

**SUBCHAPTER D. RISK-BASED CAPITAL AND SURPLUS AND OTHER
REQUIREMENTS
28 TAC §7.402**

1. INTRODUCTION. The Texas Department of Insurance adopts amendments to 28 Texas Administrative Code §7.402, concerning risk-based capital (RBC) and surplus requirements for insurers and health maintenance organizations (HMOs). The amendments to §7.402 establish the sources of information insurers and HMOs will use in determining RBC requirements, including requiring use of the most current version of RBC formulas and RBC instructions adopted by the National Association of Insurance Commissioners (NAIC) except as provided by statute or TDI rule.

Section 7.402 is adopted with changes to the proposed text published in the January 2, 2015, issue of the *Texas Register* (40 TexReg 7).

2. REASONED JUSTIFICATION. The RBC requirement is a method of ensuring that an insurer or HMO (collectively referred to as *carriers*) has an appropriate level of policyholder surplus after taking into account the underwriting, financial, and investment risks of a carrier. The NAIC RBC formulas and RBC instructions provide TDI with a widely used regulatory tool to identify the minimum amount of capital and surplus appropriate for a carrier to support its overall business operations considering its size and risk exposure.

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Amended § 7.402(d) lists the sources of information that insurers and HMOs must use to determine a carrier's RBC requirement. The sources of information are, in order of priority: Texas statutes, TDI rules and commissioner orders, and the NAIC RBC formulas and RBC instructions for carriers. The amendments do not change the current priority of the sources of information in existing §7.402(f) concerning the procedure for resolving conflicts between the sources. Making these sources continuous provides carriers greater certainty of information for planning their RBC needs, and enables them to timely complete and file their reports with TDI.

In establishing these sources and requirements, the commissioner has not delegated authority to others. The commissioner may by rule amend the NAIC RBC formulas and instructions for filings with TDI. The commissioner may also issue orders specifically affecting an individual carrier that could impact RBC formulas. The commissioner also retains exclusive authority to enforce the requirements in these rules.

The procedure for amending a source will depend on the circumstance and provision involved. The commissioner may propose rules or issue orders. Under existing law, interested persons may petition the commissioner for rules or otherwise bring to the commissioner's attention the need for action to address a problem.

The NAIC's RBC formulas and RBC instructions provide a uniform national standard for evaluating a carrier's capital needs. The NAIC RBC formulas and RBC instructions are adopted by regulators through a deliberative process, which includes a series of open meetings that offer the insurance industry and public the opportunity to

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comment on the proposed NAIC RBC formulas and RBC instructions. The NAIC RBC formulas and RBC instructions are published annually by the NAIC to reflect any changes to the prior year's NAIC RBC formulas and RBC instructions made through this process.

TDI uses the NAIC RBC formulas and RBC instructions as a source for evaluating a Texas carrier's capital needs, unless a TDI rule or other state law provides otherwise or a carrier is subject to a commissioner order concerning its capital requirements. TDI maintains a current copy of the NAIC RBC formulas and RBC instructions available for public inspection in the Financial Analysis Section, Financial Regulation Division, Texas Department of Insurance, William P. Hobby Jr. State Office Building, Tower Number III, Third Floor, Mail Code 303-1A, 333 Guadalupe, Austin, Texas 78701. TDI will continue to maintain a copy of subsequent versions of the NAIC RBC formulas and RBC instructions available for inspection at that location. Amendments to §7.402 are discussed in the following paragraphs.

The designation of §7.402(b)(3) has been amended to reflect that the existing paragraph includes carriers that file the NAIC Health Annual Statement in addition to HMOs.

TDI adds the definition of "carrier" in §7.402(c), because the existing requirements of §7.402 apply to a variety of regulated entities. This amendment has been applied in conforming changes throughout §7.402. The conforming change to the term "carrier" is not a substantive change in requirements because it does not affect the current application of §7.402.

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In this adoption, TDI has determined that, in addition to the changes marked in the proposal for the term “carrier,” two additional changes are required. The two additional changes are nonsubstantive and do not change any of the existing requirements under this section, affect persons not already subject to the requirement, or create new costs. The first change substitutes the term “carrier” for “insurer” in the first sentence of §7.402(g)(1). The change must be made in this adoption to make the three references in that sentence consistent.

The second change is in §7.402(g)(7). TDI has replaced the term “insurer” in the last sentence of this provision with “health maintenance organization or certain health carrier.” The change is necessary to be consistent with the first sentence in this provision, which establishes a requirement for HMOs or health carriers described in subsection (b)(3). In addition, because the initial reference is to both an HMO and a health carrier, TDI believes that use of the entire initial reference is necessary to avoid possible confusion with only using the term carrier.

Other definitions have been amended to conform to other proposed changes in §7.402 and to better identify references, including §7.68 of this title. TDI has removed references to an annual statement “blank” to be consistent with §7.68.

For reasons previously discussed in this adoption, TDI has amended §7.402(d) to list in order of priority the sources of information that carriers must use when determining RBC. In response to comments, TDI removed the provision for directives and instructions from §7.402(d)(3). Allowing for “directives” and “instructions” was considered as a means of allowing carriers to request a permitted

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practice that might affect an RBC calculation under this section in manner that would be similar to a requested practice under §7.18(f). The process was not intended as a means for TDI to create requirements.

The adopted amendments to §7.402(g)(5), (6), (7), and (8) directly link the requirements with the entities listed in §7.402(b). These changes to §7.402(g)(5), (6), (7), and (8) are not substantive and do not change requirements or affect the current application of §7.402.

TDI has made additional amendments to §7.402(g) (5), (6), (7), and (8) in response to a comment. The commenter requested that §7.402(g)(6) be revised to include the combined ratio language stated in the NAIC Property and Casualty RBC instructions and suggested that similar changes might be made to §7.402(g) (5), (7), and (8).

TDI declines to make the change to §7.402(g)(6) proposed by the commenter, because the combined ratio is stated in the RBC instructions, which is a source document under §7.402(d). However, in response to the comment, TDI has made a clarifying change to the second sentence in §7.402(g)(6) to refer to the “RBC formula and RBC instructions.” The amendment is consistent with the existing requirement in §7.402(d) and (e) to use the RBC formula and RBC instructions.

TDI has also made similar changes to §7.402(g) (5), (7), and (8) in response to the comment. TDI amended the first sentence of §7.402(g) (5) and (8) and the second sentence of §7.402(g)(7) to include a reference to the “RBC formula and RBC instructions” as the source of the calculations. The amendments clarify the procedure

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under §7.402(g)(5), (7), and (8) and are consistent with the existing requirement in §7.402(d) and (e) to use the RBC formula and RBC instructions.

The trend test and formula used to calculate in §7.402(g) (5), (6), (7), and (8) were not marked for change in the proposal. However, each provision was published in the proposal and each affected stakeholder had notice that the proposal affected them and the opportunity to comment. In response to a comment, TDI elected to make changes to §7.402(g) (5), (6), (7), and (8) clarifying that under the existing requirements in §7.402(d) and (e), the RBC formula and RBC instructions must be used for the trend test. The amendments to §7.402(g) (5), (6), (7), and (8) in this adoption do not change any of the existing requirements under this section, affect persons not already subject to the requirement, or create new costs.

TDI has also made a nonsubstantive amendment to the first sentence of §7.402(g)(1) to replace the word “institutes” with the word “triggers.” The change referring to triggering a company action level is now consistent with similar references in §7.402(g)(1) - (8). TDI has made additional nonsubstantive amendments to §7.402 to reflect updated TDI style guidelines. The nonsubstantive amendments do not change any of the existing requirements under this section, affect persons not already subject to the requirement, or create new costs.

3. SUMMARY OF COMMENTS AND AGENCY RESPONSE.

Comment: A commenter requests that §7.402(d)(3) be revised to clarify what constitutes a “directive” or “instruction” and requests that §7.402(d)(3) be revised so that

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it states more clearly who is authorized to issue the directives and instructions that factor into the determination of a carrier's RBC.

Agency Response: TDI has decided to remove the provision for directives and instructions from §7.402(d)(3). Allowing for "directives" and "instructions" was considered as a means of allowing carriers to request a permitted practice that might affect an RBC calculation under this section in manner similar to those practices under §7.18(f). The process was not intended as a means for TDI to create requirements.

Comment: A commenter requests that the guidance on the trend test in §7.402(g)(6) be revised to include the combined ratio language in the NAIC Property and Casualty RBC instructions. The commenter asserts that the change is necessary to ensure that the NAIC RBC requirements are applied consistently in all states. The commenter suggests adding "and the combined ratio is greater than 120 percent" to the end of the first sentence in §7.402(g)(6) will make the clarification. The commenter suggested that similar changes might be relevant for §7.402(g) (5), (7), and (8).

Agency Response: TDI agrees with the commenter that changes should be made to clarify §7.402(g) (5), (6), (7), and (8). TDI declines to make the change to §7.402(g)(6) proposed by the commenter because the combined ratio is stated in the RBC instructions, which is a source document under §7.402(d). However, in response to the comment, TDI has made a clarifying change to the second sentence in §7.402(g)(6) to refer to the "RBC formula and RBC instructions." The amendment is consistent with the existing requirement in §7.402(d) and (e) to use the RBC formula and RBC instructions.

TDI has also made similar changes to §7.402(g) (5), (7), and (8) in response to the comment. TDI amended the first sentence of §7.402(g) (5) and (8) and the second sentence of §7.402(g)(7) to include a reference to the “RBC formula and RBC instructions” as the source of the calculations. The amendments clarify the procedure under §7.402(g)(5), (7), and (8) and are consistent with the existing requirement in §7.402(d) and (e) to use the RBC formula and RBC instructions.

The trend test and formula used to calculate in §7.402(g) (5), (6), (7), and (8) were not marked for change in the proposal. However, each provision was published in the proposal and each affected stakeholder had notice that the proposal affected them and the opportunity to comment. As a result of a comment, TDI elected to make changes to §7.402(g) (5), (6), (7), and (8) clarifying that under the existing requirements in §7.402(d) and (e), the RBC formula and RBC instructions must be used for the trend test. The amendments to §7.402(g) (5), (6), (7), and (8) in this adoption do not change any of the existing requirements under this section, affect persons not already subject to the requirement, or create new costs.

4. NAMES OF THOSE COMMENTING ON THE PROPOSAL.

For with changes: National Association of Mutual Insurance Companies; and Superior HealthPlan, Inc., a Centene company.

5. STATUTORY AUTHORITY. The amendments are adopted under Insurance Code §§404.004, 404.005, 441.005, 441.051, 822.210, 822.211, 841.205, 841.206,

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841.410, 841.414, 843.404, 884.054, 884.206, 885.401, 982.105, 982.106, and 36.001. Section 404.004 provides that the commissioner's authority to increase any capital and surplus requirements prevails over the general provisions of the Insurance Code relating to specific companies, and §404.005 authorizes the commissioner to set standards for evaluating the financial condition of an insurer. Under §441.005, the commissioner may adopt reasonable rules as necessary to implement and supplement the purposes of Chapter 441.

Section 441.051 specifies the circumstances in which an insurer is considered insolvent, delinquent, or threatened with delinquency and includes certain statutorily specified conditions, including if an insurer's required surplus, capital, or capital stock is impaired to an extent prohibited by law. Section 822.210 authorizes the commissioner to adopt rules or guidelines to require an insurer to maintain capital and surplus levels in excess of statutory minimum levels to ensure financial solvency of insurers for the protection of policyholders and insurers. Section 822.211 specifies the actions the commissioner may take if an insurance company does not comply with the capital and surplus requirements of Chapter 822.

Section 841.205 authorizes the commissioner to adopt rules or guidelines to require an insurer that writes life or annuity contracts or assumes liability on or indemnifies one person for any risk under an accident and health insurance policy, or a combination of these policies, in an amount that exceeds \$10,000, to maintain capital and surplus levels in excess of statutory minimum levels to assure financial solvency of insurers for the protection of policyholders and insurers. Section 841.206

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authorizes the commissioner to take regulatory action if the commissioner determines that a life, accident, or health insurance company's capital or surplus is impaired in violation of §841.206.

Section 841.410(b) and (c) require a limited-purpose subsidiary life insurance company to comply with the RBC requirements, and maintain RBC in an amount that is at least equal to 300 percent of the authorized control level of RBC adopted by the commissioner. Section 841.414(c) requires a limited-purpose subsidiary life insurance company to file annually with the commissioner a report of the limited-purpose subsidiary life insurance company's RBC level as of the end of the preceding calendar year containing the information required by the RBC instructions adopted by the commissioner.

Section 843.404 authorizes the commissioner to adopt rules to require an HMO to maintain capital and surplus levels in excess of statutory minimum levels to ensure financial solvency of HMOs for the protection of enrollees. Section 884.054 specifies the capital stock and surplus requirements for stipulated premium insurance companies. Section 884.206 authorizes the commissioner to adopt rules to require an insurer that writes or assumes life insurance, annuity contracts, or accident and health insurance for a risk to one person in an amount that exceeds \$10,000 to maintain capital and surplus levels in excess of statutory minimum levels to ensure financial solvency of an insurer for the protection of policyholders and other insurers.

Section 885.401 requires each fraternal benefit society to file an annual report on the society's financial condition, including any information the commissioner

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considers necessary to demonstrate the society's business and method of operation, and authorizes TDI to use the annual report in determining a society's financial solvency.

Section 982.105 specifies the capital, stock, and surplus requirements for foreign or alien life, health, or accident insurance companies. Section 982.106 specifies the capital, stock, and surplus requirements for foreign or alien insurance companies other than life, health, or accident insurance companies. Section 36.001 authorizes the commissioner to adopt any rules necessary and appropriate to implement the powers and duties of TDI under the Insurance Code and other laws of this state.

6. CROSS REFERENCE TO STATUTE. The proposed amendments to §7.402 affect the following statutes: Insurance Code §§404.004, 404.005, 441.005, 441.051, 822.210, 822.211, 841.205, 841.206, 841.410, 841.414, 843.404, 884.054, 884.206, 885.401, 982.105, and 982.106

7. TEXT.

§7.402. Risk-Based Capital and Surplus Requirements for Insurers and HMOs.

(a) Purpose. The purpose of implementing a risk-based capital and surplus provision is to require a minimum level of capital and surplus to absorb the financial, underwriting, and investment risks assumed by a carrier.

(b) Scope.

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(1) Life companies. This section applies to any carrier authorized to do business in Texas as an insurance company that writes or assumes a life insurance or annuity contract or assumes liability on or indemnifies one person for any risk under an accident and health insurance policy, or any combination of these policies, in an amount that exceeds \$10,000 including: capital stock companies, mutual life companies, limited purpose subsidiary life insurance companies, and stipulated premium insurance companies.

(2) Property and casualty companies. This section applies to all domestic, foreign, and alien property and casualty companies subject to the provisions of Insurance Code §822.210 and §982.106, including county mutual insurance companies that do not meet the express criteria contained in Insurance Code §912.056(f), but excluding monoline financial guaranty insurers, monoline mortgage guaranty insurers, title insurers, and those insurers subject to Insurance Code §822.205.

(3) Health maintenance organizations and certain health carriers. This section applies to all domestic and foreign health maintenance organizations subject to the provisions of Insurance Code Chapter 843 and carriers that file the NAIC Health Annual Statement with TDI under TDI filing requirements.

(4) Fraternal benefit societies. This section applies to all domestic and foreign fraternal benefit societies.

(c) Definitions. The following words and terms, when used in this section, have the following meanings, unless the context clearly indicates otherwise.

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(1) Annual financial statement--The annual statement to be used by carriers under §7.68 of this title.

(2) Authorized control level--The result determined using the sources of information under subsection (d) of this section, including the RBC formula in accord with the RBC instructions.

(3) Carrier--An insurer, health maintenance organization, or fraternal benefit society included within the scope of subsection (b) of this section.

(4) NAIC--National Association of Insurance Commissioners.

(5) RBC--Risk-based capital.

(6) RBC formula--NAIC risk-based capital formula.

(7) RBC instructions--NAIC Risk-Based Capital Report Including Overview and Instructions for Companies.

(8) Total adjusted capital--A carrier's adjusted statutory capital and surplus as determined using the sources of information under subsection (d) of this section, including the RBC formula in accord with the RBC instructions.

(d) Sources of information for determining RBC. The commissioner reserves all authority and discretion to resolve any issues in Texas concerning RBC. The commissioner and carriers will refer to the sources in paragraphs (1) - (4) of this subsection in the respective order of priority listed to determine RBC:

(1) Texas statutes;

(2) TDI rules;

(3) commissioner orders; and

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(4) except as provided in this section, as applicable to the carrier:

(A) the NAIC Life Risk-Based Capital Report Including Overview and Instructions for Companies, which includes the RBC formula, for the period being reported.

(B) the NAIC Fraternal Risk-Based Capital Report Including Overview and Instructions for Companies, which includes the RBC formula, for the period being reported.

(C) the NAIC Property and Casualty Risk-Based Capital Report Including Overview and Instructions for Companies, which includes the RBC formula, for the period being reported.

(D) the NAIC Health Risk-Based Capital Report Including Overview and Instructions for Companies, which includes the RBC formula, for the period being reported.

(e) Filing requirements. All carriers must file electronic versions of the RBC reports and any supplemental RBC forms and reports with the NAIC in accord with and by the due dates specified in sources of information for determining RBC listed in subsection (d) of this section, including the RBC instructions.

(f) Conflicts. In the event of a conflict between the Insurance Code, any TDI rule, any specific requirement of this section, and the RBC formula or the RBC instructions, the Insurance Code, rule, or specific requirement of this section takes precedence and in all respects controls. The requirements of this section do not repeal, modify, or amend any TDI rule or any Insurance Code provision.

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(g) Actions of commissioner. The level of risk-based capital is calculated and reported annually. Depending on the results computed by the risk-based capital formula, the commissioner of insurance may take a number of remedial actions, as considered necessary. The ratio result of the total adjusted capital-to-authorized control level risk-based capital requires the following actions related to a carrier within the specified ranges:

(1) A carrier reporting total adjusted capital of 150 percent to 200 percent of authorized control level risk-based capital triggers a company action level under which the carrier must prepare a comprehensive financial plan that identifies the conditions that contribute to the carrier's financial condition. The plan must contain proposals to correct areas of substantial regulatory concern and projections of the carrier's financial condition, both with and without the proposed corrections. The plan must list the key assumptions underlying the projections and identify the concerns associated with the carrier's business. The RBC plan must be submitted within 45 days of filing the RBC report with the NAIC. After review, the commissioner will notify the carrier if the plan is satisfactory or not satisfactory. If the commissioner notifies the carrier that the plan is not satisfactory, the carrier must prepare a revised plan and submit it to the commissioner. Failure to file this comprehensive financial plan triggers the regulatory action level described in this subsection.

(2) A carrier reporting total adjusted capital of 100 percent to 150 percent of authorized control level risk-based capital triggers a regulatory action level initiative. At this action level, a carrier must file an RBC plan or revised RBC plan

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within 45 days of filing the RBC report with the NAIC, and the commissioner must perform any examinations or analyses to the carrier's business and operations that are deemed necessary. The commissioner may issue orders specifying corrective actions to be taken or may require other appropriate action.

(3) A carrier reporting total adjusted capital of 70 percent to 100 percent of authorized control level risk-based capital triggers an authorized control level. In addition to the remedies available at the carrier and regulatory action levels described in this subsection, the commissioner may take other action deemed necessary, including initiating a regulatory intervention to place a carrier under regulatory control.

(4) A carrier reporting total adjusted capital of less than 70 percent of authorized control level triggers a mandatory control level that subjects the carrier to one of the following actions:

(A) being placed in supervision or conservation;

(B) being determined to be in hazardous financial condition as provided by Insurance Code Chapter 404 and §8.3 of this title regardless of percentage of assets in excess of liabilities;

(C) being determined to be impaired as provided by Insurance Code §§404.051 and 404.052 or 841.206; or

(D) any other applicable sanctions under the Insurance Code.

(5) A life company described in subsection (b)(1) of this section is subject to a trend test described in the RBC formula and RBC instructions, if its total

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adjusted capital-to-authorized control level risk-based capital is between 200 percent and 300 percent. Any life insurer that trends below 190 percent of total adjusted capital-to-authorized control level risk-based capital triggers the company action level.

(6) A property and casualty company described in subsection (b)(2) of this section is subject to a trend test if its total adjusted capital-to-authorized control level risk-based capital is between 200 percent and 300 percent. If the result of the trend test as determined by the RBC formula and RBC instructions is "YES," the insurer triggers regulatory attention at the company action level.

(7) A health maintenance organization or health carrier described in subsection (b)(3) of this section is subject to a trend test if its total adjusted capital-to-authorized control level risk-based capital is between 200 percent and 300 percent and triggers the trend test determined in accord with the trend test calculation included in the Health RBC instructions. If the result of the trend test as determined by the RBC formula and RBC instructions is "YES," the health maintenance organization or certain health carrier triggers regulatory attention at the company action level.

(8) A fraternal benefit society described in subsection (b)(4) of this section is subject to a trend test described in the RBC formula and RBC instructions, if its total adjusted capital-to-authorized control level risk-based capital is between 200 percent and 300 percent. Any fraternal benefit society that trends below 190 percent of total

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adjusted capital-to-authorized control level risk-based capital triggers the company action level.

(h) Prohibition on announcements. Except as required under this section, a carrier, agent, or other person engaged in the business of insurance under the Insurance Code is prohibited from making, publishing, disseminating, circulating, or placing before the public, or causing, directly or indirectly to be made, published, disseminated, circulated, or placed before the public, in a newspaper, magazine, or other publication, or in the form of a notice, circular, pamphlet, letter, poster, over any radio or television station, or in any other way, an advertisement, announcement, or statement containing an assertion, representation, or statement with regard to any component derived in the calculation. Any violation of this subsection may be considered a violation of Insurance Code Chapter 541, regulating unfair methods of competition and unfair or deceptive acts or practices.

(i) Prohibition on use in ratemaking. The RBC instructions and any related filings are intended solely for use by the commissioner in monitoring the solvency of carriers and in taking corrective action with respect to carriers. The RBC instructions and any related filings may not be:

- (1) used by the commissioner for ratemaking;
- (2) considered or introduced as evidence in any rate proceeding; or
- (3) used by the commissioner to calculate or derive any elements of an appropriate premium level or rate of return for any line of insurance that a carrier or any affiliate is authorized to write.

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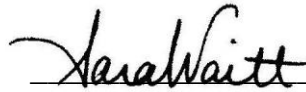
TITLE 28. INSURANCE
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(j) Limitations. The requirements of this section do not reduce the amount of capital and surplus otherwise required by the Insurance Code, TDI rules, or by authority of the commissioner as provided by law.

8. CERTIFICATION. This agency certifies that legal counsel has reviewed the adopted sections and finds them to be a valid exercise of the agency's legal authority.

Issued at Austin, Texas on **June 10, 2015.**



Sara Waitt
General Counsel
Texas Department of Insurance

The commissioner adopts the amendments to 28 TAC §7.402.



David C. Mattax
Commissioner of Insurance