

BILL ANALYSIS

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C.S.H.B. 4338
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Committee Report (Substituted)

AUTHOR'S / SPONSOR'S STATEMENT OF INTENT

Weaknesses in the existing regulatory system have been brought to the forefront during the current economic downturn. Several title insurance agents have failed, leaving files in the middle of closing, offices and file storage facilities padlocked, and Texas Department of Insurance (TDI) staff uncertain whether to place the agent into receivership or into the hands of the Texas Title Insurance Guaranty Association. On the last day of July 2008, one of the largest independent title insurance companies in Texas was shut down by its out-of-state owners with no warning to its underwriters, employees, customers, or landlords, or TDI. TDI had just completed an escrow audit of the agent and was reasonably certain that there were no shortages in the escrow account. This belief prevented TDI from referring the case to the Guaranty Association. Because of the size of the agent and the fact that TDI and the association were also involved with other failed agents, TDI's resources were stretched very thin, and TDI and the agent's underwriters were forced to devise a system to deal with the files that were in various stages of closing with upwards of \$12 million needing to be funded.

While extraordinary efforts by TDI staff and the underwriters allowed this failed agent's customers to have their transactions closed, existing liens paid, and documents recorded all with no known loss of funds, it became apparent that changes to the title insurance act were needed to head off similar problems in the future. However, the out-of-state owner of the agent placed it in bankruptcy in another state. Since current Texas law does not specify that funds owed to an agent's underwriter or another agent for providing title evidence or closing services be held in trust by the agent, neither the underwriters nor the numerous agents that sold information to the failed agent are likely to receive a cent of their money. At least holding the money in trust moves the underwriter and other agents into a more secure position. This bill allows the commissioner of insurance more flexibility in handling impaired title insurance agents and companies.

C.S.H.B. 4338 amends current law relating to title insurance agents and title insurance companies.

RULEMAKING AUTHORITY

Rulemaking authority is expressly granted to the commissioner of insurance in SECTION 12 (Section 2651.0021, Insurance Code), SECTION 13 (Section 2651.011, Insurance Code), SECTION 14 (Section 2651.012, Insurance Code), SECTION 15 (Section 2651.158, Insurance Code), SECTION 16 (Section 2651.206, Insurance Code), and SECTION 21 of this bill.

SECTION BY SECTION ANALYSIS

SECTION 1. Amends Section 2501.004(b), Insurance Code, to require the Texas Department of Insurance (TDI), to provide for the safety and protection of policyholders, to require that an abstract plant be geographically arranged, cover a period beginning not later than January 1, 1979, and be kept current, and be adequate for use in insuring titles, as determined by TDI. Makes a nonsubstantive change.

SECTION 2. Amends Section 2602.002(a), Insurance Code, to provide that this chapter is for certain reasons, including the protection of consumers served by agents. Makes nonsubstantive changes.

SECTION 3. Amends Sections 2602.003(5) and (6), Insurance Code, to redefine "impaired agent" and "impaired title insurance company."

SECTION 4. Amends Section 2602.011(a), Insurance Code, as follows:

(a) Requires the commissioner of insurance (commissioner) to notify the Texas Title Insurance Guaranty Association (association) of the existence of an impaired title insurance company or impaired agent not later than the third day after the date on which the commissioner gives notice of the designation of impairment to the impaired title agent or direct operation.

SECTION 5. Amends Section 2602.107, Insurance Code, by adding Subsection (d), to require the association to pay from the guaranty fee account fees and reasonable and necessary expenses that TDI incurs in an examination or audit of a title agent or direct operation under this chapter and Chapter 2651 (Title Insurance Agents and Direct Operations).

SECTION 6. Amends Section 2602.110, Insurance Code, as follows:

Sec. 2602.110. New heading: EXPENSES OF ADMINISTERING IMPAIRED INSURER OR IMPAIRED AGENT. Authorizes the association to advance money necessary to pay the expenses of administering the supervision, rehabilitation, receivership, conservatorship, or, as determined by a court, other insolvency of an impaired title insurance company or impaired agent, rather than to pay expenses of administering the receivership or conservatorship estate of an impaired title insurance company or agent, on terms the association negotiates, if the company's or agent's assets are insufficient to pay those expenses.

SECTION 7. Amends Section 2602.152, Insurance Code, to require the board of directors of the association (board), annually or more frequently, to determine the amount of the guaranty fee, rather than to determine the amount of the guaranty fee, not to exceed \$5, considering the amount of money to be maintained in the guaranty fee account that is reasonably necessary for efficient future operation under this chapter.

SECTION 8. Amends Sections 2602.153(b) and (d), Insurance Code, as follows:

(b) Requires that the following claims, rather than the following covered claims, be paid from guaranty fees only and prohibits them from being paid from assessments: covered claims against trust funds or an escrow account of an impaired agent under Section 2602.252 (Claim Against Trust Funds or Escrow Account); expenses incurred in complying with Subchapter J; conservator and receiver expenses under Section 2602.254 (Certain Conservator and Receiver Expenses Covered); and administrative expenses with respect to the estate of an impaired agent under Section 2602.110 (Expenses of Receivership or Conservatorship). Makes nonsubstantive changes.

(d) Authorizes guaranty fees to be used only for payment of claims described by Subsection (b) and expenses related to an audit or an examination conducted by TDI or the association under this chapter, the supervision and coordination of such an audit, and an action required under Section 2602.452, rather than covered claims described by Subsection (b) or (c) (relating to requiring that administrative expenses be paid from the guaranty fee account) and audit and review expenses under Section 2602.103(b) (relating to requiring the association to retain one or more persons to audit and review agent escrow and trust accounts and make a report to the commissioner).

SECTION 9. Amends Sections 2602.401(a) and (b), Insurance Code, as follows:

(a) Prohibits the company, if an assessment has been made under this chapter for an impaired title insurance company or association funds have been provided for the company, on release from the supervision, rehabilitation, conservatorship, receivership, or other proceeding in which the company was found by a court of competent jurisdiction to be insolvent or otherwise unable to pay obligations as they come due, from issuing a new or renewal insurance policy until the company has repaid certain amounts.

(b) Prohibits the agent, on release from the supervision, conservatorship, rehabilitation, receivership, or other proceeding in which the agent was found by a court of competent jurisdiction to be insolvent or otherwise unable to pay obligations as they come due, subject to dischargeability, from acting as an agent, rather than issuing a new or renewal insurance policy, until the agent has repaid in full the amount of guaranty fees paid by the association, if an assessment has been made under this chapter for an impaired agent or guaranty fees have been provided for the agent.

SECTION 10. Amends Chapter 2602, Insurance Code, by adding Subchapter J, as follows:

SUBCHAPTER J. ADDITIONAL DUTIES OF ASSOCIATION

Sec. 2602.451. **APPLICABILITY.** Provides that this subchapter applies, at the commissioner's discretion and regardless of whether there are covered claims against an agent, to any agent that is designated by the commissioner as an impaired agent.

Sec. 2602.452. **ACTIONS FOR CERTAIN AGENTS.** (a) Authorizes the commissioner to require the association, at the association's expense and on behalf of an impaired agent, to take certain actions.

(b) Authorizes the association to employ or retain a person in accordance with Section 2602.103(a) (relating to the authorization of the association to employ or retain persons to perform certain necessary functions) to take the actions required by the commissioner under this section.

Sec. 2602.453. **AUTHORITY OF ASSOCIATION; COOPERATION OF OFFICERS, OWNERS, AND EMPLOYEES.** (a) Authorizes the association, on the direction of the commissioner under Section 2602.452, to implement any direction made by the commissioner and to access all books, records, account, networks, and electronic document storage and management systems as necessary to implement the commissioner's direction.

(b) Requires any present or former officer, manager, director, trustee, owner, employee, or agent of the agent, or any other person with authority over or in charge of any segment of the agent's affairs, to cooperate with the association. Defines "person" and "cooperate" for purposes of this subsection.

(c) Provides that a person who fails to cooperate as required under Subsection (b) is subject to sanctions under Chapter 82 (Sanctions), in addition to all other sanctions available under law.

SECTION 11. Amends Section 2651.002, Insurance Code, by amending Subsection (c) and adding Subsection (d), as follows:

(c) Requires that the completed application state certain information, including that the proposed agent has unencumbered assets in excess of liabilities, exclusive of the value of abstract plants, as required by Section 2651.012.

(d) Requires an agent applying for an initial license under this subchapter, except as provided by Section 2651.0021(e), to provide evidence that the agent and its management personnel have successfully completed a professional training program that complies with Section 2651.0021. Requires that the program have been completed within one year preceding the date of application.

SECTION 12. Amends Subchapter A, Chapter 2651, Insurance Code, by adding Section 2651.0021, as follows:

Sec. 2651.0021. **PROFESSIONAL TRAINING PROGRAM.** (a) Requires the commissioner to adopt by rule a professional training program (program) for a title insurance agent and the management personnel of the title insurance agent.

- (b) Requires that the program be designed to provide certain information.
- (c) Authorizes program hours to be used to satisfy the continuing education requirements established under Section 2651.204 (Continuing Education).
- (d) Requires that a program course be offered by certain entities.
- (e) Exempts an individual from the professional training requirement of this section if the individual has held in this state for at least five years a position as management personnel with a title insurance agent, or a comparable position, as determined under rules adopted by the commissioner.

SECTION 13. Amends Section 2651.011, Insurance Code, as follows:

Sec. 2651.011. New heading: PRIVILEGED COMMUNICATIONS; FINANCIAL INFORMATION. (a) Creates this subsection from existing text. Provides that any information, including a document, record, or statement, and including information provided to or received from the commissioner under Subsection (b) or (c), or any other information required or permitted to be made or disclosed to or by TDI under this subchapter, other than Section 2651.001 (License and Bond or Deposit Required), is not public information subject to Chapter 552 (Public Information), Government Code, except to the extent described by Subsection (b), rather than is a privileged communication, and is not admissible in evidence in a court action or proceeding except under a subpoena issued by a court of record. Makes nonsubstantive changes.

(b) Authorizes a title insurance company to provide information to the commissioner about a financial matter that would reasonably call into question the solvency of a title agent that the title insurance company appointed. Requires each title insurance company to provide annually to TDI a list of officers authorized to provide to TDI the information under this subsection. Provides that information provided under this subsection is not subject to Chapter 552, Government Code, except that the commissioner is authorized to release information that the commissioner received under this subsection to a title insurance company that has appointed, or that is considering appointing, the title agent. Authorizes the commissioner to also release information that the commissioner received under this subsection to a title agent under Section 2651.206, Insurance Code, if the information is evidence on which an audit report or examination report relies. Prohibits a title insurance company that receives information under this subsection from releasing the information except under a subpoena issued by a court of competent jurisdiction.

(c) Requires each title insurance agent to provide TDI, on a quarterly basis, with a copy of the agent's quarterly withholding tax report furnished by the agent to the United States Internal Revenue Service. Requires the title insurance agent to also provide to TDI proof of the payment of the tax. Requires an agent who does not have employees to certify to TDI on a quarterly basis that there has not been a material change in the agent's financial condition.

(d) Authorizes the commissioner by rule to prescribe the types of information under Subsections (b) and (c) that are privileged under Subsection (a).

SECTION 14. Amends Subchapter A, Chapter 2651, Insurance Code, by adding Sections 2651.012 and 2651.013, as follows:

Sec. 2651.012. UNENCUMBERED ASSETS. (a) Defines "principal office" and "unencumbered assets."

(b) Provides that the unencumbered assets required under this section are reserves for contingencies. Requires that the reserves be deducted from premiums for purposes of proceedings conducted under Subchapter D (Fixing and Promulgating

Premium Rates), Chapter 2703 (Policy Forms and Premium Rates). Authorizes the reserves to only be spent or released under certain conditions.

(c) Requires an agent, except as provided by Subsection (d), to maintain unencumbered assets with a market value in excess of liabilities, exclusive of the value of abstract plants, in certain amounts unless the commissioner establishes lesser amounts by rule.

(d) Exempts an agent that maintains its principal office in a county with a population of less than 10,000 from this section, except as provided by the commissioner by rule.

(e) Requires an agent that maintains a principal office in more than one county to meet the asset standards for the largest county for which the agent will hold a license.

(f) Authorizes an agent to elect to maintain unencumbered assets as required by this section or place a deposit with TDI as authorized by Section 2652.102 (Alternative to Bond).

(g) Provides that an agent that holds a license on September 1, 2009, and that has held the license for at least three years on that date is not required to comply with Subsection (c) on September 1, 2009, but is required to increase the unencumbered assets held by the agent, or make and increase the required deposit, until the agent is in compliance with the required capitalization amounts in accordance with the schedule established by this subsection. Requires the agent to hold certain unencumbered assets or to make a deposit in a certain amount.

(h) Requires an agent, if the agent has been licensed less than three years as of September 1, 2009, to have at least 50 percent of the required capitalization amount required under Subsection (c) on September 1, 2010; and 100 percent of that required capitalization amount on September 1, 2011.

(i) Provides that this subsection and Subsection (g) expire September 2, 2018.

(j) Provides that notwithstanding any other provision of this section, this section takes effect only after the commissioner adopts the form, content, and procedures for use of the surety bond authorized under Subsection (a). Requires the commissioner by rule to establish the procedures for making, filing, using, and paying for the surety bond. Authorizes the commissioner by rule, notwithstanding Subsections (g) and (h), to extend the dates established under those subsections as necessary to comply with this subsection.

Sec. 2651.013. DIVISION OF PREMIUM HELD IN TRUST; RULES. (a) Provides that the funds held by a title insurance agent that are owed to a title insurance company, another title insurance agent, or a direct operation arising from a division of premium, whether as determined under rules adopted by the commissioner or by agreement among the parties, are considered to be held in trust for the title insurance company, other title insurance agent, or direct operation.

(b) Provides that this section does not require, and prohibits the commissioner from requiring by rule, that funds described by Subsection (a) be held in a separate account or be subject to an external audit. Provides that this section does not affect TDI's or the association's authority to examine or audit a title agent or direct operation.

SECTION 15. Amends Subchapter D, Chapter 2651, Insurance Code, by adding Section 2651.158, as follows:

Sec. 2651.158. CERTIFICATION OF UNENCUMBERED ASSETS. (a) Requires that the annual audit of escrow accounts, unless the agent has elected to make a deposit with

TDI under Section 2651.012(f), be accompanied by a certification by a certified public accountant that the title insurance agent has the appropriate unencumbered assets in excess of liabilities, exclusive of the value of its abstract plants, as required by Section 2651.012.

(b) Requires the commissioner by rule to establish a procedure to be used to determine the value of categories of assets and the method by which the certification required by this section is required to be made which is prohibited from including an audit of operating accounts.

SECTION 16. Amends Subchapter E, Chapter 2651, Insurance Code, by adding Section 2651.205 and 2651.206, as follows:

Sec. 2651.205. TITLE AGENT RECORDS. (a) Provides that a landlord or storage facility, including an electronic storage facility, that accepts possession of an agent's guaranty file or other records takes possession subject to the right of access of the title insurance company involved in the transaction that the file documents, during customary business hours, for the purposes of copying the guaranty file and the obligation to maintain the confidentiality of nonpublic information in the title insurance agent's records according to state and federal laws that govern the title insurance agent.

(b) Provides that if the title insurance agent is impaired, the Texas Title Insurance Guaranty Association has the right to access the guaranty files and other records of the title insurance agent, including electronic records, for 60 days from the date of impairment, during customary business hours, for purposes of copying those records.

(c) Provides that except for the right of access granted under Subsections (a) and (b), a lien created in favor of the landlord by contract or otherwise is not impaired.

(d) Defines "title insurance agent."

Sec. 2651.206. EXAMINATION REPORTS. (a) Requires that an audit, review, or examination conducted under this chapter or Chapter 2602 (Texas Title Insurance Guaranty Association) be conducted in accordance with rules adopted by the commissioner. Requires that the rules provide that before a report from an examination, review, or audit becomes final, TDI will furnish to the title agent or direct operation a copy of the report and any evidence on which the report relies; a reasonable period of not less than 10 days after the title agent or direct operation receives the report and evidence from TDI for the title agent or direct operation to respond; an opportunity for an appeal of the examination report under a process similar to the process under Title 28 (Insurance), Part 1 (Texas Department of Insurance), Chapter 7 (Corporate and Financial Regulation), Subchapter A (Examination and Financial Analysis), Texas Administrative Code; and procedures to ensure that the report and any evidence regarding the report remain confidential and are transmitted only to designated representatives of the title agent or direct operation.

(b) Requires the commissioner to furnish the title agent or direct operation with a draft of the examination report and a copy of any evidence not later than the 10th day before the scheduled date of a meeting requested by TDI regarding a report.

(c) Provides that this section does not require TDI to turn over work papers. Provides that for purposes of this subsection, work papers are the records of an auditor or examiner of the procedures followed, the tests performed, the information obtained, and the conclusions reached that are pertinent to the audit or examination. Provides that work papers include work programs, analyses, memoranda, letters of confirmation and representation, abstracts of company documents and schedules, and commentaries prepared or obtained by the auditor or examiner that support the opinions of the auditor or examiner.

SECTION 17. Amends Section 2703.202, Insurance Code, by adding Subsections (c), (d), (e), and (f), as follows:

(c) Requires that a public hearing held under Subsection (a) (relating to the prohibition of a premium rate previously fixed by the commissioner from being changed until a certain date) or under Section 2703.206 (Commissioner Authority to Hold Hearings as Necessary), except as provided by Subsection (d), be conducted by the commissioner as a rulemaking hearing under Subchapter B (Rulemaking), Chapter 2001 (Administrative Procedure), Government Code.

(d) Requires that a public hearing held under Subsection (a) or under Section 2703.206, notwithstanding Subsection (c), at the request of a title insurance company or the public insurance counsel, be conducted by the commissioner as a contested case hearing under Subchapters C (Contested Cases: General Rights and Procedures) through H (Court Enforcement) and Subchapter Z (Miscellaneous), Chapter 2001, Government Code. Provides that nothing in this section prohibits a party from conducting discovery in a ratemaking or other proceeding or producing other information requested by TDI.

(e) Prohibits information received or requested by the commissioner as part of an audit or examination under Chapters 2602 and 2651 (Title Insurance Agents and Direct Operations) from being used for rate setting under Subchapter D, Chapter 2703.

(f) Provides that Subsections (c) through (e) apply only to a public hearing held on or after January 1, 2009.

SECTION 18. Repealers: Sections 2602.056 (Financial Statement of Board Member) and 2602.153(c) (relating to requirement that administrative expenses be paid from the guaranty fee account), Insurance Code.

SECTION 19. Provides that an abstract plant that exists on September 1, 2009, but that does not, on that date, cover a period beginning not later than January 1, 1979, as required by Section 2501.004, Insurance Code, as amended by this Act, is not required to comply with that section before January 1, 2014.

SECTION 20. Provides that Section 2651.158, Insurance Code, as added by this Act, applies beginning with annual audits conducted under Subchapter D (Annual Audit), Chapter 2651, Insurance Code, for the 2011 calendar year.

SECTION 21. Requires the commissioner to hold a hearing not later than the 120th day after the effective date of this Act. Requires the commissioner, not later than the 90th day after the date of that hearing, to issue an order prescribing the rules and forms to be used in connection with Section 2651.206, Insurance Code, as added by this Act.

SECTION 22. Effective date: September 1, 2009.