

# HOUSE BILL REPORT

## SHB 2461

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### As Amended by the Senate

**Title:** An act relating to the financial solvency of insurance companies.

**Brief Description:** Addressing the financial solvency of insurance companies.

**Sponsors:** House Committee on Business & Financial Services (originally sponsored by Representatives Kirby and Ryu; by request of Insurance Commissioner).

#### **Brief History:**

##### **Committee Activity:**

Business & Financial Services: 1/21/14, 1/31/14 [DPS];  
Appropriations Subcommittee on General Government & Information Technology:  
2/6/14 [DPS(BFS)].

##### **Floor Activity:**

Passed House: 2/17/14, 82-14.  
Senate Amended.  
Passed Senate: 3/7/14, 39-10.

#### **Brief Summary of Substitute Bill**

- Amends the statutory framework that governs insurance holding companies.
- Creates the Risk Management and Solvency Assessment Act.
- Repeals the provisions under RCW 48.31C.

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### HOUSE COMMITTEE ON BUSINESS & FINANCIAL SERVICES

**Majority Report:** The substitute bill be substituted therefor and the substitute bill do pass. Signed by 12 members: Representatives Kirby, Chair; Ryu, Vice Chair; Parker, Ranking Minority Member; Vick, Assistant Ranking Minority Member; Blake, Fagan, Habib, Hawkins, Hudgins, G. Hunt, Kochmar and MacEwen.

**Staff:** Linda Merelle (786-7092).

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### HOUSE COMMITTEE ON APPROPRIATIONS SUBCOMMITTEE ON GENERAL GOVERNMENT & INFORMATION TECHNOLOGY

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*This analysis was prepared by non-partisan legislative staff for the use of legislative members in their deliberations. This analysis is not a part of the legislation nor does it constitute a statement of legislative intent.*

**Majority Report:** The substitute bill by Committee on Business & Financial Services be substituted therefor and the substitute bill do pass. Signed by 7 members: Representatives Hudgins, Chair; Parker, Ranking Minority Member; Buys, Dunshee, S. Hunt, Jinkins and Springer.

**Minority Report:** Do not pass. Signed by 2 members: Representatives Christian and Taylor.

**Staff:** Charlie Gavigan (786-7340).

**Background:**

In 1993 the Legislature amended the insurance code to conform to the financial regulation standards and regulatory statutes recommended by the National Association of Insurance Commissioners (NAIC). The legislation addressed, among other things, insurance holding companies; insurance company examination procedures; insurer capital and surplus requirements; limitations upon individual insurance company exposure to individual risks; valuation of insurance company investments; receivership, liquidation and rehabilitation of insurance companies; and penalties that may be imposed by the Office of the Insurance Commissioner (Commissioner).

The provisions under this 1993 legislation were codified in RCW chapters 48.31B, which addressed non-health care insurers, and 48.31C, which addressed insurers who provided health care insurance.

**Summary of Substitute Bill:**

The provisions of RCW 48.31B are amended to adopt the NAIC model acts regarding holding companies and solvency assessments.

Insurance Holding Companies.

*Subsidiaries.*

A domestic insurer, alone or in cooperation with one or more persons, may organize or acquire one or more subsidiaries. The subsidiaries may conduct any kind of business authorized under RCW 48.13.061(4), examples of which include: acting as an insurance producer, surplus line broker, or title insurance agent for its parent; investing; and trading in securities. The acquisition of subsidiaries is also subject to the percentage limitations contained in Chapter 48.13 RCW, which pertains to insurer investment programs.

*Acquisition of, Control of, or Merger with Domestic Insurer.*

A person acquiring a domestic insurer must file a pre-acquisition notification with the Commissioner. The pre-acquisition notification must contain information prescribed by the NAIC.

The required statement regarding acquisition must include an agreement that it will provide an annual report regarding risk as long as the control exists and an acknowledgement that the person and all subsidiaries within its control will provide information to the Commissioner upon request as necessary to evaluate enterprise risk to the insurer.

The Commissioner must approve an exchange or other acquisition within 60 days after the required statement is declared complete and after holding a public hearing. If the proposed acquisition of control will require the approval of more than one Commissioner, the required public hearing may be held on a consolidated basis at the request of the person filing the statement.

If the Commissioner determines that the person acquiring control of the insurer must maintain or restore the capital of the insurer to the level required by rule and law, the Commissioner must make such determination no later than 60 days after the date of the notification of change in control.

If an acquisition is in violation of statutory standards, the Commissioner may enter an order requiring the insurer to cease and desist from doing business in this state with respect to the lines of insurance involved in the acquisition or deny the application of an acquired or acquiring insurer for a license to do business in this state. There is no provision that allows the involved insurer to submit a plan to remedy the anticompetitive impact of the acquisition.

Any controlling person seeking to divest its controlling interest in an insurer must give 30-days notice to the Commissioner.

#### *Registration of Insurers.*

Registration statements required to be filed by insurers must include, in addition to the existing requirements, financial statements of or within an insurance holding company system, including all affiliates if requested by the Commissioner. The statements must be in a form and format prescribed by the NAIC. They must also include statements that the insurer's board of directors oversees corporate governance and internal controls and that the insurer's officers or senior management have approved, implemented, and continue to maintain and monitor corporate governance and internal control procedures. The registration statement must also contain any other information required by the Commissioner by rule.

#### *Disclaimers of Affiliation.*

A disclaimer of affiliation is deemed to have been granted if no response to the disclaimer from the Commissioner is received within 30 days following receipt. Under the new provisions, an insurer may request and shall be granted an administrative hearing if the disclaimer is disallowed by the Commissioner.

#### *Transactions Within Insurance Holding Company.*

Transactions within an insurance holding company system must be fair and reasonable. Agreements for cost-sharing services and management must include provisions that are required by rule. Some transactions may not be entered into unless the insurer has notified

the Commissioner in writing of its intention to enter into the transaction and the Commissioner declares the notice to be sufficient. These transactions include sales, purchases, exchanges, loans or extensions of credit, guarantees or investments if the transactions are, as of the previous December 31, equal to or exceed the lesser of 3 percent of the insurer's admitted assets or 25 percent of surplus for non-life insurers, excluding health care insurers. For health insurers, notification must be given if the transaction exceeds the lesser of 5 percent of admitted assets or 25 percent of capital and surplus or net worth for health insurers. The same notification requirement applies to reinsurance pooling agreements and agreements where the reinsurance current or projected premium, or change insurer's liabilities equals or exceeds 5 percent of the insurer's surplus.

Notwithstanding the control of a domestic insurer by any person, the officers and directors of the insurer are not relieved of any obligation or liability applicable under law. The insurer must be managed to assure its separate operating identity.

At least one-third of an insurer's directors and at least one-third of the members of each committee of the insurer's board of directors must be persons who are not officers or employees of the insurer or of any entity that controls, is controlled by, or is under common control with the insurer. Regarding for-profit entity and non-profit entities, the board of directors must establish one or more committees comprised solely of directors chosen from this group. In for-profit entities, the committee or committees have responsibility for nominating candidates for director for subsequent election by shareholders or policy holders. For both for-profit and non-profit entities, the committee or committees have the responsibility for evaluating the performance of officers deemed to be principal officers of the insurer and recommending to the board of directors the selection and compensation of the principal officers.

#### *Enterprise Risk Report.*

The "ultimate controlling person," defined as a person who is not controlled by any other person, of every insurer subject to registration must file an annual enterprise risk report. An "enterprise risk" is defined in this bill as any 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 or its insurance holding company system as a whole. The report must, to the best of the ultimate controlling person's knowledge and belief, identify the material risks within the insurance holding company system that could pose enterprise risk to the insurer. The report must be filed with the lead state Commissioner of the insurance holding company system and determined by the procedures within the financial analysis handbook adopted by the NAIC. Failure to file a registration statement or enterprise risk filing within the specified time is a violation of the provisions of the insurance code.

#### *Examination of Insurers.*

The Commissioner's power to examine an insurer or its affiliates is expanded to allow the Commissioner to ascertain the financial condition of the insurer, including the enterprise risk to the insurer by the ultimate controlling party, by any entity or combination of entities within the insurance holding company system, or by the insurance holding company system. The

Commissioner may 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 contractual relationships, statutory obligations, or other method. An insurer who fails to provide requested information and does so without merit may be fined \$10,000 for each day's delay or the Commissioner may suspend or revoke the insurer's license. Any fine collected must be paid to the Washington State Office of the Treasurer for deposit into the General Fund.

#### *Supervisory Colleges.*

A "supervisory college" is defined as "a forum for cooperation and communication among involved regulators and international supervisors facilitating the effectiveness of supervision of entities which belong to an insurance group and supervision of the group as a whole on a group-wide basis and improving the legal entity supervision of the entities within the insurance group."

The Commissioner has the power 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 this title.

#### *Confidential Treatment of Documents.*

Documents, materials, or other information (Documents) in the possession or control of the Commissioner that are obtained by or disclosed in the course of an examination or investigation, and all information reported pursuant to the annual enterprise risk report and the supervisory colleges are privileged and confidential by law. They are not subject to subpoena, to discovery, or admissible in evidence in any private civil action.

The Commissioner is authorized to use the Documents in the furtherance of any regulatory or legal action brought as a part of the Commissioner's official duties. The Commissioner must not otherwise make the Documents public without the prior written consent of the insurer to which it pertains, unless the Commissioner, after giving the insurer and its affiliates who would be affected notice and an opportunity to be heard, determines that the interest of policy holders, shareholders, or the public is served by the publication.

The Commissioner or any person who has received Documents may not be required to testify in any private civil action concerning any confidential documents, materials, or information.

The Commissioner may share confidential and privileged Documents with other state, federal, and international regulatory agencies and the following: the NAIC; and state, federal, and international law enforcement authorities, including members of any supervisory college.

The recipients must agree in writing and have verified in writing the legal authority to maintain the confidentiality and privileged status of the Documents shared. The Commissioner may only share information regarding the annual enterprise risk report with commissioners of states having confidentiality statutes or rules substantially similar to those in Washington.

The Commissioner must maintain as confidential or privileged any Documents received with the notice or the understanding that the Documents are confidential or privileged under the laws of the jurisdiction that is the source of the Documents.

The Commissioner must enter into written agreements with the NAIC that govern sharing and use of information provided. Documents in the possession or control of the NAIC are confidential by law and privileged, exempt from disclosure under the Public Records Act (PRA), not subject to subpoena, and are not subject to discovery or admissible in evidence in any private civil action.

There shall be no waiver of any applicable privilege or claim of confidentiality in the Documents as a result of disclosure to the Commissioner due to authorized sharing.

#### Own Risk and Solvency Assessment.

New terms regarding an insurer's internal assessment of risk are defined:

An "own risk and solvency assessment" (ORSA) is a "confidential internal assessment, appropriate to the nature, scale, and complexity of an insurer or insurance group, conducted by that insurer or insurance group of the material and relevant risks associated with the insurer or insurance group's current business plan, and the sufficiency of capital resources to support those risks."

The "ORSA guidance manual" is the own risk and solvency assessment guidance manual developed and adopted by the NAIC as of the effective date of this act.

The "ORSA summary report" is a confidential high-level ORSA summary of an insurer or insurance group.

#### *Risk Management Framework.*

An insurer must maintain a risk management framework to assist the insurer with identifying, assessing, monitoring, managing, and reporting on its material and relevant risks.

#### *ORSA Summary Report.*

An insurer must regularly conduct an ORSA consistent with a process comparable to the ORSA guidance manual. The ORSA must be conducted annually but also at any time when there are significant changes to the risk profile of the insurer or the insurance group of which the insurer is a member.

An ORSA Summary Report (ORSA Report) must include a signature of the insurer or the insurance group's chief risk officer or other executive having responsibility for the oversight of the insurer's enterprise risk management process. Such person must attest to the best of his or her belief and knowledge that the insurer applies the enterprise risk management process described in the ORSA Report and that a copy of the ORSA Report has been provided to the insurer's Board of Directors or appropriate governing committee.

### *Confidential Treatment of Documents and Information.*

The ORSA Report and other Documents in the possession or control of the Commissioner that are obtained by, created by, or disclosed to the Commissioner or any other person under the provisions of the act are recognized as proprietary and as containing trade secrets and is confidential by law and privileged and not subject to the PRA. They are also not subject to subpoena or discovery or admissible in evidence in any private civil action. The Commissioner is authorized to use such Documents in the furtherance of any regulatory or legal action brought as a part of the Commissioner's official duties. The Commissioner must obtain the prior written consent of the insurer before making such Documents public.

Persons who have received ORSA-related Documents are not permitted or required to testify in any private civil action concerning any confidential documents, materials, or information.

### *Sharing of ORSA-Related Documents.*

The Commissioner may share ORSA-related Documents with other state, federal, and international regulatory agencies, including members of any supervisory college, the NAIC, the International Association of Insurance Supervisors, the Bank for International Settlements, and with any third-party consultants designated by the Commissioner. The recipients must agree in writing to maintain the confidentiality and privileged status of the Documents and verify in writing the legal authority to maintain confidentiality.

The Commissioner must maintain ORSA-related Documents received from regulatory officials of other foreign or domestic jurisdictions as confidential or privileged under the laws of the jurisdiction that is the source of the documents.

The Commissioner must enter into written agreements with the NAIC or a third-party consultant governing sharing and use of information provided. The agreement must provide that the recipient agrees in writing to maintain the confidentiality and privileged status of the Documents and verify in writing the legal authority to maintain confidentiality. The NAIC or a third-party consultant is prohibited from storing the information shared.

### *Intervention in Judicial or Administrative Action.*

The Commissioner must require prompt notice to be given to an insurer whose confidential information is in the possession of the NAIC or a third-party consultant when such information is subject to a request or a subpoena for disclosure or production. The Commissioner must also require the NAIC to consent to intervention by an insurer in any judicial or administrative action in which the NAIC may be required to disclose confidential information about the insurer.

### *Sanctions.*

After notice and a hearing, the Commissioner must require any insurer who fails, without cause, to file the required ORSA Report to pay a fine of \$500 for each day's delay. The maximum fine is \$100,000. The Commissioner may reduce the fine if the insurer demonstrates that the fine would impose a financial hardship to the insurer.

## **EFFECT OF SENATE AMENDMENT(S):**

Changes the procedure by which the Insurance Commissioner (Commissioner) may release confidential documents received pursuant to the insurance holding company statutes; instead of authorizing the Commissioner to publish documents determined to be in the interest of policy holders, shareholders or the public as the Commissioner deems appropriate, the Commissioner must provide advanced notice to the affected party, and the affected party must be given an opportunity to have a binding arbitration hearing regarding the disclosure of the documents.

**Appropriation:** None.

**Fiscal Note:** Available.

**Effective Date:** The bill takes effect on January 1, 2015, except for sections 14 and 32, relating to exemptions from the requirements of the Public Disclosure Act for documents, materials, or information obtained by the Insurance Commissioner, which take effect July 1, 2017.

### **Staff Summary of Public Testimony (Business & Financial Services):**

(In support) This bill was worked out with all of the stakeholders. There are several sections that are part of the model that should be included. The requirements regarding enterprise risk and the ORSA Report are new. Under ORSA there is a provision for exemptions. There are concerns for the standards for management of the domestic insurers and concerns regarding confidentiality. Those requirements should be limited to the new reports, rather than everything in possession by the Commissioner.

(In support with concerns) The stakeholder process was very inclusive. There is a concern regarding having a reporting due date in statute. It would be preferable to have the due date set by agreement between the insurer and the Commissioner. There are concerns regarding the confidentiality provisions, and the enterprise risk reporting requirement should only apply to large companies.

(Opposed) None.

### **Staff Summary of Public Testimony (Appropriations Subcommittee on General Government & Information Technology):**

(In support) This bill incorporates two National Association of Insurance Commissioners (NAIC) model laws. They have had stakeholder work done on them. The cost identified in the fiscal note comes out of the Insurance Commissioners Regulatory Account. There is a small cost to the bill, and while the Insurance Commissioner (Commissioner) does not expect to have to increase rates, the Commissioner does need expenditure authority. The legislation is necessary to maintain accreditation with the NAIC, which benefits Washington domestic insurers.

(Opposed) None.



**Persons Testifying** (Business & Financial Services): (In support) Ron Pastuch, Office of Insurance Commissioner; and Chris Bandoli, Regence Blue Shield.

(With concerns) Jean Leonard, Washington Insurers; Amber Ulvenes, Group Health; and Len Sorrin, Premera.

**Persons Testifying** (Appropriations Subcommittee on General Government & Information Technology): Jim Keogh, Office of the Insurance Commissioner.

**Persons Signed In To Testify But Not Testifying** (Business & Financial Services): None.

**Persons Signed In To Testify But Not Testifying** (Appropriations Subcommittee on General Government & Information Technology): None.