

ANALYSIS

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S.B. 1735
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AUTHOR'S / SPONSOR'S STATEMENT OF INTENT

The purpose of S.B. 1735 is to authorize the establishment of domestic Limited Purpose Subsidiary Life Insurance Companies (LPS) to allow that such LPSs are able to support excess reserves for certain life insurance policies.

Texas domiciled life insurers are currently at a disadvantage to companies domiciled in states such as Iowa that allow capital relief to their domestic life insurers. Enactment of this legislation could also promote action at the National Association of Insurance Commissioners level to set principles-based reserves closer to economic reserves. Passage of this legislation would also lead to greater availability of and lower cost of insurance for Texas citizens and businesses.

The enactment of this legislation would potentially lead to potential for greater availability of, and lower cost of, life insurance for citizens and businesses that insure with Texas domiciled life insurance companies; and incentivize life insurance companies to domicile in Texas by enhancing financial flexibility whilst maintaining prudent regulatory supervision, leading to creation of jobs for Texans and greater revenue to the state.

As proposed, S.B. 1735 amends current law relating to limited purpose subsidiary life insurance companies.

RULEMAKING AUTHORITY

This bill does not expressly grant any additional rulemaking authority to a state officer, institution, or agency.

SECTION BY SECTION ANALYSIS

SECTION 1. Amends Chapter 841, Insurance Code, by adding Subchapter I, as follows:

SUBCHAPTER I. LIMITED PURPOSE SUBSIDIARY LIFE INSURANCE COMPANIES

Sec. 841.401. DEFINITIONS. Defines, in this subchapter, "affiliated company," "material transaction," "parent," "reinsurance contract," "risk," "securitization," "security," "subsidiary company," and "surplus note."

Sec. 841.402. ORGANIZATION. (a) Authorizes a domestic life insurance company to organize a subsidiary company to which the domestic life insurance company cedes risk under a reinsurance contract.

(b) Provides that a subsidiary company organized under this subchapter:

(1) is required to be wholly owned by the domestic life insurance company that organized the subsidiary company; and

(2) is prohibited from issuing stock to any organization or individual other than the domestic life insurance company that organized the subsidiary company.

(c) Prohibits a subsidiary company from engaging in the business of insurance, except as provided by Subsection (d).

(d) Authorizes a subsidiary company to:

(1) reinsure risks of:

(A) the domestic life insurance company that organized the subsidiary company; or

(B) an affiliated company; and

(2) access alternative forms of financing.

(e) Authorizes a domestic life insurance company to invest funds from its surplus in a subsidiary company organized by the domestic life insurance company.

(f) Authorizes an officer or director of a domestic life insurance company to serve as an officer or director of a subsidiary company organized by the domestic life insurance company.

Sec. 841.403. CERTIFICATE OF AUTHORITY REQUIRED. Authorizes a subsidiary company to engage in the limited business of insurance in this state, as described by Section 841.402(d), only if the subsidiary company holds a certificate of authority issued under this subchapter.

Sec. 841.404. APPLICATION FOR CERTIFICATE OF AUTHORITY. Requires the domestic life insurance company that organizes a subsidiary company, to obtain a certificate of authority for a subsidiary company, to:

(1) pay to the Texas Department of Insurance (TDI):

(A) a fee in an amount prescribed by the commissioner of insurance (commissioner); and

(B) the reasonable expenses and costs incurred by TDI in examining the subsidiary company's application; and

(2) file with TDI:

(A) an application for a certificate of authority on a form containing information required by TDI;

(B) the subsidiary company's articles of incorporation;

(C) an affidavit made by two or more of the incorporators of the subsidiary company stating that:

(i) the subsidiary company is able to satisfy the minimum capital and surplus requirements of this subchapter;

(ii) the subsidiary company's capital and surplus are the bona fide property of the subsidiary company;

(iii) the information contained in the subsidiary's articles of incorporation is true and correct; and

(iv) the subsidiary company's investment policy takes into consideration the liquidity of the subsidiary company's assets and the reasonable preservation, administration, and management of

the assets with respect to the risks associated with the subsidiary company's reinsurance contract;

(D) a copy of the subsidiary company's reinsurance contract with the domestic life insurance company that organized the subsidiary company, and any other agreement securing the subsidiary company's obligations under the reinsurance contract; and

(E) any other statement or document required by TDI.

Sec. 841.405. ISSUANCE OF CERTIFICATE OF AUTHORITY. (a) Authorizes the commissioner to issue a certificate of authority to a subsidiary company authorizing the subsidiary company to engage in the reinsurance business if:

(1) the commissioner finds that the terms of the subsidiary company's reinsurance contract and any related transactions comply with this chapter and all other applicable provisions of this code or rules adopted under this code; and

(2) the subsidiary company maintains at least \$700,000 of unimpaired paid-in capital and \$700,000 of surplus.

(b) Authorizes the commissioner, in conjunction with the issuance of a certificate of authority under Subsection (a), to issue any order relating to the organization, licensing, or operation of the subsidiary company that the commissioner deems appropriate.

Sec. 841.406. REINSURANCE. (a) Authorizes a subsidiary company to purchase reinsurance under which the risks assumed under a reinsurance contract with the domestic life insurance company that organized the subsidiary company are ceded to the reinsurer.

(b) Prohibits a subsidiary company, unless approved in advance by the commissioner, from assuming or retaining exposure to reinsurance losses for the account of the subsidiary company, unless the exposure is funded by:

(1) proceeds from a securitization;

(2) premium and other amounts payable to the domestic life insurance company that organized the subsidiary company under the applicable reinsurance contract;

(3) a letter of credit;

(4) a guarantee of a parent organization; or

(5) a return on investment of the items described by Subdivision (1) or (2).

(c) Authorizes a subsidiary company to enter into a contract or conduct other commercial activities necessary to fulfill the purposes of a reinsurance contract, an insurance securitization, or this chapter, if the activity is approved in advance by the commissioner. Provides that commercial activities described by this subsection include:

(1) entering into a reinsurance contract;

(2) issuing securities;

(3) complying with the terms of contracts or securities;

(4) entering into a trust, guaranteed investment contract, swap, or other derivative, tax, administration, service reimbursement, or fiscal agent transaction;

(5) complying with trust indenture, reinsurance, or retrocession; or

(6) entering into another agreement necessary or incidental to effect a reinsurance contract or an insurance securitization in compliance with this chapter.

(d) Prohibits a reinsurance contract from containing a provision for payment by the subsidiary company to any person other than the domestic life insurance company that organized the subsidiary company, or any receiver of that company, for the discharge of the subsidiary company's obligations under the reinsurance contract, unless otherwise approved in advance by the commissioner.

Sec. 841.407. **REVOCATION OF CERTIFICATE OF AUTHORITY.** Requires TDI to revoke a subsidiary company's certificate of authority if the subsidiary company fails to maintain unimpaired paid-in capital and surplus in the amounts required under Section 841.405(a)(2).

Sec. 841.408. **DIVIDENDS AND DISTRIBUTIONS.** (a) Prohibits a subsidiary company from paying a dividend or distribution if the dividend or distribution:

(1) does not decrease the subsidiary company's unimpaired paid-in capital and surplus below the minimum amounts required under Section 841.405(a)(2); and

(2) does not impair the subsidiary company's ability to fulfill the subsidiary company's obligations under the reinsurance contract.

(b) Requires a subsidiary company to notify the commissioner at least 15 days before the subsidiary company issues a dividend or distribution. Requires that the notice include:

(1) the amount of the dividend or distribution to be issued; and

(2) a statement signed by an officer of the subsidiary company that the dividend or distribution meets the requirements of Subsection (a).

Sec. 841.409. **REQUIRED REPORTS AND NOTICE BY SUBSIDIARY COMPANY.**

(a) Requires a subsidiary company, not later than the 45th day after the closing date of a securitization, to provide the commissioner with a copy of a complete set of executed documents for the issuance of the securitization.

(b) Requires the subsidiary company, in the event of a material change in the financial condition or management of a subsidiary company, to notify the commissioner in writing not later than the fifth day after the date the material change occurs.

(c) Requires a subsidiary company to file with the commissioner:

(1) an annual actuarial opinion prepared by an actuary employed by the subsidiary company that complies with the requirements of Section 425.054 (Actuarial Opinion Required), regarding the subsidiary company's reserves for all risks assumed by the subsidiary company under the subsidiary company's reinsurance contract;

(2) a biennial actuarial opinion prepared by an independent actuary that complies with the rules of the commissioner, regarding the methods and assumptions used by the subsidiary company to set reserves; and

(3) an annual report of the subsidiary company's risk-based capital level as of the end of the preceding calendar year.

(d) Requires a subsidiary company to notify the commissioner immediately of any action by a domestic life insurance company or other person to foreclose on, or otherwise take possession of, collateral provided by the subsidiary company to secure an obligation of the subsidiary company.

(e) Provides that, notwithstanding Section 802.052 (Concurrent Filing with National Association of Insurance Commissioners) or any other law, a subsidiary company is not required to file a report, notice, or other document with the National Association of Insurance Commissioners unless required by the commissioner.

Sec. 841.410. PRIOR APPROVAL OF CERTAIN PAYMENTS. (a) Requires a subsidiary company to submit to the commissioner for prior approval a written request for authorization to make a payment of interest on, or a repayment of principal of, surplus notes and other debt obligations issued by the subsidiary company.

(b) Requires the commissioner to approve the payment described by Subsection (a) unless the commissioner determines that the payment would impair the ability of the subsidiary company or another person to fulfill the obligations of the subsidiary company or other person.

Sec. 841.411. SECURITIZATION AGREEMENTS. Requires that a document issued by a subsidiary company to prospective investors regarding the offer and sale of a surplus note or other security include a disclosure that all or part of the proceeds of the securitization will be used to fund the subsidiary company's obligations under a reinsurance contract with the domestic life insurance company that organized the subsidiary company.

Sec. 841.412. ADMITTED ASSETS. (a) Requires that the admitted assets of a subsidiary company include:

(1) proceeds from a securitization;

(2) a premium or other amount payable to the subsidiary company by the domestic life insurance company that organized the subsidiary company;

(3) a letter of credit;

(4) a guarantee of a parent company; or

(5) any other asset approved by the commissioner.

(b) Authorizes the commissioner, except as provided by Subsection (c), to reduce the amount of admitted assets previously approved by the commissioner, if the commissioner determines that the value of those assets has decreased.

(c) Prohibits the commissioner from reducing the amount of admitted assets previously approved by the commissioner if the asset is covered by the Accounting Practices and Procedures Manual of the National Association of Insurance Commissioners.

(d) Requires the commissioner to notify a subsidiary company at least 30 days before the commissioner reduces the amount of previously approved admitted

assets under Subsection (b). Requires that the notice provided by the commissioner under this subsection identify the reasons for the reduction and give the subsidiary company an opportunity to remedy any issues or deficiencies identified by the commissioner.

Sec. 841.413. LOANS. (a) Prohibits a subsidiary company from making a loan or an investment in another entity unless:

- (1) the commissioner first approves the loan or investment; and
- (2) the loan is evidenced by documentation approved by the commissioner.

(b) Authorizes a subsidiary company to issue a loan from the subsidiary company's minimum capital and surplus.

Sec. 841.414. SECURITIES. (a) Provides that a security issued by a subsidiary company is not subject to regulation as an insurance or reinsurance contract, and prohibits an investor or holder of a security issued by a subsidiary company from being considered to be conducting the business of insurance in this state solely by reason of having an interest in the security.

(b) Prohibits an underwriter's placement or selling agent, partner, commissioner, officer, member, manager, employee, representative, or advisor involved in an insurance securitization by a subsidiary company from being considered to be an insurance producer or broker, or to be conducting the business of insurance or reinsurance, solely by virtue of participating in underwriting activities relating to the securitization.

Sec. 841.415. CERTIFICATION OF ACTUARIAL OFFICER. (a) Requires the domestic life insurance company, at the time a domestic life insurance company files for a certificate of authority for a subsidiary company under Section 841.404, and by not later than the March 31 following the date on which the domestic life insurance company cedes business to the subsidiary company, to file with the commissioner a certification by a senior actuarial officer that the domestic life insurance company's transactions with a subsidiary company are not being used to an unfair advantage in the pricing of the domestic life insurance company's products.

(b) Prohibits a domestic life insurance company from being deemed as having an unfair advantage if the pricing of the policies and contracts reinsured by the subsidiary company:

- (1) reflects, at the time the policies and contracts were issued, a reasonable long-term estimate of the cost to the domestic life insurance company of an alternative third-party transaction; and
- (2) uses current pricing assumptions.

(c) Requires a domestic life insurance company to maintain documentation between examinations conducted under Subsection (a) that sets forth the methods by which the senior actuarial officer arrived at the conclusions in the certification.

SECTION 2. Effective date: January 1, 2012.