

DEPARTMENT OF COMMERCE AND CONSUMER AFFAIRS

Amendment and Compilation of Chapter 16-17
Hawaii Administrative Rules

May 1, 2019

SUMMARY

1. §16-17-2 is amended.
2. §16-17-7 is amended.
3. §16-17-10 is amended.
4. §16-17-11 is amended.
5. §16-17-11.1 is amended.
6. §16-17-12 is amended.
7. §16-17-13 is amended.
8. §16-17-14 is amended.
9. §16-17-14.1 is amended.
10. §16-17-15 is amended.
11. §16-17-16 is amended.
12. A new §16-17-17 is added.
13. Chapter 17 is compiled.

HAWAII ADMINISTRATIVE RULES

TITLE 16

DEPARTMENT OF COMMERCE AND CONSUMER AFFAIRS

CHAPTER 17

CAPTIVE INSURANCE COMPANIES

§16-17-1	Purpose and authority
§16-17-2	Definitions
§16-17-5	Repealed
§16-17-6	Fee schedule
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§16-17-15	Business plan or plan of operation amendments; changes in ownership, governing body and officers
§16-17-16	Suspension or revocation of license; fines
§16-17-17	Surety insurance

§16-17-1 Purpose and authority. The purpose of this chapter is to set forth the financial, reporting, recordkeeping, and other requirements the commissioner deems necessary for the regulation of captive insurance companies, as authorized by the captive insurance code. [Eff 5/13/91; am and comp 3/12/01; am and comp 08/18/16; comp 08/17/19] (Auth: HRS §431:19-114) (Imp: HRS §431:19-114)

§16-17-2 Definitions. For purposes of this chapter:

"Adverse financial condition" means one or more of the following conditions:

- (1) The impairment of capital resulting from an imbalance of liabilities and assets;
- (2) Financial ratios exceeding levels established by the commissioner, if any; or
- (3) The material degradation of financial results envisioned by the designated captive insurance manager or independent certified public accountant through predictive forecasting to the end of the next annual reporting period.

"Applicant captive" means a captive applying for a certificate of authority under the captive insurance code.

"Captive" or "captive insurance company" shall have the same meaning as provided for "captive insurance company" in section 431:19-101, Hawaii Revised Statutes.

"Captive insurance code" means article 19 of chapter 431, Hawaii Revised Statutes.

"Commissioner" means the insurance commissioner of the State of Hawaii or a duly authorized representative.

"Credit for reinsurance" means taking credit for reserves on risks ceded to a reinsurer by a captive on the captive's financial statements.

"Governing body" shall have the same meaning as provided in section 431:19-101, Hawaii Revised Statutes.

"Organizational documents" shall have the same meaning as provided for "organizational document" in section 431:19-101, Hawaii Revised Statutes.

"Risk retention captive" shall have the same meaning as provided for "risk retention captive insurance company" in section 431:19-101, Hawaii Revised Statutes. [Eff 5/13/91; am and comp 3/12/01; am and comp 08/18/16; am and comp 08/17/19] (Auth: HRS §431:19-114) (Imp: HRS §431:19-114)

§16-17-5 Repealed. [R 3/12/01]

§16-17-6 Fee schedule. (a) Each applicant captive shall pay to the commissioner a nonrefundable application fee of \$1,000 for examining, investigating, and processing its license application. Upon approval of the application for a certificate of authority, the applicant captive shall pay to the commissioner a license fee for the certificate of authority in the amount set forth in subsection (b). Thereafter, each captive shall pay to the commissioner a renewal fee in the amount set forth in subsection (b) for each succeeding year on or before April 1.

(b) Depending on its class, a captive shall be subject to the following license and annual renewal fees:

- (1) \$300 for each class 1 or class 2 captive insurance company;
- (2) \$500 for each class 3 captive insurance company; or
- (3) \$1,000 for each class 4 or class 5 captive insurance company.

(c) Each captive shall pay to the commissioner a nonrefundable fee of \$25 for the preparation and

issuance of each of the following: certificates of compliance, deposit, application, capital and surplus, transcript of records, annual statements, report of examination, and other certifications as may be necessary, but excluding certificates of authority.

(d) Each captive shall pay to the commissioner a nonrefundable fee of twenty-five cents per side of each page for photocopies of documents.

(e) The rates and fees charged by approved independent advisors and consultants used by the commissioner shall be subject to the review of the commissioner. [Eff 5/13/91; am and comp 3/12/01; am and comp 08/18/16; comp 08/17/19] (Auth: HRS §§431:19-102, 431:19-102.3, 431:19-106, 431:19-114, 431:19-115) (Imp: HRS §431:19-102)

§16-17-7 Examination, investigation, and financial surveillance expenses.

(a) Captive insurance companies subject to examination, investigation, or financial surveillance shall be responsible for the payment of expenses associated with the examination, investigation, or financial surveillance. Examination, investigation, and financial surveillance expenses shall include costs, mileage, and other reasonable and appropriate expenses associated with the examination, investigation, or financial surveillance, as determined by the commissioner.

(1) If insurance division staff are employed in the examination, investigation, or financial surveillance of a captive insurance company, the captive insurance company shall be liable for the following additional examination fees:

- (A) Administration at a rate of \$30 per hour or fraction thereof;
- (B) Examiner I at a rate of \$50 per hour or fraction thereof;
- (C) Examiner II at a rate of \$55 per hour or fraction thereof; and

- (D) Examiner III at a rate of \$60 per hour or fraction thereof.
- (2) If an independent contractor is employed or retained by the commissioner in the examination, investigation, or financial surveillance of a captive insurance company, the captive insurance company shall be liable for the charges of services rendered.
- (b) Upon presentation of an invoice incurred from the examination, investigation, or financial surveillance, the captive insurance companies shall pay the commissioner for the expenses incurred from the examination, investigation, or financial surveillance. The payment shall be credited to the captive insurance administrative fund. [Eff and comp 3/12/01; am and comp 08/18/16; am and comp 08/17/19] (Auth: HRS §§431:2-306, 431:19-108, 431:19-114, 431:19-115) (Imp: HRS §§431:2-306, 431:19-108, 431:19-115)

§16-17-10 Notification of material misstatement of financial condition or adverse financial condition.

(a) A captive shall require its independent certified public accountant to immediately notify the captive's governing body or audit committee in writing of any determination by the independent certified public accountant that the captive has materially misstated its financial condition in the captive's annual report or is in adverse financial condition. The independent certified public accountant shall provide written notification of material misstatement of financial condition or adverse financial condition to the commissioner within five working days of providing notice to the captive. The captive manager shall provide a written remediation or corrective action plan to the commissioner within thirty days of the independent certified public accountant providing notice to the commissioner.

(b) As used in this section, "annual report" means the National Association of Insurance Commissioners' annual statement and the audited financial statement prepared by an independent certified public accountant for a captive and required to be filed with the commissioner pursuant to section 431:19-107, Hawaii Revised Statutes. [Eff 5/13/91; am and comp 3/12/01; am and comp 08/18/16; am and comp 08/17/19] (Auth: HRS §§431:19-114, 431:19-115) (Imp: HRS §§431:19-107, 431:19-108, 431:19-115)

§16-17-11 Additional deposit requirement. (a) Whenever the commissioner deems the financial condition or change in business plan of a captive warrants additional security, the commissioner may require the captive to deposit with the commissioner, in trust for the captive, cash, securities approved by the commissioner, or an irrevocable letter of credit issued by a bank chartered by the State of Hawaii or a member bank of the Federal Reserve System.

(b) The commissioner shall return the captive insurance company's deposit or letter of credit if the captive ceases doing any business, provided the commissioner is satisfied that all obligations of the company have been discharged. [Eff 5/13/91; am and comp 3/12/01; am and comp 08/17/19] (Auth: HRS §§431:19-114, 431:19-115) (Imp: HRS §§431:19-104, 431:19-105, 431:19-115)

§16-17-11.1 Risk-based capital regulatory action guidelines for risk retention captives. Risk retention captives subject to the risk-based capital requirements pursuant to sections 431:3-401 to 431:3-408, Hawaii Revised Statutes, may petition the commissioner to waive any risk-based capital regulatory action requirement if the risk retention captive can demonstrate, by filing five years of

projected pro forma financial statements of the risk retention captive, that any of the following exists:

- (1) The financial condition and support of the risk retention captive members or sponsoring organization or both is evidenced by the members or sponsoring organization or both maintaining:
 - (A) An investment grade rating from a nationally recognized statistical rating organization, or an A.M. Best rating A- or higher; or
 - (B) Equity equal to or greater than \$100 million, or equity equal to or greater than twenty times the risk retention captive's largest net retained per occurrence limit, as evidenced by the filing of at least the five most recent years of audited financial statements of the members or sponsoring organization, or both.
- (2) The risk retention captive's certificate of authority is dated prior to January 1, 2011, and based upon review of the risk retention captive's five most recent years of successful operating history, the commissioner issues a written exemption from the mandatory risk-based capital action requirements. [Eff and comp 08/18/16; am and comp 08/17/19] (Auth: HRS §§ 431:19-107, 431:19-114, 431:19-115) (Imp: HRS §431:19-107)

§16-17-12 Availability and retention of work papers of the independent certified public accountant.

(a) Each captive shall require its independent certified public accountant to make available for review by the commissioner or appointed agent work papers prepared in the conduct of the annual statement and the audit of the captive. The captive shall require that the independent certified public

accountant retain the audit work papers for a period of not less than seven years after the period being reported.

(b) The review conducted in subsection (a) shall be considered an investigation, and all work papers obtained during the course of that investigation shall be confidential in accordance with the captive insurance code. The captive shall require that the independent certified public accountant provide photocopies of any and all work papers that the commissioner deems relevant. The commissioner may retain these copies.

(c) As used in this section, "work papers" include, but are not limited to, schedules, analyses, reconciliations, abstracts, memoranda, narratives, flow charts, copies of company records, or other documents prepared or obtained by the independent certified public accountant in the conduct of the examination of the captive. [Eff 5/13/91; am and comp 3/12/01; am and comp 08/18/16; am and comp08/17/19] (Auth: HRS §§431:19-114, 431:19-115) (Imp: HRS §§431:19-102.5, 431:19-107, 431:19-108, 431:19-115)

§16-17-13 Documentation required to be held by captives in Hawaii. (a) The captive shall maintain accurate, legible, and complete original, photocopied, or electronic records of the captive's operations in its principal office in Hawaii or another Hawaii location designated by the captive and approved by the commissioner. Upon the request of the commissioner to review the captive's records, the captive shall provide the commissioner timely access to the requested documents. If any document is in a foreign language, a translation under oath of the translator shall accompany the document.

(b) Each captive shall designate in writing one of its service providers to serve as the captive's representative with respect to the maintenance and

production of the captive's records. The captive's designated representative shall be:

- (1) Physically present in Hawaii; and
- (2) Able to respond to questions about the captive, including matters related to the captive's operation, management, financial condition, investments, and insurance and reinsurance programs.

(c) All captives licensed by the State shall maintain and make ready for inspection, investigation, financial surveillance, and examination by the commissioner or the commissioner's agents any and all documents pertaining to the formation, operation, management, finances, investments, insurance, and reinsurance of each captive. These documents shall include:

- (1) The captive's corporate records, including all organizational documents, resolutions, and minutes of the captive's governing body;
- (2) Verification of the captive's principal place of business;
- (3) Records relative to the captive's capital, surplus, assets, and liabilities, including actuarial opinions, reports of independent certified public accountants, and supporting documentation;
- (4) The captive's business plan and plan of operation, including changes in management, ownership, qualifications of officers and directors, service providers, and strategic investment policy;
- (5) The captive's correspondence and filings with the commissioner and insurance division staff and with other jurisdictions;
- (6) All executed agreements materially affecting the captive's business, including insurance policies and reinsurance bordereau; and
- (7) Any other information the commissioner deems necessary. [Eff 5/13/91; am and comp 3/12/01; am and comp 08/18/16; am and comp 08/17/19] (Auth: HRS

§§431:19-114, 431:19-115) (Imp: HRS
§§431:19-108, 431:19-115)

§16-17-14 Reinsurance. (a) Reinsurance under this section shall be effected through a written agreement of reinsurance setting forth the terms, provisions, and conditions governing the reinsurance.

(b) A risk retention captive:

- (1) Shall qualify for credit for reinsurance on risks ceded to a reinsurer if the reinsurer is in compliance with chapter 431, article 4A of the Hawaii Revised Statutes; or
- (2) May qualify for credit for reinsurance on risks ceded to a reinsurer, provided the reinsurer meets the reinsurance guidelines for risk retention captives pursuant to section 16-17-14.1.

(c) A captive taking credit for reinsurance pursuant to this section shall provide copies of all reinsurance binders, slips, treaties, or agreements to the commissioner for the commissioner's review and approval. [Eff 5/13/91; am and comp 3/12/01; am and comp 08/18/16; am and comp 08/17/19] (Auth: HRS §§431:19-114, 431:19-115) (Imp: HRS §431:19-111)

§16-17-14.1 Reinsurance guidelines for risk retention captives. (a) A risk retention captive may qualify for credit for reinsurance on risks ceded to a reinsurer if:

- (1) The reinsurer maintains an A- or higher A.M. Best rating or other comparable rating from a nationally recognized statistical rating organization, the reinsurer maintains a minimum policyholder surplus in an amount acceptable to the commissioner based upon a review of the reinsurer's most recent audited financial statements, and the reinsurer is licensed and domiciled in a

- jurisdiction acceptable to the commissioner;
or
- (2) The reinsurer satisfies all of the following requirements and any other requirements deemed necessary by the commissioner:
- (A) The risk retention captive or its captive manager shall file annually, on or before June 30, the reinsurer's audited financial statements, which the commissioner shall analyze to assess the appropriateness of the reserve credit or the initial and continued financial condition of the reinsurer;
 - (B) The reinsurer shall demonstrate to the satisfaction of the commissioner that it maintains a ratio of net written premium, wherever written, to surplus and capital of not more than three to one;
 - (C) If the reinsurer is an affiliate of the risk retention captive, the reinsurer shall not write third-party business without prior written approval from the commissioner;
 - (D) The reinsurer shall not use cell arrangements without prior written approval from the commissioner;
 - (E) The reinsurer shall be licensed and domiciled in a jurisdiction acceptable to the commissioner; and
 - (F) The reinsurer shall submit to the examination authority of the commissioner.

For purposes of this paragraph, a reinsurer is affiliated with a risk retention captive if more than fifty per cent of the equity interests in the reinsurer are owned, directly or indirectly, by one or more members of the risk retention captive.

(b) A risk retention captive using these reinsurance guidelines shall not receive credit for reinsurance if all of its policies are ceded through:

- (1) One hundred per cent reinsurance arrangements; or
- (2) A lesser percentage approved by the commissioner, and the risk retention captive exceeds the approved percentage. While no credit for reinsurance shall be allowed for the amount in excess of the approved percentage, the risk retention captive may qualify for credit for reinsurance for the amount within the approved percentage.

(c) The commissioner shall either require a reinsurer not domiciled in the United States to include language in the reinsurance agreement stating that in the event of the reinsurer's failure to perform its obligations under the terms of its reinsurance agreement, the reinsurer shall submit to the jurisdiction of any court of competent jurisdiction in the United States or shall require the reinsurer to comply with subsection (d).

(d) For credit for reinsurance and solvency regulatory purposes, the commissioner may require an approved funds-held agreement, letter of credit, trust, or other acceptable collateral based upon unearned premium, loss and loss adjustment expense reserves, and incurred but not reported reserves.

(e) Upon application, the commissioner may waive either of the reinsurance requirements in subsection (a)(2)(B) or (a)(2)(F) if the risk retention captive or reinsurer can demonstrate to the commissioner that the reinsurer is sufficiently capitalized based upon:

- (1) An annual review of the reinsurer's most recent audited financial statements;
- (2) The reinsurer being licensed and domiciled in a jurisdiction satisfactory to the commissioner; and
- (3) The proposed reinsurance agreement adequately protecting the risk retention captive and its policyholders.

Any waiver shall be included in the plan of operation or any of its subsequent revisions or amendments, pursuant to 15 U.S.C. section 3902(d)(1). The plan

shall be submitted by the risk retention captive to the commissioner of its state of domicile and each state in which the risk retention captive intends to do business or is currently registered. Any waiver of a requirement in subsection (a) (2) shall constitute a change in the risk retention captive's plan of operation in each of those states.

(f) Upon application, the commissioner may waive the requirement in subsection (c) that a reinsurance arrangement must satisfy either subsection (c) or (d) if the risk retention captive or reinsurer can demonstrate to the commissioner that the reinsurer is sufficiently capitalized, based upon:

- (1) An annual review of the reinsurer's most recent audited financial statements;
- (2) The reinsurer being licensed and domiciled in a jurisdiction satisfactory to commissioner; and
- (3) The proposed reinsurance agreement adequately protecting the risk retention captive and its policyholders.

Any waiver shall be disclosed in Note 1 of the risk retention captive's annual statutory financial statement.

(g) Each risk retention captive or captive manager of a risk retention captive shall assess the reinsurance programs of the risk retention captives under their management, and within sixty days of the effective date of this section, shall submit a written report to the commissioner indicating whether the risk retention captives are in compliance with these guidelines. All risk retention captives that fail to submit the report in a timely manner shall be examined at the risk retention captive's expense to determine compliance with this section.

(h) This section shall become effective when this chapter becomes effective and shall apply prospectively to risk retention captives. Credit for reinsurance may be granted for a risk retention captive's reinsurers in place as of January 1, 2011, without meeting the requirements of this section. The requirements of this section shall be used for new

reinsurers not in place as of January 1, 2011, with which business is placed after January 1, 2011. [Eff and comp 08/18/16; am and comp 08/17/19] (Auth:HRS §§431:19-114, 431:19-115) (Imp: HRS §431:19-111)

§16-17-15 Business plan or plan of operation amendments; changes in ownership, governing body and officers. (a) The captive shall provide written notice and obtain prior approval from the commissioner for any change in ownership or material change to the captive's business plan or plan of operation that was filed with the commissioner upon application or as otherwise required by statute.

(b) The captive shall provide written notice to the commissioner for any nonmaterial changes to the captive's business plan or plan of operation or as otherwise required by statute.

(c) The captive shall provide written notice to the commissioner within thirty days after any change to its governing body or its officers, including submission of the completed biographical affidavit of any new member of the captive's governing body or officer. The captive shall obtain prior approval from the commissioner for any new appointment who does not already have a biographical affidavit on file with the commissioner. [Eff 5/13/91; am and comp 3/12/01; am and comp 08/18/16; am and comp 08/17/19] (Auth: HRS §§431:19-114, 431:19-115) (Imp: HRS §§431:19-106, 431:19-109, 431:19-115)

§16-17-16 Suspension or revocation of license; fines. (a) The commissioner may by order fine, suspend or revoke the license of a captive or any combination of these actions:

- (1) For any reason provided in section 431:19-109, Hawaii Revised Statutes; or
- (2) Pursuant to the captive's request.

(b) In case of suspension or revocation, the commissioner shall advise the captive of procedures and requirements for ongoing operations and winding up the captive's business. [Eff 5/13/91; am and comp 3/12/01; am and comp 08/18/16; am and comp 08/17/19] (Auth: HRS §§431:19-114, 431:19-115) (Imp: HRS §§431:19-109, 431:19-115)

§16-17-17 Surety insurance. (a) A captive may provide surety insurance under a business plan approved by the commissioner, provided that the captive maintains a ratio no greater than ten to one of the total value of outstanding bond obligations to unimpaired capital and surplus. For purposes of this subsection, intercompany or affiliated loans are considered nonadmitted assets when determining unimpaired capital and surplus under sections 431:19-104, 431:6-201, and 431:19-110, Hawaii Revised Statutes, unless an irrevocable letter of credit issued by a bank chartered by this State or a member bank of the Federal Reserve System, or other collateral approved by the commissioner, fully secures the loans.

(b) Within forty-five days of the end of each calendar quarter, the approved captive manager pursuant to section 431:19-101.4, Hawaii Revised Statutes, shall submit to the commissioner the following:

- (1) A listing of all outstanding surety obligations, including the purpose of each bond and its respective obligee, bond principal, outstanding bond value, and calculations of unearned premiums based upon the bond term. The listing shall also include attestations by an officer of the captive and the captive manager that the listing is complete and accurate;
- (2) Quarterly unaudited financial statements of the captive insurer prepared in accordance

with generally accepted accounting principles or other accounting principles prescribed or permitted under law, and attested by the captive manager and an officer of the captive;

- (3) Quarterly unaudited financial statements of the bond principal, and a statement signed by an officer or other responsible person of the bond principal as to whether there has been any written claim or notice of dispute, or lawsuit received by the bond principal relating to the contract or matter for which a bond underwritten by the captive was issued involving an amount equal to or exceeding ten percent (10%) of the face amount of the bond. For construction-related bonds, the principal shall include a construction work-in-progress report for all of the principal's construction projects supported by outstanding bonds issued by the captive;
- (4) Quarterly statutory compliance calculations for minimum required capital and surplus pursuant to sections 431:19-104, 431:6-201, and 431:19-110, Hawaii Revised Statutes; and
- (5) Any additional information required by the commissioner.

(c) In the event a claim is reported against a bond, the captive shall provide written notification to the commissioner within five working days of the claim being reported.

(d) As used in this section, "bond principal" means the entity or affiliate of the entity for whom the bond was issued by the captive." [Eff and comp 08/17/19] (Auth: HRS §§431:19-104, 431:19-107, 431:19-109, 431:19-110, 431:19-114) (Imp: HRS §§431:19-107, 431:19-109)

Amendments to and compilation of Chapter 16-17, Hawaii Administrative Rules, on the Summary Page dated May 1, 2019, were adopted on May 1, 2019, following a public hearing held on this same date, after public notices were given in the Honolulu Star-Advertiser on March 24 and 28, 2019.

These rules shall take effect ten days after filing with the Office of the Lieutenant Governor.

APPROVED:

/s/Catherine P. Awakuni Colón
CATHERINE P. AWAKUNI COLÓN
Director of Commerce and
Consumer Affairs

Date: Jul 2, 2019

/s/ David Y. Ige
DAVID Y. IGE
Governor
State of Hawaii

Date: 08-07-2019

APPROVED AS TO FORM:

/s/ Daniel Jacob
Deputy Attorney General

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Filed