GENERAL ASSEMBLY OF NORTH CAROLINA
SESSION 2001

SENATE BILL 459
RATIFIED BILL

AN ACT TO AMEND NORTH CAROLINA'S INSURANCE LAWS CONCERNING INSURANCE COMPANY RESERVING METHODS, LICENSING PROVISIONS, REINSURANCE FOR DOMESTIC COMPANIES, DOMESTIC COMPANY FORMATION, SOLVENCY PROTECTION, LIFE INSURANCE COMPANY VARIABLE ACCOUNTS, CONSOLIDATIONS, INVESTMENTS, MUTUAL INSURANCE COMPANIES, REINSURANCE INTERMEDIARIES, MORTGAGE GUARANTY INSURANCE, RISK-BASED CAPITAL REQUIREMENTS, ASSET PROTECTION, FOREIGN INSURANCE COMPANIES, PROMOTING AND HOLDING COMPANIES, HOLDING COMPANY SYSTEMS, SURPLUS LINES INSURANCE, RISK RETENTION GROUPS, INSURANCE COMPANY RECEIVERSHIPS, MANAGING GENERAL AGENTS, SELF-INSURED WORKERS' COMPENSATION, AND CONTINUING CARE RETIREMENT COMMUNITIES; AND TO ALLOW NORTH CAROLINA DOMESTIC INSURANCE COMPANIES TO FORM PROTECTED CELLS TO ACCESS ALTERNATIVE SOURCES OF CAPITAL AND ACHIEVE THE BENEFITS OF SECURITIZATION.

The General Assembly of North Carolina enacts:

PART I. INSURANCE COMPANY RESERVING METHODS.

SECTION 1.1. Article 3 of Chapter 58 of the General Statutes is amended by adding the following new section to read:

"**§ 58-3-72. Premium deficiency reserves.**

(a) In determining the financial condition of any casualty, fidelity, and surety company and any fire and marine company referred to in G.S. 58-7-75, and in any financial statement or report of the company, there shall be included in the liabilities of the company premium deficiency reserves at least equal to the amounts required under this section. The date as of which the determination, statement, or report is made is known as the 'date of determination.'

(b) For all recorded unearned premium reserves, a premium deficiency reserve shall be calculated to include the amount by which the anticipated losses, loss adjustment expenses, commissions and other acquisition costs, and maintenance costs exceed the sum of those unearned premium reserves and any related expected future installment premiums as of the date of determination.

(c) Except as provided in subsection (f) of this section, commissions, other acquisition costs, and premium taxes do not have to be considered in the determination of the premium deficiency reserve, to the extent that they have previously been incurred.

(d) Except as provided in subsection (f) of this section, no reduction shall be taken for anticipated investment income in the determination of the premium deficiency reserve.

(e) For purposes of determining if a premium deficiency exists, insurance contracts shall be grouped in a manner consistent with the way in which such policies are marketed or serviced.

(f) If the Commissioner determines that the premium deficiency reserves of any company that have been calculated in accordance with this section are inadequate or

excessive, the Commissioner may prescribe any other basis that will produce adequate and reasonable reserves."

SECTION 1.2. G.S. 58-3-81 reads as rewritten:

"**§ 58-3-81. Loss and loss expense reserves of casualty insurance and surety companies.**

(a) In determining the financial condition of any casualty insurance or surety company and in any financial statement or report of any such company, there shall be included in the liabilities of ~~such~~ that company loss reserves and loss expense reserves at least equal to the amounts required under ~~the provisions of~~ this ~~section, and the~~ section. The amount of ~~such~~ those reserves shall be diminished by an allowance or credit for reinsurance recoverable from assuming ~~insurers~~ reinsurers in accordance with ~~G.S. 58-7-21.~~G.S. 58-7-21 or G.S. 58-7-26. The date as of which ~~such~~ the determination, statement, or report is made is ~~hereinafter referred to~~ known as the date of determination.

(b) For all outstanding losses and loss expenses, the reserves shall be valued as of the date of determination and shall include the following:

(1) ~~The aggregate estimated amounts due or to become due on account of all known losses and claims and loss expenses incurred but not paid, including the estimated liability on any notice received by the company of the occurrence of any event which may result in a loss; and~~ The aggregate estimated amounts due for losses and loss adjustment expenses on account of all known claims.

(2) ~~The aggregate amounts of liability for all losses and loss expenses incurred but on which no notice has been received, estimated in accordance with the company's prior experience, if any, otherwise in accordance with the experience of similar companies under similar contracts of insurance. The estimated liabilities for such losses under all its bonds, policies, or contracts of fidelity insurance, shall be not less than ten percent (10%) of the net premiums in force thereon, and the estimated liabilities for all such losses under all its surety contracts shall be not less than five percent (5%) of the net premium in force thereon.~~ The aggregate estimated amounts due for losses and loss adjustment expenses on account of all unknown, incurred but not reported claims.

(c) ~~Except as provided in subsection (e) of this section, the minimum reserves for outstanding losses and loss expenses under policies of personal injury liability insurance and under policies of employers' liability insurance, where the losses were incurred during the three years immediately preceding the date of determination, shall be calculated in accordance with any method adopted or approved by the NAIC and shall be not less than the aggregate of the estimated unpaid losses and loss expenses for claims incurred computed in accordance with subsection (b) of this section.~~ Except as provided in subsection (e) of this section, the minimum loss and loss expense reserves for workers' compensation insurance shall be determined as follows:

(1) In the case of indemnity benefits where tabular reserves are prescribed for the reporting of such benefits under the Workers' Compensation Statistical Plan (WCSP) of the National Council on Compensation Insurance, the minimum reserve shall be the result obtained by the application of the appropriate pension table in the WCSP, unless the reserve required by any method adopted or approved by the NAIC is greater, in which case that greater reserve shall be used.

(2) In all other cases, including other indemnity benefits, medical benefits, and loss adjustment expense, the reserve shall be determined by subsection (b) of this section, unless the reserve required by any method adopted or approved by the NAIC is greater, in which case that greater reserve shall be used.

~~(d) The minimum reserves for outstanding losses and loss expenses under policies of workers' compensation insurance, except as provided in subsection (e) of this section, shall be computed as follows:~~

~~(1) For all such compensation policies where losses were incurred more than three years prior to the date of determination, such reserves shall be the sum of the present values, at three and one-half percent (3 1/2%) interest per annum, of the determined and estimated unpaid losses computed on an individual case basis plus the estimated unpaid loss expenses computed in accordance with subsection (b) of this section.~~

~~(2) Where losses were incurred during the three years immediately preceding the date of determination, such reserves shall be the sum of the reserves for each year, which shall be calculated in accordance with any method adopted or approved by the NAIC and shall be not less than the sum of the present values, at three and one-half percent (3 1/2%) interest per annum, of the determined and estimated unpaid losses computed on an individual case basis plus the estimated unpaid loss expenses computed in accordance with subsection (b) of this section.~~

(e) Whenever in the judgment of the Commissioner the loss and loss expense reserves of any casualty or surety company doing business in this State calculated in accordance with the foregoing provisions are inadequate or excessive, he may prescribe any other basis that will produce adequate and reasonable reserves.

(f) Every casualty insurance and every surety company doing business in this State shall keep a complete and itemized record showing all losses and claims on which it has received notices, including all notices received by it of the occurrence of any event that may result in a loss."

PART II. INSURANCE COMPANY LICENSING PROVISIONS.

SECTION 2.1. G.S. 58-3-90 is repealed.

SECTION 2.2. G.S. 58-3-100 reads as rewritten:

"**§ 58-3-100. ~~Revocation, suspension and refusal to renew license.~~ Insurance company licensing provisions.**

(a) ~~The Commissioner may revoke, suspend, or refuse to renew the license of any insurer if:~~ The Commissioner may, after notice and opportunity for a hearing, revoke, suspend, restrict, or refuse to renew the license of any insurer if:

(1) The insurer fails or refuses to comply with any law, order or rule applicable to the insurer.

(2) The insurer's financial condition is unsound, or its assets above its liabilities, exclusive of capital, are less than the amount of its capital or required minimum surplus.

(3) The insurer has published or made to the Department or to the public any false statement or report.

(4) The insurer or any of the insurer's officers, directors, employees, or other representatives ~~refuses~~ refuse to submit to any examination authorized by ~~law.~~law or refuse to perform any legal obligation in relation to an examination.

(5) The insurer is found to make a practice of unduly engaging in litigation or of delaying the investigation of claims or the adjustment or payment of valid claims.

(b) Any suspension, revocation or refusal to renew an insurer's license under this section may also be made applicable to the license or registration of any ~~natural person~~ individual regulated under this Chapter who is a party to any of the causes for licensing sanctions listed in subsection (a) of this section.

(c) The Commissioner may impose a civil penalty under G.S. 58-2-70 if an HMO, service corporation, MEWA, or insurer fails to acknowledge a claim within 30 days after receiving written or electronic notice of the claim, but only if the notice contains sufficient information for the insurer to identify the specific coverage involved. Acknowledgement of the claim shall be ~~made to the claimant or his legal representative advising that the claim is being investigated; or shall be a payment of the claim; or shall be a bona fide written offer of settlement; or shall be a written denial of the claim.~~ one of the following:

(1) A statement made to the claimant or to the claimant's legal representative advising that the claim is being investigated.

(2) Payment of the claim.

(3) A bona fide written offer of settlement.

(4) A written denial of the claim.

A claimant includes an insured, a health care provider, or a health care facility that is responsible for directly making the claim with an ~~insurer.~~ insurer, HMO, service corporation, or MEWA. This subsection does not apply to HMOs, service corporations, MEWAs or insurers subject to G.S. 58-3-225.

(d) If a foreign insurance company's license is suspended or revoked, the Commissioner shall cause written notification of the suspension or revocation to be given to all of the company's agents in this State. Until the Commissioner restores the company's license, the company shall not write any new business in this State.

(e) The Commissioner may, after considering the standards under G.S. 58-30-60(b), restrict an insurer's license by prohibiting or limiting the kind or amount of insurance written by that insurer. For a foreign insurer, this restriction relates to the insurer's business conducted in this State. The Commissioner shall remove any restriction under this subsection once the Commissioner determines that the operations of the insurer are no longer hazardous to the public or the insurer's policyholders or creditors. As used in this subsection, 'insurer' includes an HMO, service corporation, and MEWA."

SECTION 2.3. This Part becomes effective July 1, 2001.

PART III. REINSURANCE FOR DOMESTIC COMPANIES.

SECTION 3.1. G.S. 58-7-21 reads as rewritten:

"**§ 58-7-21. Credit allowed a domestic ceding insurer.**

(a) ~~As used in this section and in G.S. 58-7-26, 58-7-30, and 58-7-31:~~

~~(1) "Reinsurance" means a transfer of insurance risk from a ceding insurer to an assuming insurer.~~

~~(2) "Insurance risk" means an uncertainty regarding the ultimate amount of any claim payment (underwriting risk) or an uncertainty regarding the timing of the payments (timing risk), or both.~~

The purpose of this section and G.S. 58-7-26 is to protect the interest of insureds, claimants, ceding insurers, assuming insurers, and the public generally. The General Assembly declares its intent is to ensure adequate regulation of insurers and reinsurers and adequate protection for those to whom they owe obligations. In furtherance of that interest, the General Assembly provides a mandate that upon the insolvency of an alien insurer or reinsurer that provides security to fund its United States obligations in accordance with this section and G.S. 58-7-26, the assets representing the security shall be maintained in the United States and claims shall be filed with and valued by the state insurance commissioner with regulatory oversight, and the assets shall be distributed, in accordance with the insurance laws of the state in which the trust is domiciled that are applicable to the liquidation of domestic United States insurance companies. The General Assembly declares that the matters contained in this section and G.S. 58-7-26 are fundamental to the business of insurance in accordance with 15 U.S.C. §§ 1011-1012.

(b) Credit for reinsurance shall be allowed a domestic ceding insurer as either an asset or a ~~deduction~~ reduction from liability on account of reinsurance ceded only when the reinsurer meets the requirements of subdivisions (1), (2), (3), (4), or (5) of this subsection. Credit shall be allowed under subdivision (1), (2), or (3) of this subsection only with regard to cessions of those kinds or classes of business in which the assuming insurer is licensed or otherwise permitted to write or assume in its state of domicile or, in the case of a United States branch of an alien assuming insurer, in the state through which it is entered and licensed to transact insurance or reinsurance. ~~If meeting the requirements of subdivisions (3) or (4) of this subsection, the reinsurer must also meet the requirements of subdivision (6) of this subsection.~~Credit shall be allowed under subdivision (3) or (4) of this subsection only if the applicable requirements of subdivision (6) of this section have been satisfied.

(1) Credit shall be allowed when the reinsurance is ceded to an assuming insurer that is licensed to transact insurance or reinsurance in this State.

(2) Credit shall be allowed when the reinsurance is ceded to an assuming insurer that is accredited as a reinsurer in this State. An accredited reinsurer is one that:

a. Files with the Commissioner evidence of its submission to this State's jurisdiction;

b. Submits to this State's authority to examine its books and records;

c. Is licensed to transact insurance or reinsurance in at least one state, or in the case of a United States branch of an alien assuming insurer is entered through and licensed to transact insurance or reinsurance in at least one state;

d. Files annually with the Commissioner a copy of its annual statement filed with the insurance regulator of its state of domicile, a copy of its most recent audited financial statement, and a fee of five hundred dollars ($500.00); and either

1. Maintains a policyholders' surplus in an amount that is not less than twenty million dollars ($20,000,000) and whose accreditation has not been denied by the Commissioner within 90 days after its submission; or

2. Maintains a policyholders' surplus in an amount less than twenty million dollars ($20,000,000) and whose accreditation has been approved by the Commissioner.

~~No credit~~ Credit shall not be allowed a domestic ceding insurer if the assuming insurer's accreditation has been revoked by the Commissioner after notice and opportunity for a hearing.

(3) Credit shall be allowed when the reinsurance is ceded to an assuming insurer that is domiciled ~~and licensed~~ in, or in the case of a United States branch of an alien assuming insurer is entered through, a state that uses standards regarding credit for reinsurance substantially similar to those applicable under this section and the assuming insurer or United States branch of an alien assuming insurer:

a. Maintains a policyholders' surplus in an amount not less than twenty million dollars ($20,000,000); and

b. Submits to the authority of this State to examine its books and records.

~~However, the~~ The requirement in sub-subdivision (3)a. of this subsection does not apply to reinsurance ceded and assumed under pooling arrangements among insurers in the same holding company system.

(4) a. Credit shall be allowed when the reinsurance is ceded to an assuming insurer that maintains a trust fund in a qualified United States financial institution, as defined in G.S. 58-7-26(b), for the payment of the valid claims of its United States ~~policyholders and~~ ceding insurers, their assigns and successors in interest. The assuming insurer shall report annually to the Commissioner information substantially the same as that required to be reported on the NAIC Annual Statement form by licensed insurers to enable the Commissioner to determine the sufficiency of the trust fund. The assuming insurer shall submit to examination of its books and records by the Commissioner and bear the expense of examination. ~~In the case of a single assuming insurer, the trust shall consist of a trusteed account representing the assuming insurer's liabilities attributable to business written in the United States and, in addition, the assuming insurer shall maintain a trusteed surplus of not less than twenty million dollars ($20,000,000). In the case of a group of insurers, which includes individual unincorporated underwriters, the trust shall consist of a trusteed account representing the group's liabilities attributable to business written in the United States and, in addition, the group shall maintain a trusteed surplus of which one hundred million dollars ($100,000,000) shall be held jointly for the benefit of United States ceding insurers of any member of the group; and the group shall make available to the Commissioner an annual certification of the solvency of each underwriter by the group's domiciliary regulator and its independent certified public accountants.~~

~~b.~~ ~~In the case of a group of incorporated insurers under common administration which (i) complies with the filing requirements contained in the previous paragraph, (ii) has continuously transacted an insurance business outside the United States for at least three years immediately before making application for accreditation, (iii) submits to this State's authority to examine its books and records, and (iv) has aggregate policyholders' surplus of ten billion dollars ($10,000,000,000); the trust shall be in an amount equal to the group's several liabilities attributable to business ceded by United States ceding insurers to any member of the group under reinsurance contracts issued in the name of the group. In addition, the group shall maintain a joint trusteed surplus of which one hundred million dollars ($100,000,000) shall be held jointly for the benefit of United States ceding insurers of any member of the group as additional security for any such liabilities, and each member of the group shall make available to the Commissioner an annual certification of the member's solvency by the member's domiciliary regulator and its independent public accountant.~~

b1. Credit for reinsurance shall not be granted under this subdivision unless the form of the trust and any amendments to the trust have been approved by:

1. The insurance regulator of the state where the trust is domiciled; or
2. The insurance regulator of another state who, pursuant to the terms of the trust instrument, has accepted principal regulatory oversight of the trust.

b2. The form of the trust and any trust amendments also shall be filed with the insurance regulator of every state in which the ceding insurer beneficiaries of the trust are domiciled. The trust instrument shall provide that contested claims shall be valid and enforceable upon the final order of any court of competent jurisdiction in the United States. The trust shall vest legal title to its assets in its trustees for the benefit of the assuming insurer's United States ceding insurers, their assigns, and successors in interest. The trust and the assuming insurer shall be subject to examination as determined by the Commissioner.

b3. The trust shall remain in effect for as long as the assuming insurer has outstanding obligations due under the reinsurance agreements subject to the trust. No later than February 28 of each year, the trustees of the trust shall report to the Commissioner in writing the balance of the trust, shall list the trust's investments at the end of the preceding year, and shall certify the date of termination of the trust, if so planned, or shall certify that the trust will not expire before the following December 31.

c. ~~The trust shall be established in a form approved by the Commissioner. The trust instrument shall provide that contested claims shall be valid and enforceable upon the final order of any court of competent jurisdiction in the United States. The trust shall vest legal title to its assets in the trustees of the trust for its United States policyholders and ceding insurers, their assigns and successors in interest. The trust and the assuming insurer shall be subject to examination as determined by the Commissioner. The trust shall remain in effect for as long as the assuming insurer has outstanding obligations due under the reinsurance agreements subject to the trust.~~

The following requirements apply to the following categories of assuming insurer:

1. The trust fund for a single assuming insurer shall consist of funds in trust in an amount not less than the assuming insurer's liabilities attributable to reinsurance ceded by United States ceding insurers, and, in addition, the assuming insurer shall maintain a surplus in trust of not less than twenty million dollars ($20,000,000).

2. In the case of a group including incorporated and individual unincorporated underwriters:

   I. For reinsurance ceded under reinsurance agreements with an inception, amendment, or renewal date on or after August 1, 1995, the trust shall consist of an account in trust in an amount not less than the group's several liabilities attributable to business ceded by United States domiciled ceding insurers to any member of the group.

   II. For reinsurance ceded under reinsurance agreements with an inception date on or before July 31, 1995, and not amended or renewed after that date, notwithstanding the other provisions of this section and G.S. 58-7-26, the trust shall consist of an account in trust in an amount not less than the group's several insurance and

reinsurance liabilities attributable to business written in the United States.

In addition to these trusts, the group shall maintain in trust a surplus of which one hundred million dollars ($100,000,000) shall be held jointly for the benefit of the United States domiciled ceding insurers of any member of the group for all years of account. Each incorporated member of the group shall not be engaged in any business other than underwriting as a member of the group and shall be subject to the same level of regulation and solvency control by the group's domiciliary insurance regulator as are the unincorporated members. Within 90 days after its financial statements are due to be filed with the group's domiciliary insurance regulator, the group shall provide to the Commissioner an annual certification by the group's domiciliary insurance regulator of the solvency of each underwriter member or, if a certification is unavailable, financial statements prepared by independent public accountants of each underwriter member of the group.

~~d. No later than February 28 of each year the trustees of the trust shall report to the Commissioner in writing, setting forth the balance of the trust and listing the trust's investments at the end of the preceding year, and shall certify the date of termination of the trust, if so planned, or certify that the trust shall not expire before the next following December 31.~~

(5) Credit shall be allowed when the reinsurance is ceded to an assuming insurer not meeting the requirements of subdivisions (1), (2), (3), or (4) of this subsection, but only with respect to the insurance of risks located in jurisdictions where the reinsurance is required by applicable law or regulation of that jurisdiction.

(6) If the assuming insurer is not licensed or accredited to transact insurance or reinsurance in this State, the credit permitted by subdivisions (3) and (4) of this subsection shall not be allowed unless the assuming insurer agrees in the reinsurance agreements:

a. That if the assuming insurer fails to perform its obligations under the terms of the reinsurance agreement, the assuming insurer, at the ceding insurer's request, shall submit to the jurisdiction of any court of competent jurisdiction in any state of the United States, shall comply with all requirements necessary to give the court jurisdiction, and shall abide by the final decision of the court or of any appellate court if there is an appeal; and

b. To designate the Commissioner or a designated attorney as its true and lawful attorney upon whom may be served any lawful process in any action, suit, or proceeding begun by or on behalf of the ceding company.

This subdivision does not affect the obligation of the parties to a reinsurance agreement to arbitrate their disputes, if ~~such an~~ the obligation is created in the agreement.

(7) If the assuming insurer does not meet the requirements of subdivision (1), (2), or (3) of this subsection, the credit permitted by subdivision (4) of this subsection shall not be allowed unless the assuming insurer agrees in the trust agreements to the following conditions:

a. Notwithstanding any other provisions in the trust instrument, if the trust fund is inadequate because it contains an amount less than the amount required by sub-subdivision (4)c. of this subsection, or if the grantor of the trust has been declared insolvent or placed into receivership, rehabilitation, liquidation, or similar proceedings under the laws of its state or country of domicile, the trustee shall comply with an order of the public official with regulatory oversight over the trust or with an order of a court of competent jurisdiction directing the trustee to transfer to the public official with regulatory oversight all of the assets of the trust fund.

b. The assets shall be distributed by, and claims shall be filed with and valued by, the public official with regulatory oversight in accordance with the laws of the state in which the trust is domiciled that are applicable to the liquidation of domestic insurance companies.

c. If the public official with regulatory oversight determines that the assets of the trust fund or any part thereof are not necessary to satisfy the claims of the United States ceding insurers of the grantor of the trust, those assets shall be returned by the public official with regulatory oversight to the trustee for distribution in accordance with the trust agreement.

d. The grantor shall waive any right otherwise available to it under United States law that is inconsistent with this provision.

(c) This section applies to all reinsurance cessions made on or after January 1, 1992, under reinsurance agreements that have an inception, anniversary, or renewal date on or after January 1, 1992."

SECTION 3.2. G.S. 58-7-26 reads as rewritten:

"**§ 58-7-26. ~~Reduction~~ Asset or reduction from liability for reinsurance ceded by a domestic insurer to an assuming ~~insurer.~~insurer not meeting the requirements of G.S. 58-7-21.**

(a) ~~A~~ An asset or a reduction from liability for reinsurance ceded by a domestic insurer to an assuming insurer not meeting the requirements of G.S. 58-7-21 shall be allowed in an amount not exceeding the liabilities carried by the ceding ~~insurer; and such~~ insurer. The reduction shall be in the amount of funds held by or on behalf of the ceding insurer, including funds held in trust for the ceding insurer, under a reinsurance contract with the assuming insurer as security for the payment of obligations thereunder, if the security is held in the United States subject to withdrawal solely by, and under the exclusive control of, the ceding insurer; or, in the case of a trust, held in a qualified United States financial institution as defined in subsection (c) of this section. This security may be in the form of:

(1) Cash;

(2) Securities that are listed by the Securities Valuation Office of the NAIC and qualifying as admitted assets;

(3) Clean, irrevocable, unconditional letters of credit, issued or confirmed by a qualified United States financial institution, as defined in subsection (b) of this section, no later than December 31 of the year for which the filing is being made, and in the possession ~~of~~ of, or in trust for, the ceding company on or before the filing date of its annual statement. Letters of credit meeting applicable standards of issuer acceptability as of the dates of their issuance (or confirmation) shall, notwithstanding the issuing (or confirming) institution's subsequent failure to meet applicable standards of issuer acceptability, continue to be acceptable as security until their expiration, extension, renewal, modification or amendment, whichever occurs first; or

(4) Any other form of security acceptable to the Commissioner.

(b) For purposes of subdivision (a)(3) of this section, a "qualified United States financial institution" means an institution that:

(1) Is organized, or in the case of a United States office of a foreign banking organization licensed, under the laws of the United States or any of its states;

(2) Is regulated, supervised, and examined by United States federal or state authorities having regulatory authority over banks and trust companies; and

(3) Has been determined by either the Commissioner or the Securities Valuation Office of the NAIC to meet such standards of financial condition and standing as are considered necessary and appropriate to regulate the quality of financial institutions whose letters of credit will be acceptable to the Commissioner.

(c) A "qualified United States financial institution" means, for purposes of those provisions of this section specifying those institutions that are eligible to act as a fiduciary of a trust, an institution that:

(1) Is organized, or in the case of a United States branch or agency office of a foreign banking organization licensed, under the laws of the United States or any of its states and has been granted authority to operate with fiduciary powers; and

(2) Is regulated, supervised, and examined by federal or state authorities having regulatory authority over banks and trust companies.

(d) This section applies to all reinsurance cessions made on or after January 1, 1992, under reinsurance agreements that have an inception, anniversary, or renewal date on or after January 1, 1992."

SECTION 3.3. G.S. 58-7-30 reads as rewritten:

"**§ 58-7-30. ~~Insolvency of~~ Insolvent ceding ~~insurer; exceptions; written reinsurance agreements.~~insurer.**

(a) Notwithstanding any other provision of this Article, no credit shall be allowed, as an admitted asset or as a ~~deduction~~ reduction from liability, to any ceding insurer for reinsurance, unless the reinsurance is payable by the assuming insurer, on the basis of reported claims allowed by the court overseeing the liquidation against the ceding insurer under the contract or contracts reinsured without diminution because of the insolvency of the ceding insurer, directly to the ceding insurer or to its domiciliary receiver except (1) where the contract or other written agreement specifically provides for another payee of the reinsurance in the event of the insolvency of the ceding insurer or (2) where the assuming insurer, with the consent of the direct insured or insureds, has assumed the policy obligations of the ceding insurer as direct obligations of the assuming insurer to the payees under the policies and in substitution of the obligations of the ceding insurer to the payees.

(b) No credit shall be allowed, as an admitted asset or as a ~~deduction~~ reduction from liability, to any ceding insurer for reinsurance, unless the reinsurance is documented by a policy, certificate, treaty, or other form of agreement that is properly executed by an authorized officer of the assuming insurer. If the reinsurance is ceded through an underwriting manager or agent, the manager or agent shall provide to the domestic ceding insurer evidence of the manager or agent's authority to assume reinsurance for and on behalf of the assuming insurer. The evidence shall consist of either an acceptable letter of authority executed by an authorized officer of the assuming insurer or a copy of the actual agency agreement between the underwriting manager or agent and the assuming insurer; and the evidence shall be specific as to the classes of business within the authority and as to the term of the authority. If there is any conflict between this subsection and Article 9 of this Chapter, the provisions of Article 9 govern.

(c) The reinsurance agreement may provide that the domiciliary liquidator of an insolvent ceding insurer shall give written notice to the assuming insurer of the

pendency of a claim against the ceding insurer on the contract reinsured within a reasonable time after the claim is filed in the liquidation proceeding. During the pendency of the claim, any assuming insurer may investigate the claim and interpose at its own expense in the proceeding where the claim is to be adjudicated, any defenses which it deems available to the ceding insurer or its liquidator. The expense may be filed as a claim against the insolvent ceding insurer to the extent of a proportionate share of the benefit which may accrue to the ceding insurer solely as a result of the defense undertaken by the assuming insurer. Where two or more assuming insurers are involved in the same claim and a majority in interest elect to interpose a defense to the claim, the expense shall be apportioned in accordance with the terms of the reinsurance agreement as though the expense had been incurred by the ceding insurer."

SECTION 3.4. G.S. 58-7-31(c) reads as rewritten:

"(c) Notwithstanding subsection ~~(a)~~(b) of this section, an insurer may, with the prior approval of the Commissioner, take such reserve credit or establish such asset as the Commissioner deems to be consistent with the insurance laws or rules of this State, including actuarial interpretations or standards adopted by the Commissioner."

SECTION 3.5. G.S. 58-7-31(d)(1) reads as rewritten:

"(1) Reinsurance agreements entered into after October 1, 1993, that involve the reinsurance of business issued prior to the effective date of the reinsurance agreements, along with any subsequent amendments thereto, shall be filed by the ceding company with the Commissioner within 30 days after its date of execution. Each filing shall include data detailing the ~~final~~ financial impact of the transaction. The ceding insurer's actuary who signs the financial statement actuarial opinion with respect to valuation of reserves shall consider this statute and any applicable actuarial standards of practice when determining the proper credit in financial statements filed with the Commissioner. The actuary should maintain adequate documentation and be prepared upon request to describe the actuarial work performed for inclusion in the financial statements and to demonstrate that such work conforms to this statute."

SECTION 3.6. G.S. 58-57-85 is repealed.

SECTION 3.7. Sections 3.1 and 3.2 of this act apply to all reinsurance cessions made on or after January 1, 2002, under reinsurance agreements that have an inception, anniversary, or renewal date on or after January 1, 2002. The remainder of this part is effective when it becomes law.

PART IV. DOMESTIC COMPANY FORMATION AND RELOCATION.

SECTION 4.1. Article 7 of Chapter 58 of the General Statutes is amended by adding the following new section to read:

"**§ 58-7-37. Background of incorporators and proposed management personnel.**

(a) Before a license is issued to a new domestic insurance company, each key person must furnish the Commissioner a complete set of the applicant's fingerprints and a recent passport size full-face photograph of the applicant. The applicant's fingerprints shall be certified by an authorized law enforcement officer. The fingerprints of every applicant shall be forwarded to the State Bureau of Investigation for a search of the applicant's criminal history record file, if any. If warranted, the State Bureau of Investigation shall forward a set of the fingerprints to the Federal Bureau of Investigation for a national criminal history record check. An applicant shall pay the cost of the State and any national criminal history record check of the applicant.

(b) As used in this section, 'key person' means a proposed officer, director, or any other individual who will be in a position to influence the operating decisions of a domestic insurance company.

(c) The Commissioner may refuse to approve the formation or initial license of a new domestic insurance company under this Article if, after notice to the applicant and

an opportunity for a hearing, the Commissioner finds as to the incorporators or other key person any one or more of the following conditions:

(1) Any untrue material statement regarding the background or experience of any incorporator or other key person;

(2) Violation of, or noncompliance with, any insurance laws, or of any rule or order of the Commissioner or of a commissioner of another state by any incorporator or other key person;

(3) Obtaining or attempting to obtain the license through misrepresentation or fraud;

(4) An incorporator or other key person has been convicted of a felony;

(5) An incorporator or other key person has been found to have committed any unfair trade practice or fraud;

(6) An incorporator or other key person has used fraudulent, coercive, or dishonest practices, or has acted in a manner that is incompetent, untrustworthy, or financially irresponsible; or

(7) An incorporator or other key person has held such a position in another insurance company that has had its license suspended or revoked by any state.

(d) If the Commissioner disapproves of the formation or initial license, the Commissioner shall notify the applicant and advise the applicant in writing of the reasons for the disapproval. Within 30 days after receipt of notification, the applicant may make written demand upon the Commissioner for a hearing to determine the reasonableness of the Commissioner's action. The hearing shall be scheduled within 30 days after the date of receipt of the written demand.

(e) For the purposes of investigation under this section, the Commissioner shall have all the power conferred by G.S. 58-2-50 and other applicable provisions of this Chapter.

(f) The Commissioner may adopt rules to set standards for obtaining background information on each incorporator or other key person of a proposed new domestic insurance company."

SECTION 4.2. G.S. 58-7-70 reads as rewritten:

"**§ 58-7-70. Effects of redomestication.**

The license, agent appointments and licenses, rates, and other items that the Commissioner authorizes or grants, in his discretion, that are in existence at the time any insurer licensed ~~to transact the business of insurance in this State~~ by the Commissioner transfers its corporate domicile to this or any other state by merger, consolidation, or any other lawful method, shall continue in full force and effect upon ~~such~~ the transfer if ~~such~~ the insurer remains duly licensed ~~to transact the business of insurance in this State.~~by the Commissioner. All outstanding policies of any transferring insurer shall remain in full force and effect and need not be endorsed as to any new name of the insurer or its new location unless so ordered by the Commissioner. Every transferring insurer shall file new policy forms with the Commissioner on or before the effective date of the transfer, but may use existing policy forms with appropriate endorsements if allowed by, and under such conditions as approved by, the Commissioner: Provided, however, every such transferring insurer shall (i) notify the Commissioner of the details of the proposed transfer and (ii) promptly file any resulting amendments to corporate documents filed or required to be filed with the Commissioner."

PART V. INSURANCE COMPANY SOLVENCY PROTECTION.

SECTION 5.1. G.S. 58-7-75(10) reads as rewritten:

"(10) Impairment of Capital and/or Surplus. – Whenever the Commissioner finds from a financial statement made by any company, or from a report of examination of any company, that its admitted assets are less than the aggregate amount of its liabilities and its outstanding capital

~~stock and/or~~ stock, required minimum surplus, or both, the Commissioner shall ~~determine~~ determine, in accordance with G.S. 58-2-165 and other applicable provisions of this Chapter, the amount of the impairment of ~~capital and/or surplus~~ capital, surplus, or both and issue an order in writing requiring the company to eliminate the impairment within such period of not more than 90 days as the Commissioner shall designate. The Commissioner may, by order served upon the company, prohibit the company from issuing any new policies while the impairment exists. If at the expiration of the designated period the company has not satisfied the Commissioner that the impairment has been eliminated, an order for the rehabilitation or liquidation of the company may be entered as provided in Article 30 of this Chapter."

SECTION 5.2. G.S. 58-7-130 reads as rewritten:

"**§ 58-7-130. ~~Payment of dividends impairing financial soundness of company or detrimental to policyholders.~~Dividends and distributions to stockholders.**

(a) Each domestic insurance company in North Carolina shall be restricted by the Commissioner from the payment of any dividends or other distributions to its stockholders whenever the Commissioner determines from examination of ~~such~~ the company's financial condition that the payment of future dividends or other distributions would cause a hazardous financial condition, impair the financial soundness of the company or be detrimental to its policyholders, and ~~such~~ those restrictions shall continue in force until ~~such future date when~~ the Commissioner ~~may~~ specifically ~~permit~~ permits the payment of dividends or other distributions to stockholders by the company through a written authorization. ~~Nothing contained in this section and no action taken by the Commissioner shall in any way restrict the liability of stockholders under G.S. 58-7-125.~~

(b) No domestic stock insurance company shall declare dividends to its stockholders except from the unassigned surplus of the company as reflected in the company's most recent financial statement filed with the Commissioner under G.S. 58-2-165.

(c) A transfer out of paid-in and contributed surplus to common or preferred capital stock will be permitted on a case-by-case basis, with the Commissioner's prior approval, depending on the necessity for a company to make the transfer.

(d) Nothing in this section and no action taken by the Commissioner in any way restricts the liability of stockholders under G.S. 58-7-125.

(e) Dividends and other distributions paid to stockholders are subject to the requirements and limitations of G.S. 58-19-25(d) and G.S. 58-19-30(c)."

PART VI. LIFE INSURANCE COMPANY VARIABLE ACCOUNTS.

SECTION 6.1. G.S. 58-7-95(b) reads as rewritten:

"(b) Any domestic life insurance company may, pursuant to resolution of its board of directors, establish one or more separate accounts and may allocate to such account or accounts amounts ~~received or retained in connection with variable contracts~~ (including without limitation proceeds applied under optional modes of settlement or under dividend options) to provide for life ~~insurance~~ insurance, guaranteed investment contracts, or annuities (and benefits incidental thereto) payable in fixed or variable amounts or both."

SECTION 6.2. G.S. 58-7-95(c) reads as rewritten:

"(c) In addition to the amounts allocated under subsection (b), such company may allocate from its general accounts to such separate account or accounts additional amounts, which may include an initial allocation to establish such account; provided, ~~that the aggregate amount so allocated shall not exceed one per centum (1%) of its admitted assets as of the preceding December 31, or one million dollars ($1,000,000), whichever is less, and, provided further,~~ that such company shall be entitled to withdraw

at any time, in whole or in part, its participation in any separate account to which funds have been allocated as provided in this subsection (c), and to receive, upon withdrawal, its proportionate share of the value of the assets of the separate account at the time of withdrawal."

SECTION 6.3. G.S. 58-7-95(e) and G.S. 58-7-95(f) are repealed.

SECTION 6.4. G.S. 58-7-95(g) reads as rewritten:

"(g) ~~The limitations provided in subsections (e) and (f) above shall not apply to the investment with respect to a separate account in the securities of an investment company registered under the Investment Company Act of 1940, provided that the investments of such investment company comply in substance with subsections (e) and (f) hereof.~~The life insurance company shall maintain in each separate account assets with a value at least equal to the reserves and other contract liabilities with respect to the account, except as may otherwise be approved by the Commissioner."

PART VII. INSURANCE COMPANY CONSOLIDATION.

SECTION 7.1. G.S. 58-7-150(a) reads as rewritten:

"(a) A domestic insurer may consolidate with another insurer, subject to the following conditions:

(1) The plan of consolidation must be submitted to and be approved by the Commissioner ~~in advance of~~ before the consolidation.

(2) The Commissioner shall not approve ~~any such plan unless, after a hearing, he~~ the plan unless the Commissioner finds that it is fair, equitable to policyholders, consistent with law, and will not conflict with the public interest. If the Commissioner ~~fails to approve~~ disapproves the plan, ~~he~~ the Commissioner shall state ~~his~~ the reasons for ~~such failure in his order made on such hearing.~~the disapproval and call for a hearing.

(3) No director, officer, member or subscriber of any such insurer, except as is expressly provided by the plan of consolidation, shall receive any fee, commission, other compensation or valuable consideration whatever, for in any manner aiding, promoting or assisting in the consolidation.

(4) Any consolidation as to an incorporated domestic insurer shall in other respects be governed by the general laws of this State relating to business ~~corporations, except that the~~ corporations. The consolidation of a domestic mutual insurer may be effected by vote of two thirds of the members voting thereon pursuant to such notice and procedure as the Commissioner may prescribe."

SECTION 7.2. G.S. 58-7-150(b) reads as rewritten:

"(b) Reinsurance of all or substantially all of the insurance ~~in force~~ obligations or risks of existing or in-force policies of a domestic insurer by another insurer under an ~~agreement whereby the reinsuring company succeeds to all of the liabilities of and supplants the domestic insurance company thereon~~ assumption reinsurance agreement, as defined in G.S. 58-10-25(a)(2), shall be deemed a consolidation for the purposes of this section. This section does not apply to consolidations to the extent regulated by Article 19 or other Articles of this Chapter."

PART VIII. INSURANCE COMPANY INVESTMENTS.

SECTION 8.1. G.S. 58-7-170(b) reads as rewritten:

"(b) Investments eligible under subsection (a), except investments acquired under G.S. 58-7-183, are subject to the following ~~limitations:~~limitations, other limitations of this section, and any other limitations that are expressly provided for in any provision under which the investment is authorized:

(1) The cost of investments made by insurers in stock authorized by G.S. 58-7-173 shall not exceed twenty-five percent (25%) of the insurer's

admitted assets, provided that no more than twenty percent (20%) of the insurer's admitted assets shall be invested in common stock; and the cost of an investment in stock of any one corporation shall not exceed three percent (3%) of the insurer's admitted assets. Notwithstanding any other provision in this Chapter, the financial statement carrying value of all stock investments shall be used for the purpose of determining the asset value against which the percentage limitations are to be applied.

(2) ~~Other limitations, if any, that are expressly provided for in any provision under which the investment is authorized.~~The cost of Canadian investments authorized by G.S. 58-7-173 shall not exceed forty percent (40%) of the insurer's admitted assets in the aggregate, provided that no more than twenty-five percent (25%) of the insurer's admitted assets shall be invested in Canadian investments authorized by G.S. 58-7-173(11)."

SECTION 8.2. G.S. 58-7-170(d) reads as rewritten:

"(d) Without the Commissioner's prior written approval, the cost of investments ~~in bonds, debentures, notes, commercial paper, or other debt obligations issued, assumed, or guaranteed by any solvent United States institution, any state, Canada, or any Canadian province,~~ permitted under G.S. 58-7-173 and G.S. 58-7-178, and that are classified as medium to lower quality obligations, other than obligations of subsidiaries or affiliated corporations as that term is defined in ~~G.S. 58-7-177,~~ G.S. 58-19-5, shall be limited to:

(1) No more than twenty percent (20%) of an insurer's admitted assets;
(2) No more than ten percent (10%) of an insurer's admitted assets in obligations that have been given a rating of 4, 5, or 6 by the Securities Valuation Office of the NAIC;
(3) No more than three percent (3%) of an insurer's admitted assets in obligations that have been given a rating of 5 or 6 by the Securities Valuation Office of the NAIC; and
(4) No more than one percent (1%) of an insurer's admitted assets in obligations that have been given a rating of 6 by the Securities Valuation Office of the NAIC.

(5), (6) Repealed by Session Laws 1993, c. 452, s. 11."

SECTION 8.3. G.S. 58-7-173(9) reads as rewritten:

"(9) Bonds, debentures, or other securities of public housing authorities, issued under the Housing Act, of 1949, the Municipal Housing Commission Act, or the Rural Housing Commission Act, or issued by any public housing authority or agency in the United States, if the bonds, debentures, or other securities are secured by a pledge of annual contributions to be paid by the United States or any United States ~~agency; and the cost of investments made under this subdivision shall not exceed the lesser of three percent (3%) of the insurer's admitted assets or ten percent (10%) of the insurer's capital and surplus.~~agency."

SECTION 8.4. G.S. 58-7-173(10) reads as rewritten:

"(10) Obligations issued, assumed, or guaranteed by the International Bank for Reconstruction and Development, the International Finance Corporation, the Inter-American Development Bank, the Asian Development Bank, or the African Development Bank; and the cost of investments made under this subdivision in any one institution shall not exceed ~~the lesser of~~ three percent (3%) of the insurer admitted ~~assets or ten percent (10%) of the insurer's capital and surplus.~~assets."

SECTION 8.5. G.S. 58-7-173(11) reads as rewritten:

"(11) Bonds, notes, or other interest-bearing or interest-accruing obligations of any solvent institution organized under the laws of the United

States, of any state, Canada or any Canadian province; provided such instruments are rated and valued by the Securities Valuation Office of the NAIC. The cost of investments made under this subdivision in ~~issuers from any one industry shall not exceed ten percent (10%) of an insurer's admitted assets, and the cost of investments made in~~ any one issuer shall not exceed three percent (3%) of an insurer's admitted ~~assets or ten percent (10%) of an insurer's capital and surplus, whichever is greater. As used in this subdivision, "industry" means a distinct and recognized area of economic activity that consists of the production, manufacture, or distribution of common goods, products, commodities, or services.~~assets."

SECTION 8.6. G.S. 58-7-173(12) reads as rewritten:

"(12) Secured obligations of duly constituted churches and of church-holding companies; and the cost of investments made under this subdivision shall not exceed ~~the lesser of one percent (1%)~~ three percent (3%) of the insurer's admitted ~~assets or five percent (5%) of the insurer's capital and surplus.~~assets."

SECTION 8.7. G.S. 58-7-173(14) reads as rewritten:

"(14) Share or savings accounts of savings and loan associations or building and loan ~~associations; and the cost of investments made under this subdivision shall not exceed the lesser of three percent (3%) of the insurer's admitted assets or five percent (5%) of the insurer's capital and surplus.~~associations."

SECTION 8.8. G.S. 58-7-173(16) reads as rewritten:

"(16) Stocks, common or preferred, of any corporation created or existing under the laws of the United States, any U.S. territory, Canada or any Canadian province, or of any state. An insurer may invest in stocks, common or preferred, of any corporation created or existing under the laws of any foreign country other than Canada ~~if the stocks are listed and traded on a national securities exchange in the United States or if the investment in stocks of any corporation created or existing under the laws of any foreign country are first approved by the Commissioner. Nothing in this section applies to qualifying investments made by an insurer in a foreign country under authority of G.S. 58-7-178.~~subject to the provisions of G.S. 58-7-178."

SECTION 8.9. G.S. 58-7-177 is repealed.

SECTION 8.10. G.S. 58-23-26(c) reads as rewritten:

"(c) Each pool is subject to G.S. 58-2-131, 58-2-132, 58-2-133, 58-2-134, 58-2-150, 58-2-155, 58-2-165, 58-2-180, 58-2-185, 58-2-190, 58-2-200, 58-3-71, 58-3-75, 58-3-81, 58-3-105, 58-6-5, 58-7-21, 58-7-26, 58-7-30, 58-7-31, 58-7-50, 58-7-55, 58-7-140, 58-7-160, 58-7-162, 58-7-163, 58-7-165, 58-7-167, 58-7-168, 58-7-170, 58-7-172, 58-7-173, 58-7-175, ~~58-7-177,~~ 58-7-179, 58-7-180, 58-7-183, 58-7-185, 58-7-187, 58-7-188, 58-7-192, 58-7-193, 58-7-195, 58-7-197, 58-7-200, and Articles 13, 19, and 34 of this Chapter. Annual financial statements required by G.S. 58-2-165 shall be filed by each pool within 60 days after the end of the pool's fiscal year, subject to extension by the Commissioner."

SECTION 8.11. G.S. 58-7-178 reads as rewritten:

"**§ 58-7-178. Foreign or territorial investments.**

(a) An insurer authorized to transact insurance in a foreign country or any U.S. territory may have funds invested in securities that may be required for that authority and for the transaction of that ~~business.~~business, provided the funds and securities are substantially of the same kinds, classes, and investment grades as those otherwise eligible for investment under this Chapter. ~~Canadian securities eligible for investment under other provisions of this Chapter are not subject to this section. Unless disapproved by the Commissioner:~~

~~(1) An insurer may invest in Eurodollar certificates of deposit issued by foreign branches of United States commercial banks.~~

~~(2) In addition to Canadian securities eligible for investment and to investments in countries in which an insurer transacts insurance, an insurer may invest in bonds, notes, or stocks of any foreign country or alien corporation if the security meets the general requirements of G.S. 58-7-167 and does not exceed, in total, five~~ percent (5%) of admitted assets.

The aggregate amount of investments under this subsection shall not exceed the amount that the insurer is required by law to invest in the foreign country or United States territory, or one and one-half times the amount of reserves and other obligations under the contracts, whichever is greater.

(b) An insurer, whether or not it is authorized to do business or has outstanding insurance contracts on lives or risks in any foreign country, may invest in bonds, notes, or stocks of any foreign country or alien corporation that are substantially of the same kinds, classes, and investment grades as those otherwise eligible for investment under this Chapter. The aggregate amount of investments under this subsection shall not exceed ten percent (10%) of the insurer's admitted assets, provided that the cost of investments in any foreign country under this subsection shall not exceed three percent (3%) of the insurer's admitted assets.

(c) Canadian securities eligible for investment under other provisions of this Chapter are not subject to this section."

SECTION 8.12. G.S. 58-7-185(a)(2) reads as rewritten:

"(2) Except with the Commissioner's consent, securities issued by any corporation or enterprise, the controlling interest of which is or will after acquisition by the insurer be held directly or indirectly by the insurer or any combination of the insurer and the insurer's directors, officers, parent corporation, subsidiaries, or controlling stockholders. Investments in subsidiaries under ~~G.S. 58-7-177~~ G.S. 58-19-10 are not subject to this provision."

SECTION 8.13. G.S. 58-7-185(a)(3) is repealed.

SECTION 8.14. G.S. 58-7-192(d) reads as rewritten:

"(d) No valuations under this section shall be greater than any applicable valuation or method contained in the latest edition of the NAIC ~~publication~~ publications entitled 'Valuations of ~~Securities',~~ Securities' or the 'Accounting Practices and Procedures Manual', unless the Commissioner determines that another valuation method is appropriate when it results in a more conservative valuation."

SECTION 8.15. G.S. 58-7-200(b) reads as rewritten:

"(b) ~~Notwithstanding any expressed or implied prohibitions, an insurer may effect or maintain bona fide hedging transactions pertaining to securities otherwise eligible for investment under this section, including, but not limited to (i) financial futures contracts, warrants, options, calls and other rights to purchase; and (ii) puts and other rights to require another person to purchase the securities. The contracts, options, calls, puts and rights shall be traded on a securities exchange or board of trade regulated under the laws of the United States. For the purposes of this subsection, "bona fide hedging transaction" means a purchase or sale of such a contract, warrant, option, call, put or right, entered into for the purpose of offsetting changes in the market value of a security held by the company.~~An insurer may engage in derivative transactions under the provisions and limitations of G.S. 58-7-205."

SECTION 8.16. G.S. 58-7-200(c) reads as rewritten:

"(c) ~~No insurer shall make any direct or indirect loan to any of its directors, officers, or controlling stockholders; nor shall the insurer make any loan to any other person in which the officer, director, or stockholder is substantially interested; nor shall any such director, officer, or stockholder directly or indirectly accept any such loan.~~ No insurer shall directly or indirectly invest in, or lend its funds to, any of its directors,

officers, controlling stockholders, or any other person in which an officer, director, or controlling stockholder is substantially interested, nor shall any director, officer, or controlling stockholder directly or indirectly accept the funds."

SECTION 8.17. Article 7 of Chapter 58 of the General Statutes is amended by adding the following new section to read:

"**§ 58-7-205. Derivative transactions.**

(a) As used in this section, the following terms have the following meanings:

(1) 'Business entity' includes a sole proprietorship, corporation, limited liability company, association, partnership, joint stock company, joint venture, mutual fund, trust, joint tenancy or other similar form of business organization, whether for-profit or not-for-profit.

(2) 'Counterparty exposure' amount means:

a. The amount of credit risk attributable to a derivative instrument entered into with a business entity other than through a qualified exchange, qualified foreign exchange, or cleared through a qualified clearinghouse ('over-the-counter derivative instrument'). The amount of credit risk equals:

1. The market value of the over-the-counter derivative instrument if the liquidation of the derivative instrument would result in a final cash payment to the insurer; or

2. Zero if the liquidation of the derivative instrument would not result in a final cash payment to the insurer.

b. If over-the-counter derivative instruments are entered into under a written master agreement which provides for netting of payments owed by the respective parties and the domicile of the counterparty is either within the United States or, if not within the United States, within a foreign jurisdiction listed in the Purposes and Procedures of the Securities Valuation Office of the NAIC as eligible for netting, the net amount of credit risk shall be the greater of zero or the net sum of:

1. The market value of the over-the-counter derivative instruments entered into under the agreement, the liquidation of which would result in a final cash payment to the insurer; and

2. The market value of the over-the-counter derivative instruments entered into under the agreement, the liquidation of which would result in a final cash payment by the insurer to the business entity.

c. For open transactions, market value shall be determined at the end of the most recent quarter of the insurer's fiscal year and shall be reduced by the market value of acceptable collateral held by the insurer or placed in escrow by one or both parties.

(3) 'Derivative instrument' means an agreement, option, instrument, or a series or combination thereof:

a. To make or take delivery of, or assume or relinquish, a specified amount of one or more underlying interests, or to make a cash settlement in lieu thereof; or

b. That has a price, performance, value, or cash flow based primarily upon the actual or expected price level, performance, value, or cash flow of one or more underlying interests.

Derivative instruments include options, warrants used in a hedging transaction and not attached to another financial instrument, caps, floors, collars, swaps, forwards, futures, and any other agreements, options, or instruments substantially similar thereto or any series or combination thereof. Derivative instruments shall additionally include

any agreements, options, or instruments permitted under rules adopted under subsection (c) of this section. Derivative instruments shall not include an investment authorized by G.S. 58-7-173, 58-7-175, 58-7-178, 58-7-179, 58-7-180, and 58-7-187.

(4) 'Derivative transaction' means any transaction involving the use of one or more derivative instruments.

(5) 'Qualified clearinghouse' means a clearinghouse for, and subject to the rules of, a qualified exchange or a qualified foreign exchange. The clearinghouse provides clearing services, including acting as a counterparty to each of the parties to a transaction such that the parties no longer have credit risk as to each other.

(6) 'Qualified exchange' means:

a. A securities exchange registered as a national securities exchange, or a securities market regulated under the Securities Exchange Act of 1934 (15 U.S.C. §§ 78, et seq.), as amended;

b. A board of trade or commodities exchange designated as a contract market by the Commodity Futures Trading Commission, or any successor thereof;

c. Private Offerings, Resales and Trading through Automated Linkages (PORTAL);

d. A designated offshore securities market as defined in Securities Exchange Commission Regulation S, 17 C.F.R. Part 230, as amended; or

e. A qualified foreign exchange.

(7) 'Qualified foreign exchange' means a foreign exchange, board of trade, or contract market located outside the United States, its territories or possessions:

a. That has received regulatory comparability relief under Commodity Futures Trading Commission Rule 30.10 (as set forth in Appendix C to Part 30 of the CFTC's Regulations, 17 C.F.R. Part 30);

b. That is, or its members are, subject to the jurisdiction of a foreign futures authority that has received regulatory comparability relief under Commodity Futures Trading Commission Rule 30.10 (as set forth in Appendix C to Part 30 of the CFTC's Regulations, 17 C.F.R. Part 30) as to futures transactions in the jurisdiction where the exchange, board of trade, or contract market is located; or

c. Upon which foreign stock index futures contracts are listed that are the subject of no-action relief issued by the CFTC's Office of General Counsel, but an exchange, board of trade, or contract market that qualifies as a 'qualified foreign exchange' only under this paragraph shall only be a 'qualified foreign exchange' as to foreign stock index futures contracts that are the subject of the no-action relief under this paragraph.

(8) 'Replication transaction' means a derivative transaction that is intended to replicate the investment in one or more assets that an insurer is authorized to acquire or sell under this section or G.S. 58-7-165. A derivative transaction that is entered into as a hedging transaction shall not be considered a replication transaction.

(b) An insurer may, directly or indirectly through an investment subsidiary, engage in derivative transactions under this section under the following conditions:

(1) An insurer may use derivative instruments under this section to engage in hedging transactions and certain income generation transactions as may be further defined by rules adopted by the Commissioner.

(2) An insurer shall be able to demonstrate to the Commissioner the intended hedging characteristics and the ongoing effectiveness of the derivative transaction or combination of the transactions through cash flow testing or other appropriate analyses.

(c) The Commissioner may adopt reasonable rules for investments and transactions under this section including, but not limited to, rules which impose financial solvency standards, valuation standards, and reporting requirements.

(d) An insurer may enter into hedging transactions under this section if, as a result of and after giving effect to the transaction:

(1) The aggregate statement value of options, caps, floors, and warrants not attached to another financial instrument purchased and used in hedging transactions then engaged in by the insurer does not exceed seven and one-half percent (7.5%) of its admitted assets;

(2) The aggregate statement value of options, caps, and floors written in hedging transactions then engaged in by the insurer does not exceed three percent (3%) of its admitted assets; and

(3) The aggregate potential exposure of collars, swaps, forwards, and futures used in hedging transactions then engaged in by the insurer does not exceed six and one-half percent (6.5%) of its admitted assets.

(e) An insurer may enter into the following types of income generation transactions if, as a result of and after giving effect to the transactions, the aggregate statement value of the fixed income assets that are subject to call or that generate the cash flows for payments under the caps or floors, plus the face value of fixed income securities underlying a derivative instrument subject to call, plus the amount of the purchase obligations under the puts, does not exceed ten percent (10%) of its admitted assets:

(1) Sales of covered call options on noncallable fixed-income securities, callable fixed-income securities if the option expires by its terms before the end of the noncallable period, or derivative instruments based on fixed income securities;

(2) Sales of covered call options on equity securities, if the insurer holds in its portfolio, or can immediately acquire through the exercise of options, warrants, or conversion rights already owned, the equity securities subject to call during the complete term of the call option sold;

(3) Sales of covered puts on investments that the insurer is permitted to acquire under this Chapter, if the insurer has escrowed or entered into a custodian agreement segregating cash or cash equivalents with a market value equal to the amount of its purchase obligations under the put during the complete term of the put option sold; or

(4) Sales of covered caps or floors, if the insurer holds in its portfolio the investments generating the cash flow to make the required payments under the caps or floors during the complete term that the cap or floor is outstanding.

(f) An insurer shall include all counterparty exposure amounts in determining compliance with the limitations of G.S. 58-7-170.

(g) Under rules that may be adopted by the Commissioner, additional transactions involving the use of derivative instruments in excess of the limits of subsection (d) of this section or for other risk management purposes may be approved by the Commissioner.

(h) An insurer shall establish guidelines and internal procedures as follows:

(1) Before engaging in a derivative transaction, an insurer shall establish written guidelines that shall be used for effecting and maintaining the transactions. The guidelines shall:

a. Address investment or, if applicable, underwriting objectives, and risk constraints such as credit risk limits;
b. Address permissible transactions and the relationship of those transactions to its operations, such as a precise identification of the risks being hedged by a derivative transaction; and
c. Require compliance with internal control procedures.

(2) An insurer shall have a system for determining whether a derivative instrument used for hedging has been effective.

(3) An insurer shall have a credit risk management system for over-the-counter derivative transactions that measures credit risk exposure using the counterparty exposure amount.

(4) An insurer's board of directors shall, in accordance with G.S. 58-7-168:
a. Approve the guidelines required by subdivision (1) of this subsection and the systems required by subdivisions (2) and (3) of this subsection; and
b. Determine whether the insurer has adequate professional personnel, technical expertise and systems to implement investment practices involving derivatives.

(i) An insurer shall maintain documentation and records relating to each derivative transaction, such as:
(1) The purpose or purposes of the transaction;
(2) The assets or liabilities to which the transaction relates;
(3) The specific derivative instrument used in the transaction;
(4) For over-the-counter derivative instrument transactions, the name of the counterparty and counterparty exposure amount; and
(5) For exchange-traded derivative instruments, the name of the exchange and the name of the firm that handled the trade.

(j) Each derivative instrument shall be:
(1) Traded on a qualified exchange;
(2) Entered into with, or guaranteed by, a business entity;
(3) Issued or written by or entered into with the issuer of the underlying interest on which the derivative instrument is based; or
(4) Entered into with a qualified foreign exchange."

SECTION 8.18. G.S. 58-67-60 reads as rewritten:

"**§ 58-67-60. Investments.**

With the exception of investments made in accordance with G.S. 58-67-35(a)(1) and (2) and G.S. 58-67-35(b), the ~~investable~~ funds of a health maintenance organization shall be invested or maintained only in ~~securities or~~ securities, other ~~investments~~ investments, or other assets permitted by the laws of this State for the investment of assets constituting the legal reserves of life insurance companies or such other securities or investments as the Commissioner may permit."

PART IX. MUTUAL INSURANCE COMPANIES.

SECTION 9.1. G.S. 58-8-5(a)(3) reads as rewritten:

"(3) ~~Said officers shall cause said certificate to be published once a week for two consecutive weeks in a newspaper in Raleigh and in the county where the company's principal office is located, or posted at the courthouse door if no newspaper be published within the county. Said printed or posted notices shall be in such form and of such size as the Commissioner may approve, and in addition to setting forth in full the certificate required in subdivision (2) shall state that application for amending the company's charter in the manner specified has been proposed by the board of directors, and shall also state the time set for a meeting of policyholders thereby called to be held at the principal~~

~~office of the company to take action on the proposed amendment. A true copy of such notice shall be filed with the Commissioner, and also with that official who performs the functions of Commissioner in each state where the company is licensed to do business. Such publication and filing of notices shall be completed at least 30 days prior to the date set therein for the meeting of policyholders and due proof thereof shall be filed with the Commissioner at least 15 days prior to the date of such meeting.~~ If the meeting at which the proposed amendment is to be considered is a special meeting, rather than a regular annual meeting of policyholders, such special meeting can be called only after the Commissioner has given his approval in ~~writing, and the published notice shall show the fact of such approval;~~writing;"

SECTION 9.2. G.S. 58-8-25 reads as rewritten:

"**§ 58-8-25. Dividends to policyholders.**

(a) Any participating or dividend-paying company, stock or mutual or foreign or domestic, that writes other than life insurance or workers' compensation insurance and employers' liability insurance in connection therewith, may declare and pay a dividend to policyholders from its ~~surplus,~~unassigned surplus, as reflected in the company's most recent annual or quarterly statement filed with the Commissioner under G.S. 58-2-165, which shall include only its surplus in excess of any required minimum surplus. No such dividend shall be paid unless it is fair and equitable and for the best interest of the company and its policyholders. In declaring any dividend to its policyholders, any such company may make reasonable classifications of policies expiring during a fixed period, upon the basis of each general kind of insurance covered by ~~such~~ those policies and by territorial divisions of the location of risks by states, except that in fixing the amount of dividends to be paid on each general kind of insurance, ~~which~~ the dividends shall be uniform in rate and applicable to the majority of risks within ~~such~~ that general kind of insurance, and exceptions may be made as to any class or classes of risk and a different rate or amount of dividends paid on ~~such~~ the class or classes if the conditions applicable to ~~such~~ the class or classes differ substantially from the condition applicable to the kind of insurance as a whole. Every such company shall have an equal rate of dividend for the same term on all policies insuring risks in the same classification. The payment of dividends to policyholders shall not be contingent upon the maintenance or renewal of the policy. All dividends shall be paid to the policyholder unless a written assignment ~~thereof be~~ of those dividends is executed. Neither the payment of dividends nor the rate ~~thereof~~ of the dividends may be guaranteed by any company, or its agent, ~~prior to~~before the declaration of the dividend by the board of directors of ~~such~~ the company. The holders of policies of insurance issued by a company in compliance with the orders of any public official, bureau or committee, in conformity with any statutory requirement or voluntary arrangement, for the issuance of insurance to risks not otherwise acceptable to the company, may be established as a separate class of risks.

(b) Any participating or dividend-paying company, stock or mutual or foreign or domestic, that writes workers' compensation insurance and employers' liability insurance in connection therewith may declare and pay a dividend to policyholders from its ~~surplus,~~ unassigned surplus, as reflected in the company's most recent statement filed with the Commissioner under G.S. 58-2-165, which shall include only its surplus in excess of any required minimum surplus. No such dividend shall be paid unless it is fair and equitable and for the best interest of the company and its policyholders. In declaring any dividend to its policyholders, any such company may make reasonable classifications of policies expiring during a fixed period. The payment of dividends to policyholders shall not be contingent upon the maintenance or renewal of the policy. All dividends shall be paid to the policyholder unless a written assignment ~~thereof be~~ of those dividends is executed. Neither the payment of dividends nor the rate ~~thereof~~ of the dividends may be guaranteed by any company, or its agent, ~~prior to~~ before the declaration of the dividend by the board of directors of ~~such~~ the company. The holders

of policies of insurance issued by a company in compliance with the orders of any public official, bureau, or committee, in conformity with any statutory requirement or voluntary arrangement, for the issuance of insurance to risks not otherwise acceptable to the company, may be established as a separate class of risks."

SECTION 9.3. The title of G.S. 58-10-1 reads as rewritten:

"**§ 58-10-1. ~~Domestic stock life insurance corporations authorized to convert into mutual corporations; procedure.~~Stock to mutual insurer conversion.**"

SECTION 9.4. The title of Part 1 of Article 10 of Chapter 58 of the General Statutes reads as rewritten:

"Article 10.
Miscellaneous Insurer Financial Provisions.
Part 1. Conversion ~~from~~ of Stock ~~to~~ and Mutual ~~Corporation.~~Insurers."

SECTION 9.5. The title of G.S. 58-10-10 reads as rewritten:

"**§ 58-10-10. Mutual ~~conversion~~ to stock ~~insurer.~~insurer conversion.**"

SECTION 9.6. Part 1 of Article 10 of Chapter 58 of the General Statutes is amended by adding a new section to read:

"**§ 58-10-12. Conversion plan requirements.**

(a) As used in this section:

(1) 'Closed block' means an allocation of assets for a defined group of in-force policies which, together with the premiums of those policies and related investment earnings, are expected to be sufficient to maintain the payments of guaranteed benefits, certain expenses, and continuation of the current dividend scale on the closed block, if experience does not change.

(2) 'Converting mutual' means a domestic mutual insurance company that has adopted a plan of conversion and an amendment to its articles of incorporation under this section that will, upon consummation, result in the domestic mutual insurance company converting into a domestic stock insurance company.

(3) 'Eligible member' means a person who:

a. Is a member of the converting mutual on the date the converting mutual's board of directors adopts a resolution proposing a plan of conversion and an amendment to the articles of incorporation; and

b. Continues to be a member of the converting mutual on the effective date of the conversion.

(4) 'Former mutual' means the domestic stock insurance company resulting from the conversion of a converting mutual to a stock insurance company under a plan of conversion and an amendment to its articles of incorporation under this section.

(5) 'Member' means a person that, according to the records, articles of incorporation, and bylaws of a converting mutual, is a member of the converting mutual.

(6) 'Membership interests' means:

a. The voting rights of members of a domestic mutual insurance company as provided by law and by the company's articles of incorporation and bylaws; and

b. The rights of members of a domestic mutual insurance company to receive cash, stock, or other consideration in the event of a conversion to a stock insurance company under this section or a dissolution as provided by the company's articles of incorporation and bylaws.

(7) 'Parent company' means a corporation that, upon the effective date of a conversion, owns all of the stock of the former mutual.

(8) 'Plan of conversion' means the plan of conversion described in subsection (b) of this section.

(b) The plan of conversion under G.S. 58-10-10 shall:

(1) Describe the manner in which the proposed conversion will occur and the insurance and any other companies that will result from or be directly affected by the conversion, including the former mutual and any parent company.

(2) Provide that the membership interests in the converting mutual will be extinguished as of the effective date of the conversion.

(3) Require the distribution to the eligible members, upon the extinguishing of their membership interests, of aggregate consideration equal to the fair value of the converting mutual.

(4) Describe the manner in which the fair value of the converting mutual has been or will be determined.

(5) Describe the form or forms and amount, if known, of consideration to be distributed to the eligible members.

(6) Specify relevant classes, categories, or groups of eligible members and describe and explain any differences in the form or forms and amount of consideration to be distributed to or among the eligible members.

(7) Require and describe the method or formula for the fair and equitable allocation of the consideration among the eligible members.

(8) Provide for the determination and preservation of the reasonable dividend expectations of eligible members and other policyholders with policies that provide for the distribution of policy dividends, through establishment of a closed block or other method acceptable to the Commissioner.

(9) Provide that each member and other policyholder of the converting mutual will receive notification of the address and telephone number of the converting mutual and the former mutual, if different, along with the notice of hearing as approved by the Commissioner.

(10) Include other provisions as the converting mutual determines to be necessary.

(c) After the adoption by the board of directors of the resolution proposing the plan of conversion under G.S. 58-10-10 and the amendment to its articles of incorporation, the converting mutual shall file with the Commissioner an application for approval of the plan and amendment. The application must contain the following information, together with any additional information as the Commissioner may require:

(1) The plan of conversion and a certificate of the secretary of the converting mutual certifying the adoption of the plan by the board of directors.

(2) A statement of the reasons for the proposed conversion and why the conversion is in the best interests of the converting mutual, the eligible members, and the other policyholders. The statement must include an analysis of the risks and benefits to the converting mutual and its members of the proposed conversion and a comparison of the risks and benefits of the conversion with the risks and benefits of reasonable alternatives to a conversion.

(3) A five-year business plan and at least two years of financial forecasts of the former mutual and any parent company.

(4) Any plans that the former mutual or any parent company may have to:

a. Raise additional capital through the issuance of stock or otherwise;

b. Sell or issue stock to any person, including any compensation or benefit plan for directors, officers, or employees under which stock may be issued;

c. Liquidate or dissolve any company or sell any material assets;
d. Merge or consolidate or pursue any other form of reorganization with any person; or
e. Make any other material change in investment policy, business, corporate structure, or management.

(5) Any plans for a delayed distribution of consideration to eligible members or restrictions on sale or transfer of stock or other securities.

(6) A copy of the form of trust agreement, if a distribution of consideration is to be delayed by more than six months after the effective date of the conversion.

(7) A plan of operation for a closed block, if a closed block is used for the preservation of the reasonable dividend expectations of eligible members and other policyholders with policies that provide for the distribution of policy dividends.

(8) Copies of the amendment to the articles of incorporation proposed by the board of directors and proposed bylaws of the former mutual and copies of the existing and any proposed articles of incorporation and bylaws of any parent company.

(9) A list of all individuals who are or have been selected to become directors or officers of the former mutual and any parent company, or the individuals who perform or will perform duties customarily performed by a director or officer, and the following information concerning each individual on the list unless the information is already on file with the Commissioner:
a. The individual's principal occupation.
b. All offices and positions the individual has held in the preceding five years.
c. Any crime of which the individual has been convicted (other than traffic violations) in the preceding 10 years.
d. Information concerning any personal bankruptcy of the individual or the individual's spouse during the previous seven years.
e. Information concerning the bankruptcy of any corporation or other entity of which the individual was an officer or director during the previous seven years.
f. Information concerning allegations of state or federal securities law violations made against the individual that within the previous 10 years resulted in (i) a determination that the individual violated state or federal securities laws; (ii) a plea of nolo contendere; or (iii) a consent decree.
g. Information concerning the suspension, revocation, or other disciplinary action during the previous 10 years of any state or federal license issued to the individual.
h. Information as to whether the individual was refused a bond during the previous 10 years.

(10) A fairness opinion addressed to the board of directors of the converting mutual from a qualified, independent financial adviser asserting:
a. That the provision of stock, cash, policy benefits, or other forms of consideration upon the extinguishing of the converting mutual's membership interests under the plan of conversion and the amendment to the articles of incorporation is fair to the eligible members, as a group, from a financial point of view; and

b. Whether the total consideration under sub-subdivision a. of this subdivision is equal to or greater than the surplus of the converting mutual.

The Commissioner may waive the fairness opinion in situations involving a straightforward issuance of stock to members of the former mutual.

(11) An actuarial opinion as to the following:

a. The reasonableness and appropriateness of the methodology or formulas used to allocate consideration among eligible members, consistent with this Article.

b. The reasonableness of the plan of operation and sufficiency of the assets allocated to the closed block, if a closed block is used for the preservation of the reasonable dividend expectations of eligible members and other policyholders with policies that provide for the distribution of policy dividends.

(12) If any of the consideration to be distributed to eligible members consists of stock or other securities, subject to the limitations of G.S. 58-10-10(b)(6), a description of the plans made by the former mutual or its parent company to assure that an active public trading market for the stock or other securities will develop within a reasonable amount of time after the effective date of the plan of conversion and that eligible members who receive stock or other securities will be able to sell their stock or other securities, subject to any delayed distribution or transfer restrictions, at reasonable cost and effort.

(13) Any additional information, documents, or materials that the converting mutual determines to be necessary.

(d) Distribution of all or part of the consideration to some or all of the eligible members may be delayed, or restrictions on sale or transfer of any stock or other securities to be distributed to eligible members may be required, for a reasonable period of time following the effective date of the conversion. However, the period of time shall not exceed six months unless otherwise approved by the Commissioner.

(e) Except as specifically provided in a plan of conversion, for five years following the effective date of the conversion, no person or persons acting in concert (other than the former mutual, any parent company, or any employee benefit plans or trusts sponsored by the former mutual or a parent company) shall directly or indirectly acquire, or agree or offer to acquire, in any manner the beneficial ownership of five percent (5%) or more of the outstanding shares of any class of a voting security of the former mutual or any parent company without the prior approval of the Commissioner of a statement filed by that person with the Commissioner. The statement shall contain the information required by G.S. 58-19-15(b) and any other information required by the Commissioner. The Commissioner shall not approve an acquisition under this subsection unless the Commissioner finds that:

(1) The requirements of G.S. 58-19-15(e) will be satisfied.

(2) The acquisition will not frustrate the plan of conversion or the amendment to the articles of incorporation as approved by the members and the Commissioner.

(3) The boards of directors of the former mutual and any parent company have approved the acquisition.

(4) The acquisition would be in the best interest of the present and future policyholders of the former mutual without regard to any interest of policyholders as shareholders of the former mutual or any parent company."

PART X. REINSURANCE INTERMEDIARIES.

SECTION 10.1. G.S. 58-9-6(a) reads as rewritten:

"(a) The Commissioner shall issue an intermediary license or an exemption from the license, subject to G.S. 58-9-2(b)(2) or G.S. 58-9-2(c)(3), to any person who has complied with the requirements of this Article. A license issued to a non corporate entity authorizes all of the members of the entity and any designated employees to act as intermediaries under the license, and those persons shall be named in the application and any supplements. A license issued to a corporation authorizes all of the officers and any designated employees and directors of the corporation to act as intermediaries on behalf of the corporation, and those persons shall be named in the application and any supplements."

SECTION 10.2. G.S. 58-9-11(b) reads as rewritten:

"(b) An insurer shall not engage the services of any person to act as a broker on its behalf unless the person is licensed under ~~G.S. 58-9-6.~~G.S. 58-9-6 or exempted under this Article. An insurer shall not employ an individual who is employed by a broker with which it transacts business, unless the broker is under common control with the insurer under Article 19 of this Chapter."

SECTION 10.3. G.S. 58-9-21(a) reads as rewritten:

"(a) A reinsurer shall not engage the services of any person to act as a manager on its behalf unless the person is licensed under ~~G.S. 58-9-6.~~G.S. 58-9-6 or exempted under this Article."

PART XI. MORTGAGE GUARANTY INSURANCE.

SECTION 11. Article 10 of Chapter 58 of the General Statutes is amended by adding the following new Part to read:

"Part 5. Mortgage Guaranty Insurance.

"**§ 58-10-120. Definitions.**

As used in this Part:

(1) 'Mortgage guaranty insurers report of policyholders position' means the annual supplementary report required by the Commissioner.

(2) 'Policyholders position' means the contingency reserve established under G.S. 58-10-135 and policyholders' surplus. 'Minimum policyholders position' is calculated as described in G.S. 58-10-125.

(3) 'Policyholders surplus' means an insurer's net worth; the difference between its assets and liabilities, as reported in its annual statement.

"**§ 58-10-125. Minimum policyholders position.**

(a) For the purpose of complying with G.S. 58-7-75, a mortgage guaranty insurer shall maintain at all times a minimum policyholders position in the amount required by this section. The policyholders position shall be net of reinsurance ceded but shall include reinsurance assumed.

(b) If a mortgage guaranty insurer does not have the minimum amount of policyholders position required by this section it shall cease transacting new business until the time that its policyholders position is in compliance with this section.

(c) If a policy of mortgage guaranty insurance insures individual loans with a percentage claim settlement option on those loans, a mortgage guaranty insurer shall maintain a policyholders position based on each one hundred dollars ($100.00) of the face amount of the mortgage, the percentage coverage, and the loan-to-value category. The minimum amount of policyholders position shall be calculated in the following manner:

(1) If the loan-to-value is greater than seventy-five percent (75%), the minimum policyholders position per one hundred dollars ($100.00) of the face amount of the mortgage for the specific percent coverage shall be as shown in the schedule below:

Percent Coverage	Policyholders Position Per $100 of the Face Amount of the Mortgage	Percent Coverage	Policyholders Position Per $100 of the Face Amount of the Mortgage

5	$0.20	55	$1.50
10	0.40	60	1.55
15	0.60	65	1.60
20	0.80	70	1.65
25	1.00	75	1.75
30	1.10	80	1.80
35	1.20	85	1.85
40	1.30	90	1.90
45	1.35	95	1.95
50	1.40	100	2.00

(2) If the loan-to-value is at least fifty percent (50%) and not more than seventy-five percent (75%), the minimum amount of the policyholders position shall be fifty percent (50%) of the minimum of the amount calculated under subdivision (c)(1) of this section.

(3) If the loan-to-value is less than fifty percent (50%), the minimum amount of policyholders position shall be twenty-five percent (25%) of the amount calculated under subdivision (c)(1) of this section.

(d) If a policy of mortgage guaranty insurance provides coverage on a group of loans subject to an aggregate loss limit, the policyholders position shall be:

(1) If the equity is not more than fifty percent (50%) and is at least twenty percent (20%), or equity plus prior insurance or a deductible is at least twenty-five percent (25%) and not more than fifty-five percent (55%), the minimum amount of policyholders position shall be calculated as follows:

Percent Coverage	Policyholders Position Per $100 of the Face Amount of the Mortgage	Percent Coverage	Policyholders Position Per $100 of the Face Amount of the Mortgage
1	$0.30	50	$0.825
5	0.50	60	0.85
10	0.60	70	0.875
15	0.65	75	0.90
20	0.70	80	0.925
25	0.75	90	0.95
30	0.775	100	1.00
40	0.80		

(2) If the equity is less than twenty percent (20%), or the equity plus prior insurance or a deductible is less than twenty-five percent (25%), the minimum amount of policyholders position shall be two hundred percent (200%) of the amount required by subdivision (d)(1) of this section.

(3) If the equity is more than fifty percent (50%), or the equity plus prior insurance or a deductible is more than fifty-five percent (55%), the minimum amount of policyholders position shall be fifty percent (50%) of the amount required by subdivision (d)(1) of this section.

(e) If a policy of mortgage guaranty insurance provides for layers of coverage, deductibles, or excess reinsurance, the minimum amount of policyholders position shall be computed by subtraction of the minimum position for the lower percentage coverage limit from the minimum position for the upper or greater coverage limit.

(f) If a policy of mortgage guaranty insurance provides for coverage on loans secured by junior liens, the policyholders position shall be:

(1) If the policy provides coverage on individual loans, the minimum amount of policyholders position shall be calculated as in subsection (c) of this section as follows:
a. The loan-to-value percent is the entire loan indebtedness on the property divided by the value of the property;
b. The percent coverage is the insured portion of the junior loan divided by the entire loan indebtedness on the collateral property; and
c. The face amount of the insured mortgage is the entire loan indebtedness on the property.
(2) If the policy provides coverage on a group of loans subject to an aggregate loss limit, the policyholders position shall be calculated according to subsection (d) of this section as follows:
a. The equity is the complement of the loan-to-value percent calculated as in subdivision (d)(1) of this section;
b. The percent coverage is calculated as in subdivision (d)(1) of this section; and
c. The face amount of the insured mortgage is the entire loan indebtedness on the property.

(g) If a policy of mortgage guaranty insurance provides for coverage on leases, the policyholders position shall be four dollars ($4.00) for each one hundred dollars ($100.00) of the insured amount of the lease.

(h) If a policy of mortgage guaranty insurance insures loans with a percentage loss settlement option coverage between any of the entries in the schedules in this section, then the factor for policyholders position per one hundred dollars ($100.00) of the face amount of the mortgage shall be prorated between the factors for the nearest percent coverage listed.

"**§ 58-10-130. Unearned premium reserve.**

(a) The unearned premium reserve shall be computed as follows:
(1) The unearned premium reserve for premiums paid in advance annually shall be calculated on the monthly pro rata fractional basis.
(2) Premiums paid in advance for 10-year coverage shall be placed in the unearned premium reserve and shall be released from this reserve as follows:
a. 1st month - 1/132;
b. 2nd through 12th month - 2/132 each month;
c. 13th month - 3/264;
d. 14th through 120th month - 1/132 per month;
e. 121st month - 1/264.
(3) Premiums paid in advance for periods in excess of 10 years. During the first 10 years of coverage the unearned portion of the premium shall be the premium collected minus an amount equal to the premium that would have been earned had the applicable premium for 10 years of coverage been received. The premium remaining after 10 years shall be released from the unearned premium reserve monthly pro rata over the remaining term of coverage.

(b) Fifty percent (50%) of the premium remaining after establishment of the premium reserve specified in subsection (a) of this section shall be maintained as a special contingency reservation of premium and reported in the financial statement as a liability.

(c) The case basis method shall be used to determine the loss reserve which shall include a reserve for claims reported and unpaid and a reserve for claims incurred but not reported.

"**§ 58-10-135. Contingency reserve.**

(a) Subject to G.S. 58-7-21, a mortgage guaranty insurer shall make an annual contribution to the contingency reserve which in the aggregate shall be the greater of:

(1) Fifty percent (50%) of the net earned premium reported in the annual statement; or

(2) The sum of:

a. The policyholders position established under G.S. 58-10-125 on residential buildings designed for occupancy by not more than four families divided by seven;

b. The policyholders position established under G.S. 58-10-125 on residential buildings designed for occupancy by five or more families divided by five;

c. The policyholders position established under G.S. 58-10-125 on buildings occupied for industrial or commercial purposes divided by three; and

d. The policyholders position established under G.S. 58-10-125 for leases divided by 10.

(b) If the mortgage guaranty coverage is not expressly provided for in this section, the Commissioner may establish a rate formula factor that will produce a contingency reserve adequate for the risk assumed.

(c) The contingency reserve established by this section shall be maintained for 120 months. That portion of the contingency reserve established and maintained for more than 120 months shall be released and shall no longer constitute part of the contingency reserve.

(d) With the approval of the Commissioner, withdrawals may be made from the contingency reserve when incurred losses and incurred loss expenses exceed the greater of either thirty-five percent (35%) of the net earned premium or seventy percent (70%) of the amount which subsection (a) of this section requires to be contributed to the contingency reserve in such year. On a quarterly basis, provisional withdrawals may be made from the contingency reserve in an amount not to exceed seventy-five percent (75%) of the withdrawal calculated in accordance with subdivision (d)(1) of G.S. 58-10-125.

(e) With the approval of the Commissioner, a mortgage guaranty insurer may withdraw from the contingency reserve any amounts which are in excess of the minimum policyholders position as filed with the most recently filed annual statement. In reviewing a request for withdrawal pursuant to this subsection, the Commissioner may consider loss development and trends. If any portion of the contingency reserve for which withdrawal is requested pursuant to this subsection is maintained by a reinsurer, the Commissioner may also consider the financial condition of the reinsurer. If any portion of the contingency reserve for which withdrawal is requested pursuant to this subsection is maintained in a segregated account or segregated trust and such withdrawal would result in funds being removed from the segregated account or segregated trust, the Commissioner may also consider the financial condition of the reinsurer.

(f) Releases and withdrawals from the contingency reserve shall be accounted for on a first-in-first-out basis as prescribed by the Commissioner.

(g) The calculations to develop the contingency reserve shall be made in the following sequence:

(1) The additions required by subsections (a) and (b) of this section;

(2) The releases permitted by subsection (c) of this section;

(3) The withdrawals permitted by subsection (d) of this section; and

(4) The withdrawals permitted by subsection (e) of this section.

(h) Whenever the laws or regulations of another jurisdiction in which a mortgage guaranty insurer, subject to the requirements of this Part is licensed, require a larger unearned premium reserve or a larger contingency reserve in the aggregate than that set

forth in this Part, the establishment and maintenance of the larger unearned premium reserve or contingency reserve shall be deemed to be in compliance with this Part."

PART XII. RISK-BASED CAPITAL REQUIREMENTS.

SECTION 12.1. G.S. 58-12-2(3) reads as rewritten:

"(3) Domestic insurer. – Any insurance company or health organization organized in this State under Article ~~77~~ 7, 15, 65, or 67 of this Chapter."

SECTION 12.2. G.S. 58-12-2(4) reads as rewritten:

"(4) Foreign insurer. – Any insurance company or health organization that is admitted to do business in this State under Article 16 or 67 of this Chapter but is not domiciled in this State."

SECTION 12.3. G.S. 58-12-2 is amended by adding the following new subdivision to read:

"(4b) Health organization. – Any health maintenance organization, limited health service organization, dental or vision plan, hospital, medical, or dental indemnity or service corporation, or other organization licensed under Article 65 or 67 of this Chapter. 'Health organization' does not include an insurer that is licensed as either a life or health insurer or a property or casualty insurer under this Chapter and that is otherwise subject to either the life or property and casualty risk-based capital requirements."

SECTION 12.4. G.S. 58-12-6(d) reads as rewritten:

"(d) A property or casualty insurer's risk-based capital and a health organization's risk-based capital shall be determined in accordance with the formula set forth in the risk-based capital instructions. The formula shall take into account (and may adjust for the covariance between):

(1) Asset risk;
(2) Credit risk;
(3) Underwriting risk; and
(4) All business and other relevant risks set forth in the risk-based capital instructions, determined in each case by applying the factors in the manner set forth in the risk-based capital instructions."

SECTION 12.5. G.S. 58-12-11(a)(1)a. reads as rewritten:

"a. The insurer's total adjusted capital is greater than or equal to its regulatory action level risk-based capital but less than its company action level risk-based ~~capital;~~ capital, if the insurer is a property or casualty insurer or a health organization; or".

SECTION 12.6. G.S. 58-12-11(b)(3) reads as rewritten:

"(3) Provides forecasts of the insurer's financial results in the current year and at least the four succeeding years, both in the absence of proposed corrective actions and giving effect to the proposed corrective actions, including forecasts of statutory operating income, net income, capital, or surplus (the forecasts for both new and renewal business should include separate forecasts for each major line of business and separately identify each significant income, expense, and benefit component). For a health organization, the forecasted financial results shall be for the current year and at least two succeeding years and shall include statutory balance sheets, operating income, net income, capital and surplus, and risk-based capital levels."

SECTION 12.7. G.S. 58-12-25(b) reads as rewritten:

"(b) In the event of a mandatory control level ~~event,~~ event with respect to a life insurer or a health organization, the Commissioner shall take actions as are necessary to cause the insurer to be placed under regulatory control under Article 30 of this Chapter. The mandatory control level event is sufficient grounds for the Commissioner to take

action under Article 30 of this Chapter, and the Commissioner shall have the rights, powers, and duties with respect to the insurer as are set forth in Article 30 of this Chapter. If the Commissioner takes actions pursuant to an adjusted risk-based capital report, the insurer shall be entitled to such protections as are afforded to insurers under the provisions of Article 30 of this Chapter pertaining to summary proceedings. Notwithstanding any of the foregoing, the Commissioner may forego action for up to 90 days after the mandatory control level event if the Commissioner finds there is a reasonable expectation that the mandatory control level event may be eliminated within the 90-day period."

SECTION 12.8. G.S. 58-12-25 is amended by adding the following new subsection to read:

"(c) In the event of a mandatory control level event with respect to a property and casualty insurer, the Commissioner shall take actions as are necessary to cause the insurer to be placed under regulatory control under Article 30 of this Chapter, or, in the case of an insurer which is writing no business and which is running off its existing business, may allow the insurer to continue its runoff under the supervision of the Commissioner. In either event, the mandatory control level event is sufficient grounds for the Commissioner to take action under Article 30 of this Chapter, and the Commissioner shall have the rights, powers, and duties with respect to the insurer as are set forth in Article 30 of this Chapter. If the Commissioner takes actions under an adjusted risk-based capital report, the insurer shall be entitled to such protections as are afforded to insurers under the provisions of Article 30 of this Chapter pertaining to summary proceedings. Notwithstanding any of the foregoing, the Commissioner may forego action for up to 90 days after the mandatory control level event if the Commissioner finds there is a reasonable expectation that the mandatory control level event may be eliminated within the 90-day period."

SECTION 12.9. Article 12 of Chapter 58 of the General Statutes is amended by adding the following new section to read:

"**§ 58-12-65. Health organization phase-in provision.**

For risk-based capital reports required to be filed by health organizations with respect to calendar year 2001, the following requirements apply in lieu of the provisions of G.S. 58-12-11, 58-12-16, 58-12-21, and 58-12-25:

(1) In the event of a company action level event with respect to a domestic insurer, the Commissioner shall take no regulatory action under this Article.

(2) In the event of a regulatory action level event under G.S. 58-12-16(a)(1), (2), or (3), the Commissioner shall take the actions required under G.S. 58-12-11.

(3) In the event of a regulatory action level event under G.S. 58-12-16(a)(4), (5), (6), (7), (8), or (9), or an authorized control level event, the Commissioner shall take the actions required under G.S. 58-12-16 with respect to the insurer.

(4) In the event of a mandatory control level event with respect to an insurer, the Commissioner shall take the actions required under G.S. 58-12-21 with respect to the insurer."

SECTION 12.10. Article 12 of Chapter 58 of the General Statutes is amended by adding a new section to read:

"**§ 58-12-70. HMO net worth requirements.**

The Commissioner may require an HMO to have and maintain a larger amount of net worth than prescribed in G.S. 58-67-110, based upon the principles of risk-based capital as determined by the NAIC or the Commissioner."

PART XIII. INSURANCE COMPANY ASSET PROTECTION.

SECTION 13.1. G.S. 58-13-10 reads as rewritten:

"**§ 58-13-10. Scope.**

This Article applies to all domestic insurers and to all kinds of insurance written by those insurers under ~~Articles 1 through 68 of~~ this Chapter. Foreign insurers shall comply in substance with the requirements and limitations of this Article. ~~This Article does not apply to variable contracts for which separate accounts are required to be maintained nor to statutory deposits that are required to be maintained by insurance regulatory agencies as a requirement for doing business in such jurisdictions.~~This Article does not apply to the following:

(1) Variable contracts or guaranteed investment contracts for which separate accounts are required to be maintained.

(2) Statutory deposits that are required by insurance regulatory agencies to be maintained as a requirement for doing business in such jurisdictions.

(3) Real estate, authorized under G.S. 58-7-187, encumbered by a mortgage loan with a first lien."

SECTION 13.2. G.S. 58-13-15(3) reads as rewritten:

"(3) "Reserve assets" means those assets of an insurer that are authorized investments for policy reserves in accordance with ~~Articles 1 through 64 of this Chapter and G.S. 58-65-95.~~this Chapter."

SECTION 13.3. G.S. 58-13-15(4) reads as rewritten:

"(4) "Policyholder-related liabilities" means those liabilities that are required to be established by an insurer for all of its outstanding insurance policies in accordance with ~~Articles 1 through 64 of this Chapter and G.S. 58-65-95.~~this Chapter."

SECTION 13.4. G.S. 58-13-20(b) reads as rewritten:

"(b) The Commissioner has the right to examine any of such assets, reinsurance agreements, or deposit arrangements at any time in accordance with his authority to make examinations of insurers as conferred by other provisions ~~of Articles 1 through 64~~ of this Chapter."

PART XIV. FOREIGN INSURANCE COMPANIES.

SECTION 14.1. G.S. 58-16-5 reads as rewritten:

"**§ 58-16-5. Conditions of ~~admission.~~licensure.**

A foreign or alien insurance company may be ~~admitted and authorized~~ licensed to do business when it:

(1) Deposits with the Commissioner a certified copy of its charter or certificate of organization and a statement of its financial condition and business, in ~~such~~ the form and detail ~~as he~~ that the Commissioner requires, signed and sworn to by its president and secretary or other proper officer, and pays for the filing of this statement the sum required by law.

(2) Satisfies the Commissioner that it is fully and legally organized under the laws of its state or government to do the business it proposes to ~~transact,~~ transact as direct insurance or assumed reinsurance, and that it has been successful in the conduct of ~~such~~ the business; that it has, if a stock company, a free surplus and a fully paid-up and unimpaired capital, exclusive of stockholders' obligations of any description of an amount not less than that required for the organization of a domestic company writing the same kinds of business; and if a mutual company that its free surplus is not less than that required for the organization of a domestic company writing the same kind of business, and that ~~such~~ the capital, surplus, and other funds are invested ~~in substantial~~ substantially in accordance with the requirements of ~~Articles 1 through 64 of~~ this Chapter.

(3) Repealed by Session Laws 1995, c. 517, s. 6.

(4) Repealed by Session Laws 1987, c. 629, s. 20.

(5) Files with the Commissioner a certificate that it has complied with the laws of the state or government under which it was organized and is authorized to make contracts of insurance.

(6) Satisfies the Commissioner that it is in substantial compliance with ~~the provisions of~~ G.S. 58-7-21, 58-7-26, 58-7-30, and 58-7-31 and Article 13 of this Chapter.

(7) Satisfies the Commissioner that it is in compliance with the company name requirements of G.S. 58-7-35.

(8) Satisfies the Commissioner that the operation of the company in this State would not be hazardous to prospective policyholders, creditors, or the general public.

(9) Satisfies the Commissioner that it is in substantial compliance with the requirements of G.S. 58-7-37 pertaining to the background of its officers and directors.

(10) Files with the Commissioner an instrument appointing the Commissioner as the company's agent on whom any legal process under G.S. 58-16-30 may be served. This appointment is irrevocable as long as any liability of the company remains outstanding in this State. A copy of this instrument, certified by the Commissioner, is sufficient evidence of this appointment; and service upon the Commissioner is sufficient service upon the company."

SECTION 14.2. G.S. 58-16-6 reads as rewritten:

"**§ 58-16-6. Conditions of continued licensure.**

In order for a foreign insurance company to continue to be licensed, it shall report any changes in the documents filed under G.S. 58-16-5(1) or G.S. 58-16-5(5), maintain the amounts of capital and surplus specified in G.S. 58-16-5(2), and remain in substantial compliance with the statutes listed in ~~G.S. 58-16-5(6) and G.S. 58-16-5(7).~~ G.S. 58-16-5(6), (7), and (8)."

PART XV. PROMOTING AND HOLDING COMPANIES.

SECTION 15. Article 18 of Chapter 58 of the General Statutes, comprising G.S. 58-18-1 through G.S. 58-18-25 is repealed.

PART XVI. INSURANCE HOLDING COMPANY SYSTEMS.

SECTION 16.1. G.S. 58-19-5(5) reads as rewritten:

"(5) "Person" means an individual, corporation, partnership, limited liability company, association, joint stock company, trust, unincorporated organization, or any similar entity or any combination of the foregoing acting in concert."

SECTION 16.2. The introductory paragraph of G.S. 58-19-10(b) reads as rewritten:

"(b) In addition to investments in common stock, preferred stock, debt obligations, and other securities permitted under ~~all other sections of Articles 1 through 64 of~~ this Chapter, a domestic insurer may also:".

SECTION 16.3. G.S. 58-19-10(b)(1) reads as rewritten:

"(1) Invest, in common stock, preferred stock, debt obligations, and other securities of one or more subsidiaries, amounts that do not exceed the lesser of ten percent (10%) of ~~such~~ the insurer's admitted assets or fifty percent (50%) of ~~such~~ the insurer's ~~surplus as regards policyholders,~~ policyholders' surplus, provided that after ~~such~~ those investments, the insurer's ~~surplus as regards policyholders~~ policyholders' surplus will be reasonable in relation to the insurer's outstanding liabilities and adequate to its financial needs. In calculating the amount of ~~such~~ the investments, investments in domestic or foreign insurance subsidiaries and health maintenance organizations shall be excluded, and there

shall be included: (i) total net monies or other consideration expended and obligations assumed in the acquisition or formation of a subsidiary, including all organizational expenses and contributions to capital and surplus of ~~such~~the subsidiary whether or not represented by the purchase of capital stock or issuance of other securities; and (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;".

SECTION 16.4. G.S. 58-19-10(b)(3) reads as rewritten:

"(3) With the approval of the Commissioner, invest any greater amount in common stock, preferred stock, debt obligations, or other securities of one or more subsidiaries; provided that after such investment the insurer's ~~surplus as regards policyholders~~ policyholders' surplus will be reasonable in relation to the insurer's outstanding liabilities and adequate to its financial needs."

SECTION 16.5. G.S. 58-19-15(h) reads as rewritten:

"(h) The provisions of this section do not apply to any offer, request, invitation, agreement, or acquisition that the Commissioner by order exempts therefrom as (i) not having been made or entered into for the purpose and not having the effect of changing or influencing the control of a domestic insurer, or (ii) as otherwise not comprehended within the purposes of this section. Any acquisition of stock of a former domestic mutual insurer by a parent company that occurs in connection with the conversion of a mutual insurer to a stock insurer under G.S. 58-10-10 is not subject to this section, provided that no person acquires control of the parent company."

SECTION 16.6. G.S. 58-19-25(a) reads as rewritten:

"(a) Every insurer that is licensed to do business in this State and that is a member of an insurance holding company system shall register with the Commissioner, except a foreign insurer subject to the registration requirements and standards adopted by statute or regulation in the jurisdiction of its domicile that are substantially similar to those contained ~~in this section and G.S. 58-19-30 or a provision such as the following: Each registered insurer shall keep current the information required to be disclosed in its registration statement by reporting all material changes or additions within 15 days after the end of the month in which it learns of each change or addition. The insurer shall also file a copy of its registration statement and any amendments to the statement in each state in which that insurer is authorized to do business if requested by the insurance regulator of that state.~~ in:

(1) This section.

(2) G.S. 58-19-30(a), G.S. 58-19-30(c), and G.S. 58-19-30(d).

(3) G.S. 58-19-30(b) or a statutory or regulatory provision such as the following: Each registered insurer shall keep current the information required to be disclosed in its registration statement by reporting all material changes or additions within 15 days after the end of the month in which it learns of each change or addition. The insurer shall also file a copy of its registration statement and any amendments to the statement in each state in which that insurer is authorized to do business, if requested by the insurance regulator of that state.

Any insurer that is subject to registration under this section shall register within 30 days after it becomes subject to registration, and an amendment to the registration statement shall be filed by ~~March 1~~ April 1 of each year for the previous calendar year; unless the Commissioner for good cause shown extends the time for registration or filing, and then within the extended time. All registration statements shall contain a summary, on a form prescribed by the Commissioner, outlining all items in the current registration statement representing changes from the prior registration statement. The Commissioner may require any insurer that is a member of a holding company system that is not subject to

registration under this section to furnish a copy of the registration statement or other information filed by the insurance company with the insurance regulator of its domiciliary jurisdiction."

SECTION 16.7. G.S. 58-19-30(b)(4) reads as rewritten:

"(4) All management agreements, service contracts, guarantees, or cost-sharing arrangements."

PART XVII. SURPLUS LINES INSURANCE.

SECTION 17.1. G.S. 58-21-20(a)(2) reads as rewritten:

"(2) Qualifies under one of the following subdivisions:

a. Has capital and surplus or its equivalent under the laws of its domiciliary jurisdiction, which equals either:

1. This State's minimum capital and surplus requirements under G.S. 58-7-75, or
2. Fifteen million dollars ($15,000,000),

whichever is greater, except that nonadmitted insurers already qualified under this Article must have ten million dollars ($10,000,000) by December 31, 1991, twelve million five hundred thousand dollars ($12,500,000) by December 31, 1992, and fifteen million dollars ($15,000,000) by December 31, 1993. The requirements of this sub-subdivision may be satisfied by an insurer possessing less than the commitment capital and surplus upon an affirmative finding of acceptability by the Commissioner. The finding shall be based upon such factors as quality of management, capital and surplus of any parent company, company underwriting profit and investment income trends, and the insurer's record and reputation within the industry. In no event shall the Commissioner make an affirmative finding of acceptability when the insurer's capital and surplus is less than four million five hundred thousand dollars ($4,500,000).

In addition, an alien insurer qualifies under this subdivision if it complies with the capital and surplus requirements of this subdivision and maintains in the United States an irrevocable trust fund in either a national bank or a member of the Federal Reserve System, in an amount not less than ~~two million five hundred thousand dollars ($2,500,000)~~ five million four hundred thousand dollars ($5,400,000) for the protection of all of its policyholders in the United States, and the trust fund consists of cash, securities, letters of credit, or of investment of substantially the same character and quality as those which are eligible investments for the capital and statutory reserves of admitted insurers authorized to write like kinds of insurance in this State. The trust fund, which shall be included in any calculation of capital and surplus or its equivalent, shall have an expiration date which at no time shall be less than five years; or

b. In the case of any Lloyd's plans or other similar ~~unincorporated~~ group of insurers, which ~~includes individual insurers,~~ consists of unincorporated individual insurers, or a combination of both unincorporated and incorporated insurers, maintains a trust fund in an amount of not less than ~~fifty million dollars ($50,000,000)~~ one hundred million dollars ($100,000,000) as security to the full amount thereof for all policyholders and creditors in the United States of each member of the group, and the trust shall

likewise comply with the terms and conditions established in subdivision (2)a. of this section for alien insurers; and

c. In the case of an "insurance exchange" created by the laws of individual states, maintain capital and surplus, or the substantial equivalent thereof, of not less than ~~fifty million dollars ($50,000,000)~~ seventy-five million dollars ($75,000,000) in the aggregate. For insurance exchanges which maintain funds in an amount of not less than fifteen million dollars ($15,000,000) for the protection of all insurance exchange policyholders, each individual syndicate shall maintain minimum capital and surplus, or the substantial equivalent thereof, of not less than ~~three million dollars ($3,000,000).~~ five million dollars ($5,000,000). If the insurance exchange does not maintain funds in an amount of not less than fifteen million dollars ($15,000,000) for the protection of all insurance exchange policyholders, each individual syndicate shall meet the minimum capital and surplus requirements of subdivision (2)a. of this section.

d. In the case of a group of incorporated insurers under common administration, which has continuously transacted an insurance business outside the United States for at least three years immediately before this time, and which submits to this State's authority to examine its books and records and bears the expense of the examination, and maintains an aggregate policyholders' surplus of not less than ten billion dollars ($10,000,000,000), and maintains in trust a surplus of not less than one hundred million dollars ($100,000,000) for the benefit of United States surplus lines policyholders of any member of the group, and each insurer maintains capital and surplus of not less than twenty-five million dollars ($25,000,000) per company."

SECTION 17.2. G.S. 58-21-30 reads as rewritten:

"**§ 58-21-30. Withdrawal of eligibility from a surplus lines insurer.**

If at any time the Commissioner has reason to believe that an eligible surplus lines insurer:

(1) Is in unsound financial ~~condition,~~condition or has acted in an untrustworthy manner,
(2) Is no longer eligible under G.S. 58-21-20,
(3) Has willfully violated the laws of this State, or
(4) Does not make reasonably prompt payment of just losses and claims in this State or elsewhere, the Commissioner may declare it ineligible. The Commissioner shall promptly mail notice of all such declarations to each surplus lines licensee."

PART XVIII. RISK RETENTION GROUPS.

SECTION 18. G.S. 58-22-10(3) reads as rewritten:

"(3) "Hazardous financial condition" means that, based on its present or reasonably anticipated financial condition, a risk retention ~~group,~~ group is insolvent or, although not yet financially impaired or insolvent, is unlikely to be able:

a. To meet obligations to policyholders with respect to known claims and reasonably anticipated claims; or
b. To pay other obligations in the normal course of business."

PART XIX. INSURANCE COMPANY RECEIVERSHIPS.

SECTION 19. G.S. 58-30-75(7) reads as rewritten:

"(7) Without first obtaining the written consent of the ~~Commissioner pursuant to G.S. 58-7-150,~~ Commissioner, the insurer has (i) transferred, or attempted to transfer, in a manner contrary to Article 19 of this Chapter, substantially its entire property or business, or (ii) has entered into any transaction, the effect of which is to merge, consolidate, or reinsure substantially its entire property or business in or with the property or business of any other person."

PART XX. MANAGING GENERAL AGENTS.

SECTION 20.1. G.S. 58-34-2(a) reads as rewritten:

"(a) As used in this Article:

(1) "Control", including the terms "controlling", "controlled by", and "under common control", means the direct or indirect possession of the power to direct or cause the direction of the management and policies of a person, whether through the ownership of voting securities, by contract other than a commercial contract for goods or nonmanagement services, or otherwise, unless the power is the result of an official position with or corporate office held by the person.

(1a) "Custodial agreement" means any agreement or contract under which any person is delegated authority to safekeep assets of the insurer.

(2) "Insurer" means a domestic insurer but does not mean a reciprocal regulated under Article 15 of this Chapter.

(2a) "Management contract" means any agreement or contract under which any person is delegated management duties or control of an insurer or transfers a substantial part of any major function of an insurer, such as adjustment of losses, production of business, investment of assets, or general servicing of the insurer's business.

(3) "Managing general agent" or "MGA" means any person who manages all or part of the insurance business of an insurer (including the management of a separate division, department, or underwriting office) and acts as an agent for the insurer, whether known as a managing general agent, manager, or other similar term, who, with or without the authority, either separately or together with persons under common control, produces, directly or indirectly, and underwrites an amount of gross direct written premium equal to or more than five percent (5%) of the policyholder surplus as reported in the last annual statement of the insurer in any one quarter or year together with one or more of the following activities related to the business produced: (i) adjusts or pays any claims, or (ii) negotiates reinsurance on behalf of the insurer. "MGA" does not mean an employee of the insurer; an underwriting manager who, pursuant to contract, manages all or part of the insurance operations of the insurer, is under common control with the insurer, is subject to Article 19 of this Chapter, and whose compensation is not based on the volume of premiums written; a person who, under Article 15 of this Chapter, is designated and authorized by subscribers as the attorney-in-fact for a reciprocal having authority to obligate them on reciprocal and other insurance contracts; or a U.S. Manager of the United States branch of an alien insurer.

(4) "Qualified actuary" means a person who meets the standards of a qualified actuary as specified in the NAIC Annual Statement Instructions, as amended or clarified by rule, order, directive, or bulletin of the Department, for the type of insurer for which the MGA is establishing loss reserves.

(5) "Underwrite" means the authority to accept or reject risk on behalf of the insurer."

SECTION 20.2. G.S. 58-34-2(j) reads as rewritten:

"(j) The Commissioner shall disapprove any such contract that:

(1) Does not contain the required contract provisions specified in subsection (d) of this section;

(2) Subjects the insurer to excessive charges for expenses or commission;

(3) Vests in the MGA any control over the management of the affairs of the insurer to the exclusion of the board of directors of the insurer;

(4) Is entered into with any person if the person or its officers and directors are of known bad character or have been affiliated directly or indirectly through ownership, control, management, reinsurance transactions, or other insurance or business relationships with any person known to have been involved in the improper manipulation of assets, accounts, or reinsurance; or

(5) Is determined by the Commissioner to contain provisions that are not fair and reasonable to the insurer.

Failure of the Commissioner to disapprove any such contract within 30 days after the contract has been filed with the Commissioner constitutes the Commissioner's approval of the contract. An insurer may continue to accept business from ~~such~~ the person until the Commissioner disapproves the contract. Any disapproval shall be in writing. The Commissioner ~~may, after a hearing held under G.S. 58-2-50,~~ may withdraw approval of any contract the Commissioner has previously approved ~~upon finding~~ if the Commissioner determines that the basis of the original approval no longer exists or that the contract has, in actual operation, shown itself to be subject to disapproval on any of the grounds in this subsection. If the Commissioner withdraws approval of a contract, the Commissioner shall give the insurer notice of, and written reasons for, the withdrawal of approval. The Commissioner shall grant any party to the contract a hearing upon request."

SECTION 20.3. G.S. 58-34-10 reads as rewritten:

"**§ 58-34-10. Management contracts.**

(a) Subject to G.S. 58-19-30(b)(4), any domestic insurer that enters into a management contract or custodial agreement must file that contract or agreement with the Commissioner on or before its effective date. ~~As used in this section, "management contract" means any agreement or contract under which any person is delegated management duties or control of an insurer, or transfers a substantial part of any major function of an insurer, such as adjustment of losses, production of business, investment of assets, or general servicing of the insurer's business.~~

(b) Any domestic insurer that has a management contract or custodial agreement shall file a statement with the initial filing of that contract that discloses (i) criteria on which charges to the insurer are based for that contract; (ii) whether management personnel or other employees of the insurer are to be performing management functions and receiving any remuneration therefor through that contract in addition to the compensation by way of salary received directly from the insurer for their services; (iii) whether the contract transfers substantial control of the insurer or any of the powers vested in the board of directors, by statute, articles of incorporation, or bylaws, or substantially all of the basic functions of the insurer's management; (iv) biographical information for each officer and director of the management firm; and (v) other information concerning the contract or the management or custodian firm as may be included from time to time in any registration forms adopted or approved by the Commissioner. ~~Such~~ The statement shall be filed on a form prescribed by the Commissioner.

(c) Any domestic insurer that amends or cancels a management contract or custodial agreement filed ~~pursuant to~~ under subsection (a) of this section shall notify the Commissioner ~~thereof~~ within 15 business days after the amendment or cancellation. If

the contract is amended, the notice shall provide a copy of the amended contract and shall disclose if the amendment affects any of the items in subsection (b) of this section. The Commissioner may prescribe a form to be used to provide notice under this subsection.

(d) Any domestic insurer that has a management contract or custodial agreement shall file a statement on or before March 1 of each year, for the preceding calendar year, disclosing (i) total charges incurred by the insurer under the contract; (ii) any salaries, commissions, or other valuable consideration paid by the insurer directly to any officer, director, or shareholder of the management or custodian firm; and (iii) other information concerning the contract or the management or custodian firm as may be included from time to time in any registration forms adopted or approved by the Commissioner. The Commissioner may prescribe a form to be used to provide the information required by this subsection.

(e) Any domestic insurer that has a management contract may request an exemption from the filing requirements of this section if the contract is for a group of affiliated insurers on a pooled funds basis or service company management basis, where costs to the individual member insurers are charged on an actually incurred or closely estimated basis. The request for an exemption must be in writing, must explain the basis for the exemption, and must be received by the Commissioner on or before the effective date of the contract. As used in this subsection, "affiliated" has the same meaning as in G.S. 58-19-5(1). Management contracts exempted under this subsection must still be reduced to written form."

SECTION 20.4. G.S. 58-34-15 reads as rewritten:

"**§ 58-34-15. Grounds for disapproval.**

(a) The Commissioner must disapprove any management contract or custodial agreement filed under G.S. 58-34-10 if, at any time, the Commissioner finds:

(1) That the service or management charges are based upon criteria unrelated either to the managed insurer's profits or to the reasonable customary and usual charges for ~~such~~ the services or are based on factors unrelated to the value of ~~such~~ the services to the insurer; or

(2) That management personnel or other employees of the insurer are to be performing management functions and receiving any remuneration ~~therefor~~for those functions through the management or service contract in addition to the compensation by way of salary received directly from the insurer for their services; or

(3) That the contract would transfer substantial control of the insurer or any of the powers vested in the board of directors, by statute, articles of incorporation, or bylaws, or substantially all of the basic functions of the insurance company management; or

(4) That the contract contains provisions that would be clearly detrimental to the best interest of policyholders, stockholders, or members of the insurer; or

(5) That the officers and directors of the management or custodial firm are of known bad character or have been affiliated, directly or indirectly, through ownership, control, management, reinsurance transactions, or other insurance or business relations with any person known to have been involved in the improper manipulation of assets, accounts, or reinsurance.

(6) That the custodial agreement is not substantially the same as the form adopted by the Commissioner.

(b) If the Commissioner disapproves any management ~~contract,~~ contract or custodial agreement, notice of ~~such action~~ the disapproval shall be given to the insurer ~~assigning~~ stating the reasons ~~therefor~~ for the disapproval in writing. The Commissioner shall grant any party to the contract a ~~hearing upon request according to G.S. 58-2-50.~~hearing if the party requests a hearing."

SECTION 20.5. G.S. 58-67-30 reads as rewritten:

"**§ 58-67-30. Management and ~~exclusive contracts.~~exclusive agreements; custodial agreements.**

(a) No health maintenance organization shall enter into an exclusive ~~agency contract or management contract~~ agency, management, or custodial agreement unless the ~~contract~~ agreement is first filed with the Commissioner and approved under this section within 45 days after filing or such reasonable extended period as the Commissioner shall specify by notice that is given within the 45 day period.

(b) The Commissioner shall disapprove ~~a contract~~ an agreement submitted under subsection (a) of this section if ~~he finds that:~~the Commissioner determines that the agreement:

(1) ~~It subjects~~ Subjects the health maintenance organization to excessive charges;

(2) ~~The contract extends~~ Extends for an unreasonable period of time;

(3) ~~The contract does~~ Does not contain fair and adequate standards of performance;

(4) ~~The persons empowered~~ Enables persons under the contract to manage the health maintenance organization ~~are not~~ who are not sufficiently trustworthy, competent, experienced, and free from conflict of interest to manage the health maintenance organization with due regard for the interests of its enrollees, creditors, or the public; or

(5) ~~The contract contains~~ Contains provisions that impair the interests of the organization's enrollees, creditors, or the public."

PART XXI. SELF-INSURED WORKERS' COMPENSATION.

SECTION 21.1. G.S. 58-47-60(9) reads as rewritten:

"(9) "Hazardous financial condition" means that, based on its present or reasonably anticipated financial condition, a person is insolvent or, although not financially impaired or insolvent, is unlikely to be ~~able to meet obligations for known claims and reasonably anticipated claims or to pay other obligations in the normal course of business.~~able:

a. To meet obligations for known claims and reasonably anticipated claims; or

b. To pay other obligations in the normal course of business."

SECTION 21.2. G.S. 58-47-80 reads as rewritten:

"**§ 58-47-80. Assets and invested assets.**

Funds shall be held and invested by the board under G.S. 58-7-160, 58-7-162, 58-7-163, 58-7-165, 58-7-167, 58-7-168, 58-7-170, 58-7-172, 58-7-173, ~~58-7-177,~~ 58-7-178, 58-7-179, 58-7-180, 58-7-183, 58-7-185, 58-7-187, 58-7-188, 58-7-192, 58-7-193, 58-7-195, 58-7-197, ~~and 58-7-200.~~ 58-7-200, and 58-19-10."

SECTION 21.3. Part 3 of Article 47 of Chapter 58 of the General Statutes, comprising G.S. 58-47-210 through G.S. 58-47-220, is repealed.

PART XXII. CONTINUING CARE RETIREMENT COMMUNITIES.

SECTION 22.1. G.S. 58-64-005(a) reads as rewritten:

"(a) No provider shall engage in the business of offering or providing continuing care in this State without a license to do so obtained from the Commissioner as provided in this Article. It is a Class 1 misdemeanor for any person, other than a provider licensed under this Article, to advertise or market to the general public any product similar to continuing care through the use of such terms as 'life care', 'continuing care', or 'guaranteed care for life', or similar terms, words, or phrases. The licensing process may involve a series of steps pursuant to rules adopted by the Commissioner under this Article."

SECTION 22.2. G.S. 58-64-20 is amended by adding the following new subsections:

"(e) The disclosure statement shall be in plain English and in language understandable by a layperson and combine simplicity and accuracy to fully advise residents of the items required by this section.

(f) The Department may require a provider to alter or amend its disclosure statement in order to provide full and fair disclosure to prospective residents. The Department may also require the revision of a disclosure statement which it finds to be unnecessarily complex, confusing or illegible."

SECTION 22.3 G.S. 58-64-40(b) reads as rewritten:

"(b) The board of directors or other governing body of a facility or its designated representative shall hold ~~annual~~ semiannual meetings with the residents of the facility for free discussions of subjects including, but not limited to, income, expenditures, and financial trends and problems as they apply to the facility and discussions of proposed changes in policies, programs, and services. Upon request of the most representative residents' organization, a member of the governing body of the provider, such as a board member, a general partner, or a principal owner shall attend such meetings. Residents shall be entitled to at least seven days advance notice of each meeting. An agenda and any materials that will be distributed by the governing body at the meetings shall remain available upon request to residents."

PART XXIII. MISCELLANEOUS TECHNICAL AMENDMENTS.

SECTION 23.1. The title of Article 4 of Chapter 58 of the General Statutes reads as rewritten:

"Article 4.

NAIC ~~Insurance Regulatory Information System.~~Filing Requirements."

SECTION 23.2. G.S. 58-5-63(a) reads as rewritten:

"(a) All insurance companies making deposits under this Article are entitled to interest on those ~~deposits, which shall remain in the deposit accounts.~~ deposits. The right to interest is subject to a company paying its insurance policy liabilities. If any company fails to pay those liabilities, interest accruing after the failure is payable to the Commissioner for the payment of those liabilities under subsection (b) of this section."

PART XXIV. INSURER INSOLVENCY REFUND THRESHOLDS.

SECTION 24.1. G.S. 58-5-70 reads as rewritten:

"**§ 58-5-70. Lien of policyholders; action to enforce.**

Upon the securities deposited with the Commissioner by any foreign or alien insurance company, the holders of all contracts of the company who are citizens or residents of this State at the time, or who hold policies issued upon property in the State, shall have a lien for ~~the~~ amounts in excess of fifty dollars ($50.00) due them, respectively, under or in consequence of the contracts for losses, equitable values, return premiums, or otherwise, and shall be entitled to be paid ratably out of the proceeds of the securities, if the proceeds are not sufficient to pay all of the contract holders. When any foreign or alien insurance company depositing securities under this Article becomes insolvent or bankrupt or makes an assignment for the benefit of its creditors, any holder of the contract may begin an action in the Superior Court of the County of Wake to enforce the lien for the benefit of all the holders of the contracts. The Commissioner shall be a party to the suit, and the funds shall be distributed by the court, but the cost of the action shall not be adjudged against the Commissioner."

SECTION 24.2. G.S. 58-30-10(12) reads as rewritten:

"(12) 'General assets' means all real, personal, or other property that is not specifically mortgaged, pledged, hypothecated, deposited, or otherwise encumbered for the security or benefit of specified persons or classes of persons. As to specifically encumbered property, 'general assets' includes all such property or its proceeds in excess of the amount necessary to discharge the sum or sums secured thereby. Assets that are held in trust and on deposit for the security or benefit of all

policyholders in more than one state or all policyholders and creditors in more than one state shall be treated as 'general assets'. No person shall have a claim against general assets unless that claim is in an amount in excess of fifty dollars ($50.00)."

SECTION 24.3. G.S. 58-30-10(19) reads as rewritten:

"(19) 'Special deposit claim' means any claim in excess of fifty dollars ($50.00) secured by a deposit made pursuant to statute for the security or benefit of a limited class or classes of persons, but does not include any claim secured by general assets."

SECTION 24.4. G.S. 58-48-95(c) reads as rewritten:

"(c) The Association shall account to the Commissioner and the insolvent insurer for all deposits received from the Commissioner under this ~~section, and shall repay to the Commissioner a portion of the deposits received, which shall be equal to the total amount of the claims against the insolvent insurer that are not covered claims under this Article solely by reason that the amount of the claim is fifty dollars ($50.00) or less. This repayment does not prejudice the rights of the Association with regard to the portion of the deposit repaid to the Commissioner.~~ section. After the deposits of the insolvent insurer received by the Association under this section have been expended by the Association for the purposes set out in this section, the member insurers shall be assessed as provided by this Article to pay any remaining liabilities of the Association arising under this Article."

SECTION 24.5. This section applies to estates that are pending.

PART XXV. DOMESTIC COMPANY PROTECTED CELLS.

SECTION 25. Article 10 of Chapter 58 of the General Statutes is amended by adding the following new Part:

"Part 4. Protected Cell Companies.

"**§ 58-10-75. Purpose and legislative intent.**

This Part provides 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. Investors in fully funded insurance securitization transactions provide funds that are available to pay the insurer's insurance obligations or to repay the investors or both. The creation of protected cells is intended to be a means to achieve more efficiencies in conducting insurance securitizations.

"**§ 58-10-80. Definitions.**

As used in this Part, unless the context requires otherwise, the following terms have the following meanings:

(1) 'Domestic insurer' means an insurer domiciled in the State of North Carolina.

(2) 'Fully funded' means that, with respect to any exposure attributed to a protected cell, the market 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 the 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 its incurring a specified level of losses under its insurance or reinsurance contracts.

(5) 'Fair value' means the amount at which that asset (or liability) could be bought (or incurred) or sold (or settled) in a current transaction between willing parties, that is, other than in a forced or liquidation sale. Quoted marked prices in active markets are the best evidence of fair value and shall be used as the basis for the measurement, if available. If a quoted market price is available, the fair value is the

product of the number of trading units times market price. If quoted market prices are not available, the estimate of fair value shall be based on the best information available. 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. 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. 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. 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. 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. All available evidence shall be considered in developing estimates of expected future cash flows. The weight given to the evidence shall be commensurate with the extent to which the evidence can be verified objectively. 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) 'Nonindemnity 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 Chapter 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 or more protected cells.

(11) 'Protected cell company insurance securitization' means the issuance of debt instruments, the proceeds from which support the exposures attributed to the protected cell, by a protected cell company where repayment of principal or interest, or both, to investors under the transaction terms is contingent upon the occurrence or nonoccurrence of an event with respect to which the protected cell company is exposed to loss under insurance or reinsurance contracts it has issued.

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

"**§ 58-10-85. Establishment of protected cells.**

(a) A protected cell company may establish one or more protected cells with the prior written approval of the Commissioner of a plan of operation or amendments submitted by the protected cell company with respect to each protected cell in connection with an insurance securitization. Upon the Commissioner's written approval of the plan of operation, which plan shall include the specific business objectives and investment guidelines of the protected cell, the protected cell company, in accordance with the approved plan of operation, may 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. A protected cell shall have its own distinct name or designation, which shall include the words 'protected cell.' The protected cell company shall transfer all assets attributable to a protected cell to one or more separately established and identified protected cell accounts bearing the name or designation of that protected cell. Protected cell assets must be held in the protected cell accounts for the purpose of satisfying the obligations of that protected cell.

(b) All attributions of assets and liabilities between a protected cell and the general account must be in accordance with the plan of operation approved by the Commissioner. A protected cell company may make no other attribution of assets or liabilities between the protected cell company's general account and its protected cells. 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, must be in cash or in readily marketable securities with established market values.

(c) The creation of a protected cell does not create, with respect to that protected cell, a legal person separate from the protected cell company. Amounts attributed to a protected cell under this Chapter, including assets transferred to a protected cell account, are owned by the protected cell company, and the protected cell company may not be, or may not hold itself out to be, a trustee with respect to those protected cell assets of that protected cell account. Notwithstanding the provisions of this subsection, the protected cell company may 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 and otherwise allowed under applicable law.

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

(1) Separate and separately identifiable from the assets and liabilities of the protected cell company's general account; and

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

Notwithstanding the provisions of this subsection, if this subsection is violated, the remedy of tracing is 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. The remedy of tracing is not an exclusive remedy.

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

"**§ 58-10-90. Use and operation of protected cells.**

(a) 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. 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) The income, gains and losses, realized or unrealized, from protected cell assets and protected cell liabilities must 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. 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 this Chapter and the investments in a protected cell or cells may not be taken into account in applying the investment limitations otherwise applicable to the investments of the protected cell company.

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

(d) A protected cell company, with respect to any of its protected cells, shall engage in fully funded indemnity triggered insurance securitization to support in full the protected cell exposures attributable to that protected cell. A protected cell company insurance securitization that is nonindemnity triggered shall qualify as an insurance securitization under the terms of this Chapter only after the Commissioner adopts rules addressing the methods of funding of the portion of this risk that is not indemnity based and addressing accounting, disclosure, risk-based capital treatment, and assessing risks associated with the securitizations. A protected cell company insurance securitization that is not fully funded, whether indemnity triggered or nonindemnity triggered, is prohibited. Protected cell assets may be used to pay interest or other consideration on any outstanding debt or other obligation attributable to that protected cell, and nothing in this subsection may be construed or interpreted to 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) 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. In addition, 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. Notwithstanding the provisions of this subsection and subject to the provisions of this Chapter and any other applicable law or rule, the failure to include such language in the contracts or other documentation may not be used as the sole basis by creditors, reinsurers, or other claimants to circumvent the provisions of this Part.

(f) 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. Under no circumstances may a protected cell 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 in accordance with the plan approved by the Commissioner, the protected cell company voluntarily shall close out the protected cell account.

"**§ 58-10-95. Reach of creditors and other claimants.**

(a) Protected cell assets shall only be available to the creditors of the protected cell company that are creditors with respect to that protected cell and, accordingly, are entitled, in conformity with this Chapter, to have recourse to the protected cell assets attributable to that protected cell and are absolutely protected from the creditors of the protected cell company that are not creditors with respect to that protected cell and who, accordingly, are not entitled to have recourse to the protected cell assets attributable to that protected cell. Creditors with respect to a protected cell are not entitled to have

recourse against the protected cell assets of other protected cells or the assets or the protected cell company's general account. Protected cell assets are only available to creditors of a protected cell company after all protected cell liabilities have been extinguished or otherwise provided for in accordance with 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, with respect to a protected cell:

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

(2) That obligation of the protected cell company does 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, with respect to that obligation, is not 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 extends only to, and that creditor, with respect to that obligation, is entitled to have recourse only to the assets of the protected cell company's general account.

(d) The activities, assets, and obligations relating to a protected cell are not subject to the provisions of Articles 48 and 62 of this Chapter, and neither a protected cell nor a protected cell company may 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. Nothing in this subsection affects the activities or obligations of an insurer's general account.

(e) The establishment of one or more protected cells alone does not constitute 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.

"**§ 58-10-100. Conservation, rehabilitation, or liquidation of protected cell companies.**

(a) Notwithstanding any other provision of law or rule, upon an order of conservation, rehabilitation, or liquidation of a protected cell company, the receiver shall deal with the protected cell company's assets and liabilities, including protected cell assets and protected cell liabilities, in accordance with the requirements set forth in this Part.

(b) With respect to amounts recoverable under a protected cell company insurance securitization, the amount recoverable by the receiver may 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 provisions to the contrary in the contracts or other documentation governing the protected cell company insurance securitization.

"**§ 58-10-105. No transaction of an insurance business.**

A protected cell company insurance securitization may not be deemed to be an insurance or reinsurance contract. An investor in a protected cell company insurance securitization, by sole means of this investment, may not be deemed to be conducting an insurance business in this State. 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 may 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 that business.

"**§ 58-10-110. Authority to adopt rules.**

The Commissioner may adopt rules necessary to effectuate the purposes of this Part."

PART XXVI. EFFECT OF HEADINGS.

SECTION 26. The headings to the parts of this act are a convenience to the reader and for reference only. The headings do not expand, limit, or define the text of this act.

PART XXVII. SEVERABILITY.

SECTION 27. If any section or provision of this act is declared unconstitutional, preempted, or otherwise invalid by the courts, it does not affect the validity of the act as a whole or any part other than the part so declared to be unconstitutional, preempted, or otherwise invalid.

PART XXVIII. EFFECTIVE DATES.

SECTION 28. Except as otherwise provided in this act, this act is effective when it becomes law.

In the General Assembly read three times and ratified this the 6th day of June, 2001.

_____
Beverly E. Perdue
President of the Senate

_____
James B. Black
Speaker of the House of Representatives

_____
Michael F. Easley
Governor

Approved _____.m. this _____ day of _____, 2001