

## **SUBCHAPTER E. TEXAS WINDSTORM INSURANCE ASSOCIATION**

### **DIVISION 1. Plan of Operation 28 TAC §5.4001**

**1. INTRODUCTION.** The Texas Department of Insurance proposes amendments to §5.4001(c), concerning provisions in the Texas Windstorm Insurance Association (Association) plan of operation for the financial operations of the Association. The amendments are necessary to authorize the Association to prepare financial information on a calendar year basis only rather than on both a calendar year and syndicate year basis, to calculate assessments for member companies on a calendar year basis rather than a syndicate year basis when funds available to the Association are insufficient to pay operating costs and/or catastrophe losses, and to eliminate a minimum cap (20 percent of a company's percentage of the net direct statewide property insurance market) and a maximum cap (170 percent of a company's percentage of the same market) on a member company's Association assessment percentage.

Under the Insurance Code §2210.051, the Association is composed of all insurers authorized to transact property insurance in this state and operates pursuant to Chapter 2210 of the Insurance Code. The purpose of Chapter 2210 is to provide an adequate market for windstorm and hail insurance. Chapter 2210 "provides a method by which adequate windstorm, hail, and fire insurance may be obtained in certain designated portions of this state." The funding structure for the Association established in Chapter 2210 of the Insurance Code

includes assessments to member companies in the event that the Association's operating costs and/or catastrophe losses exceed the Association's premium and other revenue.

The Insurance Code §2210.151 requires the Commissioner to adopt by rule a plan of operation for the Association to provide Texas windstorm and hail insurance in catastrophe areas. The Insurance Code §2210.152(a)(2)(A) requires the plan of operation to include a plan for the equitable assessment of the members of the Association to defray losses and expenses. The Insurance Code §2210.052(a) specifies that Association members shall be assessed Association operating expenses and losses in the proportion that the net direct premiums of a member bears to the aggregate net direct premiums of all members, and the Insurance Code §2210.052(c) specifies this proportion shall be determined annually in a manner provided by the plan of operation. (As used in this proposal, terms such as "net direct premiums," "voluntary writings in the catastrophe areas," "voluntary premiums for the catastrophe areas," and "similar insurance voluntarily written in the catastrophe areas," refer to windstorm and hail insurance.) The Insurance Code §2210.052(d) specifies that members are entitled to a credit for similar insurance voluntarily written in the catastrophe areas and that the credit shall reduce the member's share of the Association's expenses and losses in accordance with the plan of operation. The Insurance Code §2210.054(a) requires the Association to file annually with the Department a statement summarizing the transactions, conditions, operations and affairs of the Association during the preceding year. The Insurance Code §2210.054(a)

also requires that the statement shall cover periods designated by the Department, and the Insurance Code §2210.054(b)(3) requires the statement to be in a form prescribed by the Department. Section 5.4001(b)(8) of the plan of operation requires the Association to submit to the Department an “annual report” on a calendar year basis. Section 5.4001(c)(1)(C)(i) of the plan of operation requires the Association to prepare each year a “statement of earnings” on a syndicate year basis.

On January 9, 2008, the Association filed a petition (Ref. No. P-0108-01) with the Department, seeking to amend the plan of operation to provide that a calendar year rather than a syndicate year be used to prepare the yearly Association statement of earnings and to determine the amount of assessment that would be charged to member companies in the event that funds available to the Association are inadequate to meet operating costs and/or catastrophe losses. On March 24, 2008, the Association filed a second petition (Ref. No. P-0308-05), seeking to amend the plan of operation to eliminate minimum and maximum caps as specified in §5.4001(c)(2)(B) and §5.4001(c)(2)(B)(i) of the plan of operation to adjust the calculation of a member company’s assessment percentage. Because the two petitions request amendments to the same section of the plan of operation, this proposal addresses the requests in both petitions.

**Proposal to Change from Syndicate Year Basis to Calendar Year Basis for Association Calculations.** The proposed amendments to §5.4001(c)(1)(C)(i), §5.4001(c)(1)(C)(ii), and §5.4001(c)(2)(B) of the plan of operation are necessary because the plan of operation in these paragraphs and

subparagraphs currently requires the Association to use a syndicate year as a basis for calculations for two purposes: (i) to prepare each year an Association statement of earnings required by §5.4001(c)(1)(C)(i) of the plan of operation; and (ii) to calculate pursuant to §5.4001(c)(2)(B) of the plan of operation the total amount of member company assessments needed at a particular time to pay operating expenses and/or catastrophe losses and then to calculate pursuant to §5.4001(c)(1)(C)(ii) of the plan of operation the specific amount of the assessment each member company is required to pay. This proposal amends §5.4001(c)(1)(C)(i), §5.4001(c)(1)(C)(ii) and §5.4001(c)(2)(B) of the plan of operation to allow the Association to use a calendar year basis rather than a syndicate year basis for calculations for these two specified purposes.

Generally, calculations done on a calendar year basis are less cumbersome and time-consuming than calculations based on a syndicate year, can be prepared and finalized earlier, and reflect more current information. Thus, changing from the syndicate year basis for calculations for the Association to the calendar year basis for calculations is consistent with the requirements of the Insurance Code §2210.152(a)(1) that the plan of operation provide for the efficient and economical administration of the Association.

A syndicate year is determined by the effective and the expiration dates of a policy. For example, syndicate year 2007 covers all policies with an effective date beginning in 2007. Under the syndicate year system, earnings and losses cannot be fully determined until the syndicate year closes. The syndicate year closes when all policies with an effective date in 2007 expire, typically twelve

months after the date a policy became effective. Therefore, earnings and losses from syndicate year 2007 will not be fully determined until late in the year 2008. Calculations done by syndicate year attempt to link earnings and losses according to actual policy cycles and require the books for a syndicate year to be kept open for approximately two years.

A calendar year is determined by the Gregorian calendar beginning each year on January 1 and ending on December 31. All premiums and revenue taken in during a particular calendar year are added together, and losses and expenses incurred during the same calendar year are subtracted from the calendar year total of premiums and revenue. Calendar year premiums, revenue, and losses can be determined quickly after the close of the calendar year on December 31.

*Using a Calendar Year as a Basis for the Statement of Earnings.*

The Insurance Code §2210.054(a) requires the Association to file annually with the Department a statement summarizing the transactions, conditions, operations and affairs of the Association during the preceding year. Subsections (a) and (b)(3) of the Insurance Code §2210.054 require that the statement cover periods designated by the Department.

Section 5.4001(b)(8) of the plan of operation requires that the Association “file with the Department annually a statement which shall summarize the transactions, conditions, operations, and affairs of the Association during the preceding calendar year.” The report required by §5.4001(b)(8) of the plan of

operation is the Association's "annual report" and is prepared on a calendar year basis. No amendment to §5.4001(b)(8) is proposed.

Section 5.4001(c)(1)(C)(i) of the plan of operation currently provides that "Each year the Association will prepare a statement of earnings by syndicate year. All premiums written, commissions paid, unearned and earned premiums, loss and loss expenses paid and pending will be charged to the syndicate year. All general expense and interest income received will be charged or credited to the current syndicate year."

Section 5.4001(b)(8) and §5.4001(c)(1)(C)(i) of the plan of operation require that the Association keep two sets of books for its financial reporting: one by calendar year for the annual report and one by syndicate year for the statement of earnings.

References in §5.4001(c)(1)(C)(i) of the plan of operation to a "syndicate" year are proposed to be deleted and replaced with the term "calendar" year and the explanation of a "syndicate" year in §5.4001(c)(1)(C)(i) of the plan of operation is proposed to be deleted. The proposed amendments to §5.4001(c)(1)(C)(i) of the plan of operation will eliminate the current requirement that the Association keep two sets of books, one by syndicate year and one by calendar year. The required financial reports of the Association, such as the annual report and the statement of earnings, will be uniformly made on a calendar year basis. The proposed amendments to §5.4001(c)(1)(C)(i) of the plan of operation will allow the Association to complete the statement of earnings following the close of a calendar year on December 31, rather than at the

completion of the syndicate year many months later. The Association statement of earnings based on a calendar year will be produced more efficiently by the Association, be understood more easily by the member companies and the public, and be based on more current information. The book-keeping obligations of the Association will become less burdensome.

*Using a Calendar Year as a Basis for Association Assessments.*

The Insurance Code §2210.152(a)(2)(A) requires the Association plan of operation to include a plan for the equitable assessment of the member companies to defray losses and expenses. Pursuant to §5.4001(c)(2)(A) of the plan of operation, the member companies may be required to pay assessments to the Association to adequately provide for the operating expenses of the Association and/or for catastrophe losses. If the board of directors of the Association determines that the funds then available to the Association are insufficient for either or both purposes, the board assesses member companies under the authority of §5.4001(c)(2)(A)(ii) of the plan of operation in reasonable and necessary amounts to provide for the operating expenses and/or catastrophe losses.

The plan of operation currently requires in §5.4001(c)(2)(B) that the board of directors determine the amount of assessment required for operating expenses and/or catastrophe losses using syndicate year calculations. For example, under the current system of calculating assessments by syndicate year, if a storm occurs in September 2008 and an assessment is necessary, the Association must determine how much of the assessment is due to Association

policies with an effective date in 2007 (which may still be in effect in September 2008) and how much is due to policies with an effective date in 2008. Generally, in order to calculate each member company's share of an assessment, the assessment is multiplied by each member company's assessment percentage. The assessment percentage is determined annually and is generally described as the ratio of the member company's net direct premiums written statewide to the aggregate net direct premiums written statewide by all members of the Association, adjusted by a credit for each member company's voluntary premiums written in the catastrophe areas.

Using the example of a storm occurring in September 2008 and using the syndicate year basis of calculation required by §5.4001(c)(2)(C)(ii), the member company's assessment percentage applicable to 2007 will be multiplied by the amount of the assessment due to Association policies with an effective date in 2007 (syndicate year 2007), and the member company's assessment percentage applicable to 2008 will be multiplied by the amount of the assessment due to Association policies with an effective date in 2008 (syndicate year 2008). The resulting two figures will be added together to determine each company's total assessment amount for the single event occurring in September 2008.

However, there are two problems inherent in using a syndicate year as a basis of calculation: (i) final figures for syndicate years are frequently not available at the time of an assessment and require later reconciliation; and (ii) the current use of a syndicate year basis in determining assessments delays the

effect of increases or decreases in voluntary writings in the catastrophe areas on the amount of a member company's assessment.

Using the September 2008 example, some of the premiums, revenue, expenses, and losses for Association policies with an effective date in 2007 that have not expired as of the date of the loss in September 2008, and much of the premiums, revenue, expenses, and losses for Association policies with an effective date in 2008 in effect as of the date of the loss, are not yet known. After the assessment is made, calculations for syndicate year 2007 must be finalized; and then even later in 2009, calculations for syndicate year 2008 must be completed. The assessment for the September 2008 storm must be reconciled against the final accounting for syndicate years 2007 and 2008. If member companies overpaid their share of an assessment, they receive a refund; if member companies underpaid their share of an assessment, they receive an additional notice of assessment.

As the September 2008 example illustrates, policies with effective dates in two different years are usually in effect at the time of an assessment. Section 5.4001(c)(1)(C)(ii) of the plan of operation currently requires that the assessment portion for the prior syndicate year be multiplied by the member company's prior year's assessment percentage and that the assessment portion for the current syndicate year be multiplied by the member company's assessment percentage for the current year. Assessment percentages, which are determined annually, are required by §5.4001(c)(2)(B) and §5.4001(c)(2)(B)(i) of the plan of operation to be adjusted by a credit for similar insurance voluntarily written in the

catastrophe areas. Therefore, part of an assessment determined under the current plan of operation is based on an assessment percentage applicable to a prior syndicate year, which may not reflect recent voluntary writings in the catastrophe areas, or may reflect voluntary writings no longer in effect.

Section 5.4001(c)(1)(C)(ii), §5.4001(c)(2)(B), and §5.4001(c)(2)(B)(i) of the plan of operation are proposed to be amended to delete references to “syndicate” year and replace them with the term “calendar” year so that assessments will be calculated on a calendar year basis. Using the September 2008 example and using the proposed calendar year basis of calculation, the Association will determine the amount of assessment needed after the storm according to the premium and revenue available to date for calendar year 2008, including available funds in the catastrophe reserve trust fund and from reinsurance proceeds, if applicable. Because the proposed amendments will make the determination of the assessment based on the calendar year only, the Association will use one set of figures rather than the two sets of figures required by the syndicate year basis, and the assessment will be easier to prepare. There will be no need to refer to 2007 calculations for the Association’s earnings and losses, because the assessment amount will be based on insured losses, operating expenses, and premiums and other revenue transactions of the Association that occurred during calendar year 2008. Under most circumstances, calculations for an assessment prepared on a calendar year basis will eliminate the need to reconcile final figures, reducing the need for refunds or further assessments. Under the proposed amendments, all of an

assessment will be determined using the current assessment percentage, which reflects member companies' most recent voluntary writings in the catastrophe areas. Eliminating the delay in the effect of member companies' increased or decreased voluntary writings in the catastrophe areas will provide an incentive to all member companies to maintain or provide similar insurance in the catastrophe areas, which may reduce property owners' reliance on the Association to provide windstorm and hail insurance coverage.

**Proposal to Eliminate Minimum and Maximum Caps on Member Companies' Assessment Percentages.** The Insurance Code §2210.052(a) and §2210.052(c) specify that Association members shall be assessed Association operating expenses and losses in the proportion that the net direct premiums of a member bears to the aggregate net direct premiums of all members and that this proportion shall be determined annually in a manner provided by the plan of operation. The Insurance Code §2210.052(b) requires the Department to review data and information it considers necessary to determine the annual assessment percentage and to provide that information to the Association. The Insurance Code §2210.152(a)(2)(A) requires the plan of operation to include a plan for the equitable assessment of the members of the Association to defray losses and expenses. The Insurance Code §2210.052(d) specifies that members are entitled to a credit for similar insurance voluntarily written in the catastrophe areas and that this credit is to be used to reduce a member's assessment percentage in accordance with the plan of operation. The plan of operation in §5.4001(c)(2)(B) and §5.4001(c)(2)(B)(i) specifies the

minimum and maximum caps to be used to adjust the calculation of a member company's assessment percentage. The proposed amendments to §5.4001(c)(2)(B) and §5.4001(c)(2)(B)(i) will eliminate these minimum and maximum caps. The following explains the existing method of applying the minimum and maximum caps and why the resulting assessment percentages are not reflective of voluntary writings in the catastrophe areas and why the elimination of minimum and maximum caps on companies' Association assessment percentages will result in assessment percentages that more accurately reflect the credit for a member company's voluntary writings in the catastrophe areas, or lack thereof.

Pursuant to §5.4001(c)(2)(B) and §5.4001(c)(2)(B)(iv) of the plan of operation, as a part of the regular operations of the Association, the Association receives information from the Department on the aggregate net direct premiums written in the state during the preceding calendar year and the net direct premiums written in the state by each member company during the same period. Each member company's percentage of the net direct premiums written in the state is calculated from those annual figures. Thus, a company's assessment percentage for 2008 is based on premium information supplied to the Department for calendar year 2007.

To implement the requirement in the Insurance Code §2210.052(d) that members are entitled to a credit for similar insurance voluntarily written in the catastrophe areas, §5.4001(c)(2)(B)(i) of the plan of operation requires the determination of a member company's "normal required quota" of business in the

catastrophe areas for the preceding calendar year. A member company's normal required quota of business in the catastrophe areas is calculated by multiplying its percentage of the net direct statewide market for the preceding calendar year by the total premiums written in the catastrophe areas (which are total Association premiums plus total voluntary premiums for the catastrophe areas) during the preceding calendar year. The total of the company's actual written premiums in the catastrophe areas for the preceding calendar year is then subtracted from the member company's normal required quota for the same time period. The difference is then divided by the total of all member companies' normal required quotas for the preceding calendar year minus their actual written premiums in the catastrophe areas during the preceding calendar year. The resulting quotient is a member company's unadjusted assessment percentage for the following calendar year.

Currently, pursuant to §5.4001(c)(2)(B)(i) of the plan of operation, the member company's unadjusted assessment percentage is then compared to its percentage of net direct statewide premiums written during the preceding calendar year. If the member company's unadjusted assessment percentage is less than 20 percent of the company's percentage of the net direct statewide premiums written during the preceding calendar year, the unadjusted assessment percentage is adjusted upward to 20 percent of the company's percentage of net direct statewide premiums written during the preceding calendar year (minimum cap). If the company's unadjusted assessment percentage is more than 170 percent of the company's percent of the net direct

statewide premiums written during the preceding calendar year, the quotient is adjusted downward to 170 percent of the company's percentage of net direct statewide premiums written during the preceding calendar year (maximum cap). While the application of minimum and maximum caps to the assessment percentage is required by the plan of operation, it is not required by Chapter 2210 of the Insurance Code. The adjusted assessment percentage (after the application of an offset factor designed to ensure that the sum of all member companies' assessment percentages totals 100 percent) is the net assessment percentage for a member company for the following calendar year.

If, pursuant to the Insurance Code §2210.052, §2210.058, and §2210.152(a)(2)(A), an assessment is necessary, the net assessment percentage for a member company is then multiplied by the total amount of assessment the board of directors has determined is needed pursuant to §5.4001(c)(2)(B) of the plan of operation. Under §5.4001(c)(2)(D)(i) of the plan of operation, the member company must remit this amount within 30 days of the receipt of the notice of assessment or have its certificate of authority to transact the business of insurance suspended by the Commissioner until such time as the Association certifies to the Commissioner that such assessment has been paid in full.

Therefore, the proposed amendments to §5.4001(c)(2)(B) and §5.4001(c)(2)(B)(i) of the plan of operation are necessary to eliminate the application of minimum and maximum caps on member companies' Association assessment percentages because the use of the caps results in assessment

percentages that are not reflective of voluntary writings in the catastrophe areas. The elimination of minimum and maximum caps on companies' Association assessment percentages will result in assessment percentages that more accurately reflect a member company's voluntary insurance writings in the catastrophe areas, or lack thereof.

Additionally, the elimination of the minimum cap allows a member company to fully realize the benefits of its voluntary writings in the catastrophe areas and results in a less costly assessment for the company if an assessment is necessary. Under current §5.4001(c)(2)(B)(i) of the plan of operation, a company that has written its entire normal required quota in the catastrophe areas during the preceding calendar year would have an unadjusted assessment percentage calculated at less than 20 percent of its percentage of net direct statewide premiums written during the preceding calendar year. The unadjusted assessment percentage would nonetheless be adjusted upward to 20 percent of its percentage of net direct statewide premiums written during the preceding calendar year, resulting in a loss of credit for voluntary writings greater than zero percent but less than 20 percent of a company's percentage of net direct statewide premiums written during the preceding calendar year. Under the proposed amendments to §5.4001(c)(2)(B)(i) of the plan of operation, a member company's unadjusted assessment percentage ranging from any percentage greater than zero to 20 percent of its percentage of net direct statewide premiums written will become the net assessment percentage (after application

of a final offset factor) reflecting full credit for voluntary writings in the catastrophe area during the preceding calendar year.

Conversely, under current §5.4001(c)(2)(B)(i) of the plan of operation, a company with a sizable market share but a small amount of voluntary writings in the catastrophe areas during the preceding calendar year, may have an unadjusted assessment percentage calculated that is more than 170 percent of its percentage of net direct statewide premiums written during the preceding calendar year. The assessment percentage is nonetheless adjusted down to 170 percent of its percentage of net direct statewide premiums written during the preceding calendar year. Thus, the maximum cap, in effect, provides a member company a credit for voluntary writings that do not exist. Under the proposed amendments to §5.4001(c)(2)(B)(i) of the plan of operation, a member company with relatively few or no voluntary writings in the catastrophe areas during the preceding calendar year will not have its assessment percentage capped at 170 percent of the company's percentage of net direct statewide premium written for the preceding calendar year, which will result in a more costly assessment for the company.

The following amendments are proposed to the chart in §5.4001(c)(2)(B)(i) which illustrates the calculations of §5.4001(c)(2)(B)(i) of the plan of operation. The title of the chart is proposed to be changed to "TEXAS WINDSTORM INSURANCE ASSOCIATION PROCEDURE FOR CALCULATING MEMBER ASSESSMENT PERCENTAGES INCLUDING CREDIT FOR VOLUNTARY WRITINGS." This is necessary to update the current name of the Association and to use the

more current terminology “assessment percentage” instead of “pool participation.” An amendment is proposed to delete a reference in Column 2 of the chart to “40%,” which was formerly used to arrive at a calculation for total statewide net direct written premiums and is now obsolete and replace it with “50%,” which is currently used to arrive at a calculation for statewide net direct written premiums according to §5.4001(c)(2)(B)(i). An amendment is proposed to delete a reference in Column 4 to the obsolete name “TCPIA” and replace it with a reference to the “Association.” In Column 8, the proposed amendments delete the term “assignment” from the title and replace it with the phrase “Association assessment percentage.” The proposed amendments delete the phrase “assignment after offset factor” from the title of Column 9, and replace it with the phrase “net Association assessment percentage,” to indicate that this is the final step in the calculations. The proposed amendments add the phrase “(after application of offset)” under the title in Column 9. This is necessary because the phrase indicates that the application of an offset factor that ensures that the sum of all member companies’ assessment percentages total 100 percent is the final step in the assessment percentage calculation. The application of an offset factor, however, is a statistical adjustment that is not affected by this rule proposal. The proposed amendments delete all of Columns 10 and 11 because they refer to the application of minimum and maximum caps and delete two obsolete footnotes to the chart.

**Proposed Non-substantive Changes.** The proposed amendments also delete references in §5.4001(c) of the plan of operation to the obsolete name

“Texas Catastrophe Property Insurance Association” and replace them with references to the “Association.” For purposes of consistency throughout the subsection, the proposed amendments delete the use of the term “premium” and replace it with the term “premiums” and delete the use of the term “area” and replace it with the term “areas.” The use of the term “areas” is necessary because more than one catastrophe area has been designated by the Commissioner pursuant to the Insurance Code §2210.005. The proposed amendments delete all of §5.4001(c)(2)(B)(ii) and §5.4001(c)(2)(B)(iii) of the plan of operation because these provisions specify obsolete assessment procedures. The proposed amendments also redesignate current §5.4001(c)(2)(B)(iv) of the plan of operation as §5.4001(c)(2)(B)(ii) and conform references to the Insurance Code throughout §5.4001(c) of the plan of operation to the updated references enacted in the non-substantive Insurance Code revision by the 79th Legislature in HB 2017, effective April 1, 2007. Proposed amendments also correct non-substantive capitalization, punctuation, and typographical errors throughout the subsection.

**2. FISCAL NOTE.** Marilyn Hamilton, Associate Commissioner of the Property and Casualty Program, has determined that for each year of the first five years the proposed amendments will be in effect, there will be no fiscal impact to state and local governments as a result of the enforcement or administration of the proposal. There will be no measurable effect on local employment or the local economy as a result of the proposal.

**3. PUBLIC BENEFIT/COST NOTE.** Ms. Hamilton has further determined that for each year of the first five years the proposed amendments are in effect, the public benefit and costs anticipated as a result of administering the proposed amendments will be as follows.

**Proposal to Change from Syndicate Year Basis to Calendar Year Basis for Association Calculations.**

*Using a Calendar Year as a Basis for the Statement of Earnings.*

The public benefit of the proposed amendments to §5.4001(c)(1)(C) of the plan of operation will be an improved Association plan of operation that will provide for a more efficient and economical administration of the Association, as mandated by the Insurance Code §2210.152(a)(1). The components of the statement of earnings required by §5.4001(c)(1)(C) of the plan of operation will be determined sooner and more efficiently. The Association statement of earnings will be based on more current information and will be prepared sooner because the data on which the report is based will be available sooner. As a result, the Association statement of earnings will be easier for the member companies and the public to understand.

There will be a small cost savings to the Association in preparing the statement of earnings because both the annual report and the statement of earnings will be based on the same information. Pursuant to §5.4001(b)(8), the current plan of operation requires a summary of the transactions, conditions, operation and affairs of the Association for the previous calendar year for the

annual report, and pursuant to §5.4001(c)(1)(C)(i), the current plan of operation also requires a report of premiums written, commissions paid, unearned and earned premiums, loss and loss expenses paid and pending for the previous syndicate year for the statement of earnings. The information required for the annual report is more extensive than the information required for the statement of earnings, but the time period of the compiled information for the annual report is different from that of the statement of earnings. Under the proposed amendments, the information compiled for the annual report by calendar year will be used for both the annual report and the statement of earnings. There will be no cost to the member companies resulting from the proposed amendments to the plan of operation specifying that the Association prepare a statement of earnings on a calendar year basis.

*Using a Calendar Year as a Basis for Association Assessments.*

The public benefits of the proposed amendments to §5.4001(c)(1)(C)(ii) and §5.4001(c)(2)(B) of the plan of operation will be an improved Association plan of operation that will provide for (i) a more efficient and economical administration of the Association; (ii) the more equitable assessment of member companies to defray losses and expenses; and (iii) more accurate credit for similar insurance voluntarily written in the catastrophe areas based on more up-to-date data.

The Association will realize some time savings in the event of an assessment because only one set of calculations is needed to determine member companies' assessments using a calendar year basis, as opposed to the two sets of calculations needed to determine member companies'

assessments using a syndicate year basis. Calculations using a syndicate year basis always require consideration of two syndicate years, even though only a single event may be involved.

Pursuant to §5.4001(c)(2)(A)(ii) of the plan of operation, which is not proposed to be amended, the Association board of directors first determines the size of the assessment reasonable and necessary to provide for Association operating expenses and/or catastrophe losses. Under the current syndicate year basis of calculation required by §5.4001(c)(2)(B), the total assessment is apportioned into an assessment for the prior syndicate year (because policies from that year will still be in effect) and an assessment for the current syndicate year. The member companies' assessment percentages for each syndicate year is multiplied by the apportionment of the assessment for that syndicate year, and the two figures are added together to determine a member company's total assessment for a single event.

Under the proposed amendments, the total assessment will be determined as required by §5.4001(c)(2)(A)(ii). However, there will be no need to apportion the assessment by syndicate year; it will all be applicable to the current calendar year. The member company's assessment percentage for the current calendar year will be multiplied by the assessment amount. This will result in a member company's assessment being determined in one step under the proposal compared to multiple steps under the current procedure.

Another benefit will be the elimination of supplemental notices of assessment made necessary by the syndicate year basis of calculation. The

Association estimates that the mailing expense to member companies of supplemental notices of assessment necessary to reconcile calculations based on a syndicate year is approximately \$1,000 for an event that would result in an assessment. Thus, it is anticipated that the Association will save that amount in operating expenses per assessment if assessments were calculated on a calendar year basis rather than a syndicate year basis.

There will be some benefit to the member companies because assessments based on a calendar year will require the companies to only respond to a single notice of assessment rather than to an initial notice and a supplemental notice as required for assessments based on a syndicate year.

The current use of a syndicate year basis in determining assessments delays the effect of increases or decreases in voluntary writings in the catastrophe areas on the size of a member company's assessment because part of an assessment is based on an assessment percentage applicable to a prior syndicate year. Eliminating this delay is an important public benefit because it will provide an incentive to all member companies to maintain or provide similar insurance in the catastrophe areas, thereby reducing property owners' reliance on the Association to provide windstorm and hail insurance coverage.

In the event of an assessment, if a calendar year is used as the basis for calculating assessments rather than a syndicate year, member companies will benefit if the company has increased voluntary writings in the catastrophe areas during the most recently completed calendar year. Conversely, a member company that has decreased voluntary writings during the most recently

completed calendar year will be subject to a greater assessment in the current calendar year as a result of the decrease in voluntary writings.

**Proposal to Eliminate Minimum and Maximum Caps on Member Companies' Assessment Percentages.** The public benefit anticipated as a result of administering the proposed amendments eliminating minimum and maximum caps on a member company's assessment percentage will be that the company's credit for voluntary writings will more accurately and equitably reflect the company's actual voluntary writings. This is consistent with the Insurance Code §2210.052(d) and §2210.152(a)(2)(A) which provide that a member company is entitled to receive credit for similar insurance voluntarily written in the catastrophe areas in accordance with the plan of operation and that the plan of operation include a plan for the equitable assessment of the members of the Association to defray losses and expenses. A member company's unadjusted assessment percentage greater than zero percent but less than 20 percent of its percentage of net direct statewide premiums written will not be adjusted up to 20 percent, but will reflect the actual credit for similar insurance voluntarily written in the catastrophe areas in the preceding calendar year. A member with few or no voluntary writings in the catastrophe areas will no longer have an assessment percentage capped at 170 percent of its percentage of net direct statewide premiums written. Thus, the Association's assessment of members to defray losses and expenses will also be more equitable because member companies writing voluntary insurance in the catastrophe areas will receive full credit for their voluntary writings in the preceding calendar year, and member companies with

no or few voluntary writings in the catastrophe areas in the preceding calendar year will no longer receive credit for voluntary writings that do not exist. Thus, while the total of the assessment to all member companies will remain the same because the total assessment is based under §5.4001(c)(2)(A)(ii) on the amount the Association's board of directors has determined is "reasonable and necessary to provide for such operating expense and/or such catastrophe loss," an individual member company's assessment percentage of the total assessment may increase or decrease because of the elimination of the minimum and maximum caps on assessment percentages.

There will be no additional costs to the Association for the elimination of the application of minimum and maximum caps in the calculation of assessment percentages.

**4. ECONOMIC IMPACT STATEMENT AND REGULATORY FLEXIBILITY ANALYSIS FOR SMALL AND MICRO BUSINESSES.** The Government Code §2006.002(c) requires that if a proposed rule may have an economic impact on small businesses, state agencies must prepare as part of the rulemaking process an economic impact statement that assesses the potential impact of the proposed rule on small businesses and a regulatory flexibility analysis that considers alternative methods of achieving the purpose of the rule. The Government Code §2006.001(a)(2) defines "small business" as a legal entity, including a corporation, partnership, or sole proprietorship, that is formed for the purpose of making a profit; is independently owned and operated, and has fewer

than 100 employees or less than \$6 million in annual gross receipts. The Government Code §2006.001(a)(1) defines “micro business” similarly to “small business” but specifies that such a business may not have more than 20 employees. The Government Code §2006.001(a)(1) does not specify a maximum level of gross receipts for a “micro business.” The persons that are required to comply with the proposed amendments are the Association and the member companies required to pay assessments when funds available to the Association are insufficient to provide adequately for operating expenses of the Association and/or the Association’s catastrophe losses.

**The Association Is Not a Small Business.** The Association does not meet the definition of a “small business” under the Government Code §2006.001(a)(2). The Association is an “Association ... composed of all property insurers authorized to engage in the business of property insurance in this state,” formed under the authority of the Insurance Code §2210.051. It is not a corporation, partnership, nor sole proprietorship. It is not formed for the purpose of making a profit, but to provide a method by which adequate windstorm and hail insurance may be made available in certain designated portions of this state, as mandated by the Insurance Code §2210.001. Under the Insurance Code §2210.056, the net earnings of the Association may not inure to the benefit of private shareholders or individuals, and the assets of the Association may not be used other than to satisfy claims on policies, make investments authorized under applicable law, pay reasonable and necessary administrative expenses, and purchase reinsurance or prepare for or mitigate the effects of catastrophic natural

events. Under the Insurance Code §2210.452, all premium and other revenue of the Association in excess of incurred losses and operating expenses is paid to a catastrophe reserve trust fund or a reinsurance program approved by the Commissioner. Further, under the Insurance Code §§2210.056 and 2210.452, on the dissolution of the Association, all assets revert to the state. The Association is not “independently owned and operated.” In addition to not being owned by its members, under the Insurance Code §§2210.101 and 2210.102, the Association operates with a nine member board of directors responsible and accountable to the Commissioner. The Association provides windstorm and hail insurance according to a plan of operation as specified by the Insurance Code §2210.152 and adopted by the Commissioner by rule pursuant to the Insurance Code §2210.151. Further, the Association has approximately 150 employees and net receipts over \$6 million. Therefore, an economic impact statement and a regulatory flexibility analysis is not required for the Association because the Association as governed by the provisions of Chapter 2210 of the Insurance Code is not a small business for purposes of the Government Code §2006.002(c).

**The Effect of the Proposed Amendments on Small or Micro Businesses.**

*Change from Syndicate Year Basis to Calendar Year Basis for Association Calculations.* The Department has determined that the change in computation of data for the Association statement of earnings will not affect any small or micro businesses under the Government Code §2006.002(c) because

there will be no additional costs to any member company, regardless of size, including small and micro businesses, as a result of the proposed amendment to change the computation of data for the Association statement of earnings from a syndicate year basis to a calendar year basis.

The Department is unable to determine the effect of the computation of an assessment on a calendar year basis rather than a syndicate year basis on small or micro businesses because one important variable, the timing of a storm, is unpredictable; and other important variables are dependent upon the business calculations of various entities.

One variable that cannot be predicted is the date of the occurrence of a storm. Under a syndicate year basis for assessment calculations, if a storm occurs early in a year, a large percentage of the policies in effect will have become effective in the prior year, and the assessment percentage applicable to the prior year will be applicable to a greater amount of the losses. If a storm occurs late in the same year, a larger number of the policies in effect will have become effective in the current year, and the current assessment percentage will be applicable to a greater amount of the losses.

The assessment percentage for each member company is governed by the Insurance Code §2210.052 and §5.4001(c)(2)(B)(i) of the plan of operation and is calculated using the same method whether a syndicate year basis for assessment calculations is used or a calendar year basis for assessment calculations is used. The assessment percentage is determined annually and is generally described as the ratio of the member company's net direct premiums

written statewide to the aggregate net direct premiums written statewide by all members of the Association, adjusted by a credit for each member company's voluntary premiums written in the catastrophe areas. The assessment percentage for a small or micro business that is a member company can change from year to year depending on changes in the company's percentage of net direct premiums written statewide and/or changes in the company's participation in voluntary writings in the catastrophe areas. Changes in the voluntary writings of other businesses, such as an increase or decrease of percentage of net direct premiums written statewide and an increase or decrease of their voluntary writings in the catastrophe areas, also affect calculations of small or micro businesses' percentage of net direct premiums written statewide and their percentage of voluntary premiums written in the catastrophe areas. In general, if a company of any size, including a small or micro business, writes more premiums in the catastrophe areas and its percentage of net direct premium written statewide stays the same, its assessment percentage will adjust downward. If a company writes less premiums in the catastrophe areas and its percentage of net direct premiums written statewide stays the same, its assessment percentage will adjust upward.

Under a calendar year basis of assessment, the assessment percentage of each member company relies exclusively on data for the company from the most recently completed calendar year. Under the proposed amendments, if an assessment is made, any member company regardless of size, including a small or micro business, will have its share of the assessment calculated solely by an

assessment percentage that reflects the most current data on each company's market share in the statewide market and its voluntary writings in the catastrophe areas.

In accordance with the Government Code §2006.002(c-1), the Department has determined that even though the proposal to calculate member company assessments on a calendar year basis rather than a syndicate year basis may have an adverse economic impact on small or micro businesses that are required to comply with the proposal, the proposal does not require a regulatory flexibility analysis mandated by the Government Code §2006.002(c)(2). Section 2006.002(c)(2) requires a state agency, before adopting a rule that may have an adverse economic effect on small or micro businesses, to prepare a regulatory flexibility analysis that includes the agency's consideration of alternative methods of achieving the purpose of the proposed rule. Section 2006.002(c-1) of the Government Code requires that the regulatory flexibility analysis "consider, if consistent with the health, safety, and environmental and economic welfare of the state, using regulatory methods that will accomplish the objectives of applicable rules while minimizing adverse impacts on small businesses." Section 2001.002(g) of the Government Code requires the Attorney General, in consultation with the Comptroller, to prepare guidelines to assist a state agency: (i) in determining a proposed rule's potential adverse economic effects on small businesses; and (ii) in identifying and evaluating alternative methods of achieving the purpose of a proposed rule. According to these Attorney General guidelines published in the February 1, 2008 edition of the *Texas Register* (33 *TexReg* 985):

“An agency is not required to consider alternatives that, while possibly minimizing adverse impacts on small businesses would not be protective of the health, safety and environmental and economic welfare of the state [footnote deleted]. One example clearly fits within this exception. Agencies may be required to adopt as rules specific fees or specific standards and procedures under a legislative or federal mandate. In such a situation, the mandated language may be considered *per se* consistent with the health, safety, or environmental and economic welfare of the state and the agency need not consider other regulatory methods.” The calculation of a member company’s assessment percentage under Chapter 2210 of the Insurance Code constitutes specific standards and procedures proposed under legislative mandates that (i) there be “a plan for the equitable assessment of the members of the Association to defray losses and expenses” as provided in the Insurance Code §2210.152(a)(2)(A); and (ii) Association members be assessed Association operating expenses and/or losses in the proportion that the net direct premiums of a member bears to the aggregate net direct premiums of all members as provided in the Insurance Code §2210.052(a).

Under the Insurance Code §2210.001, the purpose of Chapter 2210 is to provide an adequate market for windstorm and hail insurance in this state. Chapter 2210 “provides a method by which adequate windstorm, hail, and fire insurance may be obtained in certain designated portions of this state.” The Insurance Code §2210.051(a) requires all property insurers authorized to engage in property insurance in the state to be members of the Association.

The Insurance Code §2210.152(a)(2)(A) requires the plan of operation to include “a plan for the equitable assessment of the members of the Association to defray losses and expenses.” Because all property insurers authorized to engage in property insurance in the state are required to be members, the establishment of an equitable assessment plan requires developing assessment procedures equitable to all members, regardless of size.

The Insurance Code §2210.052(a) specifies that Association members shall be assessed Association operating expenses and/or losses in the proportion that the net direct premiums of a member bears to the aggregate net direct premiums of all members, and the Insurance Code §2210.052(c) specifies that this proportion shall be determined annually in a manner provided by the plan of operation.

The proposed amendment to §5.4001(c)(2)(B) of the plan of operation to change the determination of a member company’s assessment from a syndicate year basis to a calendar year basis will eliminate the current delay in the effect of increases or decreases in voluntary writings on the size of a member company’s assessment. Therefore, if a small or micro business increases its voluntary writings in the designated catastrophe areas, the small or micro business will have a reduced assessment and will have it earlier than under the current syndicate year basis for calculating assessments. Alternatively, if a small or micro business decreases its voluntary writings in the designated catastrophe areas, the small or micro business will have an increased assessment and will have it earlier than under the current syndicate year basis for calculating

assessments. In either situation, the outcome can be influenced by the small or micro business by the business decisions that it makes.

Because all of the member companies' assessments, regardless of the size of the company, will be determined on the same calendar year and because all of the member companies will have the incentive to increase their writing of windstorm and hail coverage in the designated catastrophe areas, the change from the syndicate year basis to the calendar year basis for the determination of a member company's assessment is consistent with the requirements in the Insurance Code §2210.152(a)(2)(A) and §2210.052(a). The calculation method of a member company's assessment percentage under Chapter 2210 of the Insurance Code constitutes specific standards and procedures proposed under legislative mandates that (i) there be "a plan for the equitable assessment of the members of the Association to defray losses and expenses" as provided in the Insurance Code §2210.152(a)(2)(A); and (ii) Association members be assessed Association operating expenses and/or losses in the proportion that the net direct premiums of a member bears to the aggregate net direct premiums of all members as provided in the Insurance Code §2210.052(a). Exempting small and micro businesses from assessment or applying a different method of assessment is not consistent with the legislative mandates (i) that there be "a plan for the equitable assessment of the members of the Association to defray losses and expenses" as provided in the Insurance Code §2210.152(a)(2)(A); and (ii) that Association members be assessed Association operating expenses and/or losses in the proportion that the net direct premiums of a member bears to

the aggregate net direct premiums of all members as provided in the Insurance Code §2210.052(a). Accordingly, the costs for small and micro businesses attributable to this proposal are a result of these legislative mandates. Therefore, in accordance with the Attorney General guidelines issued pursuant to the Government Code §2001.002(g), the legislative mandates “may be considered *per se* consistent with the health, safety, or environmental and economic welfare of the state and the agency need not consider other regulatory methods.”

*Elimination of Minimum and Maximum Caps on Member Companies' Assessment Percentages.* The proposal to eliminate the application of minimum and maximum caps on assessment percentages may have an adverse economic effect on approximately four to five small or micro businesses that are members of the Association. Pursuant to the Insurance Code §2210.051(a), all property insurers authorized to engage in the business of property insurance in this state are required to be members of the Association, as required by the Insurance Code §2210.051(a). As Association members, these four to five small or micro businesses may be assessed pursuant to §5.4001(c)(2)(A) of the plan of operation if funds available to the Association are of insufficient size to adequately provide for the Association's operating expenses and/or catastrophe losses.

The Association has modeled projected changes in the assessment percentages for all member companies based on the elimination of the application of minimum and maximum caps. Based on this modeling information, four small or micro businesses were identified.

The effect on the four companies will be: (i) Company A's assessment percentage was calculated in 2007 as 0.042%. If the minimum and maximum caps had been eliminated in 2007, Company A's assessment percentage would have slightly increased to 0.045% (+0.003%). (ii) Company B's assessment percentage was calculated in 2007 as 0.036%. If the minimum and maximum caps had been eliminated in 2007, Company B's assessment percentage would have increased to 0.040% (+0.004%). (iii) Company C's assessment percentage was calculated in 2007 as 0.006%. If the minimum and maximum caps had been eliminated, Company C's assessment percentage would not change. (iv) Company D's assessment percentage was calculated in 2007 as 0.002%. If the minimum and maximum caps had been eliminated in 2007, Company D's assessment percentage also would not change. Thus, based on these four companies, the elimination of the minimum and maximum caps will either have an effect of slightly increasing an assessment percent by 0.003 to 0.004 percent, or have no effect on an individual small or micro business's assessment percentage.

The Association has also modeled the projected assessment percentages if current trends relating to withdrawals from the voluntary market in the catastrophe areas are factored into the same calculations to estimate what may happen in future years. Under these estimates, the projected assessment percentages for Company A, B, and C would decrease after the elimination of the minimum and maximum caps, and Company D's projected assessment percentage would remain the same. Company A's projected assessment

percentage after the elimination of minimum and maximum caps would be 0.039% (-0.003%); Company B's projected assessment percentage would be 0.032% (-0.004%); Company C's projected assessment percentage would be 0.005% (-0.001%); and Company D's projected assessment percentage would be 0.002% (no change).

In accordance with the Government Code §2006.002(c-1), the Department has determined that even though the proposal to eliminate minimum and maximum caps from the Association plan of operation may have an adverse economic impact on small or micro businesses that are required to comply with the proposal, the proposal does not require a regulatory flexibility analysis mandated by the Government Code §2006.002(c)(2). Section 2006.002(c)(2) requires a state agency, before adopting a rule that may have an adverse economic effect on small businesses, to prepare a regulatory flexibility analysis that includes the agency's consideration of alternative methods of achieving the purpose of the proposed rule. Section 2006.002(c-1) of the Government Code requires that the regulatory flexibility analysis "consider, if consistent with the health, safety, and environmental and economic welfare of the state, using regulatory methods that will accomplish the objectives of applicable rules while minimizing adverse impacts on small businesses." Section 2001.002(g) of the Government Code requires the Attorney General, in consultation with the Comptroller, to prepare guidelines to assist a state agency: (i) in determining a proposed rule's potential adverse economic effects on small businesses; and (ii) in identifying and evaluating alternative methods of achieving the purpose of a

proposed rule. According to these Attorney General guidelines published in the February 1, 2008 edition of the *Texas Register* (33 *TexReg* 985) “An agency is not required to consider alternatives that, while possibly minimizing adverse impacts on small businesses would not be protective of the health, safety and environmental and economic welfare of the state [footnote deleted]. One example clearly fits within this exception. Agencies may be required to adopt as rules specific fees or specific standards and procedures under a legislative or federal mandate. In such a situation, the mandated language may be considered *per se* consistent with the health, safety, or environmental and economic welfare of the state and the agency need not consider other regulatory methods.”

The amendment of the procedure in the plan of operation used to determine a member company’s assessment percentage, in this instance, by eliminating a minimum cap (20 percent of a company’s percentage of the net direct statewide property insurance market) and a maximum cap (170 percent of a company’s percentage of the same market) on a member company’s Association assessment percentage, constitutes proposing as rules specific standards and procedures under a legislative mandate. The legislative mandates are (i) that there be “a plan for the equitable assessment of the members of the Association to defray losses and expenses” as provided in the Insurance Code §2210.152(a)(2)(A); (ii) that Association members be assessed Association operating expenses and/or losses in the proportion that the net direct premiums of a member bears to the aggregate net direct premiums of all members as provided in the Insurance Code §2210.052(a); and (iii) that the plan

of operation include a credit for similar insurance voluntarily written in the catastrophe areas as provided in the Insurance Code §2210.052(d).

Under the Insurance Code §2210.001, the purpose of Chapter 2210 is to provide an adequate market for windstorm and hail insurance in this state. Chapter 2210 “provides a method by which adequate windstorm, hail, and fire insurance may be obtained in certain designated portions of this state.” The Insurance Code §2210.051(a) requires all property insurers authorized to engage in property insurance in the state to become members of the Association.

The Insurance Code §2210.152(a)(2)(A) requires the plan of operation to include “a plan for the equitable assessment of the members of the Association to defray losses and expenses.” Because all property insurers authorized to engage in property insurance in the state are required to be members, the establishment of an equitable assessment plan requires developing assessment procedures equitable to all members, regardless of size.

The Insurance Code §2210.052(a) specifies that Association members shall be assessed Association operating expenses and/or losses in the proportion that the net direct premiums of a member bears to the aggregate net direct premiums of all members, and the Insurance Code §2210.052(c) specifies that this proportion shall be determined annually in a manner provided by the plan of operation.

The Insurance Code §2210.052(d) specifies that the plan of operation shall provide that members are entitled to a credit for similar insurance voluntarily written in the catastrophe areas and that the credit should reduce the member

company's proportion of participation in the expenses and losses of the Association.

The proposed amendment to §5.4001(c)(2)(B)(1) of the plan of operation to eliminate the use of minimum and maximum caps will allow each member company to receive its full credit for similar insurance voluntarily written in the catastrophe areas, instead of requiring a minimum percentage of 20 percent of a member's percentage of the net direct statewide premiums written. Member companies that have few or no voluntary writings in the catastrophe area will no longer receive a credit limiting their assessment percentage to 170 percent of their percentage of the net direct statewide premiums written. The elimination of the caps for all member companies' assessment percentages is consistent with the requirement in the Insurance Code §2210.152(a)(2)(A) that the plan of operation include a plan for the equitable assessment of the members and the requirement in the Insurance Code §2210.052(d) that the plan of operation include a credit for similar insurance voluntary written in the catastrophe areas.

Exempting small and micro businesses from the elimination of minimum or maximum caps may not prove beneficial to small or micro businesses because the assessment percentage for a small or micro business would be required to be adjusted upward to a minimum of 20 percent of the company's percentage of the net direct statewide property insurance market if in the future the company's credit for voluntary writings in the catastrophe areas reduced the company's assessment percentage to a lesser percentage than the minimum cap.

Exempting small and micro businesses from the elimination of minimum and maximum caps is not consistent with the legislative mandates (i) that there be “a plan for the equitable assessment of the members of the Association to defray losses and expenses” as provided in the Insurance Code §2210.152(a)(2)(A); (ii) that Association members be assessed Association operating expenses and/or losses in the proportion that the net direct premiums of a member bears to the aggregate net direct premiums of all members as provided in the Insurance Code §2210.052(a); and (iii) that the plan of operation include a credit for similar insurance voluntarily written in the catastrophe areas as provided in the Insurance Code §2210.052(d). Accordingly, the costs attributable to this proposal are a result of these legislative mandates. Therefore, in accordance with the Attorney General guidelines issued pursuant to the Government Code §2001.002(g), the legislative mandates “may be considered *per se* consistent with the health, safety, or environmental and economic welfare of the state and the agency need not consider other regulatory methods.”

**5. TAKINGS IMPACT ASSESSMENT.** The Department has determined that no private real property interests are affected by this proposal and that this proposal does not restrict or limit an owner’s right to property that would otherwise exist in the absence of government action and, therefore, does not constitute a taking or require a takings impact assessment under the Government Code §2007.043.

**6. REQUEST FOR PUBLIC COMMENT.** To be considered, written comments on the proposal must be submitted no later than 5:00 p.m. on August 5, 2008, to Gene C. Jarmon, General Counsel and Chief Clerk, Mail Code 113-2A, Texas Department of Insurance, P. O. Box 149104, Austin, Texas 78714-9104. An additional copy of the comment must be simultaneously submitted to Marilyn Hamilton, Associate Commissioner, Property and Casualty Program, Mail Code 104-PC, Texas Department of Insurance, P. O. Box 149104, Austin, Texas 78714-9104.

The Commissioner will consider the adoption of the proposed amendments in a public hearing under Docket No. 2686, scheduled for July 18, 2008, at 9:30 a.m., in Room 100 of the William P. Hobby, Jr., State Office Building, 333 Guadalupe Street, Austin, Texas 78701. Written and oral comments presented at the hearing will be considered.

**7. STATUTORY AUTHORITY.** The amendments are proposed pursuant to the Insurance Code Chapter 2210 and §36.001. The Insurance Code §2210.151 requires the Commissioner by rule to adopt the Association plan of operation to provide Texas windstorm and hail insurance in the catastrophe areas. The Insurance Code §2210.152(a)(1) requires that the plan of operation provide for the efficient, economical, fair, and non-discriminatory administration of the Association.

The Insurance Code §2210.054 requires the Association to file an annual statement containing information prescribed by the Department and in the form prescribed by the Department.

The Insurance Code §2210.152(a)(2)(A) requires the plan of operation to include a plan for the equitable assessment of the members of the Association to defray losses and expenses. The Insurance Code §2210.052(a) requires that a member company share in the losses and/or expenses of the Association based on the proportion that the net direct premiums of that member during the preceding calendar year bears to the aggregate net direct premiums by all members of the Association. Under the Insurance Code §2210.052(c), a member company's share of the losses and/or expenses of the Association is required to be determined annually and in the manner provided by the plan of operation. In the determination of a member company's share of the losses and/or expenses of the Association, the Insurance Code §2210.052(d) specifies that members are entitled to a credit for insurance voluntarily written in the catastrophe areas. The Insurance Code §2210.052(d) also requires that the method for calculating the credit be contained in the plan of operation. The Insurance Code §2210.053(b) encourages the Department to develop a program designed to create incentives for insurers to write voluntary windstorm and hail insurance in the catastrophe areas.

Pursuant to the Insurance Code §2210.153(a)(1), the Association may present a recommendation for a change in the plan of operation to the Department. The Insurance Code §2210.153(b) requires proposed changes to

the plan of operation to be in writing in the manner prescribed by the Commissioner. The proposed change does not take effect unless adopted by the Commissioner by rule. The Insurance Code §36.001 authorizes the Commissioner of Insurance to adopt any rules necessary and appropriate to implement the powers and duties of the Texas Department of Insurance under the Insurance Code and other laws of this state.

**8. CROSS REFERENCE TO STATUTE.** The following statutes are affected by this proposal:

<u>Rule</u>	<u>Statute</u>
§5.4001	Insurance Code Chapter 2210

**9. TEXT.**

**DIVISION 1. PLAN OF OPERATION**

**§5.4001. Plan of Operation**

(a) – (b) (No change.)

(c) Financial Operation of the Association.

(1) Collection, investment, and allocation of funds.

(A) – (B) (No change.)

(C) Allocation.

(i) Each year the association will prepare a statement of earnings by calendar [~~syndicate~~] year. All premiums written, commissions paid, unearned and earned premiums, loss and loss expenses paid and pending

will be charged to the calendar [~~syndicate~~] year. All general expense and interest income received will be charged or credited to the current calendar [~~syndicate~~] year. [~~Syndicate year is determined by the effective date of a policy. For example, policies written in calendar year 1972 with an effective date of 1972 will be charged to the syndicate year 1972. All premiums and loss-loss expense transactions affecting these policies will be assigned to syndicate year 1972. Likewise, all premiums and loss-loss expense transactions in calendar year 1972 affecting policies with an effective date of 1971 will be charged to syndicate year 1971.~~]

(ii) Each company will apply their participation percentage applicable to each calendar [~~syndicate~~] year.

(2) Assessment of members.

(A) (No change.)

(B) Amount of assessment. The board of directors shall determine which members of the association shall participate in any assessment for operating expenses and/or catastrophe losses. This determination shall be computed on a [~~syndicate year basis rather than on a~~] calendar year basis. The designated members of the association shall participate in any assessment levied in the proportion that the net direct premiums of such member written in this state during the preceding calendar year bears to the aggregate net direct premiums written in this state by all members of the association as furnished to the association by the Department after review of annual statements, other reports, and required statistics; provided, however, that if at the time of such

assessment the Department has not furnished to the association information necessary to compute a member's participation during the preceding calendar year, then each member's participation shall be based upon information furnished to the association from the last calendar year in which such information is available and, upon obtaining the necessary information from the Department, the association shall reassess or refund to each member such amounts as are necessary to properly reflect such member's participation; provided, further, that a member shall be entitled to receive the following credit for insurance, similar to catastrophe insurance, written in such catastrophe areas. [~~area, except that in no event shall the final percentage of participation after application for credit for voluntary writings in the catastrophe area be less than 20% nor more than 190% of the company's percentage of statewide windstorm and hail premiums modified by applicable offset factors, nor more than 170% of the company's percentage of statewide windstorm and hail premium modified by applicable offset factors for policies with inception dates on and after January 1, 1984.~~]

(i) Participation in the association [~~Texas Catastrophe Property Insurance Association~~] for policies after January 1, 1988. Procedure for determining the percent of participation respecting association policies with inception dates on or after January 1, 1988, for members of the association [~~Texas Catastrophe Property Insurance Association~~] reflecting credit for voluntary premiums written in the designated areas [~~area~~]. (All premiums are for the most recent preceding calendar year ending December 31, as furnished by the Department.) Column 1(a): Statewide net direct premiums for extended

coverage and other allied lines. Column 1(b): Statewide net direct premiums for extended coverage and other allied lines portion of the multiple peril line. Column 1(c): Statewide net direct premiums for homeowners and farm and ranch owners. Column 2: The sum of the statewide net direct premiums at 90% of the extended coverage and other allied lines, and 50% of the homeowners and farm and ranch owner's, or such percentage as may be determined in accordance with subsection (a)(2)(i)(III) of this section (90% of Column [~~column~~] 1(a) [~~%+~~] plus 90% of Column [~~column~~] 1(b) plus 50% of Column [~~column~~] 1(c)). Column 3: Each company's percentage of the net direct premiums as described in Column [~~column~~] 2, which is the basis for indicating normal required participation in the association [~~Texas Catastrophe Property Insurance Association~~] prior to credits for voluntary writings in the designated areas [~~area~~]. Column 4: Total windstorm and hail premiums in the designated areas [~~area~~] (association premiums plus voluntary premiums). Column 5: Normal company quota of total windstorm and hail premiums [~~∴~~] (Column [~~column~~] 3 x Column [~~column~~] 4). Column 6: Each company's voluntary writings in the designated areas [~~area~~] multiplied by the same percentages as shown in Column [~~column~~] 2. Note: Maximum credit shall be limited to company's normal quota. Column 7: Each company's maximum possible allocation after applying credits for voluntary writings (Column [~~column~~] 5 minus Column [~~column~~] 6). Negative allocation to be shown as zero. Column 8: Percentage participation of each member company in the association [~~Texas Catastrophe Property Insurance Association~~], prior to application of offset. Note: The offset figure measures the excess

premiums developed by the maximum credit [credits] in Column [column] 6. Column 9: Percentage participation of each member company in the association. [~~Texas Catastrophe Property Insurance Association prior to application of minimum-maximum factors. Column 10 Assignment after application of 20% minimum or 170% maximum of column 3. Column 11 Net assignment of association. (After application of offset following minimum-maximum limitations).~~]

[~~(ii) Participation in Texas Catastrophe Property Insurance Association for policies after January 1, 1983. Procedure for determining the percent of participation respecting association policies with inception dates on and after January 1, 1983, through December 31, 1987, inclusive, for members of the Texas Catastrophe Property Insurance Association reflecting credit for voluntary premiums written in the designated area. (All premiums are for the most recent preceding calendar year ending December 31.)~~  
Column 1(a) ~~Statewide direct written premiums for extended coverage from Texas annual statement, page 14, line 2, column 1, and other allied lines from line 3, column 1. Column 1(b) Statewide direct written premiums for the extended coverage and other allied lines portion of the multiple peril line from Texas annual statement, page 14, line 8, column 1. Column 1(c) Statewide direct written premiums for homeowners and farm and ranch owners from Texas annual statement, page 14, line 4, column 1, and line 5, column 1. Column 2 The sum of the statewide direct written premiums at 90% of the extended coverage and other allied lines, and 50% of the homeowners and farm and ranch owners, or~~

~~such percentage as may be determined in accordance with subsection (a)(2)(i)(III) of this section. (90% of column 1(a)%+ 90% of column 1(b)%+ 50% of column 1(c).) Column 3 Each company's percentage of the net direct premiums as described in column 2, which is the basis for indicating normal required participation in the Texas Catastrophe Property Insurance Association prior to credits for voluntary writings in the designated area. Column 4 Total windstorm and hail premiums in the designated area (association premiums plus voluntary premiums). Column 5 Normal company quota of total windstorm and hail premiums: column 3 x column 4. Column 6 Each company's voluntary writings in the designated area multiplied by the same percentage as shown in column 2 previously. Note: Maximum credit shall be limited to company's normal quota. Column 7 Each company's maximum possible allocation after applying credits for voluntary writings (column 5 minus column 6). Negative allocation to be shown as zero. Column 8 Percentage participation of each member company in Texas Catastrophe Property Insurance Association, prior to application of offset. Note: The offset figure measures the excess premiums developed by maximum credits in column 6. Column 9 Percentage participation of each member company in Texas Catastrophe Property Insurance Association prior to application of minimum-maximum factors. Column 10 Assignment after application of 20% minimum or 190% maximum of column 3 for policies with an inception date during 1983 or 170% maximum of column 3 for policies with inception dates on or after January 1, 1984. Column 11 Net assignment in association. (After application of offset following minimum-maximum limitations.)]~~

~~[(iii) Participation in Texas Catastrophe Property Insurance Association for policies after January 1, 1978. Procedure for determining the percent of participation respecting association policies with inception dates on and after January 1, 1978, through December 31, 1982, inclusive, for members of the Texas Catastrophe Property Insurance Association reflecting credit for voluntary premiums written in the designated area. (All premiums are for the most recent preceding calendar year ending December 31.)~~

~~Column 1(a) Statewide direct written premiums for extended coverage from Texas annual statement, page 14, line 2, column 1. Column 1(b) Statewide direct written premiums for the extended coverage portion of the multiple peril line from Texas annual statement, page 14, line 8, column 1. Column 1(c) Statewide direct written premiums for homeowners and farm and ranch owners from Texas annual statement, page 14, line 4, column 1. Column 2 The sum of the statewide direct written premiums at 90% of the extended coverage and 40% of the homeowners. (90% column 1(a)%+ 90% of column 1(b)%+ 40% of column 1(c).) Column 3 Each company's percentage of the net direct premiums as described in Column 2, which is the basis for indicating normal required participation in the Texas Catastrophe Property Insurance Association prior to credits for voluntary writings in the designated area. Column 4 Total windstorm and hail premiums in the designated area. (association premiums plus voluntary premiums). Column 5 Normal company quota of total windstorm and hail premiums: column 3 x 4. Column 6 Each company's voluntary writings in the designated area multiplied by the same percentages as shown in column 2~~

~~previously. Note: Maximum credit shall be limited to company's normal quota.  
Column 7 Each company's maximum possible allocation after applying credits for  
voluntary writings (column 5 minus column 6). Negative allocation to be shown  
as zero. Column 8 Percentage participation of each member company in the  
Texas Catastrophe Property Insurance Association, prior to application of offset.  
Note: The offset figure measures the excess premiums developed by maximum  
credits in column 6. Column 9 Percentage participation of each member  
company in Texas Catastrophe Property Insurance Association prior to  
application of minimum-maximum factors. Column 10 Assignment after  
application of 20% minimum or 100% maximum of column 3. Column 11 Net  
assignment in association. (After application of offset following minimum-  
maximum limitations.)]~~

**TEXAS WINDSTORM [CATASTROPHE PROPERTY] INSURANCE ASSOCIATION**  
**[4.] PROCEDURE FOR CALCULATING MEMBER ASSESSMENT**  
**PERCENTAGES [POOL PARTICIPATION] INCLUDING**  
**CREDIT FOR VOLUNTARY WRITINGS**

[1]	[2]	[3]	[4]
STATEWIDE DIRECT WRITTEN PREMIUMS [PREMIUM]	NET DIRECT WRITTEN PREMIUMS [PREMIUM]	COMPANY PERCENT OF STATEWIDE PREMIUMS WRITTEN	TOTAL PREMIUMS [PREMIUMS] IN CATASTROPHE AREAS [AREA]
(a)(b)(c) E.C. CMP HO	Total of Col. [1](a) & (b) x 90% Col. [1](c) x 50% [Col. [1](c) x 40% (50%)*]	[2] ÷ Total of [2]	(ASSOCIATION [TCPIA] + VOLUNTARY)
[5]	[6]	[7]	[8]
NORMAL REQUIRED QUOTA IN DESIGNATED AREAS [AREA]	CREDIT FOR COMPANY'S VOLUNTARY PREMIUMS	DIFFERENCE BETWEEN NORMAL REQUIRED PARTICIPATION AND VOLUNTARY CREDIT PREMIUMS	ASSOCIATION ASSESSMENT PERCENTAGE [ASSIGNMENT IN ASSOCIATION] PRIOR TO OFFSET
([3] x [4])	(not to exceed column [5])	([5] – [6])	[7] ÷ Total of [7]
[9]	[[10]]	[[11]]	
NET ASSOCIATION ASSESSMENT PERCENTAGE [ASSIGNMENT AFTER OFFSET FACTOR]	[ASSIGNMENT AFTER APPLICATION OF]	[NET ASSIGNMENT IN ASSOCIATION]	
(After application of offset)	[20% minimum or 190% maximum of Column [3] (170% maximum)**]	[After application of offset following minimum-maximum limitations]	

[\* For association policies effective on and after January 1, 1983.]

[\*\* For association policies effective on and after January 1, 1984.]

(ii)[(iv)] The Department shall furnish to the association the amount of net direct premiums of each member company written on property in this state and the aggregate net direct premiums written on property in this state by all member companies during the preceding calendar year as reported by member companies to the Department. Within a reasonable time after the receipt of same from the Department, the association shall notify each member company, in writing, sent by certified mail, the amount of the net direct premiums written on property in this state during the preceding calendar year by the member company to whom notice is given, including the net direct premiums of [Ø] similar insurance voluntarily written in the catastrophe areas, upon which such company's percentage of participation will be determined. Such notice shall state that such notification, and the content thereof, is an act, ruling, or decision of the association and that the member company to whom such notice is given shall be entitled to appeal therefrom within 30 days from the date of such act, ruling, or decision as shown on said notice in accordance with the Insurance Code §2210.551 [~~Article 21.49, §9~~]. Thereafter, the association shall determine the percentage of participation for each member company in the manner provided in the plan of operation and shall notify each member company thereof, in writing, sent by certified mail. Such notice shall state that such notification, and the content thereof, is an act, ruling, or decision of the association insofar as the mathematical determination of the percentage of participation is concerned and that the member company to whom such notice is given shall be entitled to appeal therefrom within 30 days from the date of such

act, ruling, or decision as shown on said notice in accordance with the Insurance Code §2210.551 [~~Article 21.49, §9~~].

(iii)[(v)] To assist the association in determining each member insurer's percentage of participation as soon as possible in the calendar year, each member insurer shall furnish to the association on or before March 1 of each year a copy of its Exhibit of Premiums and Losses (Statutory Page 14 Data) for the State of Texas that is filed annually with the Department as part of the insurer's Texas Fire and Casualty Annual Statement Form 2.

(C) Notice of assessment. Notice of assessment shall be sent to each member, within 30 days of the meeting of the board of directors at which such assessment was levied, by certified mail, return receipt requested, addressed to the office of such member as it appears on the books of the Association. Such notice shall state the member's allocated amount of assessment and shall inform each member of the sanctions imposed by subparagraph (D) of this paragraph for the failure to pay such assessment within the time prescribed by this section. Such notice shall also state that such notification, and the content thereof, is an act, ruling, or decision of the association insofar as the amount of the assessment for such company is concerned and that a member company to whom such notice is given shall be entitled to appeal therefrom within 30 days from the date of such act, ruling, or decision as shown on said notice, in accordance with the Insurance Code §2210.551 [~~Article 21.49, §9~~]; provided, however, that the right of appeal provided for herein shall not include the subject matter of any act, ruling, or

decision of the association determining the amount of net direct premiums [~~premium~~] of such member company or the percentage of participation for such member company when notice of the amount of such net direct premiums [~~premium~~] or such percentage of participation has previously been given by the association in accordance with subparagraph (B)(ii) [~~(B)(iv)~~] of this paragraph. The time period for an appeal of an act, ruling, or decision of the association respecting net direct premiums or percentage of participation is computed from the date of the act, ruling, or decision of the association respecting same.

(D) – (E) (No change.)

(3) Use of funds.

(A) – (B) (No change.)

(d) – (e) (No change.)

**10. CERTIFICATION.** This agency hereby certifies that the proposal has been reviewed by legal counsel and found to be within the agency's authority to adopt.

Issued at Austin, Texas, on \_\_\_\_\_, 2008.

---

Gene C. Jarmon  
General Counsel and Chief Clerk  
Texas Department of Insurance