

INSURANCE CODE

TITLE 4. REGULATION OF SOLVENCY

SUBTITLE B. RESERVES AND INVESTMENTS

CHAPTER 424. INVESTMENTS FOR CERTAIN INSURERS

SUBCHAPTER A. GENERAL PROVISIONS

Sec. 424.001. DEFINITIONS. In this chapter:

(1) "Insurer" means any insurer organized under the laws of this state other than an insurer writing life, health, and accident insurance.

(2) "Minimum capital and surplus" means the minimum amount of capital stock and minimum amount of surplus required of an insurer under Section [822.054](#) or [822.210](#).

(3) "Securities valuation office" means the Securities Valuation Office of the National Association of Insurance Commissioners.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. [2017](#)), Sec. 1, eff. April 1, 2007.

Sec. 424.002. INAPPLICABILITY OF CERTAIN LAW. The definition of "state" assigned by Section [311.005](#), Government Code, does not apply to this chapter.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. [2017](#)), Sec. 1, eff. April 1, 2007.

SUBCHAPTER B. INVESTMENT OF FUNDS IN EXCESS

OF MINIMUM CAPITAL AND SURPLUS

Sec. 424.051. GENERAL INVESTMENT AUTHORITY SPECIFIED BY LAW. An insurer may not invest the insurer's funds in excess of minimum capital and surplus, except that an insurer may invest as otherwise authorized by this code.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. [2017](#)), Sec. 1, eff. April 1, 2007.

Sec. 424.052. ADDITIONAL GENERAL INVESTMENT AUTHORITY. An

insurer may make investments that are not otherwise authorized by this chapter or otherwise authorized by this code for the insurer if:

(1) the investment is not specifically prohibited by law and does not exceed the limits prescribed by this code;

(2) the amount of a single investment under this section does not exceed five percent of the insurer's capital and surplus in excess of the insurer's minimum capital and surplus; and

(3) the aggregate amount of all investments made by the insurer under this section does not exceed five percent of the insurer's assets.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.053. LIMITATION AS TO SINGLE ISSUER OR BORROWER.

(a) Notwithstanding Sections 424.051, 424.056-424.071, and 424.074, the aggregate amount of an insurer's investments in all or any type of securities, loans, obligations, or evidences of indebtedness of a single issuer or borrower, other than investments described by Subsection (c), may not exceed five percent of the insurer's total assets.

(b) For purposes of this section, a single issuer or borrower includes:

(1) the issuer's or borrower's majority-owned subsidiaries;

(2) the issuer's or borrower's parent; or

(3) the majority-owned subsidiaries of the issuer's or borrower's parent.

(c) This section does not apply to:

(1) an authorized investment that:

(A) is a direct obligation of or guaranteed by the full faith and credit of the United States, this state, or a political subdivision of this state; or

(B) is insured by an agency of the United States or this state; or

(2) an investment described by Section 424.061 or 424.063.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.054. APPLICABILITY OF PERCENTAGE AUTHORIZATIONS AND LIMITATIONS. (a) The percentage authorizations and limitations established by Sections 424.051, 424.053-424.071, and 424.074 apply only at the time an investment is originally acquired or a transaction is entered into and do not apply to the insurer or the investment or transaction after that time.

(b) An investment, once qualified under a law described by Subsection (a), remains qualified notwithstanding any refinancing, restructuring, or modification of the investment, except that an insurer may not refinance, restructure, or modify an investment solely to circumvent the requirements or limitations of a law described by Subsection (a).

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.055. WAIVER BY COMMISSIONER OF QUANTITATIVE LIMITATIONS. (a) Notwithstanding Sections 424.051, 424.056-424.071, and 424.074, the commissioner may waive a quantitative limitation on any investment authorized by those laws if:

(1) the insurer seeks the waiver before making the investment;

(2) a hearing is held to determine whether the waiver should be granted;

(3) the applicant seeking the waiver establishes that unreasonable or unnecessary loss or harm will result to the insurer if the commissioner denies the waiver;

(4) the excess investment will not have a material adverse effect on the insurer; and

(5) the size of the investment is reasonable in relation to the insurer's assets, capital, surplus, and liabilities.

(b) The commissioner's waiver must be in writing and may treat the resulting excess investment as a nonadmitted asset.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.056. WRITTEN INVESTMENT PLAN. (a) Each insurer's board of directors, or, if the insurer does not have a board of directors, the corresponding authority designated by the insurer's charter, bylaws, or plan of operation, shall adopt a written investment plan consistent with the requirements of:

(1) this chapter;

(2) Sections 822.204, 822.209, 861.258, and 862.002;

and

(3) other statutes governing investments by the insurer.

(b) The investment plan must:

(1) specify the diversification of the insurer's investments designed to reduce the risk of large losses, by:

(A) broad categories, such as bonds and real property loans;

(B) kinds, such as government obligations, obligations of business entities, mortgage-backed securities, and real property loans on office, retail, industrial, or residential properties;

(C) quality;

(D) maturity;

(E) type of industry; and

(F) geographical areas, as to both domestic and foreign investments;

(2) balance safety of principal with yield and growth;

(3) seek a reasonable relationship of assets and liabilities as to term and nature; and

(4) be appropriate considering the capital and surplus and the business conducted by the insurer.

(c) At least annually, the board of directors or corresponding authority shall review the adequacy of the investment plan and the implementation of the plan.

(d) An insurer shall maintain the insurer's investment plan in the insurer's principal office and provide the plan to the

commissioner or the commissioner's designee on request. The commissioner or the commissioner's designee shall maintain the plan as a privileged and confidential document. The plan is not subject to public disclosure.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.057. INVESTMENT RECORDS. An insurer shall maintain investment records covering each transaction. The insurer must be able to demonstrate at all times to the department that the insurer's investments are within the limitations imposed by the statutes listed in Section 424.056(a).

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.058. AUTHORIZED INVESTMENTS: FORM OF MINIMUM CAPITAL AND SURPLUS. An insurer may invest the insurer's funds in excess of minimum capital and surplus in any manner authorized by Section 822.204 for investment of the insurer's minimum capital and surplus.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.059. AUTHORIZED INVESTMENTS: GOVERNMENT OBLIGATIONS. An insurer may invest the insurer's funds in excess of minimum capital and surplus in a bond or other evidence of indebtedness of any state or of Canada or a province of Canada that:

- (1) is issued by the authority of law; and
- (2) at the time of purchase:
  - (A) bears interest; and
  - (B) is not in default as to principal or

interest.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.060. AUTHORIZED INVESTMENTS: STOCK OF NATIONAL OR STATE BANK. (a) An insurer may invest the insurer's funds in

excess of minimum capital and surplus in the stock of:

(1) a national bank; or

(2) a state bank of this state whose deposits are insured by the Federal Deposit Insurance Corporation.

(b) Notwithstanding Subsection (a)(2):

(1) not more than 35 percent of the total outstanding stock of a single state bank may be purchased by a single insurer; and

(2) if an insurer has invested the insurer's funds in 35 percent of a state bank's stock under this section, no other insurer may invest funds in the bank's remaining stock.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.061. AUTHORIZED INVESTMENTS: DEPOSITS IN CERTAIN FINANCIAL INSTITUTIONS. (a) Subject to this section, an insurer may invest in any type of savings deposit, time deposit, certificate of deposit, NOW account, or money market account in a solvent bank, savings and loan association, or credit union that is organized under the laws of the United States or a state, or in a branch of one of those financial institutions.

(b) An investment under this section must be made in accordance with the laws or regulations applicable to the bank, savings and loan association, or credit union.

(c) The amount of an insurer's deposits in a single bank, savings and loan association, or credit union may not exceed the greater of:

(1) 20 percent of the insurer's capital and surplus;

(2) the amount of federal or state deposit insurance coverage that applies to the deposits; or

(3) 10 percent of the amount of capital, surplus, and undivided profits of the financial institution receiving the deposits.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.062. AUTHORIZED INVESTMENTS: CERTAIN OBLIGATIONS

OF PARTNERSHIP OR CORPORATION. (a) Except as provided by this section, an insurer may invest the insurer's funds in excess of minimum capital and surplus in a stock, bond, debenture, bill of exchange, evidence of indebtedness, other commercial note or bill, or security of any partnership or dividend-paying corporation that:

- (1) is incorporated under the laws of the United States, this state, another state, Canada, or a province of Canada;
- (2) is solvent at the time of the investment; and
- (3) has not defaulted in the payment of any of the partnership's or corporation's obligations during the five years preceding the date of the investment.

(b) Except as provided by Subsection (d), an insurer may invest the insurer's funds in excess of minimum capital and surplus, and all reserves required by law, in a stock, bond, or debenture of any solvent corporation that is incorporated under the laws of the United States, this state, another state, Canada, or a province of Canada.

(c) Funds invested under Subsection (a) may not be invested in the stock of an oil, manufacturing, or mercantile corporation unless the corporation has, at the time of the investment:

- (1) a net worth of at least \$250,000, if the corporation is organized under the laws of this state; or
- (2) a combined capital, surplus, and undivided profits of at least \$2.5 million, if the corporation is not organized under the laws of this state.

(d) An insurer may not invest the insurer's funds in:

- (1) the insurer's own stock or in any stock on account of which the holders or owners of the stock may be liable for an assessment other than taxes; or
- (2) any stock, bond, or other security issued by a corporation with respect to which a majority of the stock having voting powers is directly or indirectly owned by or for the benefit of an officer or director of the insurer, unless the insurer has been in continuous operation for at least five years.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.063. AUTHORIZED INVESTMENTS: MUTUAL FUNDS. An insurer may invest the insurer's funds in excess of minimum capital and surplus in shares of a mutual fund engaged in business under the Investment Company Act of 1940 (15 U.S.C. Section 80a-1 et seq.), as amended, if:

(1) the mutual fund is solvent and has at least \$1 million of net assets as of the date of the mutual fund's latest annual or more recent certified audited financial statement; and

(2) the amount of the insurer's investment in a single mutual fund does not exceed 15 percent of the insurer's capital and surplus.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.064. AUTHORIZED INVESTMENTS: REAL PROPERTY. (a) Subject to this section, an insurer may invest the insurer's funds in excess of minimum capital and surplus in real property to the extent authorized by other provisions of this code.

(b) An insurer with admitted assets of more than \$500 million may own investment real property other than real property authorized by another provision of this code, or participations in that other investment real property, if the property is materially enhanced in value by:

(1) the construction of durable, permanent-type buildings and other improvements that cost an amount at least equal to the cost of the real property, excluding buildings and improvements at the time the property is acquired; or

(2) the construction, commenced before the second anniversary of the date the real property is acquired, of buildings and improvements described by Subdivision (1).

(c) The amount invested by an insurer in a single investment real property and improvements, or in any interest in real property and improvements, may not exceed five percent of the insurer's admitted assets in excess of \$500 million. The total amount invested by an insurer in investment real property and improvements may not exceed 15 percent of the insurer's admitted assets in excess of \$500 million.



(d) Except as provided by Section 862.002, an insurer may not own, develop, or hold an equity interest in any residential property or subdivision, single or multiunit family dwelling property, or undeveloped real property to subdivide for or develop residential, single or multiunit family dwellings. This subsection does not apply to an insurer with admitted assets of \$10 billion or more.

(e) The investment authority granted by this section is in addition to and separate from the investment authority granted by Section 862.002, except that an insurer may not invest in any real property that, when added to properties acquired by the insurer under Section 862.002, would exceed the limitations prescribed by that section.

(f) An insurer's admitted assets are determined from the insurer's annual statements that are made as of the December 31 that precedes the date of the determination and are filed with the department as required by law. The value of any investment made under this section is subject to the appraisal requirement of Section 862.002.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Amended by:

Acts 2013, 83rd Leg., R.S., Ch. 1175 (S.B. 841), Sec. 1, eff. September 1, 2013.

Sec. 424.065. ACTING AS REAL ESTATE BROKER OR SALESPERSON PROHIBITED. An insurer defined in Section 822.001 or 822.201 or another insurer specifically made subject to Sections 424.051, 424.053-424.071, and 424.074 may not engage in the business of a broker or salesperson as defined by Chapter 1101, Occupations Code, except that the insurer may hold, improve, maintain, manage, rent, lease, sell, exchange, or convey any of the real property interests legally owned as investments under this code.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.066. AUTHORIZED INVESTMENTS: OBLIGATIONS SECURED

BY REAL PROPERTY LOANS. (a) Subject to this section, an insurer may invest the insurer's funds in excess of minimum capital and surplus in a bond, note, or evidence of indebtedness, or a participation in a bond, note, or evidence of indebtedness, that is secured by a valid first lien on real property or a leasehold estate in real property located in the United States or in any state, commonwealth, territory, or possession of the United States.

(b) The amount of an obligation secured by a first lien on real property or a leasehold estate in real property may exceed 90 percent of the value of the real property or leasehold estate only if:

(1) the amount does not exceed 100 percent of the value of the real property or leasehold estate and the insurer or one or more wholly owned subsidiaries of the insurer owns, in the aggregate, a 10 percent or greater equity interest in the real property or leasehold estate;

(2) the amount does not exceed 95 percent of the value of the real property and:

(A) the property contains only a dwelling designed exclusively for occupancy by not more than four families for residential purposes; and

(B) the portion of the unpaid balance of the obligation that exceeds 90 percent of the value of the real property is guaranteed or insured by a mortgage guaranty insurer authorized to engage in business in this state; or

(3) the amount exceeds 90 percent of the value of the real property only to the extent the obligation is insured or guaranteed by:

(A) this state;

(B) the United States;

(C) the Federal Housing Administration under the National Housing Act (12 U.S.C. Section 1701 et seq.), as amended; or

(D) any other agency or instrumentality of the United States.

(c) The term of an obligation secured by a first lien on a leasehold estate in real property and improvements located on the

property may not exceed a period equal to four-fifths of the unexpired term of the leasehold estate, and the obligation must fully amortize during that period. The term of the leasehold estate may not expire sooner than the 10th anniversary of the expiration date of the term of the obligation.

(d) An obligation secured by a first lien on a leasehold estate in real property and improvements located on the property must be payable in equal monthly, quarterly, semiannual, or annual payments of principal plus accrued interest to the date of the principal payment.

(e) An insurer's investment in a single obligation under this section may not exceed 10 percent of the insurer's capital and surplus. An insurer's aggregate investments under this section may not exceed 30 percent of the insurer's assets.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.067. AUTHORIZED INVESTMENTS: TRANSPORTATION EQUIPMENT. An insurer may invest the insurer's funds in excess of minimum capital and surplus in:

(1) an adequately secured equipment trust obligation, certificate, or other instrument evidencing an interest in transportation equipment wholly or partly located in the United States; and

(2) a right to receive determined portions of rental, purchase, or other fixed obligatory payments for the use or purchase of the equipment.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.068. AUTHORIZED INVESTMENTS: INVESTMENT IN FOREIGN JURISDICTION. (a) In addition to the investments in Canada authorized by Sections 424.051, 424.058-424.071, and 424.074 and subject to this section, an insurer may invest the insurer's funds in excess of minimum capital and surplus in a foreign commonwealth, territory, or possession of the United States or a foreign country other than Canada, or invest in debt

obligations and investments within a foreign commonwealth, territory, or possession of the United States or within a foreign country other than Canada if:

(1) the investment is similar to investments the insurer is authorized by Sections [424.051](#), [424.058-424.071](#), and [424.074](#) to make within the United States or Canada; and

(2) the debt obligation or investment is rated one or two by the securities valuation office.

(b) The aggregate amount of an insurer's investments in a single foreign jurisdiction under Sections [424.051](#), [424.058-424.071](#), and [424.074](#) or of an insurer's debt obligations or investments within a single foreign jurisdiction may not exceed:

(1) as to a foreign jurisdiction that is given a sovereign debt rating of one by the securities valuation office, 10 percent of the insurer's admitted assets;

(2) as to a debt obligation or investment within a foreign jurisdiction that is rated one or two by the securities valuation office, 10 percent of the insurer's admitted assets; or

(3) as to any foreign investment other than an investment described by Subdivision (1) or (2), five percent of the insurer's admitted assets.

(c) The amount of investments made under this section may not exceed the sum of:

(1) the amounts authorized by Section [424.073](#); and

(2) 20 percent of the insurer's assets.

(d) The combined total of the amount of investments made under this section, the amount of similar investments made within the United States and Canada, and any amounts of investments authorized by Section [424.073](#) may not exceed any limitation prescribed by Sections [424.051](#), [424.058-424.071](#), and [424.074](#).

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. [2017](#)), Sec. 1, eff. April 1, 2007.

Amended by:

Acts 2013, 83rd Leg., R.S., Ch. 1175 (S.B. [841](#)), Sec. 2, eff. September 1, 2013.

Sec. 424.069. AUTHORIZED INVESTMENTS: CERTAIN LOANS. An

insurer may invest the insurer's funds in excess of minimum capital and surplus in a loan on the pledge of any mortgage, stock, bond, or other evidence of indebtedness acceptable as an investment under Sections 424.051, 424.053-424.071, and 424.074, if the current value of the mortgage, stock, bond, or other evidence of indebtedness is at least 25 percent more than the amount of the loan.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.070. AUTHORIZED INVESTMENTS: OBLIGATIONS OF LOCAL GOVERNMENTAL ENTITIES. (a) Subject to this section, an insurer may invest the insurer's funds in excess of minimum capital and surplus in a bond or other interest-bearing evidence of indebtedness of a:

- (1) county or subdivision of a county;
- (2) municipality;
- (3) road district;
- (4) turnpike district or authority;
- (5) water district;
- (6) school district;
- (7) sanitary or navigation district; or

(8) municipally owned revenue water system, sewer system, or electric utility company with respect to which the municipality has appropriated, pledged, or otherwise provided for special revenues to meet the principal and interest payments of the bond or other evidence of indebtedness.

(b) A bond or other evidence of indebtedness of a navigation district is an authorized investment under this section only if:

- (1) the navigation district is located wholly or partly in a county that has a population of at least 100,000; and
- (2) the interest due on the bond or other evidence of indebtedness has never been in default.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.071. AUTHORIZED INVESTMENTS: THE UNIVERSITY OF

TEXAS. An insurer may invest the insurer's funds in excess of minimum capital and surplus in an interest-bearing note or bond of The University of Texas issued under the laws of this state.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.072. AUTHORIZED INVESTMENTS: BONDS ISSUED, ASSUMED, OR GUARANTEED IN INTERNATIONAL MARKET. An insurer may invest the insurer's funds in excess of minimum capital and surplus in bonds issued, assumed, or guaranteed by any of the following international financial institutions in which the United States is a member:

- (1) the Inter-American Development Bank;
- (2) the International Bank for Reconstruction and Development (the World Bank);
- (3) the African Development Bank;
- (4) the Asian Development Bank; or
- (5) the International Finance Corporation.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.073. AUTHORIZED INVESTMENTS: INSURER ENGAGED IN BUSINESS IN FOREIGN COUNTRY. (a) Subject to this section, an insurer authorized by the law of a foreign country to engage in a line of insurance in which the insurer is authorized to engage in this state may invest in foreign securities originating in the foreign country of the same kind as the domestic securities originating in the United States in which the insurer is authorized to invest under Sections 424.051, 424.053-424.071, and 424.074.

(b) The aggregate amount of an insurer's investments made under this section in a single country may not exceed by more than 10 percent at any time the lesser of:

- (1) the amount of funds required by the law of the foreign country to be maintained in securities originating in that country; or
- (2) the amount of total unearned premium reserves, reinsurance reserves, loss reserves, and any other liabilities

required by the law of this state to be carried by the insurer that are directly attributable to the particular insurance policies or contracts on residents or property located in the foreign country.

(c) This section does not authorize an insurer to invest in a foreign security originating in a foreign country with respect to which the president of the United States or other federal authority has refused to exercise the authority to issue guarantees on projects in the country to citizens or corporations of the United States against loss by reason of inconvertibility of currency, expropriation, confiscation, war, revolution, or insurrection because the foreign country has failed to enter into arrangements for the security of American property as required by the president or other federal authority for the issuance of those guarantees.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.074. OTHER SPECIFICALLY AUTHORIZED INVESTMENTS. An insurer may invest the insurer's funds in excess of minimum capital and surplus in:

- (1) a savings account as authorized by Chapter 65, Finance Code;
- (2) a bond or other indebtedness as authorized by Sections 435.045 and 435.046, Government Code;
- (3) a bond issued under Subchapter B, Chapter 1505, Government Code;
- (4) a bond as authorized by Subchapter B, Chapter 284, Transportation Code;
- (5) a municipal bond issued under Sections 51.038 and 51.039, Water Code;
- (6) an insured account or evidence of indebtedness as authorized by Section 1, Chapter 160, General Laws, Acts of the 43rd Legislature, Regular Session, 1933 (Article 842a, Vernon's Texas Civil Statutes);
- (7) an insured or guaranteed obligation as authorized by Chapter 230, Acts of the 49th Legislature, Regular Session, 1945 (Article 842a-1, Vernon's Texas Civil Statutes);
- (8) a bond issued under Section 1, Chapter 1, page 427,

General Laws, Acts of the 46th Legislature, Regular Session, 1939 (Article [1269k-1](#), Vernon's Texas Civil Statutes);

(9) a bond as authorized by Section 24, Chapter 110, Acts of the 51st Legislature, Regular Session, 1949 (Article 8280-133, Vernon's Texas Civil Statutes);

(10) a bond as authorized by Section 19, Chapter 340, Acts of the 51st Legislature, Regular Session, 1949 (Article 8280-137, Vernon's Texas Civil Statutes);

(11) a bond as authorized by Section 10, Chapter 398, Acts of the 51st Legislature, Regular Session, 1949 (Article 8280-138, Vernon's Texas Civil Statutes);

(12) a bond as authorized by Section 18, Chapter 465, Acts of the 51st Legislature, Regular Session, 1949 (Article 8280-139, Vernon's Texas Civil Statutes); or

(13) another investment specifically authorized by law.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. [2017](#)), Sec. 1, eff. April 1, 2007.

#### SUBCHAPTER C. INVESTMENT POOLS

Sec. 424.101. DEFINITIONS. In this subchapter:

(1) "Business entity" means an association, corporation, joint stock company, joint venture, limited liability company, mutual fund trust, partnership, or other similar form of business organization, regardless of whether organized for profit.

(2) "Obligation" means:

(A) a bond, note, debenture, trust certificate, including an equipment certificate, or production payment;

(B) a negotiable bank certificate of deposit, bankers' acceptance, credit tenant loan, or other loan secured by financing net leases; or

(C) any other evidence of indebtedness for the payment of money or participation certificates or other evidences of an interest in an obligation otherwise described by this subdivision, whether constituting a general obligation of the issuer or payable only out of certain revenues or certain funds



pledged or otherwise dedicated for payment.

(3) "Qualified bank" means a national bank, state bank, or trust company that:

(A) is at all times adequately capitalized as determined by the standards adopted by the United States banking regulators; and

(B) is either a member of the Federal Reserve System or regulated by state banking laws.

(4) "Repurchase transaction," "reverse repurchase transaction," and "securities lending transaction" have the meanings assigned by Section [424.151](#).

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. [2017](#)), Sec. 1, eff. April 1, 2007.

Sec. 424.102. AUTHORITY TO INVEST IN POOL. An insurer may acquire investments and participate in an investment pool that is qualified under Section [424.103](#)(b) and the investments of which are limited to investments authorized for:

(1) a short-term investment pool under Section [424.104](#); or

(2) an authorized investment pool under Section [424.107](#).

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. [2017](#)), Sec. 1, eff. April 1, 2007.

Sec. 424.103. INVESTMENT POOL REQUIREMENTS AND QUALIFICATIONS. (a) An investment pool must be a business entity.

(b) To be qualified, an investment pool must:

(1) have a written pooling agreement and a pool manager that comply with the requirements of this subchapter; and

(2) comply with Subsection (c).

(c) The investment pool may not:

(1) acquire securities issued, assumed, guaranteed, or insured by the investing insurer or an affiliate of the investing insurer;

(2) borrow or incur indebtedness for borrowed money, except for securities lending and reverse repurchase transactions

that meet the requirements of this subchapter; or

(3) permit the aggregate value of securities loaned or sold to, purchased from, or invested in a single business entity at the time of the loan, sale, purchase, or investment to exceed 10 percent of the pool's total assets.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.104. AUTHORIZED INVESTMENTS FOR SHORT-TERM INVESTMENT POOL. A short-term investment pool may contain only:

- (1) obligations described by Section 424.105;
- (2) money market funds described by Section 424.106;

or

(3) repurchase, reverse repurchase, and securities lending transactions that meet the requirements of Subchapter D.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.105. SHORT-TERM INVESTMENT POOL: CERTAIN SHORT-TERM OBLIGATIONS. (a) Obligations contained in a short-term investment pool must meet the requirements of this section.

(b) The obligations must:

(1) have a rating by the securities valuation office of one or two, or an equivalent rating issued by a nationally recognized statistical rating organization recognized by the securities valuation office; or

(2) be issued by an issuer with outstanding obligations that have a rating described by Subdivision (1).

(c) The obligations must have:

(1) a remaining maturity of 397 days or less or a put that:

(A) entitles the holder to receive the principal amount of the obligation; and

(B) may be exercised through maturity at specified intervals not exceeding 397 days; or

(2) a remaining maturity of three years or less and a floating interest rate that resets at least quarterly on the basis

of a current short-term index and is not subject to a maximum limit, if the obligations do not have an interest rate that varies inversely to market interest rate changes.

(d) For purposes of this section, a current short-term index is:

- (1) a federal funds rate;
- (2) the prime rate;
- (3) the rate for treasury bills;
- (4) the London InterBank Offered Rate; or
- (5) the rate for commercial paper.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.106. SHORT-TERM INVESTMENT POOL: CERTAIN MONEY MARKET FUNDS. A short-term investment pool may contain a money market fund as described by 17 C.F.R. Section 270.2a-7 under the Investment Company Act of 1940 (15 U.S.C. Section 80a-1 et seq.), as amended, that is:

- (1) a government money market fund that at all times:
  - (A) invests only in obligations issued, guaranteed, or insured by the United States or collateralized repurchase agreements composed of those obligations; and
  - (B) qualifies for investment without a reserve under the Purposes and Procedures Manual of the securities valuation office or a successor publication; or

- (2) a class one money market fund that at all times qualifies for investment using the bond class one reserve factor described by the Purposes and Procedures Manual of the securities valuation office.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.107. AUTHORIZED INVESTMENTS FOR AUTHORIZED INVESTMENT POOL; LIMITATION. (a) An authorized investment pool may contain only investments that a participating insurer is authorized to acquire by provisions of this code other than this subchapter.

(b) The insurer's total of proportionate ownership interests in a single authorized investment held by an authorized investment pool and the insurer's direct investments in that authorized investment may not exceed the limit prescribed by the applicable authorizing provision.

(c) In addition to the limitation described by Subsection (b), an insurer is subject to the limitations described by Section [424.108](#).

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. [2017](#)), Sec. 1, eff. April 1, 2007.

Sec. 424.108. GENERAL INSURER INVESTMENT LIMITATIONS. An insurer may not acquire an investment in an investment pool if, as a result of and after making the investment, the aggregate amount of investments held by the insurer under this subchapter at the time of the investment:

(1) in a single investment pool would exceed 10 percent of the insurer's admitted assets;

(2) in all investment pools investing in investments authorized under Section [424.107](#) would exceed 25 percent of the insurer's admitted assets; or

(3) in all investment pools would exceed 35 percent of the insurer's admitted assets.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. [2017](#)), Sec. 1, eff. April 1, 2007.

Sec. 424.109. DESIGNATION OF POOL MANAGER; QUALIFICATIONS.

(a) The pooling agreement for an investment pool must designate a pool manager.

(b) The pool manager must be organized under the laws of the United States or a state and must be:

(1) the investing insurer, an affiliated insurer, or a business entity affiliated with the insurer;

(2) a qualified bank;

(3) a business entity registered under the Investment Advisers Act of 1940 (15 U.S.C. Section 80b-1 et seq.), as amended;

(4) the attorney-in-fact of a reciprocal or

interinsurance exchange; or

(5) the United States manager or an affiliate or subsidiary of the United States manager of a United States branch of an alien insurer.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.110. POOL MANAGER TO MAINTAIN ASSETS; CUSTODY AGREEMENT. (a) The pool manager shall maintain the assets of the investment pool in one or more accounts, in the name of or on behalf of the pool, under a custody agreement with a qualified bank.

(b) The custody agreement must:

(1) state and recognize the claims and rights of each participant;

(2) acknowledge that the investment pool's underlying assets are held solely for the benefit of each participant in proportion to the aggregate amount of the participant's investments in the pool; and

(3) contain an agreement that the pool's underlying assets may not be commingled with the general assets of the custodian qualified bank or any other person.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.111. POOLING AGREEMENT PROVISIONS. The pooling agreement for an investment pool must provide that:

(1) 100 percent of the ownership interests in the pool must at all times be held by:

(A) an insurer and the insurer's affiliated insurers;

(B) for a pool investing solely in investments authorized under Section 424.104, the insurer and the insurer's subsidiaries and affiliates or any pension or profit-sharing plan of the insurer and the insurer's subsidiaries and affiliates; or

(C) for a United States branch of an alien insurer, subsidiaries or affiliates of the insurer's United States manager;

(2) the pool's underlying assets are held solely for the benefit of each participant and may not be commingled with the general assets of the pool manager or any other person;

(3) each participant owns an undivided interest in the pool's underlying assets in proportion to the aggregate amount of the participant's interest in the pool; and

(4) a pool participant or, if a pool participant is insolvent, bankrupt, or in receivership, the participant's trustee, receiver, conservator, or other successor-in-interest may withdraw all or any portion of the participant's investment from the pool under the terms of the pooling agreement.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.112. WITHDRAWALS AND DISTRIBUTIONS. (a) A pool participant must be able to make withdrawals on demand without penalty or other assessment on any business day, and settlement of funds must occur within a reasonable and customary period that does not exceed five business days after a withdrawal.

(b) The pooling agreement must provide that the pool manager shall make a distribution to a pool participant, at the manager's discretion:

(1) in cash in an amount equal to the fair market value at the time of the distribution of the participant's pro rata share of each of the pool's underlying assets;

(2) in kind in an amount equal to a pro rata share of each underlying asset; or

(3) in a combination of cash and in-kind distributions in an amount equal to a pro rata share of each underlying asset.

(c) A distribution under Subsection (b) must be computed after subtracting all the investment pool's applicable fees and expenses.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.113. INVESTMENT POOL RECORDS. The pool manager shall compile and maintain:

(1) detailed accounting records that show:

(A) the cash receipts and disbursements reflecting each pool participant's proportionate investment in the investment pool; and

(B) a complete description of all the pool's underlying assets, including the amount, interest rate, and maturity date, if any, of each of those assets and other appropriate designations; and

(2) other records that, on a daily basis, allow third parties to verify each participant's investment in the pool.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.114. INSPECTION OF RECORDS. The pool manager shall make records of the investment pool available for inspection by the commissioner.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.115. REPORTS OF TRANSACTIONS BETWEEN POOL AND PARTICIPANT. (a) A transaction between an investment pool and a pool participant is not subject to Subchapter C, Chapter 823, except that before entering into a pool, an insurer subject to Chapter 823 shall give the commissioner the written notice required under Section 823.103.

(b) The investment pool's investment activities and the transactions between the pool and a pool participant must be reported in the registration statement required by Subchapter B, Chapter 823.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

SUBCHAPTER D. DOLLAR ROLL, REPURCHASE, REVERSE REPURCHASE,  
AND SECURITIES LENDING TRANSACTIONS

Sec. 424.151. DEFINITIONS. In this subchapter:

(1) "Dollar roll transaction" means two simultaneous

transactions with settlement dates not more than 96 days apart, in one of which an insurer sells to a business entity, and in the other of which the insurer is obligated to purchase from the same business entity, substantially similar securities that are:

(A) mortgage-backed securities issued, assumed, or guaranteed by the Government National Mortgage Association, the Federal National Mortgage Association, the Federal Home Loan Mortgage Corporation, or a successor to one of those organizations; or

(B) other mortgage-backed securities referred to in 15 U.S.C. Section 77r-1 et seq., as amended.

(2) "Repurchase transaction" means a transaction in which an insurer purchases securities from a business entity that is obligated to repurchase the purchased securities or equivalent securities from the insurer at a specified price, either within a specified period or on demand.

(3) "Reverse repurchase transaction" means a transaction in which an insurer sells securities to a business entity and is obligated to repurchase the sold securities or equivalent securities from the business entity at a specified price, either within a specified period or on demand.

(4) "Securities lending transaction" means a transaction in which an insurer lends securities to a business entity that is obligated to return the loaned securities or equivalent securities to the insurer, either within a specified period or on demand.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.152. TRANSACTIONS AUTHORIZED. An insurer may engage in dollar roll, repurchase, reverse repurchase, and securities lending transactions as provided by this subchapter.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.153. PERIOD OF TRANSACTION. An insurer must enter into a written agreement for each transaction under this



subchapter, other than a dollar roll transaction. The agreement must require that the transaction terminate on or before the first anniversary of the transaction's inception.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.154. CASH REQUIREMENTS. With respect to cash received in a transaction under this subchapter, an insurer shall:

(1) invest the cash in accordance with this subchapter and in a manner that recognizes the liquidity needs of the transaction; or

(2) use the cash for the insurer's general corporate purposes.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.155. COLLATERAL REQUIREMENTS. (a) While a transaction under this subchapter is outstanding, the insurer or the insurer's agent or custodian shall maintain, as to acceptable collateral received in the transaction, either physically or through the book-entry system of the Federal Reserve, Depository Trust Company, Participants Trust Company, or another securities depository approved by the commissioner:

(1) possession of the collateral;

(2) a perfected security interest in the collateral; or

(3) in the case of a jurisdiction outside of the United States, title to, or the rights of a secured creditor to, the collateral.

(b) The amount of collateral required for repurchase, reverse repurchase, and securities lending transactions is the amount required under the Purposes and Procedures Manual of the securities valuation office or a successor publication.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.156. PERCENTAGE LIMITATIONS. (a) An insurer may

not enter into a transaction under this subchapter if, as a result of and after making the transaction, the aggregate amount of securities loaned or sold to or purchased from:

(1) a single business entity counterparty under this subchapter would exceed five percent of the insurer's assets; or

(2) all business entities under this subchapter would exceed 40 percent of the insurer's assets.

(b) In computing the amount sold to or purchased from a business entity counterparty under a repurchase or reverse repurchase transaction, effect may be given to netting provisions under a master written agreement.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.157. RULES. The commissioner may adopt reasonable rules and issue reasonable orders as necessary to implement this subchapter.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

#### SUBCHAPTER E. RISK CONTROL TRANSACTIONS

Sec. 424.201. DEFINITIONS. In this subchapter:

(1) "Acceptable collateral" means:

(A) cash;

(B) cash equivalents;

(C) letters of credit and direct obligations; or

(D) securities that are fully guaranteed as to

principal and interest by the United States.

(2) "Business entity" includes an association, bank, corporation, joint stock company, joint tenancy, joint venture, limited liability company, mutual fund, partnership, sole proprietorship, trust, or other similar form of business organization, regardless of whether organized for profit.

(3) "Cap" means an agreement obligating the seller to make payments to the buyer, with each payment based on the amount by which a reference price or level or the performance or value of one

or more underlying interests exceeds a predetermined number that is sometimes called the strike rate or strike price.

(4) "Cash equivalent" means an investment or security that is short-term, highly rated, highly liquid, and readily marketable. The term includes a money market fund described by Section 424.106. For purposes of this subdivision, an investment or security is:

(A) short-term if it has a remaining term to maturity of one year or less; and

(B) highly rated if it has:

(i) a rating of "P-1" by Moody's Investors Service, Inc.;

(ii) a rating of "A-1" by the Standard and Poor's Division of the McGraw Hill Companies, Inc.; or

(iii) an equivalent rating by a nationally recognized statistical rating organization recognized by the securities valuation office.

(5) "Collar" means an agreement to receive payments as the buyer of a cap, floor, or option and to make payments as the seller of a different cap, floor, or option.

(6)(A) "Counterparty exposure amount" means:

(i) for an over-the-counter derivative instrument not entered into under a written master agreement that provides for netting of payments owed by the respective parties, 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 zero, if the liquidation of the derivative instrument would not result in a final cash payment to the insurer; or

(ii) for an over-the-counter derivative instrument entered into under a written master agreement that provides for netting of payments owed by the respective parties and for which the counterparty's domiciliary jurisdiction is within the United States or a foreign jurisdiction listed in the Purposes and Procedures Manual of the securities valuation office as eligible for netting, the greater of zero or the net sum payable to the insurer in connection with all derivative instruments subject to

the written master agreement on the liquidation of the instruments in the event of the counterparty's default under the master agreement, if there is no condition precedent to the counterparty's obligation to make the payment and if there is no setoff of amounts payable under another instrument or agreement.

(B) For purposes of this subdivision, market value or the net sum payable, as applicable, must be determined at the end of the most recent quarter of the insurer's fiscal year and must be reduced by the market value of acceptable collateral held by the insurer or a custodian on the insurer's behalf.

(7) "Derivative instrument":

(A) means an agreement, option, or instrument, or a series or combination of agreements, options, or instruments:

(i) 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 instead of making or taking delivery of, or assuming or relinquishing, a specified amount of an underlying interest; or

(ii) that has a price, performance, value, or cash flow based primarily on the actual or expected price, yield, level, performance, value, or cash flow of one or more underlying interests;

(B) includes an option, a warrant not otherwise permitted to be held by the insurer under this subchapter, a cap, a floor, a collar, a swap, a swaption, a forward, a future, any other substantially similar agreement, option, or instrument, and a series or combination of those agreements, options, or instruments; and

(C) does not include a collateralized mortgage obligation, another asset-backed security, a principal-protected structured security, a floating rate security, an instrument that an insurer would otherwise be authorized to invest in or receive under a provision of this subchapter other than this subdivision, or a debt obligation of the insurer.

(8) "Derivative transaction" means a transaction involving the use of one or more derivative instruments. The term does not include a dollar roll transaction, repurchase transaction,

reverse repurchase transaction, or securities lending transaction.

(9) "Floor" means an agreement obligating the seller to make payments to the buyer, each of which is based on the amount by which a predetermined number that is sometimes called the floor price or floor rate exceeds a reference level, performance, price, or value of one or more underlying interests.

(10) "Forward" means an agreement to make or take delivery in the future of one or more underlying interests, or to effect a cash settlement, based on the actual or expected level, performance, price, or value of those interests. The term does not include a future or a spot transaction effected within a customary settlement period, a when-issued purchase, or another similar cash market transaction.

(11) "Future" means an agreement traded on a futures exchange to make or take delivery of one or more underlying interests, or to effect a cash settlement, based on the actual or expected level, performance, price, or value of those interests.

(12) "Futures exchange" means a foreign or domestic exchange, contract market, or board of trade on which trading in futures is conducted and that, in the United States, is authorized to conduct that trading by the Commodity Futures Trading Commission or a successor to that agency.

(13) "Hedging transaction" means a derivative transaction entered into and maintained to manage, with respect to an asset, liability, or portfolio of assets or liabilities, that an insurer has acquired or incurred or anticipates acquiring or incurring:

(A) the risk of a change in value, yield, price, cash flow, or quantity; or

(B) the currency exchange rate risk.

(14) "Income generation transaction" means a derivative transaction entered into to generate income. The term does not include a hedging transaction or a replication transaction.

(15) "Market value" means the price for a security or derivative instrument obtained from a generally recognized source, the most recent quotation from a generally recognized source, or if

a generally recognized source does not exist, the price determined under the terms of the instrument or in good faith by the insurer, as can be reasonably demonstrated to the commissioner on request, plus the amount of accrued but unpaid income on the security or instrument to the extent that amount is not included in the price as of the date the security or instrument is valued.

(16) "Option" means an agreement giving the buyer the right to buy or receive, referred to as a "call option," to sell or deliver, referred to as a "put option," to enter into, extend, or terminate, or to effect a cash settlement based on the actual or expected level, performance, price, spread, or value of, one or more underlying interests.

(17) "Over-the-counter derivative instrument" means a derivative instrument entered into with a business entity in a manner other than through a securities exchange or futures exchange or cleared through a qualified clearinghouse.

(18) "Potential exposure" means:

(A) as to a futures position, the amount of initial margin required for that position; or

(B) as to a swap, collar, or forward, one-half of one percent multiplied by the notional amount multiplied by the square root of the remaining years to maturity.

(19) "Qualified clearinghouse" means a clearinghouse that:

(A) is subject to the rules of a securities exchange or a futures exchange; and

(B) provides clearing services, including acting as a counterparty to each of the parties to a transaction in a manner that eliminates the parties' credit risk to each other.

(20) "Replication transaction" means a derivative transaction or a combination of derivative transactions effected separately or in conjunction with cash market investments included in the insurer's investment portfolio to replicate the risks and returns of another authorized transaction, investment, or instrument or to operate as a substitute for cash market transactions. The term does not include a hedging transaction.

(21) "Securities exchange" means:

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

(B) the Private Offerings, Resales and Trading through Automated Linkages system; or

(C) a designated offshore securities market as defined by 17 C.F.R. Section 230.902, as amended.

(22) "Swap" means an agreement to exchange or to net payments at one or more times based on the actual or expected price, yield, level, performance, or value of one or more underlying interests.

(23) "Swaption" means an option to purchase or sell a swap at a given price and time or at a series of prices and times. The term does not include a swap with an embedded option.

(24) "Underlying interest" means an asset, liability, or other interest underlying a derivative instrument or a combination of those assets, liabilities, or interests. The term includes a security, currency, rate, index, commodity, or derivative instrument.

(25) "Warrant" means an instrument under which the holder has the right to purchase or sell the underlying interest at a given price and time or at a series of prices and times stated in the warrant.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.202. RISK CONTROL TRANSACTIONS AUTHORIZED. (a) Except as provided by Subsection (b), an insurer may engage in a risk control transaction authorized by this subchapter to:

(1) protect the insurer's assets against the risk of changing asset values or interest rates;

(2) reduce risk; and

(3) generate income.

(b) An insurer with a statutory net capital and surplus as determined by the insurer's most recent financial statement required to be filed with the department that is less than the

minimum amount of capital and surplus required for a new charter and certificate of authority for the same type of insurer may not engage in a transaction authorized under this subchapter.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.203. NOTICE OF INTENT TO ENGAGE IN RISK CONTROL TRANSACTIONS REQUIRED. (a) Before an insurer with a statutory net capital and surplus of less than \$10 million engages in a transaction authorized under this subchapter, the insurer shall file a written notice with the commissioner describing:

- (1) the need to engage in the transaction;
- (2) the lack of acceptable alternatives; and
- (3) the insurer's plan to engage in the transaction.

(b) If the commissioner does not issue an order prohibiting an insurer who files a notice under Subsection (a) from engaging in the transaction on or before the 90th day after the date the commissioner receives the notice, the insurer may engage in the transaction described in the notice.

(c) For purposes of this section, an insurer's net capital and surplus are determined by the insurer's most recent financial statement required to be filed with the department.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.204. TRADING REQUIREMENTS FOR DERIVATIVE INSTRUMENTS. Each derivative instrument must be:

- (1) traded on a securities 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) in the case of futures, traded through a broker who is:

(A) registered as a futures commission merchant under the Commodity Exchange Act (7 U.S.C. Section 1 et seq.), as



amended; or

(B) exempt from that registration under 17 C.F.R. Section 30.10, adopted under the Commodity Exchange Act (7 U.S.C. Section 1 et seq.), as amended.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.205. DERIVATIVE USE PLAN. (a) Before an insurer enters into a derivative transaction, the insurer's board of directors must approve a derivative use plan as part of the insurer's investment plan otherwise required by law.

(b) The derivative use plan must:

(1) describe investment objectives and risk constraints, such as counterparty exposure amounts;

(2) define permissible transactions, identifying the risks to be hedged and the assets or liabilities being replicated; and

(3) require compliance with the insurer's internal control procedures established under Section 424.206.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.206. INTERNAL CONTROL PROCEDURES. An insurer that enters into a derivative transaction shall establish written internal control procedures that require:

(1) a quarterly report to the board of directors that reviews:

(A) each derivative transaction entered into, outstanding, or closed out;

(B) the results and effectiveness of the derivatives program; and

(C) the credit risk exposure to each counterparty for over-the-counter derivative transactions based on the counterparty exposure amount;

(2) a system for determining whether hedging or replication strategies used by the insurer have been effective;

(3) a system of reports, at least as frequent as

monthly, to the insurer's management, that include:

(A) a description of each derivative transaction entered into, outstanding, or closed out during the period since the last report;

(B) the purpose of each outstanding derivative transaction;

(C) a performance review of the derivative instrument program; and

(D) the counterparty exposure amount for each over-the-counter derivative transaction;

(4) a written authorization that identifies the responsibilities and limitations of authority of each person authorized to effect and maintain derivative transactions; and

(5) appropriate documentation for each transaction, including:

(A) the purpose of the transaction;

(B) the assets or liabilities to which the transaction relates;

(C) the specific derivative instrument used in the transaction;

(D) for an over-the-counter derivative transaction, the name of the counterparty and the counterparty exposure amount; and

(E) for an exchange-traded derivative instrument, the name of the exchange and the name of the firm that handled the transaction.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.207. ABILITY TO DEMONSTRATE HEDGING CHARACTERISTICS AND EFFECTIVENESS. An insurer must be able to demonstrate to the commissioner on request the intended hedging characteristics and continuing effectiveness of a derivative transaction or combination of transactions through:

(1) cash flow testing;

(2) duration analysis; or

(3) other appropriate analysis.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.208. OFFSETTING TRANSACTIONS. (a) Subject to this section, an insurer may purchase or sell one or more derivative instruments to wholly or partly offset a derivative instrument previously purchased or sold, without regard to the quantitative limitations of this subchapter.

(b) An offsetting transaction under this section must use the same type of derivative instrument as the derivative instrument being offset.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.209. INCLUSION OF COUNTERPARTY EXPOSURE AMOUNTS. The insurer shall include all counterparty exposure amounts in determining compliance with the limitations of this subchapter.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.210. OVERSIGHT BY COMMISSIONER. (a) Not later than the 10th day before the date an insurer is scheduled to enter into an initial hedging transaction, the insurer shall notify the commissioner in writing that:

(1) the insurer's board of directors has adopted an investment plan that authorizes hedging transactions; and

(2) each hedging transaction will comply with this subchapter.

(b) If a hedging transaction does not comply with this subchapter or if continuing the transaction may create a hazardous financial condition for the insurer that affects the insurer's policyholders or creditors or the public, the commissioner may, after notice and an opportunity for a hearing, order the insurer to take action that the commissioner determines is reasonably necessary to:

(1) remedy a hazardous financial condition; or

(2) prevent an impending hazardous financial

condition from occurring.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.211. AUTHORITY TO ENTER INTO HEDGING TRANSACTION. After providing notice under Section 424.210, an insurer may enter into a hedging transaction under this subchapter if as a result of and after making the transaction:

(1) the aggregate statement value of all outstanding caps, floors, options, swaptions, and warrants not attached to another financial instrument purchased by the insurer under this subchapter, other than a collar, does not exceed 7.5 percent of the insurer's assets;

(2) the aggregate statement value of all outstanding caps, floors, options, swaptions, and warrants written by the insurer under this subchapter, other than a collar, does not exceed three percent of the insurer's assets; and

(3) the aggregate potential exposure of all outstanding collars, forwards, futures, and swaps entered into or acquired by the insurer under this subchapter does not exceed 6.5 percent of the insurer's assets.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.212. AUTHORITY TO ENTER INTO INCOME GENERATION TRANSACTION. An insurer may enter into an income generation transaction only if:

(1) as a result of and after making the transaction, the sum of the following amounts does not exceed 10 percent of the insurer's assets:

(A) the aggregate statement value of admitted assets that at the time of the transaction are subject to call or that generate the cash flows for payments the insurer is required to make under caps and floors sold by the insurer and that at the time of the transaction are outstanding under this subchapter;

(B) the statement value of admitted assets underlying derivative instruments that at the time of the

transaction are subject to calls sold by the insurer and outstanding under this subchapter; and

(C) the purchase price of assets subject to puts that at the time of the transaction are outstanding under this subchapter; and

(2) the transaction is a sale of:

(A) a call option on assets that meets the requirements of Section 424.213;

(B) a put option on assets that meets the requirements of Section 424.214;

(C) a call option on a derivative instrument, including a swaption, that meets the requirements of Section 424.215; or

(D) a cap or floor that meets the requirements of Section 424.216.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.213. LIMITATION ON SALE OF CALL OPTION ON ASSETS. If an income generation transaction is a sale of a call option on assets, the insurer must, during the entire period the option is outstanding, hold, or have a currently exercisable right to acquire, the underlying assets.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.214. LIMITATION ON SALE OF PUT OPTION ON ASSETS. (a) If an income generation transaction is a sale of a put option on assets, the insurer must:

(1) during the entire period the option is outstanding, hold sufficient cash, cash equivalents, or interests in a short-term investment pool to purchase the underlying assets on exercise of the option; and

(2) have the ability to hold the underlying assets in the insurer's portfolio.

(b) If during the entire period the put option is outstanding the total market value of all put options sold by the

insurer exceeds two percent of the insurer's assets, the insurer shall set aside, under a custodial or escrow agreement, cash or cash equivalents that have a market value equal to the amount of the insurer's put option obligations in excess of two percent of the insurer's assets.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.215. LIMITATION ON SALE OF CALL OPTION ON DERIVATIVE INSTRUMENT. If an income generation transaction is a sale of a call option on a derivative instrument, including a swaption, the insurer must:

(1) during the entire period the call option is outstanding, hold, or have a currently exercisable right to acquire, assets generating the cash flow necessary to make any payment for which the insurer is liable under the underlying derivative instrument; and

(2) have the ability to enter into the underlying derivative transaction for the insurer's portfolio.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.216. LIMITATION ON SALE OF CAP OR FLOOR. If an income generation transaction is a sale of a cap or a floor, the insurer must, during the entire period the cap or floor is outstanding, hold, or have a currently exercisable right to acquire, assets generating the cash flow necessary to make any payment for which the insurer is liable under the cap or floor.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.217. AUTHORITY TO ENTER REPLICATION TRANSACTION.

(a) An insurer may enter into a replication transaction only with the prior written approval of the commissioner.

(b) To be eligible for approval by the commissioner:

(1) the insurer must be otherwise authorized to invest the insurer's funds under this chapter in the asset being

replicated; and

(2) the asset being replicated must be subject to all the provisions of this subchapter relating to the making of the transaction by the insurer with respect to that kind of asset as if the transaction constituted a direct investment by the insurer in the replicated asset.

(c) The commissioner may adopt rules regarding replication transactions as necessary to implement this section.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.

Sec. 424.218. RULES. The commissioner may adopt rules consistent with this subchapter that prescribe reasonable limits, standards, and guidelines for:

(1) the risk control transactions authorized under this subchapter; and

(2) plans related to those transactions.

Added by Acts 2005, 79th Leg., Ch. 727 (H.B. 2017), Sec. 1, eff. April 1, 2007.