BILL ANALYSIS

C.S.S.B. 1217
By: Middleton
Insurance
Committee Report (Substituted)

BACKGROUND AND PURPOSE

The Texas Windstorm Insurance Association (TWIA) was created by the Texas Legislature in 1971 to serve as the "insurer of last resort" and provides windstorm and hail insurance coverages to residential and commercial properties in counties along the Texas coast that cannot find coverage elsewhere. Policyholders and other stakeholders in these counties contend that previous reforms of TWIA's operations to control rates and assert greater accountability over the agency greatly improved its administration. Despite these reforms, these policyholders and stakeholders still contend that additional reforms to the agency are needed to ensure that TWIA fulfills its vital public function as the insurer of last resort on the Texas Gulf Coast. Furthermore, policyholders in these coastal counties have raised concerns that TWIA's current funding structure is not sustainable. C.S.S.B. 1217 seeks to address these issues by implementing several reforms to improve the administration of TWIA and by creating a sustainable funding structure for TWIA to ensure its ability to meet its obligations to policyholders.

CRIMINAL JUSTICE IMPACT

It is the committee's opinion that this bill does not expressly create a criminal offense, increase the punishment for an existing criminal offense or category of offenses, or change the eligibility of a person for community supervision, parole, or mandatory supervision.

RULEMAKING AUTHORITY

It is the committee's opinion that rulemaking authority is expressly granted to the commissioner of insurance in SECTION 2.17 of this bill.

ANALYSIS

C.S.S.B. 1217 amends the Insurance Code and Government Code to revise provisions relating to the Texas Windstorm Insurance Association (TWIA).

Administration and Operation of the Texas Windstorm Insurance Association

C.S.S.B. 1217 prohibits TWIA from using any money under its control to attempt to influence the passage or defeat of a legislative measure. The bill subjects a TWIA employee or member of the board of directors who violates this prohibition to immediate termination and a fine of $10,000 to be deposited in the catastrophe reserve trust fund. These provisions of the bill expressly do not prohibit a TWIA employee or board member from using money under TWIA's control to provide public information or information responsive to a request for public information. The bill establishes that TWIA is not subject to any insurance premium tax or insurance maintenance fee or tax.

C.S.S.B. 1217 increases the total number of members of TWIA's board of directors appointed by the commissioner of insurance from nine to 11 and further revises the composition of the board by doing the following:

- increases from three to five the number of members who must, as of the date of the appointment, reside in the first tier coastal counties;
- clarifies that the first tier coastal county regions must, to the extent possible, be represented by a member residing in the region;
- increases from one to two the number of members who must be licensed property and casualty agents who are not captive agents; and
- removes the condition that the three members appointed based on their residency outside of the first tier coastal counties reside more than 100 miles from the Texas coastline and requires one of those members to be the public counsel of the office of public insurance counsel or their designated appointee.

The bill requires the commissioner, not later than December 1, 2023, to appoint two additional members to the board of directors of TWIA. Accordingly, the bill gives the option for the terms of four members, as an alternative to three members, to expire on the third Tuesday of March of each year. The bill establishes that the initial term of one of the appointed board members expires on the third Tuesday of March 2026 and the initial term of one of the appointed board members expires on the third Tuesday of March 2027. A member of the board of directors serving outside the first tier coastal counties is not required to be the public insurance counsel or the public insurance counsel's designee until the first vacancy that occurs on or after the effective date of the bill's provisions relating to the administration and operation of TWIA. The bill requires a TWIA board meeting, except for an emergency meeting, to be held at a location in a first tier coastal county or second tier coastal county as determined by the TWIA board of directors. The bill repeals the requirement for insurers who are members of TWIA to nominate, from among those members, persons to fill any vacancy in the three board of director seats reserved for representatives of the insurance industry.

C.S.S.B. 1217 prohibits TWIA from automatically adjusting the amount of coverage to be purchased by a policyholder and from adjusting premiums, fees, or any other costs to policyholders for inflation without a vote by the board of directors. The bill changes the annual deadline by which TWIA must file its proposed manual rates with the Texas Department of Insurance (TDI) from August 15 to September 15.

C.S.S.B. 1217 requires TWIA to file with TDI a proposed probable maximum loss, subject to statutory provisions relating to funding levels, reinsurance and alternative risk financing mechanisms, and the prohibition against purchasing reinsurance from certain insurers or brokers. The bill provides the following with respect to the determination of probable maximum loss for such purposes:

- TWIA may not consider the cost of providing loss adjustments;
- TWIA, to the extent possible, must contract with any disinterested third parties necessary to execute any catastrophe models that were executed in the preceding storm season;
- if unable to contract for the execution of such a catastrophe model, TWIA must contract with any disinterested third party necessary to execute a catastrophe model that is substantially similar to the model for which TWIA is unable to contract;
- TWIA may contract with any disinterested third parties to execute catastrophe models in addition to the required models;
- TWIA must provide to a disinterested third party executing a catastrophe model any information necessary to comply with these provisions relating to determination of probable maximum loss;
- TWIA may not use a combination of catastrophe models to determine the probable maximum loss; and
- TWIA may use only the catastrophe model that produces the lowest probable maximum loss.

The bill requires TWIA to make any information produced in compliance with the bill's provisions relating to the determination of probable maximum loss publicly available on TWIA's website. The bill restricts TWIA to using a probable maximum loss that is approved by the commissioner. The bill authorizes the commissioner to reject a probable maximum loss filed with TDI by TWIA and to set a probable maximum loss at any amount determined by the commissioner. The bill requires the amount of loss adjustment expense, as adopted by the TWIA board for a catastrophe year and used for TWIA's rate indication for purposes of rate filing, to be considered above the probable maximum loss.

C.S.S.B. 1217 repeals provisions regarding the administration of a depopulation program by TWIA that encourages the transfer of TWIA policies to insurers through the voluntary market or assumption reinsurance.

C.S.S.B. 1217 establishes that its provisions relating to the administration and operation of TWIA take effect on passage, or, if the bill does not receive the necessary vote, September 1, 2023.

Funding of Insured Losses and Operating Expenses of Texas Windstorm Insurance Association

Legislative Findings

C.S.S.B. 1217 sets out the following legislative findings:

- the use of public securities would not be an efficient or viable long-term method to fund TWIA losses for TWIA to continue providing insurance after a catastrophic event;
- previous experience has shown that the expense to TWIA of issuing public securities, and the interest rates for those securities, would be significant and can impose significant long-term expense obligations on coastal property and casualty risks that may be avoided if the legislature provides for financing or investment from available state money to TWIA before or after a catastrophic event;
- such financing or investment would be a more efficient way to provide funding necessary for TWIA to pay losses after a catastrophic event;
- a loan or other investment from available state money to TWIA of not more than $500 million before a catastrophic event and not more than $1 billion after a catastrophic event would do the following:
    - replace the funding levels currently provided by issuing public securities;
    - be consistent with sound insurance solvency standards;
    - provide a more viable method for TWIA to have money for losses after a catastrophic event than the issuance of public securities; and
    - provide a secured investment for the state that would yield interest income for the state on state money and be adequately secured for repayment through statewide catastrophe surcharges on certain insurance policies in Texas; and
- authorizing catastrophe surcharges is a more viable method to assure repayment of loans or investments of state money after a hurricane and to ensure that TWIA can continue to provide insurance after a catastrophic event to maintain TWIA's viability for the benefit of the public and in furtherance of a public purpose.

Payment of Losses

C.S.S.B. 1217 makes provisions relating to TWIA's payment of losses applicable only to TWIA's payment of losses and operating expenses for a catastrophe year that occurs before January 1, 2024, and results in excess losses and operating expenses incurred by TWIA before that date. The bill repeals such provisions effective September 1, 2025. The bill provides the following:

- the payment of TWIA's excess losses and operating expenses incurred after December 31, 2023, must be paid as provided by the bill; and
- proceeds of public securities issued, a financing arrangement entered into, or assessments made before January 1, 2024, or as a result of any occurrence or series of occurrences in a catastrophe year that occurs before January 1, 2024, and results in

of losses in a subsequent catastrophe year unless approved by the commissioner.

incurred losses before that date may not be included in reserves available for the payment of losses in a subsequent catastrophe year unless approved by the commissioner.

The bill authorizes TWIA to pay losses it would otherwise pay through public securities by borrowing from, or entering into other financing arrangements with, the state as provided under the bill's provisions regarding state-funded catastrophe financing arrangements and investment in windstorm catastrophe financing arrangements. The bill's provisions relating to a catastrophe surcharge apply to the financing of losses to the extent necessary to secure and repay a debt obligation to the state under such a financing arrangement. The financing arrangement may also be used to enable TWIA to pay losses or obtain public securities in the same manner as a financing arrangement with a market source.

C.S.S.B. 1217 sets out provisions regarding the method for paying TWIA's insured losses and operating expenses resulting from an occurrence or series of occurrences in a catastrophe year that occurs after December 31, 2023, that are incurred after that date and are in excess of TWIA's premium and other revenue. Accordingly, the bill does the following:

- prohibits TWIA from paying such insured losses and operating expenses with premium and other revenue earned in a subsequent year;
- requires TWIA to pay such insured losses and operating expenses from TWIA's reserves available before or accrued during that catastrophe year and amounts in the catastrophe reserve trust fund available before or accrued during that catastrophe year or, for such insured losses and operating expenses not paid from those reserves, requires TWIA to arrange for financing capped at $1 billion through one or more financing arrangements entered into with the state as provided by the bill;
- requires insured losses and operating expenses for a catastrophe year not paid from reserves or a financing arrangement to be paid from member assessments capped at $1 billion for that catastrophe year;
- requires the TWIA board of directors to notify each TWIA member of the member's assessment amount, which is determined by allocating a proportion of insured losses and operating expenses to each insurer in the same manner used to determine each insurer's participation in TWIA for the year;
- prohibits a member from recouping a paid assessment through a premium surcharge or tax credit;
- authorizes a member to purchase, before any occurrence or series of occurrences, reinsurance to cover an assessment for which the member would otherwise be liable;
- requires a member to notify the board of directors, in the manner prescribed by TWIA, whether the member will be purchasing reinsurance; and
- establishes that a member that does not purchase reinsurance remains liable for any applicable imposed assessment.

The bill adds a temporary provision set to expire September 1, 2025, specifying that these provisions apply only to the payment of TWIA's losses and operating expenses for a catastrophe year that occurs after December 31, 2023, and results in excess losses and operating expenses incurred by TWIA after that date. The bill requires the commissioner, as soon as practicable after the bill's effective date and not later than December 1, 2023, to adopt rules necessary to implement these provisions.

<u>Catastrophe Reserve Trust Fund and Reinsurance and Alternate Risk Financing</u>

C.S.S.B. 1217 does the following with regard to the catastrophe reserve trust fund:

- specifies that the money in the fund the comptroller of public accounts holds outside the state treasury on behalf of TDI is on behalf of TWIA;
- authorizes TWIA to include the amounts held in the fund as an admitted asset in TWIA's financial statements;
- authorizes the Texas Treasury Safekeeping Trust Company and TWIA board of directors to recommend investments to protect the fund and create investment income;

- removes the requirement that the cost of reinsurance purchased or alternative financing mechanisms used in excess of the amount needed to maintain a certain level of loss funding be paid by member assessments;
- authorizes TWIA to obtain reinsurance at any level including excess of loss, quota share, and other forms of reinsurance to protect the solvency and viability of TWIA;
- authorizes the commissioner to consult with the board of directors regarding methods to protect the solvency and continued viability of TWIA, including by protecting the minimum balance, acquiring reinsurance, or by other means; and
- authorizes the commissioner to adopt a method or approve TWIA's method of determining the probability of one in 100 for association risks and requires the commissioner to provide any adopted or approved method to TWIA on or before February 1 of each year.

Public Securities Program

C.S.S.B. 1217 repeals statutory provisions governing TWIA's public securities program effective September 1, 2025, and, to provide a reasonable transition, authorizes TWIA to issue public securities or enter into financing arrangements with the state as provided by the bill if TWIA needs to provide funds for excess losses and operating expenses incurred before January 1, 2024, for a catastrophe year occurring before that date. The bill prohibits TWIA from issuing public securities after December 31, 2023, except to fund excess losses and operating expenses incurred before January 1, 2024.

State-Funded Catastrophe Financing Arrangements

C.S.S.B. 1217 establishes that the legislature has determined that providing catastrophe funding to TWIA by permitting TWIA to enter into a financing arrangement with the state is an acceptable use of state money and provides an efficient method for the association to pay losses following a catastrophic event. The bill requires the proceeds of a catastrophe financing arrangement entered into with the state before a catastrophic event to be deposited to the catastrophe reserve fund. The bill authorizes TWIA to enter into a catastrophe financing arrangement with the state before a catastrophic event, for not more than $500 million, and after a catastrophic event that depletes the catastrophe reserve fund, for not more than $1 billion. The bill reduces the amount available for such an agreement after a catastrophic event by the amount of any outstanding pre-event or post-event financing obtained by TWIA.

Catastrophe Surcharges

C.S.S.B. 1217 authorizes the commissioner, in consultation with the board of directors, to order a catastrophe surcharge contingent on the following:

- before a catastrophic event, TWIA enters into a financing arrangement with the state that is the basis for the surcharge; or
- after a catastrophic event, the commissioner determines that TWIA has depleted its reserves, other money, and the catastrophe reserve trust fund and TWIA enters into a financing arrangement with the state that is the basis for the surcharge.

The bill provides the following with respect to the surcharge:

- the commissioner, in consultation with the board of directors, must set the catastrophe surcharge as a percentage of premium to be collected by each applicable insurer;
- the total surcharge is capped at the amount needed to repay the debt obligation to the state under the financing arrangement that is the basis for the surcharge;
- the surcharge percentage must be set in an amount sufficient to repay the debt obligation to the state under the financing arrangement that is the basis for the surcharge and the commissioner may set the surcharge as a percentage of premium to collect the needed aggregate amount over a period of time not to exceed three years;
- the surcharge must be assessed by insurers on all applicable policyholders;

- surcharge proceeds must be deposited into the catastrophe reserve trust fund or an account designated by the comptroller for purposes of repayment of TWIA's debt obligation to the state under the financing arrangement that is the basis for the surcharge;
- the surcharge is a separate charge in addition to the premiums collected and is not subject to premium tax or commissions;
- failure by a policyholder to pay the surcharge constitutes failure to pay premium for purposes of policy cancellation; and
- the surcharge is not refundable if the policy is canceled or terminated.

The bill defines "catastrophic event" as an occurrence or a series of occurrences that occurs in a catastrophe area during a calendar year and results in insured losses and operating expenses of the association in excess of premium and other revenue of the association.

C.S.S.B. 1217 makes its surcharge provisions applicable to the following insurers:

- an insurer authorized to engage in the business of insurance in Texas that is required to be a member of TWIA, including a farm mutual insurance company that is a fronting insurer;
- a farm mutual insurance company that is not a fronting insurer only for purposes of the surcharge collection;
- an unaffiliated eligible surplus lines insurer writing the lines of business subject to the surcharge;
- TWIA; and
- the FAIR Plan Association.

The bill specifies the types of policies to which it applies and requires each policy that is assessed a surcharge to contain a prominent disclosure of the surcharge, as specified by the bill, in the documents attached to the policy. In addition, the bill does the following:

- prohibits its provisions regarding the catastrophe surcharge from being construed to require an insurer to be a TWIA member if the insurer is not otherwise required to be a member;
- clarifies that a farm mutual insurance company that is not a fronting insurer is not a TWIA member as a result of the company's collection of catastrophe surcharges or for any other reason;
- exempts a surcharge from state or local taxation;
- provides for a limitation on personal liability for an individual or entity exercising rights and responsibilities granted under the bill's surcharge provisions; and
- prohibits an insurer from collecting the surcharge on any policy issued to the state, a state agency, or a political subdivision of the state.

C.S.S.B. 1217 requires the commissioner to determine the amount available in the catastrophe reserve trust fund as of December 31 of each year and provide a written report to the governor, lieutenant governor, and speaker of the house of representatives that includes the amount available in the fund and information regarding TWIA's current financial condition. The bill requires the commissioner, as soon as practicable after the bill's effective date and not later than December 1, 2023, to adopt rules necessary to implement the bill's surcharge provisions.

Investment in Windstorm Catastrophe Financing Arrangements

C.S.S.B. 1217 requires the comptroller to invest state money to provide financing for TWIA losses in accordance with the bill and the Texas Windstorm Insurance Association Act. The bill authorizes the comptroller to enter into an appropriate financing arrangement with TWIA to provide TWIA up to $500 million in funding before a catastrophic event and up to $1 billion in funding after a catastrophic event, the financing of which must be secured and repaid by catastrophe surcharges, to fund TWIA losses arising from the catastrophic event. The bill caps the interest rate that may be included in the terms of such a financing arrangement at the sum of two percent and the lesser of either the rate set by the Federal Housing Finance Agency or the federal funds rate specified under the Uniform Commercial Code--Funds Transfers. The bill prohibits a debt obligation entered into for such a financing arrangement from exceeding 36 months to maturity.

C.S.S.B. 1217 authorizes the comptroller, directly or indirectly through a separately managed account or other investment vehicle, to use up to $1 billion of the Economic Stabilization Fund, otherwise known as the Rainy Day Fund, to provide financing under these financing arrangement provisions. The bill caps at $1 billion the aggregate amount of outstanding pre-event and post-event financing provided under an applicable financing arrangement.

Transition Provisions

C.S.S.B. 1217 makes statutory provisions pertaining to the use of TWIA assets, the board of directors' duty to call an emergency meeting, premium discounts and surcharge credits, use of the catastrophe reserve trust fund, and reinsurance applicable to the bill's provisions regarding the payment of losses incurred after December 31, 2023, and regarding a catastrophe surcharge in the same manner as provisions repealed by the bill regarding payment of losses incurred before January 1, 2024, and regarding the public securities program, respectively. The bill establishes the following:

- the payment of TWIA's excess losses and operating expenses incurred before January 1, 2024, is governed by the law as it existed on the bill's effective date and that law is continued in effect for that purpose;
- the issuance of public securities to pay TWIA's excess losses and operating expenses incurred before January 1, 2024, the use of the proceeds of those securities, the repayment or refinancing of those securities, and any other rights, obligations, or limitations with respect to those securities and proceeds are governed by the law as it existed on the bill's effective date and that law is continued in effect for that purpose; and
- proceeds of any assessments made for a catastrophe year that occurs before January 1, 2024, may not be included in reserves available for a catastrophe year that occurs after December 31, 2023, unless approved by the commissioner.

Repealed Provisions

C.S.S.B. 1217 repeals the following provisions of the Insurance Code:

- Section 2210.102(f); and
- Subchapter O, Chapter 2210.

Effective September 1, 2025, C.S.S.B. 1217 repeals the following provisions of Chapter 2210, Insurance Code:

- Subchapter B-1; and
- Subchapter M.

EFFECTIVE DATE

Except as otherwise provided, September 1, 2023.

COMPARISON OF SENATE ENGROSSED AND SUBSTITUTE

While C.S.S.B. 1217 may differ from the engrossed in minor or nonsubstantive ways, the following summarizes the substantial differences between the engrossed and committee substitute versions of the bill.

While both the engrossed and substitute include provisions relating to the administration and operation of TWIA, the substitute includes provisions absent from the engrossed relating to the funding of excess losses and operating expenses of TWIA. Specifically, the substitute includes the following provisions that were absent from the engrossed:

- related legislative findings;
- provisions establishing the applicability of provisions relating to payment of losses by TWIA;
- a specification that the catastrophe year for which excess losses and operating expenses are to be paid as provided by provisions relating to the payment of losses is a catastrophe year before January 1, 2024;
- a provision establishing that proceeds of public securities issued, a financing arrangement entered into, or assessments made before January 1, 2024, or as a result of any occurrence or series of occurrences in a catastrophe year that occurs before January 1, 2024, and results in incurred losses before that date may not be included in reserves available for the payment of losses in a subsequent catastrophe year unless approved by the commissioner;
- an authorization for TWIA to pay certain losses by borrowing from, or entering into financing arrangements with the state;
- provisions regarding the method for paying TWIA's insured losses and operating expenses resulting from an occurrence or series of occurrences in a catastrophe year that occurs before December 31, 2023, that are incurred after that date and are in excess of TWIA's premium and other revenues;
- a specification that the money in the fund the comptroller holds outside the state treasury on behalf of TDI is on behalf of TWIA;
- an authorization for TWIA to include the amounts held in the fund as an admitted asset in TWIA's financial statements;
- an authorization for the Texas Treasury Safekeeping Trust Company and the TWIA board of directors to recommend investments to protect the catastrophe reserve trust fund and create investment income;
- provisions relating to an authorization for TWIA to obtain reinsurance to protect the solvency and viability of TWIA and relating to a method of determining certain risks;
- provisions relating to state-funded catastrophe financing arrangements;
- provisions relating to a catastrophe surcharge;
- provisions relating to investment in windstorm catastrophe financing arrangements; and
- a provision repealing the following:
    - statutory provisions relating to TWIA's payment of losses following an occurrence or series of occurrences in a catastrophe area resulting in insured losses and operating expenses in excess of TWIA premium and other revenue; and
    - statutory provisions governing TWIA's public securities program.

Accordingly, the substitute includes applicable conforming, transition, and saving provisions, which did not appear in the engrossed.

The substitute omits the provision from the engrossed that required TWIA's headquarters to be located in a first or second tier coastal county.

The substitute includes a provision absent from the engrossed repealing Subchapter O, Chapter 2210, Insurance Code, which relates to the administration of a depopulation program by TWIA.

The substitute does not include a provision establishing that the bill's provisions regarding the administration and operation of TWIA apply to TWIA beginning on January 1, 2025, which was present in the engrossed.

Whereas the engrossed provided for the bill to take effect on passage, or, if the bill did not receive the necessary vote, on September 1, 2023, the substitute instead provides for the bill to take effect on September 1, 2023, except as otherwise provided by the substitute.