Ohio Legislative Service Commission

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Fiscal Note & Local Impact Statement

Bill: Sub. S.B. 140 of the 130th G.A. **Date**: May 20, 2014

Status: As Reported by House Insurance **Sponsor**: Sen. Bacon

Local Impact Statement Procedure Required: No

Contents: To make changes to the law governing insurance companies

State Fiscal Highlights

- The bill may increase the Department of Insurance's financial examination expenses to regulate and enforce the proposed alternative investment law. If there is any increase in such costs, it is likely to be minimal. Any such costs would be paid from the Superintendent's Examination Fund (Fund 5550). Any expenses from conducting such examination are paid by the company to the Superintendent and deposited into Fund 5550.
- The bill may also increase the Department of Insurance's administrative expenses related to the regulation and enforcement of various provisions governing insurance companies under this bill, including the Holding Company Systems Law. If there is any increase in such costs, it is likely to be minimal. Any such costs would be paid from the Department of Insurance Operating Fund (Fund 5540).
- The bill allows the Superintendent of Insurance to impose certain penalties. All penalties would be deposited into Fund 5540. The amount of revenue collected would depend on the compliance of insurers with the bill's requirements.
- The provision permitting the Superintendent to participate in a supervisory college would increase costs for the Department, but the increase would be permissive. In addition the Department could recover its costs by way of the permitted assessments. The bill does not specify a fund that would pay the costs or to receive revenue from the assessments.

Local Fiscal Highlights

- The provision allowing the Superintendent to petition the Court of Common Pleas of Franklin County for an order compelling a witness to appear and testify or produce documentary evidence related to the Holding Company Systems Law may increase the court costs. If there is any increase in such costs, it is likely to be minimal.

Detailed Fiscal Analysis

The bill proposes an alternative investment law and changes the law governing insurance holding company systems. The bill eliminates the petition requirement for domestic mutual companies that wish to merge or consolidate with another company and eliminates the commission created to hear and determine petitions for merger and consolidation. The bill also provides the requirements for maintaining a risk management framework and completing an own risk and solvency assessment, and provides guidance and instructions for filing an own risk and solvency assessment summary report with the Superintendent of Insurance. The bill may potentially increase penalties due to any violations related to the Holding Company System Law. Any such increase would depend on the number of such violations.

Most of the provisions have no significant fiscal effect on the state and local governments. The provisions described below may have a minimal fiscal effect on the Department of Insurance Operating Fund (Fund 5540) or the Superintendent's Examination Fund (Fund 5550). For a complete description of the bill's provisions, please see the LSC Bill Analysis.

Alternative investment law

The proposed alternative investment law would apply to the following types of insurers: small employer health care alliances, health insuring corporations, domestic legal reserve life insurance companies, mutual protective associations, mutual insurance companies, fraternal benefit societies, nonlife domestic insurance companies, and title insurance companies. The bill also applies to reciprocal or interinsurance contracts. The bill provides that such insurers may apply to the Superintendent of Insurance for permission to make investments based on the requirements under the proposed law, in lieu of making investments as specified under current law. However, the bill specifies that the assets of any separate account established by domestic life insurers that are to be applied to provide benefits and contractual payments under existing law must be invested using the requirements under current law.

The bill requires the Superintendent to consider certain criteria in determining whether to permit an entity to invest pursuant to the proposed alternative investment law, leaving some discretion to the Superintendent regarding some of the details. The bill also specifies the minimum financial security benchmarks for insurers seeking to invest under the proposed alternative investment law, and provides that the Superintendent may adopt rules to change the minimum financial security benchmark to apply to any class of insurers provided the amount established by the rule is not less than the benchmarks specified by the bill. The bill requires the Superintendent to determine the amount of minimum capital or minimum surplus for determining an insurer's minimum financial security benchmark.

The bill imposes a number of requirements on an insurer, including some on its board of directors, if the insurer chooses to make investments under the proposed alternative investment law. The requirements include reporting requirements, minimum asset requirements, and a requirement to impose internal compliance controls.

The bill specifies that, if an insurer invests in prohibited investments, that is considered a violation that may be grounds for regulatory action under current law.[1] Thus, insurers that invest in prohibited investments may be subject to a rehabilitation action filed by the Superintendent with a court of common pleas. In addition, the bill specifies that the Superintendent must set a reasonable amount of time, not to exceed five years, for disposal of a prohibited investment in hardship cases if the insurer demonstrates that the investment was legal when made or the result of a mistake made in good faith, or if the Superintendent determines that the sale of the asset would be contrary to the interests of insureds, creditors, or the general public.

The bill allows the Superintendent, if the Superintendent determines that an insurer does not meet the investment requirements under the proposed alternative investment law, after notification to the insurer of such determination, to order the insurer to make necessary changes to comply with the proposed law. In addition, if the Superintendent determines that the financial condition or current investment practice or plan of an insurer may endanger the interests of insureds, creditors, or the general public, the Superintendent may impose reasonable additional restrictions upon the admissibility or valuation of investments and may impose restrictions on the investment practices of the insurer, including prohibiting an investment or requiring the divestment of an investment. The bill allows an insurer subject to a discretionary action taken by the Superintendent to request a hearing within 30 days of the date of the order. The hearing must be held privately unless the insurer requests a public hearing.

The bill authorizes the Superintendent to adopt rules interpreting and implementing the provisions of the alternative investment law. The bill also authorizes the Superintendent to adopt rules related to certain restrictions on investment. If the Superintendent is satisfied by evidence of the solidity of an insurer and the competence of management and its investment advisors, the bill authorizes the Superintendent, after a hearing, to, by order, grant an exemption to that insurer from any such restriction adopted in rules to the extent that the Superintendent is satisfied that the interests of the insurer's insureds and creditors, as well as the general public, are protected.

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[1] O.R.C. 3903.12.

Insurance holding company systems

The bill provides certain filing requirements for any controlling person of a domestic insurer seeking to divest its controlling interest in the domestic insurer. It makes certain changes to the requirements for a registered insurer entering into certain transactions with any person in its insurance holding company system. It expands the Superintendent's authority to review proposed transactions.

The bill also requires the ultimate controlling person of every insurer subject to registration under existing law to file an annual enterprise risk report. The ultimate controlling person is required by the bill to file the report with the lead state commissioner of the insurance holding company system as determined by the procedures within the financial analysis handbook adopted by the National Association of Insurance Commissioners (NAIC). The bill specifies that the failure to file a required enterprise report would result in certain potential penalties,[2] specified in existing law for certain other offenses, to be imposed by the Superintendent. The bill also makes changes to transaction standards by registered insurers with their affiliates.

The bill authorizes the Superintendent to examine any registered insurer and its affiliates to ascertain the financial condition of the insurer, including 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. The Superintendent may order any registered insurer to produce records, books, or other information papers in the possession of the insurer and its affiliates as may be reasonably necessary to determine compliance with the Holding Company Systems Law.

The bill authorizes the Superintendent to order any registered insurer to produce information not in the possession of the insurer if the insurer can obtain access to such information pursuant to a contractual relationship, statutory obligation, or other method, in order to determine compliance with the Holding Company Systems Law. If the insurer cannot obtain the information requested by the Superintendent, the insurer must provide the Superintendent a detailed explanation of the reason that the insurer cannot obtain the information and the identity of the holder of information. The bill allows the Superintendent, after notice and hearing, to impose a penalty on the insurer of up to $500 per day whenever it appears to the Superintendent that the detailed explanation is without merit, or the Superintendent may suspend or revoke the insurer's license. If the insurer fails to comply with an order of the Superintendent, the bill authorizes the Superintendent to issue subpoenas, administer oaths, and examine under oath any person for purposes of determining compliance with the record production provisions. Under the bill, upon the failure or refusal of any person to obey

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[2] The penalties are specified in section 3901.37 of the Revised Code, which is not in the bill. They include, in specified circumstances, a civil forfeiture up to $250,000. Any such forfeiture would be deposited into Fund 5540.

a subpoena, the Superintendent may petition the Court of Common Pleas of Franklin County for an order compelling the witness to appear and testify or produce documentary evidence. Failure to obey the court order, under the bill, must be punishable as contempt of court.

The bill defines supervisory college and authorizes the Superintendent 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 by the insurer with the Holding Company Systems Law. The bill also provides that the Superintendent may initiate the establishment of a supervisory college, including clarifying its functions, and memberships. The bill specifies that each registered insurer is liable for and must pay the reasonable expenses of the Superintendent's participation in such supervisory college, including reasonable travel expenses. The Superintendent may also establish a regular assessment to the insurer for the payment of these expenses.

The bill makes changes to confidential and privileged treatment of documents, materials, or other information under the bill. The bill also requires the Superintendent to enter into written agreements with NAIC governing sharing and use of information under the Holding Company Systems Law.

Own risk and solvency assessment law

The bill requires an insurer to maintain a risk management framework to assist the insurer with identifying, assessing, monitoring, managing, and reporting on its material and relevant risks. The bill specifies that the requirement may be satisfied if the insurance group of which the insurer is a member maintains a risk management framework applicable to the operations of the insurer. Upon the request of the Superintendent, and not more than once annually, an insurer must submit to the Superintendent an own risk and solvency assessment summary report, or any combination of reports that together contain the information described in the own risk and solvency assessment guidance manual, applicable to the insurer or the insurance group of which it is a member. An insurer is exempted from these requirements if it meets certain conditions.

Automated insurance transactions

The bill makes changes related to automated transactions in the business of insurance including disclosures and notice requirements to the insured. The bill authorizes the Superintendent of Insurance to adopt rules as the Superintendent considers necessary to carry out the purposes of the bill's provisions relating to automated transactions in the business of insurance.

Reinsurance law

The bill revises regulations related to reinsurance law for insurers looking to cede certain risks via reinsurance and on the reinsurers assuming the risks. The bill specifies certification and accreditation eligibility requirements for assuming insurers.

The bill also requires the Superintendent to create and publish a list of qualified jurisdictions under which an assuming insurer licensed and domiciled in such jurisdiction is eligible to be considered by the Superintendent for certification as a certified reinsurer.[3]

The bill requires the Superintendent to assign a rating to each certified reinsurer giving due consideration to the financial strength ratings assigned to the insurer by rating agencies. The Superintendent is also required to publish a list of all certified reinsurers and their ratings. The bill specifies requirements related to certified reinsurers to secure obligations assumed from a ceding insurer within the United States. The bill also specifies criteria related to a suspension of accreditation or certification of a reinsurer that is certified by the Superintendent. Under the bill, the Superintendent may suspend or revoke the reinsurer's accreditation or certification after a hearing held pursuant to the Administrative Procedure Act. In addition, the bill eliminates the commission created to hear and determine petitions for merger and consolidation of an insurance company.

Valuation of insurance policies

The bill requires the Superintendent annually to value the reserve liabilities for all outstanding life insurance policies and annuity and pure endowment contracts for every life insurance company doing business in the state prior to the operative date of the valuation manual. The bill specifies criteria for calculating reserves requirements. The bill also specifies requirements related to minimum standard valuation. Under the bill, the reserve valuation requirement for companies under the laws of a foreign government, only applies to the company's business in the U.S. The bill specifies criteria for calculating valuation for various types of insurance policies, including individual and group annuity and pure endowment contracts, total and permanent disability benefits, accidental death benefits, and certain annuities. The bill also specifies requirements related to sharing of certain privileged information.

Fiscal effect

The bill may increase the Department of Insurance's financial examination expenses to regulate and enforce the proposed alternative investment law. Any such costs would be paid from the Superintendent's Examination Fund (Fund 5550). Currently, any expenses from conducting such examination are paid by the company to the Superintendent and deposited into Fund 5550. The bill may also increase the Department of Insurance's administrative costs to regulate and enforce the

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[3] The bill specifies that the Superintendent must also consider the list of qualified jurisdictions through the NAIC's committee process in determining qualified jurisdictions. If the Superintendent approves a jurisdiction as qualified that does not appear on the NAIC's list, the bill specifies that the Superintendent is allowed to provide justification in accordance with criteria to be developed by the Superintendent under rule or regulation. The bill also specifies eligibility criteria for jurisdictions located within and outside of the United States to be recognized as qualified jurisdictions.

requirements related to various provisions governing insurance companies under this bill, including the Holding Company Systems Law. Any increase in administrative costs would be paid from the Department of Insurance Operating Fund (Fund 5540).

Provisions related to the liquidation of an insurer that is considered financially hazardous under the Reserve Valuation, Rehabilitation, and Liquidation Law would have no fiscal effect. Currently, when an Ohio domestic insurance company becomes insolvent and requires liquidation the Superintendent of Insurance would initiate a court action to place the company in liquidation. The Office of the Ohio Insurance Liquidator is technically a private trustee's office, overseen by the Franklin County Court of Common Pleas, and it would liquidate all assets and resolve all claims against the insolvent insurance company. The Office is funded by a share of the estate left by a liquidated insurance company. Thus, the cost of liquidating such insurer would be recovered from the insurer's assets.

The provision permitting the Superintendent to participate in a supervisory college would increase costs for the Department, but the increase would be permissive. In addition the Department could recover its costs by way of the permitted assessments. The bill does not specify a fund that would pay the costs or to receive revenue from the assessments.

The bill may also increase the Franklin County Court of Common Pleas' court costs due to provisions related to the Holding Company Systems Law. The bill allows the Superintendent to petition to the Court of Common Pleas of Franklin County for an order compelling the witness to appear and testify or produce documentary evidence related to the Holding Company Systems Law.

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