DISTRICT OF COLUMBIA
DEPARTMENT OF INSURANCE AND SECURITIES REGULATION

NOTICE OF FINAL RULEMAKING

The Commissioner of the Department of Insurance and Securities Regulation, pursuant to the authority set forth in Section 18 of the Captive Insurance Company Act of 2000, effective October 21, 2000 (D.C. Law 13-192; 47 DCR 7320), took final action to adopt regulations governing the annual audit and financial reporting requirements, application process, and management requirements for captive insurance companies licensed in the District. No changes were made to the text of the proposed rules, as published with the Notice of Proposed Rulemaking in the D.C. Register on June 29, 2001 at 48 DCR 5957. These final rules shall become effective upon publication of this notice in the D.C. Register.

26 DCMR is amended by adding a new Chapter 37, Captive Insurance Companies, to read as follows:

3700 APPLICABILITY

This regulation shall apply to all captive insurance companies formed or licensed under the provisions of the Captive Insurance Company Act of 2000, effective October 21, 2000, (D.C. Law 13-192; 47 DCR 7320).

3701 ANNUAL REPORTING REQUIREMENTS

All captive insurance companies licensed to do business in the District shall annually submit to the Commissioner a report of its financial condition, verified by oath of two of its executive officers.

3702 ANNUAL AUDIT

3702.1 All captive insurance companies shall have an annual audit by an independent certified public accountant, authorized by the Commissioner and shall file such audited financial report with the Commissioner on or before June 30 for the year ending December 31 immediately preceding.

3702.2 The annual audit report shall be considered part of the captive insurance company's annual report of financial condition except with respect to the date by which it must be filed with the Commissioner.

3702.3 The annual audit shall consist of the following:

(a) Financial statements furnished pursuant to this section shall be examined by independent certified public accountants in accordance with generally accepted

auditing standards as determined by the American Institute of Certified Public Accountants.

(b) The opinion of the independent certified public accountant shall cover all years presented.

(c) The opinion shall be addressed to the captive insurance company on stationery of the accountant showing the address of issuance, shall bear original manual signatures, and shall be dated.

3702.4 The annual audit report shall include an evaluation of the internal controls of the captive insurance company relating to the methods and procedures used in the securing of assets and the reliability of the financial records, including but not limited to such controls as the system of authorization and approval and the separation of duties.

3702.5 The annual audit shall be conducted in accordance with generally accepted auditing standards.

3702.6 The accountant shall furnish the company, for inclusion in the filing of the audited annual report, a letter stating:

(a) That it is independent with respect to the captive insurance company and conforms to the standards of the profession, as contained in the Code of Professional Ethics and pronouncements of the American Institute of Certified Public Accountants and pronouncements of the Financial Accounting Standards Board.

(b) The general background and experience of the staff engaged in audit including the experience in auditing captives or other insurance companies.

(c) That the accountant understands that the audited annual report and his opinions thereon will be filed in compliance with this regulation with the Department of Insurance and Securities Regulation.

(d) That the accountant consents to the requirements of § 3705 of this regulation and that the accountant consents and agrees to make available for review by the Commissioner, his designee or his appointed agent, the work papers as defined in § 3705.

(e) That the accountant is property licensed by an appropriate District or state licensing authority and that he is a member in good standing in the American Institute of Certified Public Accountants.

3702.7 The annual audit shall include the following financial statements:

(a) Balance sheet;

(b) Statement of operations;

(c) Statement of changes in financial position;

(d) Statement of changes in capital paid up, gross paid in and contributed surplus and unassigned funds (surplus); and

(e) Notes to financial statements, which shall include those that are required by generally accepted accounting principles, including:

1. A reconciliation of differences, if any, between the audited financial report and the statement or form filed with the Commissioner;

2. A summary of ownership and relationship of the company and all affiliated corporations or companies insured by the captive; and

3. A narrative explanation of all material transactions and balances with the company.

3702.8 The annual audit shall include an opinion as to the adequacy of the captive insurance company's loss reserves and loss expense reserves. The audit of the adequacy of the captive insurance company's life, health, disability and annuity loss reserves and loss expense reserves for a captive insurance company insuring employee benefit risks shall be performed by a life actuary. The individual who certifies as to the adequacy of reserves shall be approved by the Commissioner and shall be a Fellow of the Casualty Actuarial Society, a member in good standing of the American Academy of Actuaries, or an individual who has demonstrated his competence in loss reserve evaluation to the Commissioner.

3702.9 The certification in subsection 3702.8 shall be in such form as the Commissioner deems appropriate.

3703 DESIGNATION OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANT

Captive insurance companies, after becoming subject to this regulation, shall within ninety days report to the Commissioner in writing, the name and address of the independent certified public accountant retained to conduct the annual audit set forth in this regulation.

3704 NOTIFICATION OF ADVERSE FINANCIAL CONDITION

A captive insurance company shall require the certified public accountant to immediately notify in writing the chief executive officer and all members of the Board of Directors of the company of any determination by the independent certified public accountant that the company has materially misstated its financial condition in its

report to the Commissioner. The company shall furnish such notification to the Commissioner within five working days of receipt thereof.

3705 AVAILABILITY AND MAINTENANCE OF WORKING PAPERS OF THE INDEPENDENT CERTIFIED PUBLIC ACCOUNTANT

3705.1 Each captive insurance company shall require the independent certified public accountant to make available for review by the Commissioner the work papers prepared in the conduct of the audit of the company. The company shall require that the accountant retain the audit work papers for a period of not less than five years after the period reported upon.

3705.2 The review by the Commissioner referenced in § 3705.1 shall be considered investigations and all working papers obtained during the course of such investigations shall be confidential. The captive insurance company shall require that the independent certified public accountant provide photocopies of any of the working papers which the Commissioner considers relevant. The Commissioner may retain the work papers.

3705.3 "Work Papers" as referred to in this section include, but are not necessarily limited to, schedules, analyses, reconciliations, abstracts, memoranda, narratives, flow charts, copies of company records or other documents prepared or obtained by the accountant and his employees in the conduct of their examination of the company.

3706 DEPOSIT REQUIREMENT

3706.1 Whenever the Commissioner deems that the financial condition of the captive insurance company warrants additional security, he or she may require a company to deposit in the Commissioner's custodial account cash or securities approved by the Commissioner or, alternatively, to furnish the Commissioner with a clean irrevocable letter of credit issued by a bank that has a branch located in the District of Columbia, and approved by the Commissioner.

3706.2 The captive insurance company may receive interest or dividends from said deposit or exchange the deposits for others of equal value after receiving prior written approval from the Commissioner.

3706.3 If such captive insurance company discontinues business, the Commissioner shall return such deposit only after being satisfied that all obligations of the company have been discharged.

3707 CAPITAL AND SURPLUS REQUIREMENTS

A captive insurer using a letter of credit as evidence of capital permitted by Section 9 (d) of the Act shall not enter into any agreement with the issuer of the letter of credit granting the issuer any of the following:

(a) a right of reimbursement;

(b) a right of set-off against any funds or other assets owned by the captive insurer;

(c) a lien or other interest in any assets owned by the captive insurer; or

(d) a right to draw down on the letter or credit, in whole or in part.

3708 REVIEW PANEL AND ORGANIZATIONAL EXAMINATION

3708.1 The Commissioner shall establish and maintain a review panel consisting of qualified independent reviewers to assist in the review of applications for a certificate of authority. The Commissioner, in his or her discretion, may submit an application for a certificate of authority to a qualified independent reviewer, which shall be responsible for attesting that the applicant meets all the requirements of the insurance laws and regulations of the District, and is qualified to transact the business for which it seeks a certificate of authority. If the Commissioner elects to submit the application to a qualified independent reviewer for review, the applicant shall select a reviewer from the list of qualified and authorized reviewers.

3708.2 The reviewer shall have the authority to conduct an organizational investigation or examination of the applicant. Such investigation or examination shall consist of a review of the company's corporate records, including charter, bylaws and minute books; verification of capital and surplus, applicant's business plan; qualifications of its executive officers and directors; verification of principal place of business; determination of assets and liabilities; and a review of such other factors as the reviewer deems necessary. The reviewer shall have the authority to request any records or other information from the applicant that the reviewer deems necessary to its inquiry.

3708.3 The reviewer shall file a report with the Commissioner summarizing the applicant's qualification for a certificate of authority.

3708.4 The report of referenced in § 3708.3 shall be signed, under oath, by the reviewer, and shall be considered *prima facie* evidence by the Commissioner that the applicant is entitled to do business in the District, subject to the Commissioner's authority to revoke or suspend a certificate of authority as provided in the Act.

3708.5 The applicant shall pay a nonrefundable review fee to the reviewer, in an amount not to exceed $5,000.00 for a pure captive insurer and not to exceed $7,500.00 for all other captive insurers, at the time the Commissioner submits the application to the reviewer. The amount of the review fee shall be established by agreement between the reviewer and the applicant. The review fee shall be in addition to the application fee set forth in Section 4(c) of the Act.

3708.6 A reviewer that also acts as a manager for the applicant shall not be permitted to participate in the application review process.

3709 REINSURANCE

3709.1 All reinsurance transactions of a captive insurance company shall be effected through a written agreement of reinsurance setting forth the terms, provisions and conditions governing such reinsurance.

3709.2 The Commissioner, in his or her discretion, may require that complete copies of all reinsurance treaties and contracts be filed by the domestic captive company with the Commissioner, and may be subject to his or her approval.

3710 INSURANCE MANAGERS AND INTERMEDIARIES

No person shall, in or from within the District, act as an insurance manager, broker, agent, salesman, or reinsurance intermediary for captive business without the authorization of the Commissioner.

3711 DIRECTORS

3711.1 Every company shall report to the Commissioner within thirty (30) days after any change in its executive officers or directors, including in its report a statement of the business and professional affiliations of any new executive officer or director.

3711.2 No director, officer, or employee of a company shall, except on behalf of the company, accept, or be the beneficiary of, any fee, brokerage, gift, or other emolument because of any investment, loan, deposit, purchase, sale, payment or exchange made by or for the company, but such person may receive reasonable compensation for necessary services rendered to the company in his or her usual private, professional or business capacity.

3711.3 Any profit or gain received by or on behalf of any person in violation of this section shall inure to and be recoverable by the company.

3712 CONFLICT OF INTEREST

3712.1 In addition to the investment of funds in § 3711, each company licensed in the District shall adopt a conflict of interest statement from officers, directors and key employees. The statement shall disclose that the individual has no outside commitments, personal or otherwise, that would divert him from his duty to further the interests of the company he represents, but this shall not preclude such person from being a director or officer in more than one insurance company.

3712.2 Each officer, director, and key employee shall file such disclosure with the Board of Directors yearly.

3713 SUSPENSION OR REVOCATION OF CAPTIVE LICENSE

3713.1 The Commissioner may, subject to the provisions of this section, by order suspend or revoke the license of the company:

(a) if the company has not commenced business according to its plan of operation within two years of being licensed; or

(b) if the company ceases to carry on insurance business in or from within the District;

(c) at the request of the company; or

(d) for any reason provided in section 5 of the Act.

3713.2 Before the Commissioner suspends or revokes the license of a company pursuant to section § 3713.1, the Commissioner shall give the company notice in writing of the grounds on which he proposes to suspend or revoke the license, and shall afford the company an opportunity for a hearing within the period of thirty days after receipt of notice.

3714 ACQUISITION OF CONTROL OR MERGER WITH DOMESTIC COMPANY

No person other than the issuer shall make a tender offer of or a request or invitation for tenders of, or enter into any agreement to exchange securities for, seek to acquire, or acquire in the open market or otherwise, any voting security of a domestic company if, after the consummation thereof, such person would, directly or indirectly (or by conversion or by exercise of any right to acquire) be in control of such company; and no person shall enter into an agreement to merge with or otherwise to acquire control of a domestic company without the prior written approval of the Commissioner. In considering any application for acquisition of control or merger with a domestic company, the Commissioner shall consider all of the facts and circumstances surrounding the application as well as the criteria for establishment of a company set out in this chapter.

3715 CHANGE OF BUSINESS

3715.1 Any change in the nature of the captive business from that stated in the company's plan of operation filed with the Commissioner upon application requires prior written approval from the Commissioner.

3715.2 Any change in any other information filed with the application must be filed with the Commissioner, but does not require prior written approval.

3716 CAPTIVE INSURANCE COMPANIES ISSUING ANNUITIES

3716.1 This regulation establishes reserve requirements, separate accounts and the form of the annual statement required of any captive insurance company that issues annuity contracts, which may have life or other benefits that constitute a subsidiary or incidental part of the entire contract.

3716.2 A captive insurance company that issues annuity contracts shall submit its annual report in the form of the annual statement approved by the National Association of Insurance Commissioners for life insurers, as modified or supplemented by the Commissioner.

3716.3 Any captive insurance company that issues contracts that provide variable benefits shall establish separate accounts. Such accounts shall be subject to the requirements of section 8(b)(1) of the Captive Act of 2000, effective October 21, 2000 (D.C. Law 13-192, 47 DCR 7320).

3716.4 A captive insurance company that issues annuity contracts shall maintain reserves that are actuarially sufficient to support the liabilities provided by the contracts.

3716.5 If any provision of this regulation or the application thereof to any person or circumstance is for any reason held to be invalid, the remainder of the regulation and the application of such provisions to other persons or circumstances shall not be affected thereby.