SENATE BILL No. 291

Introduced by Committee on Banking, Finance and Insurance (Senators Calderon (Chair), Correa, Cox, Florez, Harman, Kehoe, Liu, Lowenthal, Padilla, and Runner)

February 25, 2009

An act to amend Sections 1215.5 and 11136 of the Insurance Code, relating to insurance regulations.

LEGISLATIVE COUNSEL'S DIGEST

SB 291, as introduced, Committee on Banking, Finance and Insurance. Insurance regulations.

Existing law prohibits domestic insurers or commercially domiciled insurers from entering into specified transactions unless they have notified the Insurance Commissioner of their intent to enter into the transaction in advance of entering into the transaction and the commissioner fails to prohibit the transaction, as specified.

This bill would specify that tax sharing agreements are among the types of transactions for which the insurer would have to give the commissioner advanced notification of its intent to enter into the transaction, as specified.

Existing law defines a fraternal benefit society as an incorporated society or supreme lodge without capital stock conducted solely for the benefit of its members and members' beneficiaries and not for profit. Under existing law, a fraternal benefit society may issue certificates of insurance providing for the payment of life and disability insurance benefits, as specified. Existing law requires fraternal benefit societies to use, among other tables, mortality tables approved by regulation promulgated by the Insurance Commissioner for purposes of determining actuary values, as specified.

This bill would, in addition, authorize fraternal benefit societies to use mortality tables approved by bulletin issued by the commissioner for purposes of determining actuary values, as specified.

Vote: majority. Appropriation: no. Fiscal committee: no. State-mandated local program: no.

The people of the State of California do enact as follows:

SECTION 1. Section 1215.5 of the Insurance Code is amended to read:

1215.5. (a) Transactions by registered insurers with their affiliates are subject to the following standards:

(1) The terms shall be fair and reasonable.

(2) Charges or fees for services performed shall be reasonable.

(3) Expenses incurred and payment received shall be allocated to the insurer in conformity with customary insurance accounting practices consistently applied.

(4) The books, accounts, and records of each party to all transactions shall be so maintained as to clearly and accurately disclose the precise nature and details of the transactions, including accounting information that is necessary to support the reasonableness of the charges or fees to the parties.

(5) The insurer's policyholder's surplus following any dividends or distributions to shareholder affiliates shall be reasonable in relation to the insurer's outstanding liabilities and adequate to its financial needs.

(b) The following transactions involving a domestic insurer or commercially domiciled insurer, as defined in Section 1215.13, and any person in its holding company system, may be entered into only if the insurer has notified the commissioner in writing of its intention to enter into the transaction at least 30 days prior thereto, or a shorter period as the commissioner may permit, and the commissioner has not disapproved it within that period. The commissioner shall require the payment of one thousand eight hundred eighty-nine dollars ($1,889) as a fee for filings under this subdivision. The payment shall accompany the filing.

(1) Sales, purchases, exchanges, loans, extensions of credit, or investments, if the transactions are equal to or exceed:

(A) For a nonlife insurer, the ~~lessor~~ *lesser* of 3 percent of the insurer's admitted assets or 25 percent of the policyholder's surplus as of the preceding December 31st.

(B) For a life insurer, 3 percent of the insurer's admitted assets as of the preceding December 31st.

(2) Loans or extensions of credit to a person who is not an affiliate, if made with the agreement or understanding that the proceeds of the transactions, in whole or in substantial part, are to be used to make loans or extensions of credit to, to purchase assets of, or to make investments in, any affiliate of the insurer, if the transactions are equal to or exceed:

(A) For a nonlife insurer, the lesser of 3 percent of the insurer's admitted assets or 25 percent of the policyholder's surplus as of the preceding December 31st.

(B) For a life insurer, 3 percent of the insurer's admitted assets as of the preceding December 31st.

(3) Reinsurance agreements or modifications thereto in which the reinsurance premium or a change in the insurer's liabilities equals or exceeds 5 percent of the insurer's policyholder's surplus, as of the preceding December 31st, including those agreements that may require as consideration the transfer of assets from an insurer to a nonaffiliate, if an agreement or understanding exists between the insurer and nonaffiliate that any portion of the assets will be transferred to one or more affiliates of the insurer.

(4) All management agreements, service contracts, *tax sharing agreements,* and cost-sharing arrangements. However, subscription agreements or powers of attorney executed by subscribers of a reciprocal or interinsurance exchange are not required to be reported pursuant to this section if the form of the agreement was in use before 1943 and was not amended in any way to modify payments, fees, or waivers of fees or otherwise substantially amended after 1943. Payment or waiver of fees or other amounts due under subscription agreements or powers of attorney forms that were in use before 1943 and that have not been amended in any way to modify payments, fees, or waiver of fees, or otherwise substantially amended after 1943 shall not be subject to regulation pursuant to paragraph (2) of subdivision (a).

(5) Guarantees when initiated or made by a domestic or commercially domiciled insurer, provided that a guarantee that is quantifiable as to amount is not subject to the notice requirements

of this paragraph unless it exceeds the lesser of one-half of 1 percent of the insurer's admitted assets or 10 percent of surplus as regards policyholders as of the 31st day of December next preceding. Further, all guarantees that are not quantifiable as to amount are subject to the notice requirements of this paragraph.

(6) Derivative transactions or series of derivative transactions. The written filing to the commissioner shall include the type or types of derivative transactions, the affiliate or affiliates engaging with the insurer in the derivative transactions, the objective and the rationale for the derivative transaction or series of derivative transactions, the maximum maturity and economic effect of the derivative transactions, and any other information required by the commissioner. Derivative transactions entered into pursuant to this subdivision shall comply with the provisions of Section 1211.

(7) Direct or indirect acquisitions or investments in a person that controls the insurer or in an affiliate of the insurer in an amount that, together with its present holdings in those investments, exceeds 2.5 percent of the insurer's policyholder's surplus. Direct or indirect acquisitions or investments in subsidiaries acquired under Section 1215.1, or in nonsubsidiary insurance affiliates that are subject to the provisions of this article, or in subsidiaries acquired pursuant to Section 1199, are exempt from this requirement.

(8) Any material transactions, specified by regulation, that the commissioner determines may adversely affect the interests of the insurer's policyholders.

(c) A domestic insurer may not enter into transactions that are part of a plan or series of transactions with persons within the holding company system if the purpose of those transactions is to avoid the statutory threshold amount and thus avoid review. If the commissioner determines that separate transactions were entered into over any 12-month period to avoid review, the commissioner may exercise his or her authority under Section 1215.10.

(d) The commissioner, in reviewing transactions under subdivision (b), shall consider whether the transactions comply with the standards set forth in subdivision (a) and whether they may adversely affect the interests of policyholders.

(e) The commissioner shall be notified within 30 days of any investment by the insurer in any one corporation if the total

investment in the corporation by the insurance holding company system exceeds 10 percent of the corporation's voting securities.

(f) For purposes of this article, in determining whether an insurer's policyholder's surplus is reasonable in relation to the insurer's outstanding liabilities and adequate to its financial needs, the following factors, among others, shall be considered:

(1) The size of the insurer, as measured by its assets, capital and surplus, reserves, premium writings, insurance in force, and other appropriate criteria.

(2) The extent to which the insurer's business is diversified among the several lines of insurance.

(3) The number and size of risks insured in each line of business.

(4) The extent of the geographical dispersion of the insurer's insured risks.

(5) The nature and extent of the insurer's reinsurance program.

(6) The quality, diversification, and liquidity of the insurer's investment portfolio.

(7) The recent past and projected future trend in the size of the insurer's investment portfolio.

(8) The recent past and projected future trend in the size of the insurer's surplus, and the policyholder's surplus maintained by other comparable insurers.

(9) The adequacy of the insurer's reserves.

(10) The quality and liquidity of investments in subsidiaries made under Section 1215.1. The commissioner may treat any such investment as a disallowed asset for purposes of determining the adequacy of the policyholder's surplus whenever, in his or her judgment, the investment so warrants.

(11) The quality of the company's earnings and the extent to which the reported earnings include extraordinary accounting items.

(g) No insurer subject to registration under Section 1215.4 shall pay any extraordinary dividend or make any other extraordinary distribution to its stockholders until 30 days after the commissioner has received notice of the declaration thereof and has approved the payment or has not, within the 30-day period, disapproved the payment.

For purposes of this section, an extraordinary dividend or distribution is any dividend or distribution which, together with other dividends or distributions made within the preceding 12

months, exceeds the greater of (1) 10 percent of the insurer's policyholder's surplus as of the preceding December 31st, or (2) the net gain from operations of the insurer, if the insurer is a life insurer, or the net income, if the insurer is not a life insurer, for the 12-month period ending the preceding December 31st.

Notwithstanding any other provision of law, an insurer may declare an extraordinary dividend or distribution that is conditional upon the commissioner's approval. The declaration confers no rights upon stockholders until the commissioner has approved the payment of the dividend or distribution or until the commissioner has not disapproved the payment within the 30-day period referred to in this subdivision.

(h) Notwithstanding the control of a domestic insurer by any person, the officers and directors of the insurer shall not thereby be relieved of any obligation or liability to which they would otherwise be subject to by law, and the insurer shall be managed to ensure its separate operating identity consistent with the provisions of this article. However, nothing in this article shall preclude a domestic insurer from having or sharing a common management or cooperative or joint use of personnel, property, or services with one or more other persons under arrangements meeting the standards of subdivision (a).

(i) The provisions of this section do not apply to any insurer, information, or transaction exempted by the commissioner.

SEC. 2. Section 11136 of the Insurance Code is amended to read:

11136. Except as otherwise provided in Section 10489.4, such valuation shall be certified by a competent actuary or, at the expense of the society, verified by the actuary of the insurance supervisory official of the state of domicile of the society, and the legal minimum standard of valuation shall be as follows:

(a) All benefits promised by certificates issued prior to September 22, 1952, and the rates therefor shall be valued in accordance with the provisions of law applicable thereto as of the date of issuance, but not lower than the standards and interest assumptions used in the calculation of rates for such benefits.

(b) The minimum standard for the valuation of all certificates issued after September 21, 1952, and prior to January 1, 1972, shall be 3 percent per annum interest; in the case of certificates issued on and after January 1, 1972, and prior to January 1, 1980,

the minimum standard for the valuation of all such certificates shall be 4 percent per annum interest; and in the case of certificates issued on and after January 1, 1980, the minimum standard for the valuation of all single premium certificates shall be 5½ percent per annum interest and for the valuation of all other such certificates shall be 4½ percent per annum interest, and the following tables:

(1) For all ordinary certificates of life insurance issued on the standard basis, excluding any disability and accidental death benefits in such certificates—the American Men Ultimate Table of Mortality, with Bowerman's or Davis' Extension thereof, or, at the option of the society, the Commissioners 1941 Standard Ordinary Mortality Table or the Commissioners 1958 Standard Ordinary Mortality Table, using actual age of the insured for male risks and an age not more than six years younger than the actual age of the insured for female risks, and for such policies issued on or after the operative date of Section 10163.2 (i) the Commissioners 1980 Standard Ordinary Mortality Table, or (ii) at the election of the company for any one or more specified plans of life insurance, the Commissioners 1980 Standard Ordinary Mortality Table with Ten-Year Select Mortality Factors, or (iii) any ordinary mortality table, adopted after 1980 by the National Association of Insurance Commissioners, or its successor, that is approved by regulation promulgated *or bulletin issued* by the commissioner for use in determining the minimum standard of valuation for such policies.

(2) For all industrial life insurance certificates issued on the standard basis, excluding any disability and accidental death benefits in such certificates—the 1941 Standard Industrial Mortality Table, for such certificates issued prior to the operative date of Section 10163.2, and for such policies issued on or after such operative date, the Commissioners 1961 Standard Industrial Mortality Table or any industrial mortality table, adopted after 1980 by the National Association of Insurance Commissioners, or its successor, that is approved by regulation promulgated *or bulletin issued* by the commissioner for use in determining the minimum standard of valuation for such policies.

(3) For annuity and pure endowment certificates, excluding any disability and accidental death benefits in such certificates—the 1937 Standard Annuity Mortality Table, or the Annuity Mortality Table for 1949 Ultimate, or the Individual Annuity Mortality Table

for 1971, or any individual annuity mortality table, adopted after 1980 by the National Association of Insurance Commissioners, or its successor, that is approved by regulation promulgated *or bulletin issued* by the commissioner for use in determining the minimum standard of valuation for such contracts, or any modification of any of these tables approved by the commissioner.

(4) For disability benefits in or supplementary to ordinary certificates—Hunter's Disability Table or the Class 3 Disability Table (1926), modified to conform to the contractual waiting period, or the tables of Period 2 disablement rates and the 1930 to 1950 termination rates of the 1952 Disability Study of the Society of Actuaries with due regard to the type of benefit, or the 1964 Commissioners Disability Table, or any tables of disablement rates and termination rates, adopted after 1980 by the National Association of Insurance Commissioners, or its successor, that are approved by regulation promulgated *or bulletin issued* by the commissioner for use in determining the minimum standard of valuation for such policies. Any such table shall, for active lives, be combined with a mortality table permitted for calculating the reserves for life insurance certificates.

(5) For accidental death benefits in or supplementary to certificates—The Inter-Company Double Indemnity Mortality Table or the 1959 Accidental Death Benefits Table, or any accidental death benefits table, adopted after 1980 by the National Association of Insurance Commissioners, or its successor, that is approved by regulation promulgated *or bulletin issued* by the commissioner for use in determining the minimum standard of valuation for such policies. Any such table shall be combined with a mortality table permitted for calculating the reserves for life insurance certificates.

(6) For temporary accident and health benefits in or supplementary to certificates—Class 3 Disability Table (1926) with Conference Modifications or the 1964 Commissioners Disability Table, or any tables of disablement rates and termination rates, adopted after 1980 by the National Association of Insurance Commissioners, or its successor, that are approved by regulation promulgated *or bulletin issued* by the commissioner for use in determining the minimum standard of valuation for such policies.

(7) For life insurance issued upon the substandard basis and other special benefits—such tables as may be approved by the commissioner.

(c) The commissioner may, in his discretion, accept other standards for valuation if he finds that the reserves produced thereby will not be less in the aggregate than reserves computed in accordance with the minimum valuation standard prescribed. Whenever the mortality experience under the certificates valued on the same mortality table is in excess of the expected mortality according to such table for a period of three consecutive years, the commissioner may require additional reserves when in his judgment deemed necessary on account of such certificates.

(d) Notwithstanding the provisions of subdivisions (a) and (b), any society, with the consent of the insurance supervisory official of the state of domicile of the society, and under such conditions, if any, which he may impose, may establish and maintain reserves on its certificates in excess of the reserves required thereunder, but the contractual rights of any insured member shall not be affected thereby.

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