the State of New York or the Uniform Customs and Practice for Documentary Credits of the International Chamber of Commerce (Publication 290), and all drafts drawn thereunder must be presentable at a bank office in the United States.
- (6) If the letter of credit is made subject to the Uniform Customs and Practice for Documentary Credits of the International Chamber of Commerce (Publication 290), then the letter of credit must specifically address and make provision for an extension of time to draw against the letter of credit in the event that

one or more of the occurrences specified in Article 11 of Publication 290 occur.

(7) The letter of credit must be issued or confirmed by a bank authorized to issue letters of credit and which is either a member of the Federal Reserve System or is a New York State chartered bank.

(8) The aggregate of all letters of credit issued or confirmed to any one licensed insurance company by one bank on behalf of any one entity must not exceed 5% of the bank's capital and surplus, as shown in its annual report as of the end of its preceding fiscal year, as filed with the New York State Banking Department or the appropriate Federal banking regulatory agency.

Attached, as Exhibit A, is a form of letter of credit that the Department finds acceptable.

(9) If the letter of credit is issued by a bank authorized to issue letters of credit, other than a bank described in condition No. 7 then the following additional requirements must be met:

(a) the letter of credit, in a form similar to Exhibit B, must be confirmed by a bank described in condition No. 7,

(b) the issuing bank must formally designate the confirming bank as its agent for the receipt and payment of the drafts,

(c) the confirmation must be in a form similar to Exhibit C,

(d) condition No. 8 above must be met by the confirming bank, and

(e) the "evergreen clause" must provide for 60 days notice prior to expiry date for non-renewal.

(10) (a) When a letter of credit is obtained in conjunction with a reinsurance agreement, then such reinsurance agreement must contain provisions which:

(1) Require the reinsurer to provide letters of credit to the reinsured and specify what they are to cover.

(2) Stipulate that the reinsurer and reinsured agree that the letters of credit provided by the reinsurer pursuant to the provisions of the reinsurance agreement may be drawn upon at any time, notwithstanding any other provisions in such agreement, and shall be utilized by the reinsured or its successors in interest only for one or more of the following:

(i) to reimburse the reinsured for the reinsurer's share of premiums returned to the owners of policies reinsured under the reinsurance agreement on account of cancellations of such policies,

(ii) to reimburse the reinsured for the reinsurer's share of surrenders and benefits or losses paid by the reinsured under the terms and provisions of the policies reinsured under the reinsurance agreement,

(iii) to fund an account with the reinsured in an amount at least equal to the deduction, for reinsurance ceded, from the reinsured's liabilities for policies ceded under the agreement. Such amount shall include, but not be limited to, amounts for policy reserves, claims and

losses incurred and unearned premium reserves, and

(iv) to pay any other amounts the reinsured claims are due under the reinsurance agreement.

All of the foregoing should be applied without diminution because of insolvency on the part of the reinsured or reinsurer.

(b) Nothing contained in (a) above shall preclude the reinsured and reinsurer from providing for: (i) an interest payment, at a rate not in excess of the prime rate of interest, on the amounts held pursuant to (a)(2)(iii) above, and/or (ii) the return of any amounts drawn down on the letters of credit in excess of the actual amounts required for (a)(2)(i), (ii) and (iii) above, or in the case of (a)(2)(iv) above any amounts that are subsequently determined not to be due.

(c) When a letter of credit is obtained in conjunction with a reinsurance agreement covering risks other than life, where it is customary practice to provide a letter of credit for a specific purpose, then such reinsurance agreement may in lieu of (a)(2) above require that the parties enter into a "Trust Agreement" which may be incorporated into the reinsurance agreement or be a separate document. Such "Trust Agreement" shall conform in substance to Exhibit D.

(11) A letter of credit may not be used to reduce any liability for reinsurance ceded to an unauthorized reinsurer in financial statements required to be filed with this Department unless an acceptable letter of credit with the filing ceding insurer as beneficiary has been issued on or before the "as of date" of the financial statement. Further, the reduction for the letter of credit may be up to the amount available under the letter of credit but no greater than the specific obligations under the reinsurance agreement which the letter of credit was intended to secure.

(12) The conditions stated herein, shall apply to letters of credit issued, confirmed, amended or renewed on or after October 1, 1983. However, Condition No. (10)(a) shall not apply to reinsurance agreements entered into prior to October 1, 1983, provided that the reinsurance agreement does not restrict the drawing down of the letter of credit in any way and no new business is ceded under the agreement.

Kindly acknowledge receipt of this letter and direct any questions on this subject matter as follows:

Life Insurance Companies

Mr. Meyer Baruch
Supervising Examiner
New York State Insurance Dept.
Life Insurance and Companies Bureau
2 World Trade Center
New York, NY 10047

All Other Companies

Mr. Charles S. Henricks
Principal Examiner
N.Y.S. Insurance Department
Property Companies Bureau
2 World Trade Center
New York, NY 10047

Very truly yours,

[SIGNATURE]

James P. Corcoran

Superintendent of Insurance

Exhibit A

Irrevocable

Letter of Credit No. _____

To: Beneficiary

Dear Sir or Madam:

We have established this irrevocable letter of credit in your favor for drawings up to U.S. \$_____ effective immediately and expiring at our (bank address) with our close of business on _____.

We hereby undertake to promptly honor your sight draft(s) drawn on us, indicating our Credit No. _____, for all or any part of this Credit if presented at (bank address) on or before the expiry date or any automatically extended date.

Except as stated herein, this undertaking is not subject to any condition or qualification. The obligation of the Bank under this Letter of Credit shall be the individual obligation of the Bank, in no way contingent upon reimbursement with respect thereto.

It is a condition of this Letter of Credit that it shall be deemed automatically extended without amendment for one year from the expiry date hereof, or any future expiration date, unless thirty days prior to any expiration date we shall notify you by Registered Mail that we elect not to consider this Letter of Credit renewed for any such additional period.

Should you have occasion to communicate with us regarding this Credit, kindly direct your communication to the attention of our Letter of Credit Department, making specific reference to our Credit No. _____.

This letter of Credit is subject to and governed by the laws of the State of New York.

Very truly yours,

Exhibit B

Irrevocable

Letter of Credit No. _____

To: Beneficiary

Dear Sir or Madam:

We have established this irrevocable letter of credit in your favor for drawings up to U.S. \$_____ effective immediately and expiring at (bank address) with (our)(their) close of business on _____.

We hereby undertake to promptly honor your sight draft(s) drawn on us, indicating our Credit No. _____ for all or any part of this credit if presented at this Bank, or at such office of the confirming bank as shall be designated by written notice, on or before the expiry date or any automatically extended date.

Except as stated herein, this undertaking is not subject to any condition or qualification. The obligation of the Bank under this Letter of Credit shall be the individual obligation of the Bank, in no way contingent upon reimbursement with respect thereto.

It is a condition of this Letter of Credit that it shall be deemed automatically extended without amendment for one year, from the expiry date hereof, or any future expiration date, unless sixty days prior to any expiration date we shall notify you by Registered Mail that we elect not to consider this Letter of Credit renewed for any such additional period.

Should you have occasion to communicate with us regarding this Credit, kindly direct your communication to the attention of our Credit Department, making specific reference to our Credit No. _____.

This Letter of Credit is subject to and governed by the laws of the State of New York.

Very truly yours,

Exhibit C

Our No. _____

Amount U.S. \$ _____

Confirmation

Issuing Bank No. _____

Issuing Bank _____

To: Beneficiary

Dear Sir or Madam:

At the request of the issuing bank indicated above, we are enclosing their letter of credit and amendments thereto, if any, established in your favor.

We hereby confirm the credit and thereby undertake to pay on sight all drafts drawn and presented as specified therein on or before _____ or any automatically extended date of the letter of credit.

Drafts are to be presented for payment at the Office of (confirming bank's name, address, etc.)

Except as stated herein, this undertaking is not subject to any condition or qualification. The obligation of the Bank under this Confirmation shall be the individual obligation of the Bank, in no way contingent upon reimbursement with respect thereto.

Very truly yours,

Exhibit D

TRUST AGREEMENT

This Agreement between _____, (hereinafter called the "Reinsurer"), and _____, (hereinafter called "the Company").

WITNESSETH:

The Reinsurer has secured delivery to the Company of a clean, irrevocable Letter of Credit of the _____, No. _____ dated _____ in the sum of _____ Dollars (\$ _____) expiring on _____ "the Credit" securing refund and payment to the Company of Reinsurer's share of any loss(es)* ("loss(es)" whenever used herein, shall include losses and allocated loss expenses paid by the Company but not recovered from the Reinsurer, and reserves for losses reported and outstanding, losses incurred but not reported and allocated loss expenses) or unearned premium due or which may become due to the Company pursuant to the terms of a certain Reinsurance Agreement No. _____ "the Treaty" between the parties which became effective on _____.

*The items to be covered by the Letter of Credit can be modified by the parties.

Now, THEREFORE, in consideration of Reinsurer's having so applied for and secured delivery of said Letter of Credit which hereby acknowledged, the Company undertakes to use and apply any amounts which it may draw upon such Credit, without diminution because of any insolvency of the Company, for the following purposes only:

- a. To pay or reimburse itself for Reinsurer's share under the Treaty of any losses sustained (including incurred but not reported losses) or unearned premiums due to the company if not otherwise paid by the Reinsurer.
- b. To make payment to Reinsurer of any balance of said Credit in excess of the actual amount required by Paragraph (a) above.
- c. To obtain a cash deposit of Reinsurer's share under the Treaty of loss and unearned premium reserves, if Clean Irrevocable Credit No. _____ is not renewed at least _____ days before its expiration and the Reinsurer will continue thereafter to have a share in such loss and expense reserves.

IT IS FURTHER AGREED between the parties hereto that at annual intervals, or more frequently as required but never more frequently than quarterly, the balance of Credit made available shall be adjusted in the following manner:

- a. The Company shall prepare a statement showing the Reinsurer's share of any losses plus the unearned premiums on the accounting date under the Treaty.
- b. If the Reinsurer's share of losses outstanding plus unearned premiums under the Treaty shall exceed the then existing balance of the Credit made available, the Reinsurer will, within 30 days after receiving notice of such excess, secure delivery to the Company of an amendment of Clean Irrevocable Credit No. _____ increasing the amount of Credit available by the amount of such difference.
- c. Should however, the Reinsurer's share of losses plus unearned premium reserves under the Treaty be less than the balance of credit available on the accounting date, the Company shall, within 30 days after receipt of written request of Reinsurer, release such excess credit by agreeing to secure an amendment to Clean Irrevocable Credit No. _____ reducing the amount of Credit available by the amount of such excess credit.

d. The Company undertakes to use and apply any amount which it may draw upon the amended Letter of Credit solely for the purposes set forth in this Agreement.

IT IS FURTHER AGREED as between the parties hereto that said _____ Bank with or without notice of the existence of this Agreement, shall have no responsibility whatsoever in connection with its execution or, without limiting the generality of the foregoing, with the propriety of withdrawals made by the Company or the disposition of funds withdrawn, except to see that withdrawals are made only upon the order of properly authorized representatives of the Company and it is understood that the Company shall incur no obligation to said Bank in acting upon said Credit, other than as appears in the express terms thereof.

IT IS FURTHER AGREED as between the parties hereto that this Agreement is incorporated into, and made a part of the above mentioned Treaty.*

* May be a separate document.

The parties have caused this Agreement to be signed as of ____ day of _____, 19__.

By _____

The Reinsurer

By _____

The Company