The Florida Senate

BILL ANALYSIS AND FISCAL IMPACT STATEMENT

(This document is based on the provisions contained in the legislation as of the latest date listed below.)

Prepared By: The Professional Staff of the Committee on Banking and Insurance

BILL:	SB 1308
INTRODUCER:	Senator Simmons
SUBJECT:	Insurer Solvency
DATE:	March 10, 2014
REVISED:	

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	Johnson	Knudson	BI	**Pre-meeting**
2.			JU	
3.			RC	

I. Summary:

SB 1308 revises provisions within the Insurance Code relating to solvency requirements and regulatory oversight of insurers by the Office of Insurance Regulation (OIR). The bill incorporates provisions of model acts of the National Association of Insurance Commissioners (NAIC) and additional recommendations of the OIR. Some of the NAIC provisions in the bill are in response to the 2008 financial crisis and the globalization of the insurance market and are intended to enhance the regulation of insurers as well as their affiliated entities and provide more solvency tools for evaluating risks within insurance groups. The bill:

- Authorizes the OIR to implement principle-based reserving for life insurers, which would allow life insurers to calculate reserves that would reflect current mortality rates, the life insurer's business model, and its particular risk profile.
- Requires persons that acquire controlling interests to disclose enterprise risk, and requires that ultimate controlling persons must file an annual enterprise risk report with the OIR that identifies material risk within the insurance company holding company system that could pose a risk or have a material adverse effect upon the insurer.
- Provides that a presumption of control may be rebutted by filing a disclaimer of control on a form prescribed by the OIR or by providing a copy of a Schedule 13G on file with the Securities and Exchange Commission. After a disclaimer is filed, the insurer is relieved of any further duty to register or report under s. 628.461, F.S., unless the OIR disallows the disclaimer.
- Incorporates a risk-based capital trend test for life and health and property and casualty insurers and requires health maintenance organizations and prepaid limited health service organizations to file risk-based capital reports.
- Requires insurers to file actuarial opinion summaries and supporting workpapers annually and the bill provides a privilege for memoranda supporting actuarial opinions on reserves, actuarial opinion summaries and related information and provides for confidentiality of enterprise risk reports, actuarial opinion summaries, and other information.

- Authorizes the OIR to impose sanctions for noncompliance with the requirements of s. 628.461, F.S., and s. 628.801, F.S.
- Allows the OIR to participate in supervisory colleges with other regulators for the regulation of any domestic insurer that is part of an insurance holding company system with international operations.

II. Present Situation:

States primarily regulate insurance companies. The state of domicile serves as the primary regulator for insurers. Solvency regulation is designed to protect policyholders against the risk that insurers will not be able to meet their financial responsibilities. The OIR[1] is primarily responsible for monitoring the solvency of regulated insurers and examining insurers to determine compliance with applicable laws, and taking administrative action, if necessary. Solvency regulation includes the requirements for starting and operating an insurance company,[2] monitoring the financial condition of insurers through examinations and audits, and procedures for the administrative supervision,[3] rehabilitation,[4] or liquidation[5] of an insurance company if it is in unsound financial condition or insolvent.

NAIC Model Acts

The National Association of Insurance Commissioners (NAIC) is a voluntary association of insurance regulators from all 50 states. The NAIC coordinates regulation and examination of multistate insurers, provides a forum for addressing major insurance issues, and promotes uniform model laws among the states. The NAIC accreditation is a certification that legal, financial, and organizational standards are being fulfilled by the OIR. The NAIC establishes accreditation effective dates for states to adopt in substantially similar form models and acts for purposes of NAIC accreditation review. As a member of the NAIC, the OIR is required to participate in the Financial Regulation Standards and Accreditation Program. The OIR has identified model provisions or updates that need to be incorporated in the current Insurance Code for accreditation purposes. Updates to the Insurance Code relating to the Property and Casualty Trend Test of the Risk-Based Capital Model Act and the Property and Casualty Actuarial Opinion Model Law are necessary since the accreditation effective dates for these provisions were January 1, 2012, and January 1, 2010, respectively. In addition, two other NAIC model acts, Risk-Based Capital for Health Organizations and the Life Trend Test of the Risk Based Capital Model Act are necessary for accreditation effective January 1, 2015, and January 1, 2017, respectively. The accreditation effective date for amendments to the Insurance Holding Company System Regulatory Act is January 1, 2016.

[1] Section 20.121(3)(a), F.S.
[2] Sections 624.411 - 624.414, F.S.
[3] Administrative supervision allows the Department of Financial Services (DFS) to supervise the management of a consenting troubled insurance company in an attempt to cure the company's troubles rather than close it down.
[4] In rehabilitation, the DFS is authorized as receiver to conduct all business of the insurer in an attempt to place the insurance company back in sound financial condition.
[5] In liquidation, the DFS is authorized as receiver to gather the insurance company's assets, convert them to cash, distribute them to various claimants, and shut down the company.

Model Holding Company Act and Regulation

The NAIC has adopted amendments to its Insurance Holding Company System Regulatory Model Act and the Insurance Holding Company Model Regulation with Reporting Forms and Instructions. In light of the recent financial crisis, the NAIC, insurance regulators, and other stakeholders reviewed the potential impact of non-insurance operations on insurance companies in the same group to determine the best methods to evaluate the risks and activities of entities within a holding company system. The revised model act adds the concept of "enterprise risk" and requires controlled insurers to file a new annual form (Form F) detailing specified matters relating to the holding company group. The NAIC model act defines "enterprise risk" as:

> [A]ny 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 of its insurance company as a whole, including, but not limited to, anything that would cause the insurer's risk-based capital as set forth in [state requirement] or would cause the insurer to be in a hazardous financial condition.[6]

Amendments to the model act also address divestitures. Prior to the amendments to the model act, a person could divest control of an insurer without prior regulatory review as long as no single acquirer obtained control of 10 percent or more of the outstanding voting shares. Amendments to the model act generally require a person divesting control over an insurer to provide 30 days' prior notice to the regulator.

The revised model act also provides insurance regulators access to information of an insurer and its affiliates to ascertain the financial condition of the insurer, including the enterprise risk to the insurer by the ultimate controlling party. The regulator may require any insurer registered as a controlled insurer to produce information not in the possession of the insurer if the insurer can obtain access to such. If the insurer fails to obtain the requested information, the insurer is required to provide an explanation of such failure. If the regulator determines that the explanation is without merit, the regulator may require the insurer to pay a penalty for each day's delay, or may suspend or revoke the insurer's certificate of authority.[7]

The amendments to the model acts also authorize a regulator 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. Insurers would pay for expenses associated with the insurance regulator's participation in a supervisory college. State, federal, and international regulators may participate in the supervision of the insurer or its affiliates.[8] According to the NAIC Center for Insurance Policy & Research, "a supervisory college is a meeting of insurance regulators or supervisors where the topic of discussion is regulatory oversight of one specific insurance group that is writing significant amounts of insurance in other jurisdictions."[9] Supervisory colleges facilitate oversight of internationally active insurance

[6] Section 1F of the NAIC Insurance Holding Company System Regulatory Act.
[7] Section 6B of the NAIC Insurance Holding Company System Regulatory Act.
[8] Section 7 of the NAIC Insurance Holding Company System Regulatory Act.
[9] "Supervisory Colleges: A Regulatory Tool for Enhancing Supervisory Cooperation and Coordination," at http://www.naic.org/cipr_newsletter_archive/vol4_supervisory_colleges.htm (last visited on March 9, 2014).

companies at the group level and promote regulatory information sharing, subject to applicable confidentiality agreements.[10]

Risk-Based Capital for Insurers and Health Organizations

Risk-based capital (RBC) is a capital adequacy standard that represents the amount of required capital that an insurer must maintain, based on the inherent risks in the insurer's operations. It is determined by a formula that considers various risks depending on the type of insurer (e.g., subsidiary insurance companies, fixed income, equity, credit, reserves, and net written premium). The RBC standard provides a safety net for insurers, is uniform among states, and provides state insurance regulators with authority for timely corrective action.[11] The NAIC's *Risk-Based Capital for Insurers Model Act* provides that states must require both life and health and property and casualty insurers to submit RBC filings with their regulators. Presently, this requirement is incorporated in the Insurance Code; however, it does not apply to health maintenance organizations (HMOs) and prepaid limited health service organizations.[12] Prepaid limited health service organizations provide limited health services (such as dental or vision care) through an exclusive panel of providers in return for a prepayment,[13] and HMOs generally provide a range of health coverage with contracted providers.[14] The NAIC Risk-Based Capital Health Organizations Model Act will be effective as an accreditation standard beginning January 1, 2015, and applies to health maintenance organizations and prepaid limited health service organization.

In March 2006, the NAIC adopted revisions to the Risk-Based Capital for Insurers Model Act. The revisions incorporate a new Property and Casualty Trend Test for property and casualty companies. The accreditation effective date for property and casualty trend test was January 1, 2012. A statutory provision relating to a life trend test was already included in the RBC for Insurers Model Act; but the changes equalize the trigger between life and health, property, and casualty companies that prompt the need for a trend test calculation. The model was amended to cite the Property and Casualty Trend Test as a means for the company action level to be triggered.

Property and Casualty Actuarial Opinion Model Law

The NAIC Property and Casualty Actuarial Opinion Model Law specifies that states must require property and casualty insurers to submit a Statement of Actuarial Opinion, which is a public document. The model act also requires the submission of an Actuarial Opinion Summary, an Actuarial Report, and workpapers to support each actuarial opinion, which must be treated as a confidential and privileged document.

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[10] NAIC on Supervisory Colleges at http://www.naic.org/cipr_topics/topic_supervisory_college.htm. (last visited on March 9, 2014). Additionally, the linked/public records bill, SB 1300, provides for confidential and exempt treatment of regulatory information, including within the context of a supervisory college that is shared between insurance regulators and law enforcement, pursuant to confidentiality agreements.

[11] NAIC on Risk-Based Capital at http://www.naic.org/cipr_topics/topic_risk_based_capital.htm (last visited on Mar. 9, 2014).

[12] Section 624.4085, F.S.

[13] Section 636.003(7), F.S.

[14] Section 641.19(12), F.S.

Current law requires insurers (except those providing life insurance and title insurance) to provide to the OIR an annual statement of its financial condition and a statement of opinion on loss and loss adjustment expense reserves prepared by an actuary or a qualified loss reserve specialists. These insurers are also required to provide supporting work papers upon the OIR's request.[15] Currently, these materials are not exempt from ch. 119, F.S., relating to public records.

Valuation of Life Insurance and Principle-Based Reserves

For insurance purposes, reserves are liabilities that are reported on insurers' balance sheets for the ultimate payment of future losses and policyholder benefits. Reserves are often set using factors and rates determined by an insurer's actuary consistent with guidelines for insurance products established in state law consistent with NAIC models or laws. Reserve levels for insurers operating in the United States and offering certain life insurance and annuity products are set according to a state law, with rules-based formula that, some insurers claim, results in excessive reserves that detract from the insurer's ability to maximize the value of its capital.

Critics of the current formula-based approach to reserving for life insurance contend that it: (1) is static and too conservative; (2) fails to capture all the particularized risks inherent in increasingly complicated life insurance benefits and guaranties; and (3) does not reflect life insurers' business practices, such as the hedging of risk through derivatives use plans. However, reserves are subject to an annual analysis to verify the adequacy of reserves through different models, with additional reserves established if necessary. Many industry participants argue that redundant reserve requirements force reliance upon reinsurance captives in order to reduce excessive reserves and allow life insurers to use capital more effectively.

While the current formula-based approach to quantifying reserves uses standardized formulas, principle based reserves (PBR) relies upon an insurer's internal risk modeling and analysis techniques, including the use of insurer-specific claims experience with specific portfolios of business, to incorporate consideration of particularized risks and thereby to more closely tailor calculations to the actual attributes of insurer portfolios.

In response to concerns about reserves, the National Association of Insurance Commissioners (NAIC) revised the NAIC Standard Valuation Law (SVL) and the Standard Nonforfeiture Law to incorporate the NAIC Valuation Manual as the authoritative source for reserves and other requirements.[16] The revised SVL, as adopted by the NAIC, would preserve state authority to require insurers to change any assumption or method, as necessary, and authorize the regulator to engage a qualified actuary at the expense of an insurer to review compliance with the valuation manual requirements. The manual includes experience reporting, actuarial opinion and memorandum requirements, PBR reporting, and corporate governance requirements. Many of the requirements are dynamic in nature, and are responsive to fluctuations in the insurance marketplace and the economy. The requirements of the manual are applicable to life insurance contracts, accident and health contracts, and other specified contracts. Some products are not subject to PBR; however, some products, such as term life insurance policies and universal life insurance policies with a secondary guarantee[17] issued on or after the operative date of the

[15] Section 624.424, F.S.
[16] The Valuation Manual was adopted by the NAIC on December 2, 2012.
[17] A universal life policy with a secondary guarantee is also known as a no-lapse guarantee. The policy will not lapse if

manual would be subject to PBR once the manual is operative. The PBR method will be effective only after the SVL law revisions are adopted by at least 42 states representing 75 percent of total U.S. premium and then, after a 3-year transition period. However, insurers can implement PBR anytime during the transition period.

Under current Florida law, life insurers are required to calculate reserves for life insurance policies based on a standardized formula prescribed by the NAIC Model Standard Valuation Law (SVL) and codified in s. 625.121, F.S. The SVL incorporates mortality tables. The NAIC Standard Nonforfeiture Law establishes minimum benefit values if policies are surrendered or lapsed and is codified in s. 627.476, F.S. For purposes of the implementation of PBR, the NAIC revised the Standard Nonforfeiture Law to reference the Standard Valuation Law and the Valuation Manual as the source for mortality and interest rates used in nonforfeiture calculations. However, such changes would apply to policies issued on or after the operative date of the valuation manual. The PBR requirements do not apply to policies issued prior to the operative date of the valuation manual.

In 2013, seven states enacted PBR enabling legislation (Arizona, Indiana, Louisiana, Maine, New Hampshire, Rhode Island, and Tennessee). In 2013, Texas enacted the Standard Nonforfeiture Law revisions. Nine states have introduced PBR enabling legislation in 2014 (Hawaii, Illinois, Iowa, Mississippi, Nebraska, New Mexico, Ohio, Oklahoma, and Virginia). Five more states have drafted legislation for 2014 introduction (Connecticut, Florida, Georgia, Missouri, and West Virginia).[18]

III. Effect of Proposed Changes:

Examinations

Section 2 amends s. 624.319, F.S., relating to examinations, to provide that the production of documents during the course of an examination or investigation does not constitute waiver of the attorney-client or work-product privileges.

Captives

Section 5 requires insurers that reinsure through a captive insurance company to file with the OIR an annual report containing certain information specific to reinsurance assumed by each captive.

Risk-Based Capital for Insurers and Health Organizations (Sections 4, 15, 16, and 17)

The bill amends s. 624.4085, F.S., to revise the definition of the term, "life and health insurer," for purposes of risk-based capital (RBC) requirements to include HMOs and prepaid limited health service organizations that are authorized in Florida and one or more other states, jurisdictions, or countries effective January 1, 2015. The section also clarifies the RBC requirements for a life and health insurer that reports using the life and health annual statement

certain conditions are met.

[18] American Council of Life Insurers PBR Implementation Status, February 3, 2014, (on file with Senate Banking and Insurance staff).

instructions and changes a company action level event to total adjusted capital that is greater than or equal to its company action level RBC but less than the product of its authorized control level risk-based capital and 3.0.

Effective January 1, 2015, the section also defines the RBC requirements for a life and health, as well as property and casualty, insurer that reports using the health annual statement instructions and defines a company action level event as total adjusted capital that is greater than or equal to its company action level risk-based capital but less than the product of its authorized control level RBC and 3.0 and triggers the trend test calculation. An insurer that fails the Trend Test would be subject to filing a corrective action plan with the OIR.

The bill provides that prepaid limited health service organizations authorized in Florida are subject to the RBC requirements and confidentially requirements pursuant to s. 624.4085, F.S., and s. 624.40851, F.S., respectively. The bill also provides that an HMO that is authorized in one or more other states, jurisdictions, or countries is subject to the risk-based capital requirements for insurers as well as the confidentiality protections of risk-based capital information provided in s. 624.4085, F.S., and s. 624.4615, F.S., respectively. Finally, an HMO that is a member of a holding company system is subject to the acquisition and enterprise risk reporting requirements of s. 628.461, F.S., but not to the acquisition requirements for specialty insurers in s. 628.4615, F.S. These provisions are effective January 1, 2015.

Model Insurance Holding Company Act and Regulation (Sections 1, 3, 10-14)

Section 1 provides definitions of affiliate, affiliated person, control, and NAIC. The definitions of the terms, "affiliated person" and "controlling person" currently defined in s. 628.461(12), F.S., are modified and transferred. The bill revises the definition of the term, "affiliated person," to include persons affiliated through 10 percent instead of 5 percent of ownership, control, or management. The bill revises the definition of the term, "controlling person," to require a 10 percent rather than a 25 percent ownership or interest. Section 3 amends s. 624.402, F.S., to provide a technical, conforming amendment.

Section 10 amends s. 628.461, F.S., relating to acquisition of controlling stock, and specifies that the acquiring party's statement must include an agreement to file an "annual enterprise risk report," if control exists as described in Section 11 of the bill. Effective January 1, 2015, the bill provides that the person required to file the statement pursuant to s. 628.461(1), F.S., will provide the annual report specified in s. 628.801(2), F.S., if control exists. The bill provides that the presumption of control may be rebutted by filing a disclaimer of control on a form prescribed by the OFR, as required by the model act, or by providing a copy of a Schedule 13G on file with the U.S. Securities and Exchange Commission. After a disclaimer is filed, the insurer is relieved of any further duty to register or report under s. 628.461, F.S., unless the OIR disallows the disclaimer. Any controlling person of a domestic insurer that seeks to divest its controlling interest in the domestic insurer is required to file with the OIR a confidential notice of its proposed divestiture at least 30 days prior to the relinquishment of control.

Currently, s. 628.461, F.S., provides that a person or affiliated person must file a letter of notification and a statement for the OIR's approval before concluding a tender offer to acquire 5 percent or more of a domestic stock insurer or of a controlling company. The statement must

contain certain criminal, employment, and regulatory history information. Alternatively, a party acquiring less than 10 percent of the outstanding voting securities of an insurer may file a disclaimer of affiliation of control, and such disclaimer must fully disclose all material relationships and affiliation with the insurer, as well as the reason for such disclaimer (this disclaimer is mandatory for acquisitions of more than 10 percent).

During the pendency of the OIR's review of an acquisition filing, the insurer is not permitted to make a "material change" to its operation or management, unless the OIR has approved or has been notified, respectively. A "material change" consists of a disposal or obligation of 5 percent or more of the insurer's capital and surplus, or a change in management involving a person who has the authority to dispose or obligate 5 percent of the insurer's capital and surplus.

Section 11 amends s. 628.801, F.S., relating to the regulation of insurance holding companies, to amend and update the provisions of the NAIC Insurance Holding Company System Regulatory Model Act and the Insurance Holding Company System Model Regulation by incorporating reference to the 2010 version. The section requires insurers to file an annual holding company registration statement, including disclosure of material transaction between affiliates. Currently, authorized insurers are required to register with the OIR and be subject to regulation with respect to the relationship with the holding company. Pursuant to its authority under ch. 624, F.S., the OIR may examine any insurer and its affiliates registered under this section to ascertain the financial condition of the insurer, including the enterprise risk to the insurer by the ultimate controlling party.

Effective January 1, 2015, the ultimate controlling person in an insurer's holding company must identify and report material risk within the system that could pose enterprise risk to the insurer in an annual enterprise risk report filed with the OIR. The enterprise risk report will contain detailed information including the holding company's business plan, material developments concerning risk management, and rating agency information. Effective January 1, 2015, if an insurer fails to file a registration statement, a summary of the registration statement, or enterprise risk filing report within the specified time, it is a violation of this section. The section also provides criteria under which an insurer may apply for waiver of the requirements contained in s. 628.801, F.S.

Information contained in the enterprise risk report filed with OIR is confidential and exempt as provided in s. 624.4212, F.S. The bill also adds a provision that prohibits the waiver of any applicable privilege or claim of confidentiality in the enterprise risk report because of disclosures to the OIR. The bill provides that the Department of Financial Services or the OIR may use confidential and exempt information in the furtherance of any regulatory or legal action brought against an insurer as part of the official duties of the department or office.

Section 12 amends s. 628.803, F.S., relating to sanctions against an insurance holding company, to provide that a violation of s. 628.461, F.S., (i.e., the filing requirements for acquisition of controlling stock) or s. 628.801, F.S., (i.e., filing requirements for insurance holding companies) may serve as an independent basis for the OIR to disapprove dividends and distributions and place the insurer under an order of supervision pursuant to part VI of ch. 624, F.S. This provision is effective January 1, 2015.

Currently, the Insurance Code states that noncompliant insurance holding companies (and their directors, officers, employees, and agents) can be subject to a number of sanctions that include:

- A penalty, not to exceed $10,000, for failing to file registration statements or certificate of exemption;
- Civil forfeitures, not to exceed $5,000 per violation, for knowingly engaging in transactions that have not been properly filed, approved, or in accordance with commission rule; or
- A cease and desist order for engaging in transactions or entering into contracts that violate commission rules, and rescission orders if in the best interests of the policyholders, creditors, or public.

Additionally, an officer, director, or employee of an insurance holding company who willfully and knowingly submits a false statement, false report, or false filing with the intent to deceive the OIR, is guilty of a felony of the third degree.

Sections 13 and 14 create ss. 628.804 and 628.805, F.S., which authorize the creation and participation by the OIR in a supervisory college with other state, federal, and international regulators charged with supervising an insurer or its affiliates, effective January 1, 2015. The bill provides the terms and conditions of participation. With respect to participation in a supervisory college, the OIR may clarify the membership and participation of other supervisors and clarify the role of other regulators, including the establishment of a groupwide supervisor.

The bill defines, the term, "groupwide supervisor," as the chief insurance regulator for the jurisdiction who is determined by the OIR to have significant contacts with the international insurance group sufficient to conduct and coordinate groupwide supervision activities. The OIR is authorized to adopt rules to implement criteria for determining the appropriate groupwide supervisor. This language, which was requested by the OIR, is supplemental to the NAIC model provision. It is consistent with a law recently enacted in Pennsylvania. In accordance with s. 624.4212, F.S., regarding confidential information sharing, the OIR is authorized to enter into cooperative agreements with other regulators. Expenses associated with a supervisory college would be liable for the payment of reasonable expenses for the OIR's participation.

Property and Casualty Actuarial Opinion Model Law (Section 5)

The bill requires property and casualty insurers to file an annual Statement of Actuarial Opinion and Actuarial Opinion Summary in accordance with the NAIC annual statement instructions. The section also updates the Financial Services Commission's (commission's) rulemaking authority under this section to specify that rules must be in substantial conformity with the 2006 Annual Financial Reporting Model Regulation adopted by the NAIC. Life and health insurers are exempt from the reporting requirements of this section since they are governed by ss. 625.121 and 625.1212, F.S.

Proprietary business information contained in the summary is confidential and exempt under s. 624.4212, F.S. This section also protects the summary and related information from subpoena, discovery, or admissibility in any private civil action. The bill provides that the Department of Financial Services or the OIR may use confidential and exempt information in the furtherance of any regulatory or legal action brought against an insurer as part of the official duties of the department or office.

Valuation of Life Insurance and Principle Based Reserves (Sections 6, 7, 8, and 9)

Standard Valuation Law for Life Insurers

Section 6 amends s. 625.121, F.S., relating to the Standard Valuation Law for life insurance, to provide that any memorandum or other material in support of the actuarial opinion that is currently confidential and exempt from s. 119.07(1), F.S., is not subject to subpoena or discovery, or admissible in evidence in any private civil action. Currently, authorized life insurance companies are required to submit an annual actuarial opinion of reserves, reflecting the valuation of reserve liabilities. This section also provides that neither the OIR nor any person who receives information while acting under the authority of the OIR or with whom such information is shared may testify in any private civil action concerning confidential information. These changes incorporate a provision of the NAIC Standard Valuation Law that provides that this information is not subject to subpoena or discovery, and should not be admissible in any civil action in either documentary or testimonial form. The bill provides that the Department of Financial Services or the OIR may use confidential and exempt information in the furtherance of any regulatory or legal action brought against an insurer as part of the official duties of the department or office.

The bill requires the implementation of the valuation manual and PBR for policies issued on or after the operative date of the valuation manual. Section 625.121, F.S., would apply to policies and contracts issued prior to the operative date of the valuation manual

The bill creates s. 625.1212, F.S., which is applicable to the valuation of policies and contracts issued on or after the operative date of the valuation manual with some exceptions. This would include life insurance contracts, accident and health contracts, and deposit-type policies.[19] The operative date of the valuation manual is defined to mean the latter of January 1, 2017, or the first January 1 following the first July the commissioner of the OIR certifies to the Financial Services Commission that the following conditions have been met:

- The valuation manual is adopted by the NAIC by an affirmative vote of at least 42 members, or three-fourths of the members voting, whichever is greater;
- The Standard Valuation Law, as amended by the NAIC in 2009, or substantially similar legislation, is enacted by states representing greater than 75 percent of the direct premiums written as reported in the following annual statements submitted for 2008: life, accident and health annual statements; health annual statements; or fraternal annual statements; and
- The Standard Valuation Law, as amended by the NAIC in 2009, or substantially similar legislation, has been enacted by at least 42 of the 55 jurisdictions.

The bill requires the OIR to value insurer reserves annually. The OIR may accept a valuation made by another insurance state supervisory official. Insurers are required to submit an actuarial opinion of reserves and memorandum to support each actuarial opinion on an annual basis. The bill provides minimum standard of valuation with exceptions. The OIR may require an insurer to change any assumption or method. The OIR may exempt specific product forms or product lines of a domestic company that is licensed and doing business in Florida from the minimum standards of valuation and the principal-based valuation requirements if certain conditions are

[19] According to the NAIC 2010 Standard Valuation Law, the term "deposit-type contract" means contracts that do not incorporate mortality or morbidity risks and as may be specified in the valuation manual.

met. The Financial Services Commission is authorized to adopt rules to implement s. 625.1212, F.S. Such rules are not subject to s. 120.541(3), F.S.

Section 8 provides that documents and other information created, produced, or obtained pursuant to ss. 625.121 and 625.1212, F.S., are privileged, confidential, and exempt as provided in s. 624.4212, F.S. Senate Bill 1300, which creates s. 624.4212, F.S, is linked to this bill. These documents and other information are not subject to subpoena or discovery, or admissible in evidence in any private civil action. The bill provides that the Department of Financial Services or the OIR may use confidential and exempt information in the furtherance of any regulatory or legal action brought against an insurer as part of the official duties of the department or office.

This section also provides that neither the OIR nor any person who receives information while acting under the authority of the OIR or with whom such information is shared may be permitted or required to testify in any private civil action concerning such confidential and exempt information. These changes incorporate a provision of the NAIC Standard Valuation Law that provides that the information is not subject to subpoena or discovery, and should not be admissible in any civil action in either documentary or testimonial form.

Standard Nonforfeiture Law for Life Insurers

Section 9 provides for the application of the valuation manual for policies issued on or after the operative date of the manual. The bill provides technical conforming changes. The bill also addresses a potential federal income tax issue relating to life insurance contracts by establishing a 4 percent minimum interest rate. Currently, the interest rate per annum for any policy issued in a calendar year is equal to 125 percent of the calendar year statutory valuation interest for such policy as defined in the Standard Valuation Law. The 4 percent floor created by the bill is the annual effective rate used to determine the net single premium for purposes of cash-value accumulation test under Section 7702(b) of the IRC.[20] This provision would codify an amendment to Standard Nonforfeiture Law for Life Insurance, which was adopted by the NAIC.[21] According to the NAIC, the establishment of this floor would address a concern that the interest rate could decline below 4 percent, resulting in traditional life insurance being noncompliant with the maximum cash value requirements of the IRC Section 7702, and not qualify as a life insurance contract for federal income tax purposes.

Effective Date (Section 12)

Section 12 provides that except as otherwise expressly provided in the bill, the act will take effect October 1, 2014, if SB 1300 or similar legislation is adopted in the same legislative session or an extension thereof, and becomes a law.

[20] 26 U.S.C. s. 7702(a) provides that, for a contract to qualify as a life insurance contract for Federal income tax purposes, the contract must be a life insurance contract under the applicable law and must either (1) satisfy the cash value accumulation test of s. 7702(b), or (2) both meet the guideline premium requirements of § 7702(c) and fall within the cash value corridor of s. 7702(d).

[21] The NAIC Executive Committee adopted this change at the 2013 Fall NAIC Meeting.

IV. Constitutional Issues:

A. Municipality/County Mandates Restrictions:

None.

B. Public Records/Open Meetings Issues:

None.

C. Trust Funds Restrictions:

None.

V. Fiscal Impact Statement:

A. Tax/Fee Issues:

None.

B. Private Sector Impact:

Insurers may incur an indeterminate amount of administrative costs associated with complying with the additional reporting requirements and implementing principle based reserves, and the OIR's participation in the supervisory colleges. The PBR requirements would apply to policies issued on or after the operative date of the valuation manual.

Advocates of principle based reserves (PBR) state that the method will reduce redundant reserves that are required pursuant to the current formulaic approach, thereby leading to lower prices for life insurance products, increasing consumer choices of products, and freeing up capital for insurers. Insurers will have the option to phase in the PBR requirements over 3 years after the valuation manual is effective, which would be no earlier than January 1, 2017, as provided in the bill.

C. Government Sector Impact:

The bill provides greater solvency tools and regulatory authority for the OIR. The supervisory college will provide greater coordination of efforts in the examination of multistate insurers and will reduce regulatory redundancies and expenses among the state regulators.

The OIR states there is no anticipated impact for fiscal year 2014-2015.

VI. Technical Deficiencies:

Line 1467 of the bill should be amended to include a reference to SB 1308.

VII. Related Issues:

None.

VIII. Statutes Affected:

This bill substantially amends the following sections of the Florida Statutes: 624.10, 624.319, 624.402, 624.4085, 624.424, 625.121, 627.476, 628.461, 628.801, 628.803, 636.045, 641.225, and 641.255.

This bill creates the following sections of the Florida Statutes: 625.1212, 625.1214, 628.804, and 628.805.

IX. Additional Information:

A. Committee Substitute – Statement of Changes:
(Summarizing differences between the Committee Substitute and the prior version of the bill.)

None.

B. Amendments:

None.