

SENATE STAFF ANALYSIS AND ECONOMIC IMPACT STATEMENT

(This document is based on the provisions contained in the legislation as of the latest date listed below.)

BILL: CS/SB 1464

SPONSOR: Commerce, Economic Opportunities, and Consumer Services Committee and Senator Bennett

SUBJECT: Mutual Insurance Holding Companies

DATE: April 23, 2003 REVISED: _____

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	Knudson	Deffenbaugh	BI	Fav/1 amendment
2.	Kruse	Maclure	CM	Favorable/CS
3.	_____	_____	_____	_____
4.	_____	_____	_____	_____
5.	_____	_____	_____	_____
6.	_____	_____	_____	_____

I. Summary:

Committee Substitute for Senate Bill 1464 revises several provisions in ch. 628, F.S., relating to mutual insurance holding companies. The committee substitute provides that, at the time of formation of a mutual insurance holding company, policyholders of any subsidiary insurance company of a mutual insurance holding company may not be members of the mutual insurance holding company being formed unless they are policyholders of a subsidiary which was a mutual insurer which merged with the holding company being formed. The committee substitute provides that the membership of the mutual insurance holding company following formation is governed by s. 628.727, F.S. The committee substitute also clarifies that a person may be a member of a mutual insurance holding company by holding a health maintenance contract with a subsidiary health maintenance organization.

The committee substitute provides that the mechanism for a mutual insurance holding company owning solely life and health insurance subsidiaries to determine the distributive shares for each member upon dissolution, merger, or conversion of the company shall be by a formula based upon a reasonable classification of members as the Department of Insurance may approve. For any other kind of mutual insurance holding company, the committee substitute, utilizing a definition of the term "paid premiums" created in the committee substitute, provides a formula for determining a member's share of assets on the voluntary dissolution of the company, the formula for the distributive share of each member when the company merges with an intermediate holding company, and the formula for determining the corporate equity of each member when the company converts to a stock holding company. The formula compares the amount of premiums each member of the mutual insurance holding company paid during the 3 years prior to the merger, conversion, or dissolution of the mutual holding company, to the total amount of premiums paid by all members of the mutual holding company during the same 3-year

period. The committee substitute provides the option to a company to submit a fair formula to the department for approval in lieu of the formula in the committee substitute.

This committee substitute substantially amends the following sections of the Florida Statutes: 628.703, 628.709, 628.727, 628.729, 628.730, and 628.733.

II. Present Situation:

Mutual Insurance Holding Companies

A mutual insurance holding company is a form of domestic insurance corporate organization established as an alternative method for a domestic mutual (policyholder-owned) insurance company to convert to a stock (stockholder-owned) insurance company. Section 628.703(1), F.S., defines a “mutual insurance holding company” as an incorporated entity without permanent capital stock that is organized under part III of ch. 628, F.S., and whose members are determined in accordance with that part. Membership in a mutual insurance holding company must be determined in accordance with the mutual insurance holding company’s articles of incorporation and bylaws and is based upon each member holding a policy of insurance with a subsidiary insurance company or subsidiary health service corporation.¹ Section 628.441, F.S., provides the authority to convert a domestic mutual insurance company into a stock insurance company. There are several advantages to converting into a stock insurance company, including that the conversion may significantly enhance an insurer’s ability to raise capital, issue debt, and engage in mergers and acquisitions.

Formation of a Mutual Insurance Holding Company

A domestic mutual insurance company, other than a mutual insurer that issued assessable policies as a mutual insurer and which held a certificate of authority in this state on July 1, 1997, may convert into a mutual insurance holding company system with a controlled subsidiary which may consist of one or more intermediate stock holding company subsidiaries and other subsidiaries,² subject to the approval of the Department of Insurance.³ Section 628.703(2), F.S., defines “subsidiary insurance company” to mean a stock insurance company, the majority of the voting shares of the capital stock of which are at all times owned by a mutual insurance holding company. “Intermediate holding company” is defined in s. 628.703(3), F.S., as a holding company which is a subsidiary of a mutual insurance holding company, and which directly or through a subsidiary intermediate holding company owns a majority of the voting shares of the capital stock of one or more subsidiary insurance companies. The policyholders of the former domestic mutual insurance company become members of the mutual holding company in accordance with the articles of incorporation and bylaws of the mutual insurance holding company. The membership interests of the policyholders of the subsidiary insurance company become membership interests in the mutual insurance holding company. Policyholders of any other subsidiary insurance company of the mutual insurance holding company may not be

¹ Section 628.727(1), F.S.

² Section 628.709(1), F.S.

³ Effective January 7, 2003, the Department of Insurance was transferred to the Department of Financial Services and to the Office of Insurance Regulation. (ch. 2002-404, L.O.F.) Conforming changes are made in CS/CS/SB 1712. The Office of Insurance Regulation is now responsible for all matters related to the regulation of insurers.

members of the mutual insurance holding company unless they are policyholders of a subsidiary which was a mutual insurer which merged with the holding company pursuant to s. 628.715, F.S.⁴ Once the conversion occurs, it is the subsidiary stock insurance company (or an intermediate stock holding company owned by the mutual holding company) that is able to issue stock, incur debt, and engage in mergers and acquisitions without certain restrictions that limit the flexibility of mutual insurance holding companies.

Several provisions ensure that the members of the mutual insurance holding company will retain control of the newly reorganized insurer. The mutual insurance holding company must have the power to cast at least a majority of votes for election of the board of directors of each subsidiary or intermediate holding company.⁵ All of the initial stock in the new subsidiary stock insurance company must be issued either to the mutual holding company or to a wholly owned intermediate holding company. The insurance company may subsequently issue additional stock, as long as the mutual holding company directly or indirectly owns a majority of the voting shares.⁶

The Department of Insurance may only approve the reorganization plan if the department finds that the plan is fair and equitable to the mutual policyholders.⁷ The plan is then submitted to the members of the mutual insurance company, and the affirmative vote of a majority of the members is required for approval.⁸

Merger of a Mutual Insurance Holding Company with an Intermediate Holding Company

A mutual insurance holding company may merge into its intermediate holding company. When a merger occurs, the intermediate holding company assumes all the assets and liabilities of the mutual insurance holding company. All stock of the intermediate holding company owned by the old mutual insurance holding company is then distributed to all living persons who were members of the mutual insurance holding company within the 3 years prior to the merger.⁹

Conversion of a Mutual Insurance Holding Company to a Stock Holding Company

A mutual insurance holding company may also convert into a stock holding insurance company. The statute sets forth various criteria that the merger must meet in order for the Department of Insurance to approve the merger. The criteria ensure that the conversion is approved by a majority of the policyholders voting on the issue and that each member's corporate equity in the new stock company is computed fairly by a formula approved by the department, and include other provisions relating to the fair distribution of corporate stocks or equity to members.¹⁰

⁴ Section 628.709(2), F.S.

⁵ Section 628.709(1), F.S.

⁶ *Id.* at (2).

⁷ Section 628.711(4), F.S.

⁸ *Id.* at (5)(b).

⁹ Section 628.730(1), F.S.

¹⁰ Section 628.733, F.S.

Voluntary Dissolution of a Mutual Insurance Holding Company

When a mutual insurance holding company proceeds through a voluntary dissolution, any assets remaining after the discharge of its indebtedness, and expenses of administration, must be distributed to existing persons who were its members at any time within the 3-year period preceding the date the liquidation was authorized or ordered, or the date of last termination of the insurer's certificate of authority, whichever date is earlier. However, if the department has reason to believe that the management of the mutual insurance holding company has caused or encouraged the reduction of the number of members of the insurer in anticipation of liquidation and for the purpose of reducing the number of persons who may be entitled to share in distribution of the insurer's assets, the department may enlarge the 3-year qualification period by such additional time as the department deems to be reasonable.¹¹

III. Effect of Proposed Changes:

Section 1 adds subsection (4) to s. 628.703, F.S., by defining the term "paid premiums" to mean all premiums paid for insurance by a member of a mutual insurance holding company to a subsidiary insurance company. This definition is incorporated into sections 4, 5, and 6 of the committee substitute through the use of the term "paid premiums" in those sections.

Section 2 amends s. 628.709(2), F.S., to state that "at the time of formation" of a mutual insurance holding company, policyholders of any other subsidiary of the mutual insurance holding company cannot be members of the mutual insurance holding company. Current law does not allow a policyholder of any subsidiary insurance company of a mutual insurance holding company to be a member of the mutual insurance holding company *at any time* unless the person was a policyholder of a subsidiary which was a mutual insurer that merged with the holding company. This new language may only prevent membership in the mutual insurance holding company by a policyholder of a subsidiary *at the time of formation* of the mutual insurance holding company.

However, the committee substitute also mandates that after a mutual insurance company is formed, membership in the company is to be governed by s. 628.727, F.S. This requirement will allow membership after formation to be determined by the mutual insurance holding company's articles of incorporation and bylaws, and membership must also be based upon each member holding a policy of insurance with a subsidiary insurance company or subsidiary health service corporation.¹²

Section 3 amends s. 628.727(1), F.S., by clarifying that a subsidiary health service corporation is a subsidiary health maintenance organization.

Section 4 amends s. 628.729, F.S., relating to a member's share of assets upon the voluntary dissolution of a mutual insurance holding company. For a mutual insurance holding company owning solely life and health insurance subsidiaries, the distributive share for a member is determined by a formula based upon such reasonable classifications of members as the

¹¹ Section 628.729, F.S.

¹² Section 628.727(1), F.S.

Department of Insurance may approve. For all other mutual insurance holding companies, the distributive share is determined either by a formula based upon the ratio that the total amount of paid premiums paid by such member for policies of insurance during the 3-year period or part of such period during which such recipient was a member bears to the total amount of paid premiums paid by all members entitled to receive a distributive share as a result of the dissolution during such entire 3-year period, or by a fair formula submitted by the company to the department for approval. The committee substitute does not provide criteria to a company to determine what may be considered a fair formula by the department. Under current law, the department approves the classifications of members and may set the formula to calculate a member's distributive share. The department has stated that, under current law, a mutual insurance holding company may submit a proposed formula to the department for approval.

An example of the distributive share calculation using the formula in the committee substitute would be if member X of the insurance holding company paid \$5,000 in premiums over the 3 years prior to dissolution, and all qualified members paid \$500,000,000, then member X would be entitled to 1:100,000 of the dissolved company's assets.

Section 5 amends s. 628.730, F.S., to provide a formula for calculating the distributive share of each member after the merger of a mutual insurance holding company with an intermediate holding company. For a mutual insurance holding company owning solely life and health insurance subsidiaries, the distributive share for a member is determined by a formula based upon such reasonable classifications of members as the Department of Insurance may approve. For all other mutual insurance holding companies, the distributive share is determined either by a formula based upon the ratio that the total amount of paid premiums paid by such member for policies of insurance during the 3-year period or part of such period preceding the date of the merger during which the recipient was a member bears to the total amount of paid premiums paid by all members entitled to receive a distributive share as a result of such merger during such entire 3-year period, or by a fair formula submitted by the company to the department for approval. The committee substitute does not provide criteria to a company to determine what may be considered a fair formula by the department. Under current law, the department approves the classifications of members and sets the formula.

Section 6 amends s. 628.733, F.S., to provide a formula for calculating the corporate equity of each member when a mutual insurance holding company is converted into a stock holding company. For a mutual insurance holding company owning solely life and health insurance subsidiaries, the distributive share for a member is determined by a formula based upon such reasonable classifications of members as the Department of Insurance may approve, which equity may be based upon not more than the company's net assets. For all other mutual insurance holding companies, the distributive share is determined by a formula based upon the ratio that the total amount of paid premiums paid by such member during the 3-year period or part of such period during which such recipient was a member bears to the total amount of paid premiums paid by all members entitled to receive equity as a result of such conversion during such entire 3-year period and upon such reasonable classifications of members as the department may approve, unless the company submits another fair formula that is approved by the department. The committee substitute does not provide criteria to a company to determine what may be considered a fair formula by the department. The equity may not be based upon more than the company's net assets. In this case, current law does not allow the department to approve the

classifications of members but provides that the equity of each member is determined under a fair formula approved by the department, which equity must be based upon not more than the company's assets.

Section 7 provides that this act shall take effect upon becoming a law.

IV. Constitutional Issues:

A. Municipality/County Mandates Restrictions:

None.

B. Public Records/Open Meetings Issues:

None.

C. Trust Funds Restrictions:

None.

V. Economic Impact and Fiscal Note:

A. Tax/Fee Issues:

None.

B. Private Sector Impact:

The ratios used to calculate each member's share upon the conversion, merger, or dissolution of a mutual insurance holding company may create an equitable balance between long-standing and newer members of a mutual insurance holding company. Using a 3-year period to calculate each member's share may allow new members of the holding company to receive an equitable share of stock or company assets under the ratio, while ensuring that long-time members who have paid more in premiums receive a greater share than new members who have been with the company for less than 3 years. The committee substitute also allows a company to submit a formula to the Department of Insurance for approval if the company does not want to utilize the formula in the committee substitute.

C. Government Sector Impact:

None.

VI. Technical Deficiencies:

None.

VII. Related Issues:

None.

VIII. Amendments:

None.

This Senate staff analysis does not reflect the intent or official position of the bill's sponsor or the Florida Senate.
