INSURANCE
DEPARTMENT OF BANKING AND INSURANCE
OFFICE OF SOLVENCY REGULATION

Determination of Insurers in a Hazardous Financial Condition

Proposed Amendment: N.J.A.C. 11:2-27.3

Authorized By: Holly C. Bakke, Commissioner, Department of Banking and Insurance

Authority: N.J.S.A. 17:1-8.1, 17:1-15e, 17B:20-4g and 17:51A-1 et seq.

Calendar Reference: See Summary below for explanation of exception to calendar requirements.

Proposal Number: PRN 2004 –352

Submit comments by November 19, 2004 to:

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The agency proposal follows:

Summary

The Department of Banking and Insurance (Department) is proposing amendments to N.J.A.C. 11:2-27.3, which sets forth various factors which the Commissioner of the Department of Banking and Insurance (Commissioner) shall consider in determining whether an insurer is in a hazardous financial condition. A determination of hazardous financial condition provides one of the grounds for the Commissioner to take various actions, including, but not limited to, seeking an order from the Superior Court to rehabilitate, liquidate or conserve the assets of the insurer pursuant to N.J.S.A. 17B:32-31 et seq., or subjecting the insurer to administrative supervision pursuant to N.J.S.A. 17:51A-1 et seq. or taking action to revoke or non-renew an insurer's authority to transact insurance in this State.

The Department is proposing an amendment to N.J.A.C. 11:2-27.3 by adding subsection (e). The purpose of this new subsection is to clarify the factors that the Department will consider in determining whether a company is in a hazardous financial condition and whether there exists sufficient value, liquidity and diversity in the asset portfolio of life and health insurers.

The Department's proposed amendment is generally consistent with the standards of the National Association of Insurance Commissioners (NAIC). The NAIC requires, as one of the standards under its Financial Regulation Standards and Accreditation Program (Accreditation Program), that a state require a diversified investment portfolio for all domestic insurers as to type and issue, and include a requirement for liquidity. In addition, NAIC accreditation standards require a state to limit a domestic insurer's investments in non-insurance subsidiaries in a manner that is consistent with the limitations set forth in the model Insurance Holding Company System Regulatory Act adopted by the NAIC, or to have a standard substantially similar thereto. The NAIC model provision generally provides that a domestic insurer may invest in common stock, preferred stock, debt obligations and other securities of one or more subsidiaries, excluding investments in insurance subsidiaries, in amounts which do not exceed the lesser of 10 percent of such insurer's assets or 50 percent of such insurer's surplus as regards policyholders, provided that, after such investment, the insurer's surplus as regards policyholders will be reasonable in relation to the insurer's outstanding liabilities and adequate to its financial needs. N.J.S.A. 17B:20-4g limits investments by a life and health insurer in non-insurance subsidiaries to no more than eight percent of the admitted assets of the insurer. The proposed amendment incorporates this New Jersey statutory standard into the factors the Department will consider in determining whether an insurer is in a hazardous financial condition.

A 60-day comment period is provided for this notice of proposal and, therefore, pursuant to N.J.A.C. 1:30-3.3(a)5, the proposal is not subject to the provisions of N.J.A.C. 1:30-3.1 and 3.2 governing rulemaking calendars.

Social Impact

These proposed amendments will have a positive social impact on the New Jersey life and health insurance market by enhancing the Department's ability to monitor the financial status of life and health insurance companies writing in New Jersrey. The Department's proposed amendments ensure that life and health insurers are apprised of the criteria utilized by the Department in determining whether an insurer is in a hazardous financial condition. Those amendments also provide guidance for evaluating whether sufficient value, liquidity and diversity exists with respect to investments in subsidiaries of life and health insurers.

Additionally, since insurers will be fully apprised of the Department's standards, they should be in a position to take steps necessary to avoid falling into a hazardous financial condition. This should help ensure that insurers will have sufficient assets and be in a financial position to pay their obligations. The likelihood that delinquency proceedings will be instituted against an insurer will also be reduced, thereby avoiding the cost and disruption of such proceedings. This, in turn, will benefit insurers, the Department, policyholders, claimants, and the public generally.

Economic Impact

The Department believes that no adverse economic impact will be experienced by insurers as a result of the proposed amendments. Through codification of this standard, all insurers will be apprised of the standard for determining whether the factor related to sufficient values, liquidity and diversity in the insurer's asset portfolio exists. Insurers therefore should be in a position to take such action as is necessary to avoid a finding by the Commissioner of a hazardous financial condition, thereby reducing the likelihood that delinquency proceedings will be instituted against such insurers.

The Department does not believe that these amendments will result in additional cost to life and health insurers. The Department believes that these amendments codify the policies of the NAIC and the Department to which most life and health insurers already adhere.

Federal Standards Statement

A Federal standards analysis is not required because these amendments regulate the business of insurance and are not subject to any Federal requirements or standards.

Job Impact

The Department does not anticipate jobs being generated or lost as a result of these amendments.

Agriculture Industry Impact

Pursuant to N.J.S.A. 4:1C-1 et seq. the Right to Farm Act, and N.J.S.A. 52:14B-4(a) of the Administrative Procedures Act, the Department does not expect any agriculture industry impact from these proposed amendments.

Regulatory Flexibility Statement

A regulatory flexibility analysis is not required because the proposed amendments do not impose reporting, recordkeeping or other compliance requirements on “small businesses” as that term is defined in the Regulatory Flexibility Act, N.J.S.A. 52:14B-16 et seq. As noted above, the proposed amendments merely codify the standard the Department will utilize with respect to domestic life and health insurers in determining whether the factor set forth in N.J.A.C. 11:2-27.3(a)4 related to sufficient value, liquidity and diversity exists. The amendments thus provide greater guidance both to the Department and insurers with respect to the application of this factor. No specific reporting, recordkeeping, or compliance requirements are imposed by the proposed amendments.

Smart Growth Impact

The proposed amendments have no impact on the achievement of smart growth and implementation of the State Development and Redevelopment Plan.

Full text of the proposal follows (additions indicated in boldface **thus**):

11:2-27.3 Determination of hazardous financial conditions; factors

(a) - (d) (No change)

(e) With respect to the domestic life and health insurers, the factor set forth in (a)4 above shall be presumed to exist if the Commissioner finds the following:

1. The insurer has invested in common stock, preferred stock, debt obligations and other securities of one or more subsidiaries in amounts which:

i. Exceed the lesser of eight percent of such insurer's admitted assets or 50 percent of such insurer's surplus as regards policyholders; or

ii. Otherwise demonstrate after such investments that the insurer's surplus as regards policyholders is not reasonable in relation to the insurer's outstanding liabilities and adequate to its financial needs.

2. In calculating the amount of the investments referenced in (e)1 above, investments in domestic or foreign insurance subsidiaries shall be excluded, and there shall be included:

i. The total net monies or other consideration expended and obligations assumed in the acquisition or formation of a subsidiary, including all organizational

<u>expenses and contributions to capital and surplus of such subsidiary whether or not represented by the purchase of capital stock or issuance of other securities; and</u>

<u>ii. All amounts expended in acquiring additional common stock, preferred stock, debt obligations, and other securities and all contributions to the capital or surplus of a subsidiary subsequent to its acquisition or formation.</u>