

- SUBJECT:** Revising regulation of insurance holding company systems
- COMMITTEE:** Insurance — committee substitute recommended
- VOTE:** 9 ayes — Smithee, Eiland, Hancock, Nash, Sheets, L. Taylor, Torres, Vo, Walle
0 nays
- WITNESSES:** For — (*On introduced bill:*) Joe Woods, Property Casualty Insurers Association of America; (*On committee substitute:*) Jay Thompson, Texas Association of Life and Health Insurers
Against — None
On — Kevin Brady, Texas Department of Insurance; Brenda Nation, American Council of Life Insurers (ACLI)
- BACKGROUND:** Ch. 823 of the Insurance Code governs insurance holding companies and provides guidance to the insurance commissioner and the Texas Department of Insurance (TDI) in their oversight of insurance company solvency. The chapter regulates the relationships between insurance companies and their affiliates or subsidiaries. Current Texas legal requirements are largely similar to model legislation created by the National Association of Insurance Commissioners (NAIC).
Under sec. 32.022, TDI is required to submit a biennial report to the Legislature that summarizes needed changes to the laws regulating the insurance industry. CSHB 2835 is based on some of those recommendations.
Under sec. 823.002, a “person” includes an individual, corporation, partnership, association, joint stock company, trust, unincorporated organization, or similar entity, or a combination of the entities acting together.
Sec. 823.011 covers the confidentiality of information reported in insurer registrations and obtained by the commissioner during an examination.

Sec. 823.101 governs standards for transactions with affiliates and only applies to material transactions between a registered insurer and an affiliate. Sec. 823.103 applies to the notice of and the commissioner's decisions on specified transactions. These transactions include affiliate agreements, reinsurance agreements, and service agreements between affiliates.

Subch. D applies to the control of a domestic insurer, as well as acquisitions and mergers. Sec. 823.154 under this subchapter governs requirements for the acquisition or the exercise of control of a domestic insurer. Before a person with direct or indirect control of an insurer can obtain a voting security, or otherwise obtain or exercise control of the insurer, the person has to fulfill certain requirements. This provision also applies to a person who would obtain direct or indirect control after an acquisition. Sec. 823.155 covers amendments to statements filed under 823.154. Sec. 823.159 applies to hearings and determinations, and 823.160 covers deadlines for completed acquisitions.

Title 4 of the Insurance Code regulates insurer solvency. Ch. 404 specifically covers the financial condition of insurers, and ch. 441 governs the supervision and conservatorship of insurers.

DIGEST:

CSHB 2835 would amend sec. 823.002 of the Insurance Code to add definitions for "divesting person," "divestiture," and "enterprise risk." It would change the definition for "insurer" to clarify that it does not include any entity or agency of the U.S., its possessions and territories, Puerto Rico, or the District of Columbia.

Disclaimer of affiliation. CSHB 2835 would consider a disclaimer allowed if the commissioner did not notify the disclaiming party within 60 days that the disclaimer was disallowed. If the commissioner determined at any time that the information in the disclaimer was incomplete, the disclaimer could be disallowed.

The commissioner would be required to hold a hearing for a requesting party after the party's disclaimer was disallowed. A party whose disclaimer was allowed would not have to file under secs. 823.154, 823.155, 823.159, or 823.160 unless the commissioner disallowed the disclaimer due to insufficient information.

Supervisory colleges. Under CSHB 2835, the commissioner could establish a supervisory college for the purpose of determining the compliance of a domestic insurer that was part of a holding company system with international operations. The bill would allow the commissioner to clarify its functions and membership. The commissioner could participate with other entities including other state, federal, and international regulatory entities in order to assess the business and financial condition of insurers and to conduct examinations of individual insurers under the code. The commissioner's actions regarding supervisory colleges would not be construed as delegating regulatory authority to the supervisory college.

An insurer would be required to pay reasonable expenses incurred by the commissioner in participating in the supervisory college, which itself could be temporary or permanent. The commissioner could establish a regular assessment for insurers to apply to the expenses of regulation.

Confidentiality of information. The bill would make information under 823.011 confidential and privileged for all purposes. If an information recipient made a written agreement and verification of the legal authority to maintain the confidentiality and privilege of the information, the commissioner would be able to disclose the information to certain parties functioning in an official capacity. The bill would add a commissioner of insurance of another state and supervisory college members to the list of parties able to receive the information.

Under CSHB 2835, the commissioner would be required to enter into written agreements with the NAIC regarding the sharing and use of information. An agreement would have to:

- specify procedures for confidentiality measures;
- specify that ownership and control of the information remained with the commissioner;
- require notice to an insurer whose information was with the NAIC; and
- require the NAIC to consent to intervention by an insurer during a judicial or administrative proceeding where the insurer's information would be shared.

The bill would not prevent the commissioner or attorney general from using information for certain authorized use, including regulatory or other

legal action. The commissioner solely would be responsible for the handling of confidential information, and the commissioner's sharing of it would not delegate regulatory or rulemaking authority.

Registration statements and enterprise risk reports. The bill would require registration statements to be in a NAIC-prescribed or commissioner-approved form. The form would have to include the insurer's board of directors' corporate governance and internal control responsibilities, including a statement confirming that the board had adopted and implemented strategies to monitor corporate governance and internal controls.

An insurer would have to include a copy of all financial statements for the insurance holding company at the commissioner's request. An insurer could satisfy the request with either a copy of the parent company's most recent Securities and Exchange Commission (SEC) filing or a copy of an affiliate filing.

CSHB 2835 would add sec. 823.0595 to govern enterprise risk reports. The ultimate controlling person of an insurer required to file an annual registration statement would have to include an annual enterprise risk report. The report, required to be filed with the lead state commissioner of the holding company system, would have to identify material risks within the systems that could pose enterprise risk to the insurer.

Due dates for the first enterprise risk reports would be dependent upon the insurer's total direct or assumed annual premiums, with larger insurers due earlier under a graduated schedule established by the bill. The filing requirements would expire January 2, 2015.

If the commissioner determined the insurer was out of compliance with applicable risk-based capital standards or in hazardous condition, the ultimate controlling person would have to file an enterprise risk report regardless of total direct or assumed annual premiums.

An insurer or health maintenance organization (HMO) with total direct or assumed premiums of more than \$300 million but less than \$500 million could request an exemption if filing an enterprise risk report would cause undue financial or organizational hardship. The commissioner could grant the exemption if findings supported the hardship claim.

Failing to file an enterprise risk report would constitute a violation under the bill.

Transactions of registered insurers. CSHB 2835 would amend sec. 823.101 to include transactions within an insurance holding company system. Agreements, including service-sharing agreements, would have to include all provisions required by commissioner-established rules. The bill would amend the section to require insurers' notices to the commissioner to include reasons for entering into or modifying these transactions and the financial impact on the insurer. An insurer would have to notify the commissioner within 30 days of an agreement's termination.

For certain transactions under sec. 823.103, the bill would require an insurer to notify the commissioner of any changes made to agreements, including affiliate, pooling, and tax-allocation agreements. If an insurer intended to enter into transactions under this section, the insurer would have to provide notice to the commissioner that included reasons for entering into or changing the transactions and the financial impact on the insurer.

Divestitures of control. Before a person could initiate a divestiture of control of an insurer:

- the person would be required to file a statement with the commissioner that satisfied the legal requirements of acquisition statements;
- the divestiture would have to receive commissioner approval; and
- the person would have to submit a notice of divestiture on an NAIC- or commissioner-adopted form.

The person would have to provide the insurer with a copy of the statement. If the commissioner approved of the divestiture upon receipt of the acquisition statement, the divesting person would not have to provide the commissioner with a notice of divestiture.

The laws and timelines governing approval of acquisitions or control would apply to changes or divestitures of control under CSHB 2835. In making a determination for approval or denial of a divestiture of control, the commissioner would have to consider whether it would jeopardize the insurer's financial stability or prejudice the interests of policyholders or claimants.

If a proposed acquisition, change, or divestiture of control required more than one commissioner's approval, the commissioner could participate in a public hearing.

Acquisition statements. Under CSHB 2835, an acquiring person would have to agree to file annual enterprise risk reports as long as the person maintained control of the insurer. The acquiring person and all affiliates would have to provide requested information to the commissioner as often as necessary for the commissioner to evaluate enterprise risk.

An insurer required to file information under sec. 823.154 could satisfy the commissioner's request for the financial statements of an insurance holding company system by providing a copy of the parent company's most recent SEC filing.

Examinations. CSHB 2835 would allow the commissioner to request enterprise risk information to determine an insurer's financial condition or the legality of an insurer's conduct. In an examination, the commissioner could also order an insurer to submit information not in the insurer's possession if the information could be accessible through contractual relationships, statutory obligations, or other methods. If unsuccessful, the insurer would have to submit to the commissioner a detailed explanation, including the identity of the holder of the information, as to why the information could not be obtained. If the explanation was found to lack merit, the commissioner could either impose a daily penalty of least \$100 for a delay in producing the information or could suspend or revoke the insurer's license.

The commissioner could issue subpoenas, administer oaths, and examine under oath any person to determine compliance with the subchapter governing examinations. If the person did not comply with the subpoena, the commissioner could petition a court to issue an order to appear and testify, and the person would be subject to contempt of court for failure to appear. A person would be required to fully comply with the subpoena instructions. The fees associated with securing the person's attendance would be paid by the insurer being examined.

Civil remedies and sanctions. A violation under subch. D that prevented an enterprise risk determination could serve as an independent basis for disapproving dividends or distributions, and for orders issued under chs. 404 or 441.

TDI could not implement sec. 823.0595 as added by CSHB 2835 until the commissioner determined that the NAIC had disseminated an enterprise risk form and had proposed a master confidentiality agreement, and the commissioner had placed notice of that determination in the Texas Register.

The bill would take effect September 1, 2011.

NOTES:

The committee substitute made several changes to the bill, including granting the commissioner disallowance authority regarding incomplete disclaimers, limiting the use of confidential insurer information, and specifying procedures for filing annual enterprise risk reports.

The companion, SB 1431 by Carona, passed the Senate by 31-0 on April 28 and was referred to the House Insurance Committee on April 29.