HOUSE OF REPRESENTATIVES
FINAL BILL ANALYSIS

BILL #:	CS/HB 189	**FINAL HOUSE FLOOR ACTION:**	
SPONSOR(S):	Finance & Tax Committee; Cummings	117 **Y's**	0 **N's**
COMPANION BILLS:	CS/CS/SB 600	**GOVERNOR'S ACTION:**	Approved

SUMMARY ANALYSIS

CS/HB 189 passed the House on March 18, 2015, and subsequently passed the Senate on April 24, 2015.

Florida operates five insurance guaranty funds to ensure policyholders' paid insurance premiums are protected and outstanding claims are settled, up to limits provided by law, if their insurer is liquidated. Generally, a guaranty association is a not-for-profit corporation created by law directed to protect policyholders from financial losses and delays in claim payment and settlement due to the insolvency of an insurance company. A guaranty association accomplishes its mission by assuming responsibility for settling claims and refunding unearned premiums to policyholders. Insurers are required by law to participate in guaranty associations as a condition of transacting business in Florida.

The bill makes changes to two of the five guaranty funds – the Florida Insurance Guaranty Association (FIGA), which is the guaranty association for property and casualty insurance, and the Florida Life and Health Insurance Guaranty Fund (FLAHIGA), which is the guaranty association for most health and life insurers.

The bill clarifies the accounting treatment of assessments levied by FIGA and mitigates the negative impact to insurers' net worth due to a 2011 change to statutory accounting principles relating to the treatment of assessments. The bill also clarifies FLAHIGA's statutory duty to review policies, contracts, and claims of insolvent life and health insurers following both domestic and foreign liquidations or rehabilitations.

The bill has no fiscal impact on state or local government. The bill should have a positive private sector impact due to the bill's clarifications of FLAHIGA's obligations and the statutory accounting treatment of FIGA assessments.

The bill was approved by the Governor on June 16, 2015, ch. 2015-167, L.O.F., and will become effective on July 1, 2015.

I. SUBSTANTIVE INFORMATION

A. EFFECT OF CHANGES:

Insurance Guaranty Associations – Background

Chapter 631, F.S., relating to insurer insolvency and guaranty payments, governs the receivership process for insurance companies in Florida.[1] Federal law specifies that insurance companies cannot file for bankruptcy. Instead, they are either "rehabilitated" or "liquidated" by the state. In Florida, the Division of Rehabilitation and Liquidation of the Department of Financial Services (DFS) is responsible for rehabilitating or liquidating insurance companies.[2]

Florida operates five insurance guaranty funds to ensure policyholders of liquidated insurers are protected with respect to insurance premiums paid and settlement of outstanding claims, up to limits provided by law.[3] A guaranty association generally is a not-for-profit corporation created by law directed to protect policyholders from financial losses and delays in claim payment and settlement due to the insolvency of an insurance company. A guaranty association accomplishes its mission by assuming responsibility for settling claims and refunding unearned premiums[4] to policyholders. Insurers are required by law to participate in guaranty associations as a condition of transacting business in Florida.

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Florida Insurance Guaranty Association (FIGA)

Statutory provisions relating to FIGA, which was created in 1970, are contained in part II of chapter 631, F.S. FIGA operates under a board of directors and is a nonprofit corporation. FIGA is composed of all insurers licensed to sell property and casualty insurance in the state. By law, FIGA is divided into two accounts:

- the auto liability and auto physical damage account; and
- the account for all other included insurance lines (the all other account).[5]

When a property and casualty insurance company becomes insolvent, FIGA is required by law to take over the claims of the insurer and pay the claims of the company's policyholders. This ensures policyholders who have paid premiums for insurance are not left with valid yet unpaid claims. FIGA is

[1] The Bankruptcy Code expressly provides that "a domestic insurance company" may not be the subject of a federal bankruptcy proceeding. 11 U.S.C. § 109(b)(2). The exclusion of insurers from the federal bankruptcy court process is consistent with federal policy generally allowing states to regulate the business of insurance. *See* 15 U.S.C. §§ 1011- 1012 (McCarran-Ferguson Act).

[2] Typically, insurers are put into liquidation when the company is insolvent whereas insurers are put into rehabilitation for numerous reasons, one of which is an unsound financial condition. The goal of rehabilitation is to return the insurer to a sound financial condition. The goal of liquidation, however, is to dissolve the insurer. *See* s. 631.051, F.S., for the grounds for rehabilitation and s. 631.061, F.S., for the grounds for liquidation.

[3] The Florida Life and Health Insurance Guaranty Association generally is responsible for claims settlement and premium refunds for health and life insurers who are insolvent. The Florida Health Maintenance Organization Consumer Assistance Plan offers assistance to members of insolvent health maintenance organizations, and the Florida Workers' Compensation Insurance Guaranty Association is directed by law to protect policyholders of insolvent workers' compensation insurers. The Florida Self-Insurers Guaranty Association protects policyholders of insolvent individual self-insured employers for workers' compensation claims. The Florida Insurance Guaranty Association is responsible for paying claims for insolvent insurers for most remaining lines of insurance, including residential and commercial property, automobile insurance, and liability insurance, among others.

[4] The term "unearned premium" refers to that portion of a premium that is paid in advance, typically for six months or one year, and which is still owed on the unexpired portion of the policy.

[5] s. 631.55(2), F.S.

responsible for claims on residential and commercial property insurance, automobile insurance, and liability insurance, among others. Claims for property insurance are paid out of the all other account in FIGA.

In order to pay claims and to maintain the operations of an insolvent insurer, FIGA has several potential funding sources. FIGA's primary funding source is from the liquidation of assets of insolvent insurance companies domiciled in Florida. FIGA also obtains funds from the liquidation of assets of insolvent insurers domiciled in other states, but having claims in Florida.

In the event the insolvent insurer's assets are insufficient to pay all claims, FIGA can issue two types of post-insolvency assessments against property and casualty insurance companies to raise funds to pay claims. FIGA's assessments are computed and billed based on FIGA's immediate needs to pay claims. Currently, the assessment cap is 2% of net direct-written premium for regular assessments, and an additional 2% for emergency assessments for hurricane-related insolvencies.[6] FIGA has not levied an emergency assessment since 2006. FIGA last levied a regular assessment in November 2012 which was paid by insurers by December 31, 2012. This assessment amount was 0.9% of an insurer's net direct written premiums for 2011, which was levied only on the all other account.[7]

FIGA Assessment Procedure

The specific procedure used by FIGA to levy both types of assessments against member insurance companies and the procedure used by member insurance companies to recoup the assessment paid from their policyholders are found in s. 631.57(3), F.S. The procedure is generally the same for both regular and emergency assessments and is as follows:

1. FIGA's board determines an assessment is needed.
2. The board certifies the need for an assessment levy to the Office of Insurance Regulation (OIR).
3. If the certification is sufficient, the OIR issues an order to all insurance companies subject to the assessment instructing the companies to pay their share of the assessment to FIGA, based on each company's market share (direct written premium) for the previous calendar year.
4. Regular assessments must be paid by the insurance company within 30 days of the levy. Emergency assessments can be paid either in one payment at the end of the month after the assessment is levied or in 12 monthly installments, at the option of FIGA.
5. For both types of assessments, once an insurance company pays the assessment to FIGA, it may begin to recoup the assessment from its policyholders at the policy issuance or renewal. Insurers make a rate filing with the OIR to recoup the FIGA assessments from policyholders, based on expected future premiums to indicate the assessment percentage that will be added to each policy over the next 12 months.[8]

Current law requires insurers to remit excess assessment amounts collected from policyholders to FIGA if the excess amount is 15 percent or less than the total assessment paid by the insurer. Excess amounts over 15 percent of the total assessment paid are refunded by the insurer to the policyholders who paid the assessment.

[6] s. 631.57(3), F.S.
[7] FLORIDA INSURANCE GUARANTY ASSOCIATION, *Assessments*, http://www.figafacts.com/assessments (last visited January 26, 2015).
[8] *See also* Office of Insurance Regulation, *Frequently Asked Questions for FIGA Recoupment Filings*, available at http://www.figafacts.com/media/files/FAQs%20OIR-FIGA%20Assessment.pdf

Accounting for FIGA Assessments

Most insurers authorized to do business in the U.S. and its territories are required to prepare statutory financial statements to their state insurance regulators in accordance with statutory accounting principles (SAP),[9] which differs from generally acceptable accounting principles (GAAP) in a number of ways. While GAAP provides information useful to investors and other users of financial reporting (such as banks, credit rating agencies, and the U.S. Securities & Exchange Commission), SAP is developed in accordance with the concepts of consistency, recognition and conservatism, and assists state insurance departments with the regulation of the solvency of insurance companies. The ultimate objective of solvency regulation is to ensure that policyholder, contract holder and other legal obligations are met when they come due and that companies maintain capital and surplus at all times and in such forms as required by statute to provide a margin of safety. With the objective of solvency regulation, SAP focuses on the balance sheet, rather than the income statement, and emphasizes insurers' liquidity.[10]

Under both GAAP and SAP, an insurer recognizes a liability when a FIGA assessment is imposed (which reduces the insurer's surplus and net worth). However, a timing difference exists between the two principles for the recognition of an asset relating to the future recoveries of policy surcharges:

- GAAP does not treat the assessments recoverable from future premium writings as an asset, and thus results in an immediate reduction in equity and earnings in the period a FIGA assessment is billed. However, the equity reduction is eliminated the following year as the assessments are recouped from policyholders.
- On the other hand, SAP allows insurers to recognize the assessment amount likely to be recovered from future premium surcharges as an asset, which in turn offsets or eliminates the negative effect on statutory surplus, subject to certain conditions. SAP does not permit an asset to be recognized if the assessment is to be recovered from future rate structures, and limits asset recognition for accrued assessment liabilities to the extent that amount to be recovered is from in-force premiums only.[11]

Effect of the Bill on FIGA

The bill provides that the definition of "asset" for the purposes of determining an insurer's financial condition includes FIGA assessments that are levied (*before* policy surcharges are collected) result in a receivable, which is recognized as an admissible asset[12] under statutory accounting principles, to the extent the receivable is likely to be realized. This reflects and clarifies a practice of the OIR,[13] and eliminates the negative effect on statutory surplus of guaranty fund assessments. The asset must be established and recorded separately from the liability. The insurer must reduce the amount recorded as an asset if it cannot fully recoup the assessment amount because of a reduction in writings or withdrawal from the market.

For assessments that are paid *after* policy surcharges are collected pursuant to the monthly installment option, the recognition of assets is based on actual premium written offset by the obligation to FIGA.

Florida Life and Health Insurance Guaranty Association (FLAHIGA)

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[9] The OIR requires insurers to file annual SAP statements and independently audited financial reports. Section 624.424, F.S.

[10] NAIC & CENTER FOR INSURANCE POLICY AND RESEARCH, *Statutory Accounting Principles*, http://www.naic.org/cipr_topics/topic_statutory_accounting_principles.htm (last visited on January 12, 2015). Section 625.01115, F.S., provides that "statutory accounting principles" means "accounting principles as defined in the National Association of Insurance Commissioners Accounting Practices and Procedures Manual as of March 2002 and subsequent amendments thereto if the amendments remains substantially consistent."

[11] Statements of Statutory Accounting Principles, No. 35R, Guaranty Fund and Other Assessments (SSAP 35R); *see also* Thomas Howell Ferguson, P.A., *Accounting for Guaranty Fund Assessments Memorandum*, Dec. 3, 2013.

[12] NAIC Statement of Statutory Accounting Principles No. 4.

[13] OFFICE OF INSURANCE REGULATION, Supplemental Memorandum to Information Memorandum OIR-06-023M (Dec. 1, 2006). http://www.floir.com/siteDocuments/SupplementalMemo.pdf.

Statutory provisions relating to Florida Life and Health Insurance Guaranty Association (FLAHIGA), which was created in 1979, are contained in part III of chapter 631, F.S. FLAHIGA is governed by a board of directors composed of nine insurance companies and is a nonprofit corporation. All insurance companies (with limited exceptions) licensed to write life and health insurance or annuities in Florida are required, as a condition of doing business in Florida, to be a member of FLAHIGA. By law, FLAHIGA is divided into three accounts:

- the health insurance account;
- the life insurance account; and
- the annuity account.[14]

In the event a member insurer is found to be insolvent and is ordered to be liquidated by a court, a receiver takes over the insurer under court supervision and processes the assets and liabilities through liquidation. Upon liquidation, FLAHIGA automatically becomes liable for the policy obligations that the liquidated insurer owed to its Florida policyholders.[15] FLAHIGA services the policies, collects premiums and pays valid claims under the policies. FLAHIGA's rights under the policies are those that applied to the insurer prior to liquidation. FLAHIGA may cancel the policy if the insurer could have done so, but normally FLAHIGA continues the policies until the association can transfer or substitute the policies to a new, stable insurer with approval of the OIR.

Generally, direct individual or direct group life and health insurance policies, as well as individual and allocated annuity contracts issued by FLAHIGA's member insurers, are covered by FLAHIGA.[16] Current law specifies life and health policies and annuity contracts from non-licensed insurers are not covered by FLAHIGA.[17] In addition, s. 631.713(3), F.S., excludes all of the following from coverage by FLAHIGA:

- any portion or part of a variable life insurance contract or a variable annuity contract that is not guaranteed by a licensed insurer;
- any portion or part of any policy or contract under which the risk is borne by the policyholder;
- any policy or contract or part thereof assumed by the failed insurer under a contract of reinsurance, unless assumption certificates were issued;
- fraternal benefit society products;
- health maintenance insurance;
- dental service plan insurance;
- pharmaceutical service plan insurance;
- optometric service plan insurance;
- ambulance service association insurance;
- preneed funeral merchandise or service contract insurance;
- prepaid health clinic insurance;
- certain federal employees group policies; and
- any annuity contract or group annuity contract that is not issued to and owned by an individual, except to the extent of any annuity benefits guaranteed directly and not through an intermediary to an individual by an insurer under such contract or certificate.

In 2011, legislation was enacted specifying that FLAHIGA's immunity from bad faith lawsuits did not affect the FLAHIGA's obligation to pay valid insurance policy or contract claims if warranted after its independent de novo review of the policies, contracts, and claims presented to it, whether domestic or

[14] s. 631.715(2)(a), F.S.
[15] Generally, FLAHIGA covers only policyholders and certificate holders that were valid Florida residents on the date that a member insurer is declared insolvent and liquidated. However, non-residents of Florida and beneficiaries of covered persons are covered by FLAHIGA under limited circumstances (s. 631.713(2), F.S.).
[16] Allocated annuity contracts are directly issued to and owned by individuals or annuities that directly guarantee benefits to individuals by the insurer.
[17] s. 631.713, F.S.

foreign.[18] However, current law only specifies that FLAHIGA's obligation applies after a domestic (in-state) rehabilitation or liquidation, but is silent as to FLAHIGA's obligations to pay after a *foreign* (out-of-state) rehabilitation or liquidation. Consequently, current law could limit the ability of FLAHIGA to pay claims after a covered insurer is rehabilitated or liquidated in another state.

Effect of the Bill on FLAHIGA

The bill transfers the 2011 exception from immunity from FLAHIGA's powers and duties statute, s. 631.717, F.S., to s. 631.737, F.S., which pertains to FLAHIGA's duty to review claims involving covered policies, and clarifies that this duty is not limited solely to policies, contracts, and claims following domestic rehabilitations and liquidations, but also includes foreign rehabilitations and liquidations.

II. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT

A. FISCAL IMPACT ON STATE GOVERNMENT:

1. Revenues:

   None.

2. Expenditures:

   None.

B. FISCAL IMPACT ON LOCAL GOVERNMENTS:

1. Revenues:

   None.

2. Expenditures:

   None.

C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

The bill's clarification of statutory accounting for FIGA assessments should mitigate the impact of assessments on an insurer's financial statement.

D. FISCAL COMMENTS:

None.

[18] Ch. 2011-226, Laws of Fla.