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BILL ANALYSIS

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House Bill 5792 (Substitute H-1 as passed by the House)
Sponsor: Representative Pete Lund
House Committee: Insurance
Senate Committee: Insurance

Date Completed: 12-16-14

CONTENT

The bill would amend Chapter 13 (Holding Companies) of the Insurance Code to do the following:

- **Require a person seeking divestiture of its controlling interest to file a confidential notice of the proposed divestiture with the Director of the Department of Insurance and Financial Services in advance of the transaction.**
- **Require a person seeking to merge with or acquire a controlling interest in an insurer to file an annual enterprise risk report with the Director.**
- **Allow the Director to hold a public hearing to receive evidence and hear parties affected by the merger or acquisition of an insurer.**
- **Expand the transactions between a domestic insurer and a person in its holding company that are subject to a requirement for prior notice to the Director.**
- **Specify that certain documents and information disclosed to the Director would not be subject to discovery, subpoena, or the Freedom of Information Act.**
- **Allow the Director to share documents and information or enter into agreements to share documents and information with regulator and law enforcement entities.**

Acquisition & Enterprise Risk

Section 1311 of the Code prohibits a person from entering into an agreement to merge with, or acquire control of, a domestic insurer unless that person has filed with the Director a statement containing certain information, and the offer, agreement, or acquisition has been approved by the Director. Under the bill, if a person seeking to divest its controlling interest in a domestic insurer had not filed the statement required under Section 1311, the person would have to file a confidential notice of its proposed divestiture at least 30 days before the cessation of control. The Director would have to determine those instances in which the person or persons seeking to divest or to acquire a controlling interest in an insurer would be required to file to obtain approval for the transaction. The information would have to remain confidential until the conclusion of the transaction unless the Director determined that confidential treatment would interfere with enforcement of Section 1311.

The bill would require a person that filed a Section 1311 statement to file an annual enterprise risk report (required under proposed Section 1325a) for as long as the control existed, and to provide, and ensure all subsidiaries within its control provided, information to the Director upon request as necessary to evaluate enterprise risk to the insurer.

("Enterprise risk" would mean an 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, including anything that would cause the insurer to be hazardous to policyholders, creditors, and the public.)

The bill would add Section 1325a to require the ultimate controlling person of an insurer subject to registration under Chapter 13 to file an annual enterprise risk report with the Director or a jurisdiction designated by the Director. The report would have to be appropriate to the nature, scale, and complexity of the insurance holding company system's operations and would have to identify the material risks within the company system that could pose enterprise risk to the insurer. The report would not be subject to discovery, would not be admissible in a private civil action, and would not be subject to the Freedom of Information Act. The ultimate controlling person could request an exemption from the reporting requirements by filing with the Director a written statement that included the reasons why the insurer should be exempt. The Director could grant an exemption if, after review of the statement, the Director found that the enterprise risk report requirement would create an undue hardship or organizational hardship on the ultimate controlling person. Failure to file an enterprise risk report would constitute a violation of the Code.

The Code requires the Director to approve a merger or acquisition of control unless he or she determines one or more circumstances exist. The bill would allow the Director to disapprove a merger or acquisition if it were likely to be hazardous of or prejudicial to the insurance-buying public.

The Director could hold a public hearing to receive evidence and hear parties affected by the merger or acquisition. The hearing would have to be held within 30 days after the statement required under Section 1311 was filed. The Director would have to provide at least 20 days' notice of the hearing to the person that filed the statement. That person would have to give at least seven days' notice of the hearing to the insurer and other parties the Director designated. If approval of the merger would require the approval of more than one insurance commissioner, the public hearing could be held in on a consolidated basis within the United States. In connection with a domestic insurer's change of control, a determination by the Director that the person acquiring control of the insurer would have to maintain or restore the capital of the insurer to the level required by the Code would have to be made within 60 days of the date of notification under Section 1311.

Registration Statements & Reporting

An insurer subject to registration under Chapter 13 is required to file a registration statement on a form provided by the Director containing current information as to the capital structure of the insurer, agreements in force, and other information. The bill would require the registration statement to include statements that the insurer's board of directors oversaw corporate governance and internal controls, and that the officers and management had approved, implemented, and continued to maintain and monitor those procedures.

The Code provides that if the person ultimately, or intermediately, controlling an insurer is registered on a national stock exchange or is required to make periodic reports to the U.S. Securities and Exchange Commission (SEC) or other instrumentality of a state, the United States, or a foreign jurisdiction, the insurer must file those reports with the Director. The bill would require the insurer to include financial statements of or within an insurance holding company system, if requested by the Director. The insurer could satisfy this requirement by providing the Director with the most recently filed parent corporation financial statements filed with the SEC.

Transactions Requiring Prior Notice

The Code prohibits a domestic insurer and a person in its holding company from entering into certain transactions unless the insurer notifies the Director in writing at least 30 days before entering into the transaction. The bill would apply this notice requirement to the modification of an existing transaction, and would extend these provisions to the following transactions:

-- A quantifiable guarantee that exceeds the lesser of 0.5% of the insurer's admitted assets or 10% of surplus as of December 31 of the immediately preceding year.
-- An acquisition of, or investment in, a person that controls the insurer, or an affiliate of the insurer, if the amount of the transaction plus the insurer's present holding exceeds 2.5% of surplus.
-- A tax allocation agreement.
-- A cost-sharing agreement.

Director's Powers

The Code allows the Director to order an insurer registered under Chapter 13 to produce documents and other information in the insurer's or its affiliates' possession as necessary to determine the insurer's financial condition. Under the bill, this determination would include enterprise risk to the insurer by the controlling party, by combination of entities within the insurance holding company system, or by the company system on a consolidated basis. The Director also could order a registered insurer to produce information not in the insurer's possession if the insurer could obtain the information by some other method. If the insurer could not obtain the information, it would have to provide the Director with an explanation of the reason that the information could not be obtained and the identity of the holder of the information. If the Director determined that the explanation was without merit, the Director could require, after notice and hearing, the insurer to pay a civil fine of $1,000 per day for each day's delay and could suspend or revoke the insurer's license.

The bill specifies that the information and documents disclosed to the Director would not be subject to the Freedom of Information Act, and would not be subject to discovery or admissible as evidence in a private civil action. The Director, or a person who received documents or information while acting under the Director's authority, could not testify in a private civil action concerning those documents or information. The Director could share the documents and information, including confidential and privileged documents or information with other states, Federal, and international regulatory agencies, the National Association of Insurance Commissioners (NAIC), and state, Federal, and international law enforcement agencies, provided the entity agreed in writing to maintain the confidentiality and privileged status of the documents and information. The Director could receive from regulatory and law enforcement officials, and from the NAIC, information and documents, including confidential or privileged information or documents, and would have to maintain those materials as confidential or privileged. The Director could enter into agreements that provided the basis for sharing confidential information with state, Federal, and international regulatory agencies.

Documents and other information in the possession or control of the Department or the NAIC would be confidential and privileged, would not be subject to the Freedom of Information Act or subpoena, and would not be subject to discovery in a private civil action.

The Director would have to enter into written agreements with the NAIC governing sharing and use of the information, as prescribed by the bill. The sharing of information by the Director would not be a delegation of regulatory authority or rule-making, and the Director would be solely responsible for the administration, execution, and enforcement of these provisions.

The Director could participate in a supervisory college with other regulators for a domestic insurer that was part of an insurance holding company system with international operations to determine the insurer's financial condition, financial strategy, legality of conduct, and other processes or positions. The Director's authority would include initiating a supervisory college, clarifying membership of others supervisors in the supervisory college, coordinating ongoing activities, and establishing a crisis management plan. The insurer would be liable for the reasonable expenses for the Director to participate in the supervisory college, including reasonable travel expenses.

The bill also specifies that if the Director determined that a person violated Section 1311 and the violation prevented the full understanding of the enterprise risk of the insurer by affiliates or by the insurance holding company system, the violation could serve as an independent basis for disapproving dividends and for placing the insurer under an order of supervision.

MCL 500.102 et al. Legislative Analyst: Jeff Mann

FISCAL IMPACT

The bill would have a minor, but potentially positive, fiscal impact on the State and no fiscal impact on local units of government. The bill would allow the Director of the Department of Insurance and Financial Services to levy a civil fine of up to $1,000 per day upon an insurer that provided a meritless explanation as to why it was unable to produce certain information. It is unknown how much revenue would be generated from these fines, but the fines would be credited to the State General Fund.

Fiscal Analyst: Josh Sefton

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This analysis was prepared by nonpartisan Senate staff for use by the Senate in its deliberations and does not constitute an official statement of legislative intent.