

BILL ANALYSIS

C.S.H.B. 2835
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Insurance
Committee Report (Substituted)

BACKGROUND AND PURPOSE

Currently, certain insurance companies and insurers organized under Texas law or authorized to engage in the business of insurance in Texas are subject to Insurance Code provisions relating to insurance holding company systems. The current Texas requirements are substantially similar to model legislation developed by the National Association of Insurance Commissioners (NAIC). Recently, the NAIC updated the model legislation in response to lessons learned from the nation's financial crises and discussions regarding group supervision that have been taking place in the international community. The updated model legislation addresses the needs of insurance regulators to be able to assess the enterprise risk within a holding company system and its potential impact on the solvency of an insurer within the holding company system and provides transparency in holding company system operations while building on the existing firewalls that provide insurance company solvency protection.

C.S.H.B. 2835 seeks to impose requirements on certain insurance companies and insurers relating to potential enterprise risks that may spread to insurance companies and negatively impact their financial condition. The bill attempts to provide the commissioner of insurance with enhanced access to information about the financial condition of insurance holding company systems, an enhanced framework for communication with other regulators, and enhanced examination authority.

RULEMAKING AUTHORITY

It is the committee's opinion that rulemaking authority is expressly granted to the commissioner of insurance in SECTIONS 5, 9, and 12 of this bill.

ANALYSIS

C.S.H.B. 2835 amends the Insurance Code to require that a disclaimer of affiliation with an authorized insurer filed with the commissioner of insurance be deemed to have been allowed unless, not later than 60 days after the receipt of a complete disclaimer, the commissioner notifies the filing party that the disclaimer is disallowed. The bill removes a provision of law relating to the insurer's duty to register or report as a member of an insurance holding company system on the disallowance of the disclaimer. The bill removes provisions of law making the authorization for the commissioner to disallow the disclaimer contingent on the commissioner providing to each party in interest notice of and the opportunity to be heard on the disallowance and making specific findings of fact to support a disallowance. The bill authorizes the commissioner to disallow the disclaimer if the commissioner at any time determines that the information disclosed in the disclaimer is incomplete or inaccurate or is no longer accurate. The bill authorizes the party who filed the disclaimer to request an administrative hearing if the commissioner disallows the disclaimer and requires the commissioner to grant the request for the hearing.

C.S.H.B. 2835 requires that information reported for purposes of registration as a member of an insurance holding company system or the examination of an insurer's financial condition or

legality of conduct be confidential and privileged for all purposes, rather than treated confidentially and not subject to subpoena. The bill makes the authorization for the commissioner or another person to disclose such information to certain entities functioning in an official capacity conditional on the recipient of the documents or other information agreeing in writing to maintain the confidential and privileged status of the documents or other information and verifying in writing the legal authority to maintain the confidential and privileged status of the documents or information. The bill includes among the entities to which the commissioner or other person is authorized to disclose such information a commissioner of insurance of another state and members of a supervisory college described by the bill.

C.S.H.B. 2835 authorizes the Texas commissioner of insurance to share confidential and privileged information reported in an insurer's annual enterprise risk report only with the commissioner of insurance of a state that has a statute or rule substantially similar to the previously described requirements relating to confidentiality and privilege of insurer information and who agrees in writing not to disclose the information. The bill specifies that information reported for the registration and examination purposes, including information in the possession of the National Association of Insurance Commissioners (NAIC), is confidential for all purposes, including for purposes of state open records law, a response to a subpoena, or discovery or admissibility in evidence in a civil action. The bill requires the commissioner to enter into written agreements with the NAIC regarding the sharing and use of such information and sets out requirements for the agreement. The bill prohibits provisions of law relating to the confidentiality of information reported for purposes of registration as a member of an insurance holding company system or the examination of an insurer's financial condition or legality of conduct from being construed to prevent the commissioner or the attorney general from using such information for any purpose with respect to which the commissioner or the attorney general is otherwise authorized to act, including a regulatory or other legal action. The bill provides that the commissioner remains solely responsible for the administration, execution, and enforcement of state law governing insurance holding company systems and that the commissioner's sharing of information does not constitute a delegation of regulatory or rulemaking authority.

C.S.H.B. 2835 authorizes the commissioner, with respect to any insurer registered as a member of an insurance holding company system, to participate in a supervisory college for a domestic insurer that is part of an insurance holding company system with international operations in order to determine the insurer's compliance with state law governing insurance holding company systems. The bill authorizes the commissioner to initiate the establishment of a supervisory college; clarify the membership and participation of other entities in the supervisory college; clarify the functions of the supervisory college and the role of other entities in the supervisory college; establish a group-wide supervisor; coordinate the ongoing activities of the supervisory college, including meetings, regulatory activities, and processes for information sharing; and establish a crisis management plan.

C.S.H.B. 2835 authorizes the commissioner, in order to assess the business strategy, financial position, legal and regulatory position, risk exposure, risk management and governance processes, and as part of the examination of individual insurers registered as members of an insurance holding company system, to participate in a supervisory college with other entities that regulate the insurer or its affiliates, including other state, federal, and international regulatory entities. The bill authorizes the commissioner to enter into agreements relating to the confidentiality of information to cooperate with other regulatory entities. The bill prohibits its provisions relating to supervisory colleges from being construed as delegating to the supervisory college the commissioner's authority to regulate the insurer or its affiliates.

C.S.H.B. 2835 requires a registered insurer for whom a supervisory college is convened to pay the reasonable expenses of the commissioner's participation in the supervisory college. The bill authorizes a supervisory college to be convened as either a temporary or permanent forum for communication and cooperation between the entities that regulate the insurer or its affiliates and authorizes the commissioner to establish a regular assessment to the insurer for the payment of

expenses related to the regulation of the insurer.

C.S.H.B. 2835 requires the registration statement required to be filed with the Texas Department of Insurance (TDI) by an insurer registering as a member of an insurance holding company system to be in a format prescribed by the NAIC or adopted by rule of the commissioner. The bill expands the required contents of the statement to include current information about the corporate governance and internal control responsibilities of the insurer's board of directors, including a statement that the insurer's senior management or officers have approved and implemented, and continue to maintain and monitor, corporate governance and internal control procedures and that the insurer's board of directors oversees corporate governance and internal controls, and any other information that the commissioner requires by rule.

C.S.H.B. 2835 requires an insurer, on the commissioner's request, to include with the statement a copy of all financial statements for the insurance holding company system and all affiliates of the holding company system, including annual audited financial statements filed with the United States Securities and Exchange Commission under federal law. The bill authorizes an insurer, including an insurer required to file certain information before acquiring, exercising, or initiating a divestiture of control of a domestic insurer, to satisfy the previously described financial statement requirement by submitting to the commissioner the financial statements that the insurer's parent corporation most recently filed with the Securities and Exchange Commission and, if the insurer is required to submit financial statements for an affiliate, the financial statements that the affiliate most recently filed with an agency that regulates the affiliate.

C.S.H.B. 2835 requires the ultimate controlling person of each insurer required to file an annual registration as a member of an insurance holding company system to file with the registration an annual enterprise risk report. The bill requires that the report, to the best of the ultimate controlling person's knowledge, identify the material risks within the insurance holding company system that may pose enterprise risk to the insurer. The bill requires that the report be filed with the lead state commissioner of the insurance holding company system, as determined by the commissioner. The bill requires the commissioner, in determining the lead state commissioner, to consider the procedures adopted by the NAIC.

C.S.H.B. 2835 adds temporary provisions, set to expire January 2, 2015, to require the ultimate controlling person of an insurer to file the first enterprise risk report with the first annual registration statement due after the following dates: January 1, 2013, if the total direct or assumed annual premiums of the insurer were \$5 billion or more during the preceding 12-month period; January 1, 2014, if the total direct or assumed annual premiums of the insurer were more than \$1 billion but less than \$5 billion during the preceding 12-month period; January 1, 2015, if the total direct or assumed annual premiums of the insurer were more than \$500 million but less than \$1 billion during the preceding 12-month period; or January 1, 2016, if the total direct or assumed annual premiums of the insurer were \$300 million or more but less than \$500 million during the preceding 12-month period.

C.S.H.B. 2835 specifies that the ultimate controlling person of an insurer with total direct or assumed annual premiums of less than \$300 million is not required to submit an enterprise risk report. The bill requires the ultimate controlling person of an insurer that is not in compliance with applicable risk-based capital standards or that is otherwise in hazardous condition, as determined by the commissioner, to file an enterprise risk report as directed by the commissioner, regardless of total direct or assumed annual premium. The bill authorizes an insurer or health maintenance organization that in the preceding calendar year had direct written and assumed premiums of more than \$300 million but less than \$500 million to request an exemption from the enterprise risk reporting requirements by filing with the commissioner a written statement describing the undue financial or organizational hardship the insurer or health maintenance organization would suffer as a result of complying with those requirements. The bill authorizes the commissioner to grant the exemption if the commissioner finds that compliance with the reporting requirements would impose an undue financial or organizational

hardship on the insurer or health maintenance organization.

C.S.H.B. 2835 prohibits TDI from implementing the bill's enterprise risk report provisions until the date that the commissioner determines that the NAIC has promulgated an enterprise risk form and has proposed a master confidentiality agreement and places notice of that determination in the Texas Register.

C.S.H.B. 2835 establishes that the failure to file an enterprise report within the time specified for filing the report is a violation of provisions of law relating to the registration of insurance holding company systems. The bill makes standards under provisions of law relating to transactions of registered insurers with an affiliate apply to a material transaction within an insurance holding company system to which an insurer subject to a registration under specified provisions of law is a party, rather than to a material transaction between a registered insurer and an affiliate of the insurer. The bill requires an agreement, including an agreement for cost-sharing, services, or management, to include all provisions required by rule of the commissioner.

C.S.H.B. 2835 specifies that provisions of law relating to notice of and the commissioner's decision on certain large transactions of a registered insurer are applicable to an amendment or modification of an affiliate agreement previously filed under those provisions of law. The bill requires the notice of certain large transactions given by a domestic insurer to the commissioner to include the reasons for entering into or changing the transaction and the financial impact of the transaction on the domestic insurer. The bill requires a domestic insurer, not later than the 30th day after the termination of a previously filed agreement, to give notice of the termination to the commissioner.

C.S.H.B. 2835 includes among the transactions and agreements for which written notice is required to be given by a domestic insurer to the commissioner before the insurer is authorized to enter such an agreement the following agreements: an amendment or modification of certain previously filed agreements, a pooling agreement between a domestic insurer and any person in the insurer's holding company system, and a tax-allocation agreement. The bill requires the notice given to the commissioner to include the reasons for entering into or changing the transaction and the financial impact of the transaction on the domestic insurer. The bill requires a domestic insurer, not later than the 30th day after the termination of a previously filed agreement, to give notice of the termination to the commissioner.

C.S.H.B. 2835 requires a person seeking to initiate a divestiture of control of a domestic insurer to meet the requirements under state law for the acquisition or exercise of control of a domestic insurer and adds to those requirements that a person initiating a divestiture of control file with the commissioner a notice of divestiture on a form adopted by the NAIC or adopted by the commissioner by rule. The bill establishes that a divesting person is not required to provide the commissioner that notice of divestiture if an acquiring person submits the acquisition statement required by law and that acquisition is approved by the commissioner.

C.S.H.B. 2835 makes provisions of law relating to the commissioner's approval of an acquisition of control apply to the approval of a change or divestiture of control and adds to the factors that the commissioner is required to consider in approving or denying a divestiture of control the consideration of whether the divestiture may jeopardize the financial stability of the domestic insurer or prejudice the interest of the domestic insurer's policyholders and other claimants. The bill authorizes the commissioner, if a proposed acquisition, change, or divestiture of control will require the approval of more than one commissioner, to participate in a public hearing referred to in state law governing insurance holding company systems held on a consolidated basis on request of the person filing the required acquisition statement with the commissioner.

C.S.H.B. 2835 requires the person filing the statement to file the statement with the NAIC within five days of making the request for a public hearing. The bill requires a hearing conducted on a consolidated basis to be public and held within the United States before the commissioners of the

states in which the insurers are domiciled. The bill requires the commissioners to hear and receive evidence at the hearing. The bill requires the Texas commissioner of insurance to attend the hearing in person or by telecommunication. The bill specifies that provisions of law relating to the approval of an acquisition, change, or divestiture of control do not require the commissioner to hold a hearing before approving or denying an acquisition, change, or divestiture of control.

C.S.H.B. 2835 requires an acquiring person to agree to provide the required annual enterprise report for as long as the acquiring person maintains control of the insurer. The bill requires an acquiring person and all subsidiaries within the acquiring person's control in the insurance holding company system to provide to the commissioner information on request of and as deemed necessary by the commissioner to evaluate enterprise risk to the insurer.

C.S.H.B. 2835 includes among the information papers that the commissioner is authorized to order an insurance holding company system to produce to ascertain the financial condition or legality of conduct of the insurer the enterprise risk to the insurer by the ultimate controlling party, or by any entity or combination of entities within the insurance holding company system, or by the insurance holding company system on a consolidated basis.

C.S.H.B. 2835 authorizes the commissioner to order any such registered insurer to produce information not in the possession of the insurer if the insurer can obtain access to the information under contractual relationships, statutory obligations, or other methods. The bill requires the insurer, in the event that the insurer is unable to obtain the information requested by the commissioner, to provide the commissioner with a detailed explanation of the reason why the insurer is unable to obtain the information and the identity of the holder of information. The bill authorizes the commissioner after notice and hearing, if it appears to the commissioner that the insurer's explanation is without merit, to require the insurer to pay a penalty of not less than \$100 for each day the insurer delays producing the information or to suspend or revoke the insurer's license.

C.S.H.B. 2835 authorizes the commissioner to issue subpoenas, administer oaths, and examine under oath any person for purposes of determining compliance with an examination of an insurer previously described. The bill authorizes the commissioner, on the failure or refusal of a person to obey a subpoena, to petition a court of competent jurisdiction and authorizes the court, on proper showing, to enter an order compelling the witness to appear and testify or produce documentary evidence. The bill establishes that failure to obey the court order is punishable as contempt of court. The bill requires a person to attend as a witness at the place specified in the subpoena, when subpoenaed, at any location in Texas and entitles such a witness to the same fees and mileage, if claimed, as a witness in district court. The bill requires that fees, mileage, and actual expenses necessarily incurred in securing the attendance of a witness be itemized and charged against, and be paid by, the insurer being examined.

C.S.H.B. 2835 specifies that, if it appears to the commissioner that a person has committed a violation of provisions of law relating to the control, acquisition, or merger of a domestic insurer that prevents the full understanding of the enterprise risk to the insurer by affiliates or by the insurance holding company system, the violation may serve as an independent basis for disapproving dividends or distributions and for issuing certain orders relating to the financial condition or supervision and conservatorship of an insurer.

C.S.H.B. 2835 defines "divesting person," "divestiture," and "enterprise risk." The bill redefines "insurer" to exclude from that term an agency, authority, or instrumentality of the United States, its possessions and territories, the Commonwealth of Puerto Rico, the District of Columbia, or a state or political subdivision of a state, rather than the United States, a state, or an agency, authority, instrumentality, or political subdivision of a state. The bill makes conforming and nonsubstantive changes.

EFFECTIVE DATE

September 1, 2011.

COMPARISON OF ORIGINAL AND SUBSTITUTE

C.S.H.B. 2835 differs from the original by authorizing the commissioner of insurance to disallow a disclaimer of affiliation with an authorized insurer if the commissioner determines that the information disclosed in the disclaimer is incomplete or inaccurate or is no longer accurate, whereas the original authorizes the commissioner to disallow the disclaimer if the commissioner determines that the information disclosed in the disclaimer is inaccurate or is no longer accurate.

C.S.H.B. 2835 differs from the original by specifying that information reported for purposes of registration as a member of an insurance holding company system or the examination of an insurer's financial condition or legality of conduct is confidential for purposes of discovery or admissibility in evidence in a civil action, whereas the original specifies such information is admissible in evidence in a private civil action. The substitute differs from the original by requiring the commissioner to enter into written agreements with the National Association of Insurance Commissioners (NAIC) regarding the sharing and use of information provided under provisions of law relating to insurance holding company systems, whereas the original specifies the sharing and use of information provided under provisions of law relating to the registration of members of such systems. The substitute differs from the original by making requirements for the written agreement applicable to information shared with the association and its affiliates and subsidiaries under provisions of law relating to insurance holding company systems, whereas the original makes such requirements applicable to such information under provisions of law relating to the confidentiality of such information. The substitute contains a provision not included in the original prohibiting those provisions of law relating to the confidentiality of such information from being construed to prevent the commissioner or the attorney general from using information reported for registration and examination purposes for any purpose with respect to which the commissioner or the attorney general is otherwise authorized to act.

C.S.H.B. 2835, in a provision setting out the information required to be in the registration statement required to be filed with the Texas Department of Insurance (TDI) by an insurer registering as a member of an insurance holding company system, contains a statement not included in the original that the insurer's board of directors oversees corporate governance and internal controls. The substitute differs from the original by requiring an insurer to include with the registration statement a copy of all financial statements for the insurance holding company system and all affiliates of the holding company system, whereas the original requires an insurer to include a copy of all financial statements for the insurance holding company system. The substitute contains a provision not included in the original authorizing an insurer who is required to submit financial statements for an affiliate to satisfy the financial statement requirement by submitting to the commissioner the financial statements that the affiliate most recently filed with an agency that regulates the affiliate.

C.S.H.B. 2835 differs from the original by requiring the annual enterprise risk report filed by the ultimate controlling person of each insurer to be filed with the lead state commissioner of the insurance holding company system as determined by the commissioner, whereas the original requires that determination to be made by the procedures adopted by the NAIC. The substitute contains a provision not included in the original requiring the commissioner, in determining the lead state commissioner, to consider the procedures adopted by the NAIC.

C.S.H.B. 2835 differs from the original by requiring the ultimate controlling person of an insurer to file the first enterprise risk report with the first annual registration statement due after January 1, 2013, January 1, 2014, January 1, 2015, or January 1, 2016, depending on the amount of the insurer's total direct or assumed annual premiums during the preceding 12-month period,

whereas the original requires the ultimate controlling person of an insurer to file the first enterprise risk report not later than January 1, 2012, January 1, 2013, January 1, 2014, or January 1, 2015, depending on the amount of the insurer's total direct or assumed annual premiums on September 1, 2011.

C.S.H.B. 2835 differs from the original by exempting from the enterprise risk reporting requirement the ultimate controlling person of an insurer with total direct or assumed annual premiums of less than \$300 million, whereas the original exempts such an ultimate controlling person with such premiums of less than \$100 million. The substitute contains provisions not included in the original authorizing an insurer or health maintenance organization that in the preceding calendar year had direct written and assumed premiums of more than \$300 million but less than \$500 million to request an exemption from the enterprise risk reporting requirements by filing a written statement with the commissioner regarding certain undue financial or organizational hardship the insurer or organization would suffer as a result of complying with the reporting requirements and authorizing the commissioner to grant the exemption on a finding relating to such compliance and hardship.

C.S.H.B. 2835 differs from the original by requiring an acquiring person to agree to provide the required annual enterprise risk report for as long as the acquiring person maintains control of the insurer, whereas the original requires an acquiring person who is also the ultimate controlling person to agree to provide the report in that manner. The substitute differs from the original by requiring all subsidiaries within the acquiring person's control in the insurance holding company system to provide information to the commissioner on request of and as deemed necessary by the commissioner to evaluate enterprise risk to the insurer, whereas the original requires all subsidiaries within the insurer's control in the insurance holding company system to provide such information.

C.S.H.B. 2835 differs from the original by including among the information papers that the commissioner is authorized to order an insurer registered as an insurance holding company system to produce to ascertain the financial condition or legality of conduct of the insurer certain enterprise risks to the insurer, whereas the original authorizes the commissioner to examine such an insurer and its affiliates to ascertain the financial condition or legality of conduct of the insurer, including such enterprise risk. The substitute omits a provision included in the original authorizing the commissioner to order such an insurer to produce records, books, or other information in the possession of the insurer or its affiliates as are reasonably necessary to determine compliance with provisions of law governing insurance holding company systems.

C.S.H.B. 2835 contains a provision not included in the original prohibiting TDI from implementing the substitute's enterprise risk report provisions until the date that the commissioner determines that the NAIC has promulgated an enterprise risk form and has proposed a master confidentiality agreement and places notice of that determination in the Texas Register.

C.S.H.B. 2835 differs from the original in nonsubstantive ways.