

SUBJECT: Defining a fronting insurer; limiting exemptions for farm mutuals

COMMITTEE: Insurance — committee substitute recommended

VOTE: 7 ayes — Phillips, R. Anderson, Gooden, Oliverson, Paul, Sanford,
Turner

1 nay — Muñoz

1 absent — Vo

SENATE VOTE: On final passage, May 10 — 28-2 (Bettencourt, V. Taylor)

WITNESSES: None

BACKGROUND: Insurance Code, ch. 911 regulates the formation and conduct of farm mutual insurance companies.

Property and casualty tax. Sec. 221.002 imposes a 1.6 percent tax on the taxable premium receipts of each property and casualty insurer that receives gross premiums subject to taxation. Sec. 221.001(b) exempts certain institutions from this tax, including fraternal benefit societies, group hospital service corporations, stipulated premium companies, and mutual assessment associations.

Maintenance tax. Sec. 252.001 imposes a maintenance tax not to exceed 1.25 percent on gross premiums from the issuance of insurance against loss or damage from certain emergency events such as an earthquake, fire, or flood. Sec. 252.005 exempts farm mutual insurance companies from paying this tax.

TWIA membership. Sec. 2210.051 requires all authorized property insurers to maintain membership in the Texas Windstorm Insurance Association (TWIA) for the duration of their existence. TWIA provides an insurer of last resort for windstorm and hail damage in Texas's seacoast territory, and sec. 2210.052 requires each member to participate in insured

losses and operating expenses of the association. Sec. 2210.006(b) exempts farm mutual insurance companies from TWIA membership.

Observers have noted a need to address the problem of "fronting" in the insurance market. Farm mutual insurance companies are small insurers that serve vital roles in rural communities, but larger insurance companies have been paying farm mutuals to use the farm mutual name in order to avoid certain taxes. Some suggest that if fronting practices continue, farm mutual insurers no longer will be afforded the exemptions to which they are rightfully entitled.

DIGEST:

CSSB 2179 would define a "fronting insurer" as a farm mutual insurance company that:

- issued an insurance policy as the result of marketing by an insurer not affiliated with the farm mutual;
- issued an insurance policy for which an application was submitted to an insurer not affiliated with the farm mutual;
- issued an insurance policy resulting from an agreement with an insurer that was not a farm mutual solely for the purpose of being regulated as a farm mutual under Insurance Code, ch. 911; or
- ceded at least 85 percent of the company's direct written premium to one or more nonaffiliated reinsurers.

The bill would provide an exemption from the property and casualty insurance premium tax to farm mutual insurance companies and would specify that this exemption did not apply to fronting insurers.

The bill also would specify that the exemptions from maintenance tax and Texas Windstorm Insurance Association (TWIA) membership afforded to farm mutual insurers did not apply to fronting insurers.

The bill would take immediate effect if finally passed by a two-thirds record vote of the membership of each house. Otherwise, it would take effect September 1, 2017. The bill would apply only to TWIA membership required or tax liability accruing on or after its effective date.

NOTES: CSSB 2179 differs from the Senate-passed version in minor and non-substantive ways.

A companion bill, HB 3543 by Morrison, was placed on the General State Calendar for May 11.