

Hall of the House of Representatives

83rd General Assembly - Regular Session, 2001

Amendment Form

Subtitle of House Bill No. 2474

"TO CREATE PROTECTED CELLS."

Amendment No. 1 to House Bill No. 2474.

Amend House Bill No. 2474 as originally introduced:

Delete everything after the Enacting Clause and substitute

"SECTION 1. Short title.

This act may be cited as the "Protected Cell Company Act".

SECTION 2. Purpose.

This act provides:

(1) A basis for the creation of protected cells by a domestic insurer as one means of accessing alternative sources of capital and achieving the benefits of insurance securitization;

(2) Funds to investors in fully funded insurance securitization transactions that are available to pay the insurer's insurance obligations, or to repay the investors, or both; and

(3) A means to achieve more efficiencies in conducting insurance securitizations.

SECTION 3. Definitions.

For the purposes of this act:

(1) "Domestic insurer" means an insurer domiciled in the State of Arkansas;

(2) "Fully funded" means that, with respect to any exposure attributed to a protected cell, the fair value of the protected cell assets, on the date on which the insurance securitization is effected, equals or exceeds the maximum possible exposure attributable to the protected cell with respect to such exposures;

(3) "General account" means the assets and liabilities of a protected cell company other than protected cell assets and protected cell liabilities;

(4) "Indemnity trigger" means a transaction term by which relief of the issuer's obligation to repay investors is triggered by incurring a specified level of losses under its insurance or reinsurance contracts;

(5)(A) "Fair value" of an asset or liability means the amount at which that asset or liability could be bought, incurred, sold, or settled in a current transaction between willing parties that is not a forced or liquidation sale.

(B)(i) Quoted market prices in active markets are the best evidence of fair value and shall be used as the basis for the measurement, if available.

(ii) If a quoted market price is available, the fair value is the product of the number of trading units times market price.

(iii) If quoted market prices are not available, the estimate of fair value shall be based on the best information available.

(iv)(a) The estimate of fair value shall consider prices for similar assets and liabilities and the results of valuation techniques to the extent available in the circumstances.

(b) Examples of valuation techniques include the present value of estimated expected future cash flows using a discount rate commensurate with the risks involved, option-pricing models, matrix pricing, option-adjusted spread models, and fundamental analysis.

(c) Valuation techniques for measuring financial assets and liabilities and servicing assets and liabilities shall be consistent with the objective of measuring fair value. Those techniques shall incorporate assumptions that market participants would use in their estimates of values, future revenues, and future expenses, including assumptions about interest rates, default, prepayment, and volatility.

(d) In measuring financial liabilities and servicing liabilities at fair value by discounting estimated future cash flows, an objective is to use discount rates at which those liabilities could be settled in an arm's-length transaction.

(e)(1) Estimates of expected future cash flows, if used to estimate fair value, shall be the best estimate based on reasonable and supportable assumptions and projections.

(2) All available evidence shall be considered in developing estimates of expected future cash flows.

(3) The weight given to the evidence shall be commensurate with the extent to which the evidence can be verified objectively.

(4) If a range is estimated for either the amount or timing of possible cash flows, the likelihood of possible outcomes shall be considered in determining the best estimate of future cash flows;

(6) "Non-indemnity trigger" means a transaction term by which relief of the issuer's obligation to repay investors is triggered solely by some event or condition other than the individual protected cell company incurring a specified level of losses under its insurance or reinsurance contracts;

(7) "Protected cell" means an identified pool of assets and liabilities of a protected cell company segregated and insulated by means of this act from the remainder of the protected cell company's assets and liabilities;

(8) "Protected cell account" means a specifically identified bank or custodial account established by a protected cell company for the purpose of segregating the protected cell assets of one protected cell from the protected cell assets of other protected cells and from the assets of the protected cell company's general account;

(9) "Protected cell assets" means all assets, contract rights, and general intangibles identified with and attributable to a specific protected cell of a protected cell company;

(10) "Protected cell company" means a domestic insurer that has one

(1) or more protected cells;

(11) "Protected cell company insurance securitization" means:

(A) The issuance of debt instruments by a protected cell company from which the proceeds support the exposures attributed to the protected cell; and

(B) The repayment of principal or interest, or both, to investors under the transaction terms, is contingent upon the occurrence or nonoccurrence of an event which exposes the protected cell company to loss under insurance or reinsurance contracts it has issued; and

(12) "Protected cell liabilities" means all liabilities and other obligations identified with and attributable to a specific protected cell of a protected cell company.

SECTION 4. Establishment of protected cells.

(a)(1) A protected cell company may establish one (1) or more protected cells by submitting a plan of operation, or amendments to a plan, with respect to each protected cell in connection with an insurance securitization to the commissioner for prior written approval.

(2) The plan shall include, but not be limited to:

(A) The specific business objectives of the protected cell; and

(B) The investment guidelines of the protected cell.

(3) Upon receiving written approval the protected cell company may, in accordance with the approved plan of operation, attribute to the protected cell insurance obligations with respect to its insurance business and obligations relating to the insurance securitization and assets to fund the obligations.

(4) A protected cell shall have its own distinct name or designation which shall include the words "protected cell."

(5) The protected cell company shall transfer all assets attributable to a protected cell to one (1) or more separately established and identified protected cell accounts bearing the name or designation of that protected cell.

(6) Protected cell assets shall be held in the protected cell accounts for the purpose of satisfying the obligations of that protected cell.

(b)(1) All attributions of assets and liabilities between a protected cell and the general account shall be in accordance with the plan of operation approved by the commissioner.

(2) No other attribution of assets or liabilities may be made by a protected cell company between the protected cell company's general account and its protected cells.

(3) Any attribution of assets and liabilities between the general account and a protected cell, or from investors, in the form of principal on a debt instrument issued by a protected cell company in connection with a protected cell company securitization, shall be in cash or in readily marketable securities with established market values.

(c)(1) The creation of a protected cell does not create, in respect to that protected cell, a legal person separate from the protected cell company.

(2)(A) Amounts attributed to a protected cell under this act, including assets transferred to a protected cell account, are owned by the protected cell company.

(B) The protected cell company may not be, nor hold itself out to be, a trustee with respect to those protected cell assets of that protected cell account.

(3) The protected cell company may, however, allow for a security interest to attach to protected cell assets or a protected cell account when in favor of a creditor of the protected cell if allowed by applicable law.

(d)(1) This act does not prohibit the protected cell company from contracting with or arranging for an investment advisor, commodity trading advisor, or other third party to manage the protected cell assets of a protected cell.

(2) All remuneration, expenses and other compensation of the third party advisor or manager are payable from the protected cell assets of that protected cell, and not from the protected cell assets of other protected cells or the assets of the protected cell company's general account.

(e)(1) A protected cell company shall establish administrative and accounting procedures necessary to properly identify the one (1) or more protected cells of the protected cell company, and the protected cell assets and liabilities attributable to the protected cells. It shall be the duty of the directors of a protected cell company to:

(A) Keep protected cell assets and liabilities separate and separately identifiable from the assets and liabilities of the protected cell company's general account; and

(B) Keep protected cell assets and liabilities attributable to one protected cell separate and separately identifiable from protected cell assets and liabilities attributable to other protected cells.

(2)(A) If this subsection (e) is violated, the remedy of tracing shall be applicable to protected cell assets when commingled with protected cell assets of other protected cells or the assets of the protected cell company's general account.

(B) The remedy of tracing shall not be an exclusive remedy.

(f) When establishing a protected cell, the protected cell company shall attribute to the protected cell assets with a value at least equal to the reserves and other insurance liabilities attributed to that protected cell.

SECTION 5. Use and operation of protected cells.

(a)(1) The protected cell assets of a protected cell may not be charged with liabilities arising out of any other business the protected cell company may conduct.

(2) All contracts or other documentation reflecting protected cell liabilities shall clearly indicate that only the protected cell assets are available for the satisfaction of those protected cell liabilities.

(b)(1) The income, gains, and losses, realized or unrealized, from protected cell assets and liabilities shall be credited to or charged against the protected cell without regard to other income, gains, or losses of the protected cell company, including income, gains, or losses of other protected cells.

(2)(A) Amounts attributed to any protected cell and accumulations on the attributed amounts may be invested and reinvested

without regard to any requirements or limitations of Arkansas Code Title 23, Chapter 63, Subchapter 8.

(B) The investments in a protected cell or cells shall not be taken into account in applying the investment limitations applicable to the investments of the protected cell company.

(c) Assets attributed to a protected cell shall be valued at their fair value on the date of valuation.

(d)(1) A protected cell company shall, in respect to its protected cells, engage in fully funded indemnity triggered insurance securitization to support in full the protected cell exposures attributable to that protected cell.

(2) A protected cell company insurance securitization that is non-indemnity triggered shall qualify as an insurance securitization after the commissioner adopts regulations addressing the methods of funding of the portion of the risk that is not indemnity based, accounting, disclosure, risk based capital treatment, and assessing risks associated with such securitizations.

(3) A protected cell company insurance securitization that is not fully funded, whether indemnity triggered or non-indemnity triggered, is prohibited.

(4)(A) Protected cell assets may be used to pay interest or other consideration on any outstanding debt or other obligation attributable to that protected cell.

(B) Nothing in this subsection (d) shall prevent a protected cell company from entering into a swap agreement or other transaction for the account of the protected cell that has the effect of guaranteeing interest or other consideration.

(e)(1) In all protected cell company insurance securitizations, the contracts or other documentation effecting the transaction shall contain provisions identifying the protected cell to which the transaction will be attributed.

(2) The contracts or other documentation shall clearly disclose that the assets of that protected cell, and only those assets, are available to pay the obligations of that protected cell.

(3) Failure to include the language required by this subsection (e) in the contracts or other documentation shall not be used as the sole basis by creditors, reinsurers or other claimants to circumvent the provisions of this act.

(f)(1) A protected cell company shall only be authorized to attribute to a protected cell account the insurance obligations relating to the protected cell company's general account.

(2) A protected cell shall not be authorized to issue insurance or reinsurance contracts directly to policyholders or reinsureds or have any obligation to the policyholders or reinsureds of the protected cell company's general account.

(g) At the cessation of business of a protected cell, the protected cell company shall voluntarily close out the protected cell account.

SECTION 6. Reach of creditors and other claimants.

(a)(1)(A) Protected cell assets shall only be available to the creditors of the protected cell company that are creditors to that protected cell.

(B) Those creditors shall be entitled to have recourse to the protected cell assets attributable to that protected cell, and shall be absolutely protected from the creditors of the protected cell company that are not creditors in respect to that protected cell.

(C) Creditors of a protected cell shall not be entitled to have recourse against the protected cell assets of other protected cells or the assets of the protected cell company's general account.

(2) Protected cell assets shall only be available to creditors of a protected cell company after all protected cell liabilities have been extinguished or as provided for in the plan of operation relating to that protected cell.

(b) When an obligation of a protected cell company to a person arises from a transaction, or is otherwise imposed, in respect to a protected cell:

(1) That obligation of the protected cell company shall extend only to the protected cell assets attributable to that protected cell, and the person shall, with respect to that obligation, be entitled to have recourse only to the protected cell assets attributable to that protected cell; and

(2) That obligation of the protected cell company shall not extend to the protected cell assets of any other protected cell or the assets of the protected cell company's general account, and that person shall not, with respect to that obligation, be entitled to have recourse to the protected cell assets of any other protected cell or the assets of the protected cell company's general account.

(c) When an obligation of a protected cell company relates solely to the general account, the obligation of the protected cell company shall extend only to, and that creditor shall, with respect to that obligation, be entitled to have recourse only to the assets of the protected cell company's general account.

(d)(1) The activities, assets, and obligations relating to a protected cell are not subject to the laws of this state governing life and health and property and casualty guaranty or insolvency funds.

(2) A protected cell or a protected cell company shall not be assessed by or otherwise be required to contribute to any guaranty fund or guaranty association in this state with respect to the activities, assets, or obligations of a protected cell.

(3) This subsection (d) shall not affect the activities or obligations of an insurer's general account.

(e) The establishment of one (1) or more protected cells alone shall not be deemed to be a fraudulent conveyance, an intent by the protected cell company to defraud creditors, or the carrying out of business by the protected cell company for any other fraudulent purpose.

SECTION 7. Conservation, rehabilitation or liquidation of protected cell companies.

(a) Notwithstanding any provision of the Arkansas Insurance Code, or any regulation promulgated under the Arkansas Insurance Code, or any other applicable law or regulation, upon any order of conservation, rehabilitation, or liquidation of a protected cell company, the receiver shall be bound to deal with the protected cell company's assets and liabilities, including protected cell assets and protected cell liabilities, in conformance with this act.

(b) With respect to amounts recoverable under a protected cell company insurance securitization, the amount recoverable by the receiver shall not be reduced or diminished as a result of the entry of an order of conservation, rehabilitation or liquidation with respect to the protected cell company, notwithstanding any provision in the contracts or other documentation governing the protected cell company insurance securitization.

SECTION 8. No transaction of an insurance business.

(a) A protected cell company insurance securitization shall not be deemed to be an insurance or reinsurance contract.

(b) An investor in a protected cell company insurance securitization shall not, by sole means of this investment, be deemed to be transacting insurance business in this state.

(c) The underwriters or selling agents, and their partners, directors, officers, members, managers, employees, agents, representatives, and advisors, involved in a protected cell company insurance securitization, shall not be deemed to be conducting an insurance or reinsurance agency, brokerage, intermediary, advisory or consulting business by virtue of their activities in connection with the protected cell company insurance securitization.

SECTION 9. Authority to adopt regulations.

The commissioner may promulgate regulations necessary to carry out the purpose and intent of this act.

SECTION 10. EMERGENCY CLAUSE. It is found and determined by the General Assembly of the State of Arkansas that the creation and operation of protected cells are essential to the regulation of sponsored captive insurers and producer reinsurance captive insurers since these insurers are not subject to the guaranty fund. Therefore, an emergency is declared to exist and this act being immediately necessary for the preservation of the public peace, health and safety shall become effective on the date of its approval by the Governor. If the bill is neither approved nor vetoed by the Governor, it shall become effective on the expiration of the period of time during which the Governor may veto the bill. If the bill is vetoed by the Governor and the veto is overridden, it shall become effective on the date the last house overrides the veto."

The Amendment was read _____

By: Representative Hunt
PB/CDS - 031320010921
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Chief Clerk