



Recent Changes in the Regulatory Framework for Texas Insurance Holding Companies

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In an effort to move its regulatory framework for the registration of insurance holding company systems more in conformity with the National Association of Insurance Commissioners ("NAIC") model regulations, the Texas Department of Insurance (the "Department") recently adopted a series of amendments to Title 28 of the Texas Administrative Code. Published in the May 17, 2013, issue of the Texas Register (38 TexReg 20, 3033 – 3055), the amendments became effective May 26, 2013.

The amendments affect 28 Tex. Admin. Code §§7.201 – 7.205, 7.209, 7.210 and create new §§7.211 – 7.214. Of particular importance are the amendments to §§7.209 – 7.214, which include Forms A – F used as guides for preparing the various statements, notices and applications required to be filed periodically by registrant companies with the Department. The forms and their purposes are: Form A – acquisition or divestiture statement; Form B – registration statement; Form C (new) – summary of changes to the registration statement; Form D (new) – prior notice of a transaction; Form E (new) – notice of dividend or distribution; and Form F (new) – enterprise risk report.

Insurance companies and health maintenance organizations are subject to the Texas Insurance Holding Company Systems Act, codified in Insurance Code Chapter 823 (the "Code"). Texas, like most states, requires insurer participants within insurance holding company systems to file periodic reports with their state regulator in order for the regulator to monitor enterprise or system risks posed by noninsurance operations that could potentially harm the insurance company registrant's financial condition. The recent Texas regulatory changes have been adopted with an emphasis on increased transparency and enhanced disclosure in the reports filed by registrant companies, thereby allowing the Department to better evaluate contagion risks as they may develop within an insurance holding company system.

Additionally, the amendments to the Texas Administrative Code contain non-substantive changes to conform writing style, correct punctuation and grammar, update statutory references and citations, and effect other conforming changes to implement and track recent statutory modifications and re-codification of the Code.

Among the recent amendments, the following items are of particular note:

- **§7.203(g):** Insurers required to file an annual registration statement must now also concurrently file a new Form C (new §7.211), providing a summary of any material changes from the prior year's annual registration statement; Form C must be filed even if there are no material changes;
- **§7.203(k):** Subject to phase-in requirements under the Code based upon the registrant's financial size, the ultimate controlling person of an insurer is now required to file an enterprise risk report on new Form F (new §7.214);
- **§7.203(m):** Contains the substance of the disclaimer of control or affiliation filing requirements previously contained in former Form C;
- **§7.204:** Contains pre-approval requirements for certain large affiliate transactions and prior notice requirements for certain specified affiliate transactions and requires the filing of new Form D (new §7.212) for those transactions;
- **§7.204(a)(2)(D):** Amended to contain minimum contract terms for intercompany management, service, cost sharing, rental or leasing agreements;
- **§7.205:** Amended to add the concept of divestiture to Form A acquisition statements;



- **§7.209:** Form A (acquisition or divestiture statement):
 - The latest version of the NAIC biographical affidavit form is now required;
 - Requirement added that the financial projections of the insurer and the applicant must be now attached as an appendix;
 - Notice requirement added regarding divestiture of control under Code §823.0595, with the notice to include how control is being divested and the name and address of the recipient of the divestiture of control;
- **§7.210:** Form B (registration statement):
 - Amended to reflect that even though the NAIC model regulations do not include affiliates, the Department retains the authority to request affiliate financial statements;
 - Former biographical data requirements replaced with new NAIC model language;
 - Internal controls disclosure added;
 - Requirement for a copy of the charter or articles of incorporation and bylaws to be included with the filing is deleted and no longer required;
- **New §7.211:** New Form C (summary of material changes to registration statement):
 - An insurer who is required to file an annual registration statement must now also furnish a separate summary of the material changes to the registration statement;
- **New §7.212:** New Form D (prior notice of a transaction):
 - Requires a detailed description of the proposed affiliate transaction, including the reasons for entering into the transaction and the statutory basis for which the filing of the notice of transaction is required;
 - Contains specific disclosure requirements in connection with various types of transactions, including sales, purchases, exchanges, loans, guarantees and investments, reinsurance arrangements and management, cost sharing and service agreements;
- **New §7.213:** New Form E (notice of ordinary and extraordinary dividends and other distributions):
 - Consolidates the ordinary and extraordinary dividends and distributions from the former Form D and HCDividend Form;
 - The former extraordinary dividend disclosure requirements are amended to provide uniformity with the NAIC model regulations and include factors determined to be more relevant by the Department in determining the threshold for extraordinary dividends;
 - New language is adopted such that the date of the payment and amount paid, rather than the declaration and the amount of the dividend, be used to calculate the aggregate amount of dividends during the past 12 months and for proposed dividends for purposes of the extraordinary characterization threshold;
 - The definition of “earned surplus” is amended to clarify that earned surplus is defined as “unassigned funds”;
- **New §7.214:** New Form F (enterprise risk report information):
 - Form F filings requirements are subject to the Code’s financial size based phase-in;
 - When required, Form F must be filed upon an acquisition of control of any registered company; and
 - The registrant/applicant must provide disclosures regarding certain areas deemed capable of producing enterprise risk, including among other things: material developments regarding strategy, internal audit findings, compliance or risk management; developments in pending investigations or regulatory activities; and identification of any negative movement or discussions with ratings agencies.

This summary is intended to serve as a review of some of the more significant items included in the various amendments recently implemented by the Department. Because the amendments became effective May 26, 2013, Texas holding company registrants and their regulatory advisors will need to review the changes for compliance in the preparation of their future Texas filings without delay.

For more information on the matters discussed in this *Locke Lord QuickStudy*, please contact the authors:

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