

The Florida Senate
BILL ANALYSIS AND FISCAL IMPACT STATEMENT

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

Prepared By: The Professional Staff of the Committee on Judiciary

BILL: CS/SB 836

INTRODUCER: Banking and Insurance Committee and Senator Simmons

SUBJECT: Insurer Solvency

DATE: April 12, 2013 REVISED: _____

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	Johnson	Burgess	BI	Fav/CS
2.	Munroe	Cibula	JU	Favorable
3.			RC	
4.				
5.				
6.				

Please see Section VIII. for Additional Information:

A. COMMITTEE SUBSTITUTE..... Statement of Substantial Changes

B. AMENDMENTS..... Technical amendments were recommended

Amendments were recommended

Significant amendments were recommended

I. Summary:

CS/SB 836 revises provisions within the Insurance Code relating to solvency requirements and regulatory oversight of insurers by the Office of Insurance Regulation (OIR). The bill incorporates provisions of model acts and regulations that have been adopted by the National Association of Insurance Commissioners (NAIC).¹ Some of these provisions in the bill are in response to the 2008 financial crisis and the globalization of the insurance market and are intended to enhance the regulation of insurers as well as their affiliated entities and provide more solvency tools for evaluating risks within insurance groups. The bill provides the following changes:

- Requires acquirers of controlling interests to disclose enterprise risk, and requires that ultimate controlling persons must file an annual enterprise risk report with the OIR that identifies material risk within the insurance company holding company system that could pose a risk or have a material adverse effect upon the insurer;

¹ The NAIC is a voluntary association of insurance regulators from all 50 states. The NAIC was created to coordinate regulation and examination of multistate insurers, provide a forum for addressing major insurance issues, and promote uniform model laws among the states.

- Requires insurance holding companies to file an annual registration statement, including disclosure of material risks between affiliates;
- Allows the OIR to examine an insurer and its affiliates to assess enterprise risk;
- Incorporates a risk-based capital trend test for life and health and property and casualty insurers;
- Requires health maintenance organizations and prepaid limited health service organizations to file risk-based capital reports;
- Requires insurers to file actuarial opinion summaries and supporting workpapers annually;
- Provides a privilege for memoranda supporting actuarial opinions on reserves, actuarial opinion summaries and related information and provides for confidentiality of enterprise risk reports and actuarial opinion summaries;
- Authorizes the OIR to impose sanctions for noncompliance with the requirements of s. 628.461, F.S., and s. 628.801, F.S.; and
- Allows the OIR to participate in supervisory colleges with other regulators for the regulation of any domestic insurer that is part of an insurance holding company system with international operations.

As a member of the NAIC, the OIR is required to participate in the Financial Regulation Standards and Accreditation Program. For purposes of the NAIC Fall Accreditation Review, the OIR has identified model provisions or updates that are not found in the current Insurance Code that must be implemented or updated for the OIR to maintain accreditation.² The adoption of the Property and Casualty Trend Test of the Risk-Based Capital Model Act and the Property and Casualty Actuarial Opinion Model Law are necessary for purposes of accreditation in the fall 2013 since the accreditation effective dates for these provisions were January 1, 2012, and January 1, 2010, respectively. In addition, two other NAIC model acts, Risk-Based Capital for Health Organizations and the Life Trend Test of the Risk Based Capital Model Act are necessary for accreditation effective January 1, 2015, and January 1, 2017, respectively. The accreditation effective date for amendments to the Insurance Holding Company System Regulatory Act is tentatively set for January 1, 2016.

This bill substantially amends the following sections of the Florida Statutes: 624.4085, 624.424, 625.121, 628.461, 628.801, 628.803, 628.461, 636.045, 641.225, and 641.255. This bill creates the following sections of the Florida Statutes: 624.085 and 628.805.

II. Present Situation:

Insurance companies are regulated primarily by the states. The state of domicile serves as the primary regulator for insurers. Solvency regulation is designed to protect policyholders against the risk that insurers will not be able to meet their financial responsibilities. The OIR³ is primarily responsible for monitoring the solvency of regulated insurers and examining insurers to determine compliance with applicable laws, and taking administrative action, if necessary. Solvency regulation includes the requirements for starting and operating an insurance company,⁴ monitoring the financial condition of insurers through examinations and audits, and procedures

² OIR NAIC Model Act Accreditation Effective Date Chart. On file with Banking and Insurance Committee Staff.

³ Section 20.121(3)(a), F.S.

⁴ Sections 624.411 - 624.414, F.S.

for the administrative supervision,⁵ rehabilitation,⁶ or liquidation⁷ of an insurance company if it is in unsound financial condition or insolvent.

NAIC Solvency-Related Model Acts

The NAIC accreditation is a certification that legal, financial, and organizational standards are being fulfilled by the OIR. The NAIC establishes accreditation effective dates for states to adopt in substantially similar form models and acts for purposes of NAIC accreditation review.

Model Holding Company Act and Regulations

The NAIC has adopted amendments to its Insurance Holding Company System Regulatory Model Act and the Insurance Holding Company Model Regulation with Reporting Forms and Instructions. In light of the recent financial crisis, the NAIC, insurance regulators, and other stakeholders reviewed the potential impact of non-insurance operations on insurance companies in the same group to determine the best methods to evaluate the risks and activities of entities within a holding company system. The amendments to these model acts are tentatively scheduled to be effective for purposes of accreditation on January 1, 2016. The revised model act adds the concept of “enterprise risk” and requires controlled insurers to file a new annual form (Form F) detailing specified matters relating to the holding company group. The NAIC model act defines “enterprise risk” as:

[A]ny activity, circumstance, event, or series of events involving one or more affiliates of an insurer that, if not remedied promptly, is likely to have a material adverse effect upon the financial condition or liquidity of the insurer of its insurance company as a whole, including, but not limited to, anything that would cause the insurer’s risk-based capital as set forth in [state requirement] or would cause the insurer to be in a hazardous financial condition.⁸

Amendments to the model act also address divestitures. Prior to the amendments to the model act, a person could divest control of an insurer without prior regulatory review as long as no single acquirer obtained control of 10 percent or more of the outstanding voting shares. Amendments to the model act generally require a person divesting control over an insurer to provide 30 days’ prior notice to the regulator.

The revised model act also provides insurance regulators access to information of an insurer and its affiliates to ascertain the financial condition of the insurer, including the enterprise risk to the insurer by the ultimate controlling party. The regulator may require any insurer registered as a controlled insurer to produce information not in the possession of the insurer if the insurer can obtain access to such. If the insurer fails to obtain the requested information, the insurer is required to provide an explanation of such failure. If the regulator determines that the

⁵ Administrative supervision allows the Department of Financial Services (DFS) to supervise the management of a consenting troubled insurance company in an attempt to cure the company’s troubles rather than close it down.

⁶ In rehabilitation, the DFS is authorized as receiver to conduct all business of the insurer in an attempt to place the insurance company back in sound financial condition.

⁷ In liquidation, the DFS is authorized as receiver to gather the insurance company’s assets, convert them to cash, and distribute them to various claimants, and shut down the company.

⁸ Section 1F of the NAIC Insurance Holding Company System Regulatory Act.

explanation is without merit, the regulator may require the insurer to pay a penalty for each day's delay, or may suspend or revoke the insurer's certificate of authority.⁹

The amendments to the model acts also authorize a regulator to participate in a supervisory college for any domestic insurer that is part of an insurance holding company system with international operations in order to determine compliance. Insurers would pay for expenses associated with the insurance regulator's participation in a supervisory college. State, federal, and international regulators may participate in the supervision of the insurer or its affiliates.¹⁰ According to the NAIC Center for Insurance Policy & Research, "a supervisory college is a meeting of insurance regulators or supervisors where the topic of discussion is regulatory oversight of one specific insurance group that is writing significant amounts of insurance in other jurisdictions."¹¹ Supervisory colleges facilitate oversight of internationally active insurance companies at the group level and promote regulatory information sharing, subject to applicable confidentiality agreements.¹²

Risk-Based Capital for Insurers & Health Organizations

Risk-based capital (RBC) is a capital adequacy standard that represents the amount of required capital that an insurer must maintain, based on the inherent risks in the insurer's operations. It is determined by a formula that considers various risks depending on the type of insurer (e.g., subsidiary insurance companies, fixed income, equity, credit, reserves, and net written premium). The RBC provides a safety net for insurers, is uniform among states, and provides state insurance regulators with authority for timely corrective action.¹³ The NAIC's *Risk-Based Capital for Insurers Model Act* provides that states must require both life and health and property and casualty insurers to submit RBC filings with their regulators. Presently, this requirement is incorporated in the Insurance Code; however, it does not apply to health maintenance organizations (HMOs) and prepaid limited health service organizations.¹⁴ Prepaid limited health service organizations provide limited health services (such as dental or vision care) through an exclusive panel of providers in return for a prepayment,¹⁵ and HMOs generally provide a range of health coverage with contracted providers.¹⁶ The NAIC Risk-Based Capital Health Organizations Model Act will be effective as an accreditation standard beginning January 1, 2015, and applies to health maintenance organizations and prepaid limited health service organization.

⁹ Section 6B of the NAIC Insurance Holding Company System Regulatory Act.

¹⁰ Section 7 of the NAIC Insurance Holding Company System Regulatory Act.

¹¹ "Supervisory Colleges: A Regulatory Tool for Enhancing Supervisory Cooperation and Coordination," at http://www.naic.org/cipr_newsletter_archive/vol4_supervisory_colleges.htm (last visited on Apr. 10, 2013).

¹² NAIC on Supervisory Colleges at http://www.naic.org/cipr_topics/topic_supervisory_college.htm. (last visited on Apr. 10, 2013). Additionally, the linked/public records bill, SB 834, provides for confidential treatment of regulatory information, including within the context of a supervisory college that is shared between insurance regulators and law enforcement, pursuant to confidentiality agreements.

¹³ NAIC on Risk-Based Capital at http://www.naic.org/cipr_topics/topic_risk_based_capital.htm (last visited on Apr. 10, 2013).

¹⁴ Section 624.4085, F.S.

¹⁵ Section 636.003(7), F.S.

¹⁶ Section 641.19(12), F.S.

In March 2006, the NAIC adopted revisions to the Risk-Based Capital for Insurers Model Act. The revisions were made to incorporate a new Property and Casualty Trend Test for property and casualty companies. The accreditation effective date for property and casualty trend test was January 1, 2012. A statutory provision relating to a life trend test was already included in the RBC for Insurers Model Act; but the changes equalize the trigger between life and health, property, and casualty companies that prompt the need for a trend test calculation. The model was amended to cite the Property & Casualty Trend Test as a means for the company action level to be triggered. The accreditation effective date for these changes is January 1, 2017.

Property and Casualty Actuarial Opinion Model Law

The NAIC Property and Casualty Actuarial Opinion Model Law specifies that states must require property and casualty insurers to submit a Statement of Actuarial Opinion, which is a public document. The model act also requires the submission of an Actuarial Opinion Summary, an Actuarial Report, and workpapers to support each actuarial opinion, which must be treated as confidential and privileged document. The accreditation effective date for the adoption of this model act was January 1, 2010.

Current law requires insurers (except those providing life insurance and title insurance) to provide to the OIR an annual statement of its financial condition and a statement of opinion on loss and loss adjustment expense reserves prepared by an actuary or a qualified loss reserve specialists. These insurers are also required to provide supporting work papers upon the OIR's request.¹⁷ Currently, these materials are not exempt from ch. 119, F.S., relating to public records.

III. Effect of Proposed Changes:

Model Insurance Holding Company Act and Regulations

Section 1 creates s. 624.085, F.S., which establishes definitions of affiliate, affiliated person, and control. The definition of the term, "affiliated person," currently defined in s. 628.461(12)(a), F.S., is modified and transferred to this section.

Section 5 amends s. 628.461, F.S., relating to acquisition of controlling stock. The section deletes the provision in "lieu of filing an acquisition statement, a party acquiring less than 10 percent of the outstanding voting securities of an insurer, may file a disclaimer of affiliation and control."

The section specifies that the acquiring party's statement must include an agreement to file an "annual enterprise risk report," if control exists as described in section 6 of the bill. The bill adds language that states the person required to file the statement pursuant to s. 628.461(1), F.S., will provide the annual report specified in s. 628.801(2), F.S., if control exists. A provision is added that the presumption of control may be rebutted by filing a disclaimer of control, which will be in effect unless the OIR disallows the disclaimer. Any controlling person of a domestic insurer that seeks to divest its controlling interest in the domestic insurer is required to file with the OIR a confidential notice of its proposed divestiture at least 30 days prior to the relinquishment of control.

¹⁷ Section 624.424, F.S.

Currently, an individual or company must file a letter of notification and a statement for the OIR's approval before concluding a tender offer to acquire 5 percent or more of a domestic stock insurer or of a controlling company. During the pendency of the OIR's review of an acquisition filing, the insurer is not permitted to make a "material change" to its operation or management, unless the OIR has approved or been notified, respectively. A "material change" consists of a disposal or obligation of 5 percent or more of the insurer's capital and surplus, or a change in management involving a person who has the authority to dispose or obligate 5 percent of the insurer's capital and surplus

Section 6 amends s. 628.801, F.S., relating to the regulation of insurance holding companies, to amend and update the provisions of the NAIC Insurance Holding Company System Regulatory Model Act and the Insurance Holding Company System Model Regulation by incorporating reference to the 2010 version. The section requires insurers to file an annual holding company registration statement, including disclosure of material transaction between affiliates. Currently, authorized insurers are required to register with the OIR and be subject to regulation with respect to the relationship with the holding company.

Additionally, the ultimate controlling person in an insurer's holding company must identify and report material risk within the system that could pose enterprise risk to the insurer in an annual enterprise risk report filed with the OIR. The enterprise risk report will contain detailed information including the holding company's business plan, material developments concerning risk management, and rating agency information. Information contained in the enterprise risk report filed with OIR is confidential and exempt as provided in s. 624.4212, F.S. The bill also adds a provision that prohibits the waiver of any applicable privilege or claim of confidentiality in the enterprise risk report because of disclosures to the OIR.

Pursuant to its authority under ch. 624, F.S., the OIR is authorized to examine any insurer and its affiliates registered under this section to ascertain the financial condition of the insurer, including the enterprise risk to the insurer by the ultimate controlling party.

If an insurer fails to file a registration statement, a summary of the registration statement, or enterprise risk filing report within the specified time, it is a violation of this section.

The section also provides criteria under which an insurer may apply for waiver of the requirements contained in s. 628.801, F.S.

Section 7 amends s. 628.803, F.S., relating to sanctions against an insurance holding company, to provide that a violation of s. 628.461, F.S., (i.e., the filing requirements for acquisition of controlling stock) or s. 628.801, F.S., (i.e., filing requirements for insurance holding companies) may serve as an independent basis for the OIR to disapprove dividends and distributions and place the insurer under an order of supervision pursuant to part VI of ch. 624, F.S.

Currently, the Insurance Code states that noncompliant insurance holding companies (and their directors, officers, employees, and agents) can be subject to a number of sanctions that include:

- A penalty, not to exceed \$10,000, for failing to file registration statements or certificate of exemption;
- Civil forfeitures, not to exceed \$5,000 per violation, for knowingly engaging in transactions that have not been properly filed, approved, or in accordance with commission rule; or
- A cease and desist order for engaging in transactions or entering into contracts that violate commission rules, and rescission orders if in the best interests of the policyholders, creditors, or public.

Additionally, an officer, director, or employee of an insurance holding company willfully and knowingly submits a false statement, false report, or false filing with the intent to deceive the OIR, is guilty of a felony of the third degree.

Section 8 creates s. 628.805, F.S., which provides for the creation and participation by the OIR in a Supervisory College with other state, federal, and international regulators charged with supervising an insurer or its affiliates. The section provides for the terms and conditions of participation. In accordance with s. 624.4212, F.S., regarding confidential information sharing, the OIR is authorized to enter into cooperative agreements with other regulators. Expenses associated with a supervisory college would be liable for the payment of reasonable expenses for the OIR's participation.

Risk-Based Capital for Insurers and Health Organizations

Section 2 amends 624.4085, F.S., to revise the definition of the term, "life and health insurer," for purposes of risk-based capital (RBC) requirements to include HMOs and prepaid limited health service organizations that are authorized in Florida and one or more other states, jurisdictions, or countries. The section also clarifies the RBC requirements for a life and health insurer that reports using the life and health annual statement instructions and changes a company action level event to total adjusted capital that is greater than or equal to its company action level RBC but less than the product of its authorized control level risk-based capital and 3.0.

The section also defines the RBC requirements for a life and health, as well as property and casualty, insurer that reports using the health annual statement instructions and defines a company action level event as total adjusted capital that is greater than or equal to its company action level risk-based capital but less than the product of its authorized control level RBC and 3.0 and triggers the trend test calculation. An insurer that fails the Trend Test would be subject to filing a corrective action plan with the OIR.

Section 9 amends s. 636.045, F.S., relating to minimum surplus requirements, to provide that prepaid limited health service organizations authorized in Florida are subject to the RBC requirements and confidentiality requirements pursuant to s. 624.4085, F.S., and s. 624.40851, F.S., respectively.

Section 10 amends s. 641.225, F.S., relating to surplus requirements, to provide that an HMO that is authorized in one or more other states, jurisdictions, or countries is subject to the risk-based capital requirements for insurers as well as the confidentiality protections of risk-based capital information provided in ss. 624.4085, F.S., and s. 624.4615, F.S., respectively.

Section 11 amends s. 641.255, F.S., provides that an HMO that is a member of a holding company system is subject to the acquisition and enterprise risk reporting requirements of s. 628.461, F.S., but not to the acquisition requirements for specialty insurers in s. 628.4615, F.S.

Property and Casualty Actuarial Opinion Model Law

Section 3 amends s. 624.424, F.S., to require property and casualty insurers to file an annual Statement of Actuarial Opinion and Actuarial Opinion Summary in accordance with the NAIC annual statement instructions. Proprietary business information contained in the summary is confidential and exempt under s. 624.4212, F.S. This section also protects the summary and related information from subpoena, discovery, or admissibility in any private civil action. The section also updates the Financial Services Commission's rulemaking authority under this section to specify that rule must be in substantial conformity with the 2006 Annual Financial Reporting Model Regulation adopted by the NAIC.

Standard Valuation Law for Life Insurers

Section 4 amends s. 625.121, F.S., relating to the Standard Valuation Law for life insurance, to provide that any memorandum or other material in support of the actuarial opinion that is currently confidential and exempt from s. 119.07(1), F.S., is not subject to subpoena or discovery, or admissible in evidence in any private civil action. Currently, authorized life insurance companies are required to submit an annual actuarial opinion of reserves, reflecting the valuation of reserve liabilities.¹⁸ This section also provides that neither the OIR nor any person who receives information while acting under the authority of the OIR or with whom such information is shared to testify in any private civil action concerning confidential information. These changes incorporate a provision of the NAIC Standard Valuation Law that provides that this information should not be subject to subpoena or discovery, and should not be admissible in any civil action in either documentary or testimonial form.

Effective Date

Section 12 provides that the bill takes effect October 1, 2013, if SB 834 or similar legislation is adopted in the same legislative session or an extension thereof, and becomes a law.

IV. Constitutional Issues:

A. Municipality/County Mandates Restrictions:

None.

B. Public Records/Open Meetings Issues:

None.

¹⁸ Section 625.121(3)(a)1., F.S.

C. Trust Funds Restrictions:

None.

V. **Fiscal Impact Statement:**

A. Tax/Fee Issues:

None.

B. Private Sector Impact:

Insurers may incur an indeterminate amount of administrative costs in complying with the additional reporting requirements and costs associated with the OIR's participation in the supervisory colleges.

C. Government Sector Impact:

The bill provides greater solvency tools and regulatory authority for the OIR.

Greater coordination of efforts in the examination of multistate insurers will reduce regulatory redundancies and expenses among the state regulators.

VI. **Technical Deficiencies:**

None.

VII. **Related Issues:**

Incorporation by reference and delegation of legislative authority

Currently, s. 628.801, F.S. gives rulemaking authority to the Financial Services Commission to adopt rules regarding annual registration statements to be filed by insurers within a holding company. Lines 560-562 of the bill specify that the rules must be in accordance with the most recent NAIC Holding Company Model Act (adopted December 2010). The bill also requires the commission to "adopt subsequent amendments thereto *if the methodology remains substantially consistent*" (emphasis added).¹⁹

Generally, a cross-reference to a specific statute incorporates the language of the referenced statute as it existed at the time the reference was enacted, unaffected by any subsequent amendments to or repeal of the incorporated statute.²⁰ The legislature may adopt provisions of federal statutes and administrative rules made by a federal administrative body "that are in existence and in effect at the time the legislature acts, but it would be an unconstitutional delegation of legislative power for the legislature to adopt in advance any federal act or the

¹⁹ It is noted that other provisions in the current Insurance Code gives the Financial Services authority to adopt subsequent amendments to a NAIC model rule. See ss. 624.424(8)(e), F.S. and 625.121(3)(a)4., F.S.

²⁰ See *Overstreet v. Blum*, 227 So. 2d 197 (Fla. 1969); *Hecht v. Shaw*, 151 So. 333 (1933).

ruling of any federal administrative body that Congress or such administrative body might see fit to adopt in the future.”²¹

A court would likely apply this same principle in reviewing a statute that incorporates a model act promulgated by an organization, although it is uncertain whether the qualifying language “if the methodology remains substantially consistent” would change a court’s conclusion. Accordingly, while the bill may adopt the current NAIC model act in effect, it is possible that a reviewing court would not uphold that part of a statute that adopts any future amendments to that model act.²²

VIII. Additional Information:

A. Committee Substitute – Statement of Substantial Changes: (Summarizing differences between the Committee Substitute and the prior version of the bill.)

CS by Banking and Insurance on April 2, 2013

CS/SB 836 provides the following changes:

- Clarifies the applicability of civil process exemptions to confidential information provided to the OIR pertain to the life and health actuarial memorandum and other supporting documents and the filings made pursuant to the NAIC Insurance Holding Company System Regulatory Act.
- Clarifies the OIR’s authority to impose sanctions if an insurer violates s. 628.461, F.S., or s. 628.801, F.S.
- Authorizes the OIR to participate in a supervisory college for any domestic insurer that is part of insurance company system with international operations in order to determine an insurer’s compliance with ch. 628, F.S.
- Provides technical and conforming changes.

B. Amendments:

None.

This Senate Bill Analysis does not reflect the intent or official position of the bill’s introducer or the Florida Senate.

²¹ *Florida Industrial Commission v. State*, 155 Fla. 772, 21 So.2d 599 (1945). See also *Freimuth v. State*, 272 So. 2d 473 (Fla.1972); *State v. Camil*, 279 So. 2d 832 (Fla.1973).

²² Courts may sever a valid portion of laws from the remainder and continue to enforce the valid portion. *Carter v. Carter Coal Co.*, 298 U.S. 238 (1936); *Florida Hosp. Waterman, Inc. v. Buster*, 984 So. 2d 478 (Fla. 2008); *Ray v. Mortham*, 742 So. 2d 1276 (Fla. 1999); *Wright v. State*, 351 So. 2d 708 (Fla. 1977).