

BILL ANALYSIS

Senate Research Center

S.B. 1447
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Economic Development
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DIGEST

Currently, the Insurance Code does not provide a process for domestic mutual insurance companies to convert to stock insurance companies. Conversion provides an insurer with greater access to capital markets and the ability to better compete in the marketplace. Other states authorize these conversions and some Texas domestic insurance companies may redomesticate to one of these states to take advantage of those laws. This bill would allow for the conversion of mutual insurance companies to stock insurance companies and include safeguards for policyholders of the mutual insurance company.

PURPOSE

As proposed, S.B. 1447 sets forth the regulations and guidelines for the conversion of a mutual insurance company to a stock insurance company and provides safeguards for policyholders of the mutual insurance company.

RULEMAKING AUTHORITY

Rulemaking authority is granted to the commissioner of insurance in SECTION 1 (Section 15(c), Article 15.22, Insurance Code) of this bill.

SECTION BY SECTION ANALYSIS

SECTION 1. Amends Chapter 15, Insurance Code, by adding Article 15.22, as follows:

Art. 15.22. CONVERSION TO STOCK INSURANCE COMPANY

Sec. 1. DEFINITIONS. Defines "conversion plan," "converted stock company," "eligible member," "mutual insurance company," "participating policy," and "stock company."

Sec. 2. ADOPTION OF CONVERSION PLAN. Requires a mutual insurance company that seeks to convert to a stock company to adopt by an affirmative vote a conversion plan consistent with the requirements of this article. Prohibits a mutual insurance company from engaging in the business of insurance as a stock company until it complies with the requirements of this article. Requires the mutual insurance company to comply with Section 3 before a conversion plan vote.

Sec. 3. PLAN INFORMATION FILED WITH COMMISSIONER; COMMISSIONER POWERS AND DUTIES. Requires a company, no later than the 90th day after the date on which a mutual insurance company's board of directors adopts a conversion plan, to file with the commissioner of insurance (commissioner) certain items. Sets forth the guidelines relating to the approval or disapproval of a conversion plan by the commissioner. Requires the commissioner to approve a conversion plan if the commissioner finds certain facts in regard to the conversion plan. Authorizes the commissioner to retain, at the mutual insurance company's expense, a qualified expert to assist the commissioner in reviewing the conversion plan and the independent evaluation of the pro forma market value required under Section 10(b). Authorizes the commissioner to hold a hearing on the terms of the conversion plan after notice is given to certain entities and persons.

Sec. 4. AMENDMENTS; WITHDRAWAL OF PLAN. Authorizes the mutual insurance company, by an affirmative vote of two-thirds of the members of its board of directors, to amend or withdraw the conversion plan.

Sec. 5. NOTICE TO ELIGIBLE MEMBERS; COMMENTS. Sets forth the guidelines relating to notice of eligible members of the conversion plan by the mutual insurance company and comments to such a plan by those members. Requires the company to send to eligible members notice of the members meeting to vote on the conversion plan. Provides that only a combined meeting notice is required if the meeting to vote on the conversion plan is held during the mutual insurance company's annual meeting of policyholders.

Sec. 6. ELECTION; ADOPTION OF PLAN. Sets forth the guidelines relating to adoption of the conversion plan and amended articles of incorporation and of bylaws by eligible members.

Sec. 7. FILING BY CONVERTED STOCK COMPANY. Requires the converted stock company to file with the commissioner certain items by the 30th date after the date on which the eligible members adopt the conversion plan.

Sec. 8. REQUIRED PROVISIONS IN GENERAL. Requires each conversion plan to include the provisions required by this article. Sets forth certain rights of a mutual insurance company that are extinguished on the effective date of the conversion. Provides that the holder of a participating policy in effect on the date of the conversion continues to have a right to receive dividends as provided by the participating policy. Authorizes a certain converted stock company to issue the insured a nonparticipating policy as a substitute for the participating policy.

Sec. 9. SUBSCRIPTION RIGHTS. Requires each conversion plan to specify the subscription rights of eligible members. Requires the plan to include certain provisions. Authorizes the conversion plan to provide that each eligible member is to receive nontransferable subscription rights to purchase a portion of certain capital stock as an alternative to subscription rights in the converted stock company. Requires the conversion plan to provide that the subscription rights are allocated in whole shares among the eligible members using a fair and equitable formula. Authorizes the formula to consider certain factors. Requires the conversion plan to provide a fair and equitable means for allocating shares of capital stock in the event of an oversubscription to shares by eligible members exercising subscription rights under this section.

Sec. 10. SALE OF CAPITAL STOCK. (a) Requires the conversion plan to provide that any shares of capital stock not subscribed to by eligible members to be sold in a public offering. Authorizes the conversion plan, under certain conditions, to provide for the sale of those shares through a private placement or an alternative method approved by the commissioner.

(b) Requires the conversion plan to set the total price of the capital stock in an amount equal to the estimated pro forma market value of the converted stock company based on an independent evaluation by a qualified expert. Authorizes the pro forma market value to be the value estimated to be necessary to attract full subscription for the shares and to be stated as a range of values.

(c) Requires the conversion plan to set the purchase price per share of capital stock at any reasonable amount. Prohibits the minimum subscription amount from exceeding \$500. Authorizes the conversion plan to provide that the minimum number of shares a person may purchase under the conversion plan is 25 shares.

(d) Authorizes the conversion plan to provide that a person or group of persons acting in concert may not acquire more than five percent of the capital stock of the converted stock company or the stock of another corporation that is participating in the conversion plan. Provides that this limitation does not apply to an entity that purchases 100 percent of the capital stock of the converted company as part of the conversion plan approved by

the commissioner.

(e) Requires the conversion plan to provide that a director or officer of the mutual insurance company, or a person acting in concert with a director or officer, may not acquire without the permission of the commissioner any capital stock of the converted stock company or the stock of another corporation that is participating in the conversion plan before the third anniversary of the effective date of the conversion, except through a broker-dealer. Provides that this subsection does not prohibit a director or officer from certain activities.

Sec. 11. **LIMITATION ON RESALE.** Requires the conversion plan to provide that a director or officer may not sell stock purchased under Section 10 before the first anniversary of the effective date of the conversion.

Sec. 12. **HOLDER OF SURPLUS NOTE.** Requires the conversion plan to provide that the rights of a holder of a surplus note to participate in the conversion are governed by the terms of the surplus note.

Sec. 13. **REPURCHASE OF CAPITAL STOCK.** Requires the conversion plan to provide that a converted stock company, or any corporation participating in the conversion plan, may not repurchase any of its capital stock from any person before the third anniversary of the effective date of the conversion. Sets forth the application of this provision.

Sec. 14. **OPTIONAL PROVISIONS.** Authorizes the conversion plan to provide that the directors and officers of the mutual insurance company receive certain nontransferable subscription rights to purchase capital stock of the converted stock company or the stock of another corporation that is participating in the conversion plan. Sets forth purchasing guidelines relating to the aggregate number of shares that may be purchased by directors and officers of the mutual insurance company under Subsection (a). Authorizes the conversion plan to allocate to a tax-qualified employee benefit plan nontransferable subscription rights to purchase no more than 10 percent of the capital stock of the converted stock company or the stock of another corporation that is participating in the conversion plan. Provides that a tax-qualified employee benefit plan is entitled to exercise certain subscription rights. Authorizes the conversion plan to provide for the creation of a certain liquidation account for the benefit of members in the event of voluntary liquidation after conversion.

Sec. 15. **ALTERNATIVE CONVERSION PLAN.** Authorizes the board of directors to adopt a conversion plan that does not rely wholly or partially on issuing nontransferable subscription rights to members to purchase stock of the converted stock company if the commissioner finds certain conditions in regard to the alternative conversion plan. Sets forth authorized terms and conditions of the alternative conversion plan. Prohibits the commissioner from approving an alternative conversion plan that provides for the formation of a mutual holding company before the commissioner adopts rules permitting partial conversion and formation of a mutual holding company. Authorizes the commissioner to retain, at the mutual insurance company's expense, a qualified expert to assist in reviewing whether the conversion plan may be approved by the commissioner.

Sec. 16. **EFFECTIVE DATE OF CONVERSION.** Sets forth the required conditions for a conversion plan to take effect. Provides that a conversion plan takes effect when the amended articles of incorporation are filed with the office of the secretary of state.

Sec. 17. **RIGHTS OF MEMBERS WHOSE POLICIES ARE ISSUED AFTER ADOPTION OF CONVERSION PLAN AND BEFORE EFFECTIVE DATE.** Requires the mutual insurance company to send to the member to whom a policy is issued a written notice regarding the conversion plan on issuance of a policy after a conversion plan has been adopted by the board of directors but before the effective date of the conversion plan. Entitles a certain notified member of an accident and health insurance company to rescind the member's policy and receive a full refund of any amount paid for the policy no later than the 10th day after the date on which the member receives the notice. Requires certain notified

members of a property or casualty insurance company to be advised of certain rights. Provides that a member of an accident and health insurance company or a property or casualty insurance company who has made or filed a claim under the insurance policy is not entitled to a right to receive a refund under this section. Provides that a person who has exercised the rights provided by Subsection (b) or (c) is not entitled to make or file a claim under the insurance policy.

Sec. 18. CORPORATE EXISTENCE. Provides that on the effective date of the conversion, the corporate existence of the mutual insurance company continues in the converted stock company; and all assets, rights, franchises, and interests of the mutual insurance company in and to property, real, personal, and mixed or cloned, and any accompanying things in action, are vested in the converted stock company and the converted stock company assumes all the obligations and liabilities of the mutual insurance company. Provides that the directors and officers of the mutual insurance company serving on the effective date of the conversion serve as directors and officers of the converted stock company until new directors and officers of the converted stock company are elected under the articles of incorporation and bylaws of the converted stock company.

Sec. 19. CONFLICT OF INTEREST. Prohibits certain persons of the mutual insurance company from receiving certain consideration. Provides that this subsection does not prohibit the payment of reasonable fees and compensation to an attorney, accountant, or actuary for professional services performed by that person, even if the attorney, accountant, or actuary is also a director or officer of the mutual insurance company. Prohibits a converted stock company, until the second anniversary of the effective date of the conversion, from implementing any non-tax-qualified stock benefit conversion plans, except under certain conditions. Requires all the costs and expenses connected with a conversion plan to be paid for or reimbursed by the mutual insurance company or the converted stock company. Authorizes the corporation or stock company, if the conversion plan provides for participation by another corporation or stock company in the conversion plan, to pay for or reimburse all or a portion of the costs and expenses connected with the conversion plan.

Sec. 20. EFFECT OF FAILURE TO GIVE NOTICE. Provides that the mutual insurance company's failure to send a member the required notice does not impair the validity of any action taken under this article if the mutual insurance company complies substantially and in good faith with the notice requirements of this article.

Sec. 21. LIMITATION ON ACTIONS. Requires an action challenging the validity of or arising out of facts taken or proposed to be taken regarding a conversion plan under this article to be commenced by the 30th day after the effective date of that conversion plan.

Sec. 22. INSOLVENT MUTUAL INSURANCE COMPANY. Authorizes the board of directors of a mutual insurance company that is insolvent or in hazardous financial condition to request, by a majority vote, the commissioner to waive the requirements imposing notice to and policyholder approval of the planned conversion. Requires the petition to specify certain items.

Sec. 23. LAWS APPLICABLE TO CONVERTED STOCK COMPANY. Prohibits a mutual insurance company from being permitted to convert under this article if any person or any affiliate acquires control of the converted stock company, unless that person or the affiliate complies with this article. Defines "control." Provides that a stock company converted under this article has all of the rights and privileges and is subject to all of the requirements and regulations imposed on stock companies formed under this code and any other laws of this state relating to the regulation and supervision of insurance companies.

Sec. 24. AMENDMENT OF POLICIES. Authorizes a mutual insurance company to simultaneously with or at any time after the adoption of a conversion plan amend any outstanding insurance policies to extinguish the right of the holder of the policy to share in the surplus of the mutual insurance company. Provides that such an amendment is void if the conversion plan does not take effect.

SECTION 2. Effective date: September 1, 1997.

SECTION 3. Emergency clause.