

## **BILL ANALYSIS**

Senate Research Center

H.B. 909  
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Economic Development  
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Engrossed

### **DIGEST**

Currently, the statutes of the Insurance Code regarding the authorized investments of life, health and accident insurers were adopted in 1983. These statutes need to be updated to reflect current investment practices which would allow insurers to take advantage of new financial investments to maximize their financial capital. This bill would authorize various investments of life, accident and health insurers.

### **PURPOSE**

As proposed, H.B. 909 amends certain provisions of the Insurance Code, concerning authorized investments of insurers.

### **RULEMAKING AUTHORITY**

Rulemaking authority is granted to the commissioner of insurance in SECTION 3 (Section 4(u)(8)(b), Article 3.33, Insurance Code) of this bill.

### **SECTION BY SECTION ANALYSIS**

SECTION 1. Amends Section 2, Article 3.33, Insurance Code, to delete text providing that certain investment plans should seek a reasonable relationship of liabilities and assets as to term and nature.

SECTION 2. Amends Section 3, Article 3.33, Insurance Code, to require the board of directors of each insurer or corresponding authority designated by the charter, bylaws, or plan of operations of an insurer which has no board of directors to adopt a written investment plan consistent with the provisions of this article which meet certain conditions. Deletes text requiring such a board of directors or corresponding authority to adopt a written investment plan consistent with the provisions of this article. Deletes text requiring certain investment records to contain certain information.

SECTION 3. Amends Section 4, Article 3.33, Insurance Code, as follows:

Sec. 4. New heading: AUTHORIZED INVESTMENTS AND TRANSACTIONS. Provides that subject to the limitations and restrictions herein contained and, unless otherwise specified, based upon the insurer's capital, surplus and admitted assets as reported in the most recently filed statutory statement, the investments and transactions, rather than loans, described in the following subsections, and in Section 6, Article 21.49-1, and none other, are authorized.

(a)-(b) Makes no changes.

(c) Provides that asset-backed securities, among other obligations, that are issued, assumed, guaranteed, or insured by any business entity, including a limited liability company, among other entities, subject to certain conditions, are authorized investments. Authorizes an insurer to acquire counterparty exposure amounts, as defined in Subsection (u), among other obligations, in any one business entity rated by the Securities Valuation Office of the National Association of Insurance Commissioners (SVO), but not to exceed 20 percent of the insurer's statutory capital and surplus. Deletes text in reference to a business entity rated one or two by SVO. Deletes text in reference to surplus as reported in certain annual statements. Prohibits an insurer from acquiring an obligation,

counterparty exposure amount or preferred stock of any business entity if, after giving effect to the investment, the aggregate amount of certain investments exceed a certain percentage of assets. Prohibits an insurer, if the insurer attains or exceeds the limit of any one rating category referred to in this subsection, from being precluded from acquiring investments in other rating categories subject to the specific and multiple category limits applicable to those investments. Deletes existing Subsections (c)(2) and (3). Authorizes an insurer, notwithstanding the foregoing, to acquire an obligation of a business entity in which the insurer already holds, rather than has, one or more obligations if the obligation is acquired in order to protect an investment previously made in that business entity, but obligations so acquired may not exceed one-half percent of the insurer's assets. Provides that this subsection does not prohibit an insurer from acquiring an obligation as a result of a restructuring of an already held obligation or preferred stock that is rated 3, 4, 5, or 6, rather than three or lower by SVO.

(d)-(e) Makes no changes.

(f) Makes nonsubstantive changes.

(g) Insurer Investment Pools. Defines "affiliate." Authorizes an insurer to acquire investments in certain investment pools. Prohibits an insurer from acquiring an investment in a investment pool under this subsection if after giving effect to the investment, the aggregate amount of investments in all investment pools then held by the insurer would exceed 35 percent of its assets. Prohibits the investment pool, for an investment in an investment pool to be qualified under this article, from performing certain actions. Sets forth the conditions for an investment pool to be qualified under this article. Requires the pooling agreement for each investment pool to be in writing and to provide certain terms and conditions. Prohibits an investment in an investment pool from being deemed to be an affiliate transaction under Section 4, Article 21.49-1, of this code; however, each pooling agreement shall be subject to the standards of Section 4(a), Article 21.49-1, of this code and the reporting requirements of Section 3(b), Article 21.49-1 of this code. Deletes existing Subsection (g), relating to equipment trusts.

(h) Equity Interests. Provides that certain equity interests, under certain conditions, are authorized investments. Defines "business entity." Deletes existing Subsection (h), relating to common stock.

(i) Provides that preferred stock of business entities as described in Subsection (c) of this section, rather than preferred stock of corporations organized under the laws of the U.S. or any of its states, is an authorized investment; provided that, among other conditions, the investments in the preferred stock of any one business entity will not exceed 20 percent of the insurer's capital and surplus; and the preferred stock is rated by the SVO, and the aggregate investment in preferred stock rated 3, 4, 5, or 6, when added to the investments under Subsection (c)(2) do not result in the combined total of such investments exceeding the limitations specified in Subsection (c)(2). Deletes existing Subsections (i)(1) and (2). Makes a conforming change.

(j)-(m) Makes no changes.

(n) Provides that investment in other foreign countries or in commonwealths, territories, or possessions of the United States are authorized investments; provided that such investments are substantially the same types as, rather than similar to, those authorized for investment within the U.S. or Canada by other provisions of this section; such investments when added to the amount of similar investments made within the U.S. and Canada do not result in the combined total of such investments exceeding the limitations specified in Subsections (a) through (m), (o), (q) and (u), rather than through (p), of this section; and such investments may not exceed the sum of the amount of insurer's reserves attributable to the insurance business in force in foreign countries, if any, and any additional investments required by any foreign country as a condition to doing business therein, and 20, rather than five, percent of the insurer's assets of which no more than 10 percent of the

insurer's assets may be investments denominated in foreign currency that are not hedged pursuant to the provisions of Subsection (u). Deletes text providing that such investments are rated by the SVO. Makes nonsubstantive changes.

(o) Makes conforming changes.

(p) Authorizes an investment held by an insurer on the effective date of this Act, which legally authorized at the time it was made or acquired or which the insurer was authorized to hold or possess immediately prior to such effective date, but which does not conform to the requirements of the investments authorized in Subsections (a)-(o), to continue to be held by and considered as an authorized, rather than admitted, asset or transaction of the insurer under certain conditions. Makes a conforming change.

(q) Securities Lending, Repurchase, Reverse Repurchase and Dollar Roll Transactions. Defines "repurchase transaction," "reverse repurchase transaction," "securities lending transaction," and "dollar roll transaction." Authorizes an insurer to engage in securities lending, repurchase, reverse repurchase and dollar roll transactions. Requires the insurer to enter into a written agreement for all transactions, except dollar transactions, that shall require each transaction to terminate no more than one year from its inception. Requires cash received in a transaction under this section to be invested in accordance with this article and in a manner that recognizes the liquidity needs of the transaction or used by the insurer for its general corporate purposes. Requires the insurer, its agent, or custodian to maintain, as to acceptable collateral received in a transaction under this subsection, either physically or through the book entry systems of the Federal Reserve, Depository Trust Company, Participants Trust Company or other securities depositories approved by the commissioner of insurance (commissioner), certain items. Prohibits the limitations of Sections 4(c) and 5(a) from applying to the business entity counterparty exposure created by transactions under this section. Prohibits an insurer from entering into a transaction under this section if, as a result of and after giving effect to the transaction, the aggregate amount of certain securities exceed a certain amount. Provides that the amount of collateral required for securities lending, repurchase and reverse repurchase transactions is the amount required pursuant to the provisions of the *Purposes and Procedures* of SVO or such successor publication. Prohibits Article 3.39-1 from applying to transactions authorized by this subsection. Deletes existing Subsection (q), relating to special limitations for certain fixed annuity insurers.

(r) Makes no changes.

(s) Provides that money market mutual funds as defined by 17 CFR 270.2a-7 under the Investment Company Act of 1940 (15 U.S.C. 80a-1 et seq.) that may be either a certain government money market mutual fund or a certain class one money market mutual fund are authorized investments. Deletes existing Subdivisions (A)-(C). Requires money market mutual funds qualifying for listing within these categories to conform to the *Purposes and Procedures*, rather than the purposes and procedures manual, of SVO or such successor publication. Deletes reference to valuation of securities manual of the National Association of Insurance Commissioners.

(t) Requires the percentage authorizations and limitations set forth in any or, rather than and, all of the provisions of Article 3.33 to apply only at the time of the original acquisition of an investment or at the time a transaction is entered into and shall not be applicable to the insurer or such investment or transaction thereafter except as provided in Subsection (w). Requires any investment, once qualified under any subsection of this section, to remain qualified notwithstanding any refinancing, restructuring or modification of such investment provided that, the insure shall not engage in any such refinancing, restructuring or modification of any investment for the purpose of circumventing the requirements or limitations of this article. Makes conforming and nonsubstantive changes.

(u) Risk Control Transactions. Authorizes an insurer to use derivative instruments to engage in hedging transactions, replication transactions and income generation

transactions. Defines "acceptable collateral," "business entity," "cap," "cash equivalents," "short term," "highly rated," "collar," "counterparty exposure amount," "derivative instrument," "derivative transaction," "floor," "forward," "future," "futures exchange," "hedging transaction," "income generation transaction," "market value," "option," "over-the-counter derivative instrument," "potential exposure," "qualified clearinghouse," "replication transaction," "securities exchange," "swap," "swaption," "underlying interest," and "warrant." Requires the board of directors, prior to entering into any derivative transaction, to approve a certain derivative use plan, as part of the investment plan required in Section 3 of this article. Requires the insurer to establish certain written internal control procedures. Requires an insurer to be able to demonstrate to the commissioner, upon request, the intended hedging characteristics and ongoing effectiveness of the derivative transaction or combination of transactions through cash flow testing, duration analysis or other appropriate analysis. Requires an insurer to include all counterparty exposure amounts in determining compliance with the limitations of Subsection (c). Sets forth regulations relating to certain hedging transactions and certain derivative transactions. Authorizes an insurer to only enter into an income generation transaction under certain conditions. Authorizes an insurer to enter into replication transactions only with prior written approval from the commissioner and under certain conditions. Authorizes an insurer to purchase or sell one or more derivative instruments to offset, in whole or in part, any derivative instrument previously purchased or sold, without regard to the quantitative limitations of this subsection, provided that such offsetting transaction utilizes the same type of derivative instrument as the derivative instrument being offset. Sets forth the trading requirements. Prohibits Article 3.39-2 from applying to transactions authorized by this subsection.

(v) Distributions, Reinsurance, and Merger. Provides that no provision of this article prohibits the acquisition by an insurer of additional obligations, securities, or other assets if received as a dividend or as a distribution of assets, nor does this article apply to securities, obligations, or other assets accepted incident to the workout, adjustment, restructuring or similar realization of any kind of investment or transaction when deemed by the insurer's board of directors or by a committee appointed by the board of directors to be in the best interests of the insurer, if the investment or transaction had previously been authorized, nor does this article apply to assets acquired pursuant to a lawful agreement of bulk reinsurance, merger, or consolidation if such assets constituted legal and authorized investments for the ceding, merged or consolidation company. Provides that no obligation, security or other asset acquired as permitted by this subsection need be qualified under any other subsection of this article.

(w) Qualification of Investments. Provides that the qualification or disqualification of an investment under one subsection of this section does not prevent its qualification in whole or in part under another subsection, and an investment authorized by more than one subsection may be held under whichever authorizing subsection the insurer elects. Requires an investment or transaction qualified under any subsection at the time it was acquired or entered into by the insurer to continue to be qualified under that subsection. Authorizes an investment to be transferred from time to time to the authority of any subsection under which it then qualifies, whether or not it originally qualified thereunder.

SECTION 4. Amends Section 5, Article 3.33, Insurance Code, to provide that certain provisions govern and take precedence over each and every provision of Section 4, except Subsections (q), (t), and (v).

SECTION 5. Amends Section 7, Article 3.33, Insurance Code, to delete existing Subsection (e), limiting an insurer's participation in a partnership or joint venture.

SECTION 6. Amends Article 2.10, Insurance Code, to prohibit a company except any writing life, health and accident insurance, organized under the laws of this state, from investing its funds over and above its minimum capital and its minimum surplus, as provided in Article 2.02, in any other manner than, among other options, in bonds or other evidences of debt which at the time of purchase are interest-bearing and are issued by authority of law and are not in default as to principal interest,

of any of the states, or of Canada, or any province of Canada, among other entities; under certain conditions. Prohibits a company from investing its funds over and above its minimum capital and its minimum surplus, as provided in Article 2.02, in any other manner than, among other options, in shares of mutual funds doing business under the Investment Company Act of 1940 (15 U.S.C. Section 80a-1 et seq.), under certain conditions. Prohibits a company from investing its funds over and above its minimum capital and its minimum surplus, as provided in Article 2.02 in any other manner than, among other options, in investments in other foreign countries or in commonwealths, territories or possessions of the U.S., or in foreign securities originating in such foreign countries, commonwealths, territories or possessions of the U.S., under certain conditions. Makes conforming changes.

SECTION 7. Amends Article 9.18, Insurance Code, to require investments of all title insurance companies operating under the provisions of this Act to be held in cash or may be invested in, among other items, securities lending, repurchase, reverse repurchase and dollar roll transactions as provided for in Section 4(g), Article 3.33, of this code and money market funds as provided for in Section 4(s), Article 3.33, of this code.

SECTION 8. Repealers: Articles 3.39-1 and 3.39-2, Insurance Code (Repurchase Agreements; Risk Limiting Provisions).

SECTION 9. Repealer: Section 5, Article 21.39-B, Insurance Code.

SECTION 10. Effective date: September 1, 1997.

SECTION 11. Emergency clause.