

Clearinghouse Rule 20-002

PROPOSED ORDER REPEALING, RENUMBERING, RENUMBERING AND AMENDING, AMENDING, REPEALING AND RECREATING AND CREATING A RULE

Office of the Commissioner of Insurance

Rule No. Agency 145 – INS 2.02, 2.04 and 6.20, Wis. Adm. Code, proposes an order to **repeal** INS 2.02, 2.04, 6.20 (3) (a), (b), (d), and (j), (d) 5. and 8., (e) 3., (8) (j), (k), (m) and (o); **to renumber and amend** INS 6.20 (6) (d) 3. a. to c.; **to consolidate, renumber and amend** INS 6.20 (6) (e) (intro.), 1. and 2.; **to amend** INS 6.20 (4), (5) (intro.), (a) and 2. to 5., (6) (b) (intro.) and 1. to 6., (6) (c) (intro.) and 1. and 2., (6) (f) (intro.) and 1. and 2.; **to repeal and recreate** INS 6.20 (5) (a) 1., (6) (g); **to create** INS 6.20 (3) (ee), (em), (es), (hg), (hr), (jm), (6) (am), (6) (b) 5g. and 5r., (6) (d) 3p., 3t., and 3x., (6) (d) 8m., (6) (f) 3. to 6., (6) (h) 4. a. to c., (6) (i), (8g), and (8r), Wis. Adm. Code, relating to the repeal of restrictions related to the allocation of dividends to participating life insurance policies issued by a stock company, rating practices for exceeding filed rates for substandard risks, and revisions to the definition of investment terms, limitations on the investments of town mutual insurers and the permissible scope of foreign investments and affecting small business.

The statement of scope for this rule SS: 031-19, was approved by the Governor on March 13, 2019, published in Register No. 759A3 on March 18, 2019, and approved by the Commissioner on May 13, 2019.

ANALYSIS PREPARED BY THE OFFICE OF THE COMMISSIONER OF INSURANCE (OCI)

Statutes interpreted:

Sections 610.23, 620.01, 620.03, 620.21, 620.22, and 620.23, Stats.

Statutory authority:

Sections 601.41 (3), 601.42 (1g), 620.01, 620.03, 620.21, 620.22, and 620.23, Stats.

Explanation of the commissioner's authority to promulgate the proposed rule under these statutes:

The statutory authority for these rules is generally found in s. 601.41 (3), Stats., which provide for the commissioner's rule making authority in general, and s. 601.42, Stats. that authorizes the commissioner to require certain reports and other disclosure of information.

Wisconsin's investment regulations are contained in ch. 620, Stats. The commissioner has specific authority to regulate investments by rule under ss. 620.01, 620.03, 620.21, 620.22,

and 620.23, Stats. Specifically, s. 620.01 (2), Stats., provides in the scope statement, that “the chapter and the rules promulgated to interpret and implement it, apply to all insurers authorized to do business in this state.” Sections 620.03 (1) and (3), Stats., identifies that the commissioner may by rule prescribe procedural requirements and substantive restrictions for certain classes of insurers pertaining to special investments, and the commissioner may extend substantive restrictions by rule beyond 5 years if the commissioner finds that financial condition or management requires additional investment regulations to protect the interests of insureds, creditors, or the public in this state, respectively.

Section 620.21, Stats., permits the commissioner to identify investments that may be counted as admitted assets towards satisfaction of the compulsory surplus requirement or security surplus. Finally, s. 620.22, Stats., generally specifies permitted classes of investments as delineated in subs. (1) to (7), and any other investments that the commissioner authorizes by rule pursuant to s. 620.22 (8), Stats.

Related statutes or rules:

Sections 620.01, 620.03, 620.21, 620.22, and 620.23, Stats.

The plain language analysis and summary of the proposed rule:

The proposed changes to ss. Ins 2.02, 2.04 and 6.20, Wis. Adm. Code, relate to the repeal of restrictions related to the allocation of dividends to participating life insurance policies issued by a stock company, rating practices for exceeding filed rates for substandard risks, and revisions to the definition of investment terms, limitations on the investments of town mutual insurers, and the permissible scope of foreign investments. Section Ins. 2.02, Wis. Adm. Code, is proposed for repeal as the statute cited in the code provision references a statute that was repealed by Chapter 375, laws of 1975 and not replaced. Section Ins. 2.04, Wis. Adm. Code, permitted life insurance companies to exceed the maximum premium rate for coverage of a person that is classified as a substandard risk or is engaged in a hazardous occupation.

The proposed changes to s. Ins 6.20, Wis. Adm. Code, were requested by the insurance industry and are intended to modernize rules and requirements regarding the permissible investments that may be counted toward compulsory and security surplus. The proposed changes would include adding a general definition for derivative instruments and aligning Wisconsin's requirements with the National Association of Insurance Commissioners Derivative Instrument Model Regulation. Section Ins 6.20, Wis. Adm. Code, currently defines certain types of derivative instruments but does not include a general definition of derivatives. The office added a general definition that would capture all current derivative products and that also encompass derivative products developed in the future. A general definition would allow s. Ins 6.20, Wis. Adm. Code, to remain current with modern investment practices while eliminating the need to revise the code every few years keep pace with financial product innovations. In addition, better aligning office's requirements with the National Association of Insurance Commissioners' model act would promote uniform regulation across the states.

The proposed changes would also revise the amount or percentage of admitted assets which an insurer may invest in foreign assets for purposes of compulsory and security surplus. The current restrictions have not changed since 1996 and the proposed changes would allow a greater amount of investment in foreign investments. This change will better align the investment restrictions with current investment practices and modern investment risk considerations. In addition, the proposed rule adds a definition of foreign issuers.

The proposed changes to s. Ins 6.20 (6), Wis. Adm. Code, which apply to town mutual insurance companies, are intended to provide regulatory relief. This relief is in the form of a reduction in regulatory costs and improvements to the basis for investment regulation. Consolidation among commercial banks has reduced access to investment custody services, particularly for small insurers that are seen as not offering worthwhile scale as a customer. Annual minimum costs for such services range from \$6,000 to \$10,000. In addition, the size of a round lot in bonds, an important factor for the best price execution, is \$100,000, which is a scale

of individual trading too large for most town mutual insurance companies. Town mutual insurance companies will have the option to hold a diversified portfolio of mutual funds instead of individual bonds and stocks. Moreover, once a town mutual insurer has achieved a specified threshold of low risk assets, there would be no further limits on the town mutual insurer's equity holdings. In addition, the use of Morningstar ratings on mutual funds, which were intended to stand in for qualitative measures, are removed in favor of maximum expense ratios that have been set at reasonable levels while still allowing for active investment strategies.

Summary of and preliminary comparison with any existing or proposed federal regulation that is intended to address the activities to be regulated by the proposed rule:

There are no federal regulations which address these activities.

Summary of any public comments and feedback on the statement of scope of the proposed rule that the agency received at any preliminary public hearing and comment period held under s. 227.136, Stat., and a description of how and to what extent the agency took those comments and that feedback into account in drafting the proposed rule.

The office held a public hearing on April 17, 2019. Notice was published in the Wisconsin Administrative Register and on the office's website. Three members of the public appeared at the hearing in favor of the rule but did not testify. The office received one comment from counsel to the Wisconsin Council of Life Insurers in favor of promulgating the rule. The comment provided only general support for the promulgation of this rule without specific comments related to drafting.

In the course of conducting its normal business, the office received informal comments from the Wisconsin Association of Mutual Insurance Companies, Financial Fiduciaries LLC, and South Central Mutual Insurance Company. The representatives' comments included the following: town mutual insurers should not be precluded from using traditional bank investment custody accounts to hold mutual funds; expense ratio limits on mutual funds should be higher; bonds should be valued at face value rather than market value; and, custodial services should

be expanded to brokerage firms. There was positive response to the elimination of the Morningstar ratings as an investment criterion, the increase in the asset limit for a single exchange-traded fund, and the elimination of aggregate asset limits on mutual funds. The office modified the rule draft to permit town mutual insurance companies the option to use traditional investment custody accounts for mutual funds.

Comparison of similar rules in adjacent states as found by the commissioner:

Adjacent states have substantially similar derivative investment (DI) provisions however, regulation of town mutual (TM) insurer or the equivalent vary by state as these insurers only write business in one state. The citations for derivative investment and financial investment requirements for town mutuals may be found at the citations listed below.

Illinois: 215 ILCS 5/126.30 (DI), 215 ILCS 5/120 (TM)

Iowa: IA Code § 515.35 (DI), IA Code § 518.14 (TM)

Michigan: Mich. Comp. Laws §§ 500.901-500.947 (DI), N/A for TM

Minnesota: Minnesota Statute § 61A.29 (DI), MN Statutes 67A.231 (TM)

A summary of the factual data and analytical methodologies that the commissioner used in support of the proposed rule and how any related findings support the regulatory approach chosen for the proposed rule:

OCI based the definition of derivative instruments on the model definition developed by the National Association of Insurance Commissioners. The foreign investment limits were set after consultation with the insurance industry and a comprehensive review of the current foreign investment holdings of Wisconsin insurers and their capacity for further foreign investment.

Analysis and supporting documentation that the commissioner used in support of OCI's determination of the rule's effect on small businesses under s. 227.114:

This rule will have a beneficial effect on small businesses, specifically, approximately 54 town mutual insurance companies. For such small insurers, investing in mutual funds can offer lower investment overhead costs and better price execution than they can achieve on their own.

For large companies, the rule will not change the regulation of derivative instruments; it simply updates the definition of the investment types. The rule change also increases the

amount of foreign investments that may be counted towards the satisfaction of compulsory and security surplus requirements but only applies to insurers with \$500 million or more in admitted assets.

Effect on small business.

While town mutual insurance companies are not precluded from using traditional investment custody accounts, the smaller town mutual insurers could save between \$6,000 to \$10,000 per year by investing in a diversified pool of mutual funds instead of managing individual bond and stock positions. Prudent diversification of individual bond positions typically does not allow for buying \$100,000 round lots for bonds, thereby precluding town mutual insurers from getting optimal prices on their trade executions.

Agency contact person:

A copy of the full text of the proposed rule changes, analysis, and fiscal estimate may be obtained from the Web site at: <http://oci.wi.gov/ocirules.htm>

or by contacting:

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Email: karyn.culver@wisconsin.gov
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Place where comments are to be submitted and deadline for submission:

The deadline for submitting comments is 4:00 p.m. on the .

Mailing address:

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The proposed rule changes are:

SECTION 1. Ins 2.02 is repealed.

SECTION 2. Ins 2.04 is repealed.

SECTION 3. Ins 6.20 (3) (a) and (b) are repealed.

SECTION 4. Ins 6.20 (3) (am) is created to read:

Ins 6.20 (3) (am) “Derivative instrument” has the meaning contained in the accounting practices and procedures manual of the national association of insurance commissioners. Derivative instruments shall include derivatives embedded within an investment.

SECTION 5. Ins 6.20 (3) (d) is repealed.

SECTION 6. Ins 6.20 (3) (ee), (em) and (es) are created to read:

Ins 6.20 (3) (ee) “Foreign country” means any country other than the United States and Canada.

(em) “Foreign government” means any foreign governmental unit or instrumentality therein, not in the United States or Canada.

(es) “Foreign issuer” means any issuer that is not domiciled in the United States or Canada and is not a foreign government. An issuer shall not be deemed a foreign issuer if the issuer is domiciled and has operations in the United States or Canada and the primary guarantor is domiciled in the United States or Canada. An issuer shall be deemed a foreign issuer when the issuer is a shell business entity or special purpose vehicle, unless the investment is assumed, accepted, guaranteed, insured or otherwise backed by an entity domiciled in the United States or Canada that is not a shell business entity or special purpose vehicle.

SECTION 7. Ins 6.20 (3) (hg) and (hr) are created to read:

Ins 6.20 (3) (hg) “Nationally Recognized Statistical Rating Organization” or “NRSRO” means a credit rating agency registered with the U.S. securities and exchange commission, pursuant to the Credit Rating Agency Reform Act of 2006, as amended.

(hr) “No-load mutual fund” means a mutual fund whose shares are sold without any sales charges, or commissions, including sales compensation that is on an immediate or deferred basis or in some combination of immediate and deferred compensation. No-load mutual funds may impose fees for redemption, exchange, distribution, marketing, or other purposes unrelated to sales charges or commissions.

SECTION 8. Ins 6.20 (3) (j) is repealed.

SECTION 9. Ins 6.20 (4) is amended to read:

Ins 6.20 (4) GENERAL LIMITATIONS ON RESTRICTED INSURERS. No insurer restricted under s. 620.03, Stats., may invest ~~thereafter~~ in any of the following classes of assets except ~~by when the commissioner grants permission of the commissioner:~~

- (a) Any securities of an issuer who has defaulted on any payment on any debt security within the previous 5 years;
- (b) Any asset under s. 620.22 (9), Stats., ~~or~~
- (c) Any ~~financial futures contract or financial options contract~~ derivative instrument.

SECTION 10. Ins 6.20 (5) (intro.) and (a) are amended to read:

Ins 6.20 (5) (intro.) SPECIAL LIMITATIONS ON RESTRICTED INSURERS OTHER THAN TOWN MUTUALS. An insurer ~~which~~ that is restricted under s. 620.03, Stats., and ~~which~~ is not a town mutual, shall not invest in any of the following investments:

- (a) ~~Evidences~~ Bonds or evidences of indebtedness. ~~In~~ Insurers shall not invest in bonds or evidences of indebtedness under described in s. 620.22 (1), Stats., unless ~~such~~ the bonds or

evidences of indebtedness are lawfully authorized and provided that the bonds or evidences of indebtedness have at least one of the following characteristics:

SECTION 11. Ins 6.20 (5) (a) 1. is repealed and replaced to read:

Ins 6.20 (5) (a) 1. At the time of purchase have a 1 or 2 designation by the national association of insurance commissioners or equivalent ratings by an NRSRO.

SECTION 12. Ins 6.20 (5) (a) 2. to 5. are amended to read:

Ins 6.20 (5) (a) 2. ~~They are~~ The bonds or evidences of indebtedness are of a municipally owned public utility of this state created pursuant to section 3 of article XI of the constitution, and the net book value of the property pledged as security for the bonds has been established or approved by the public service commission and the total issue of the bonds does not exceed 50% of the net book value of such property; ~~or.~~

3. ~~They~~ Principal and interest are payable from revenues of a public utility or railroad owned by or held for the benefit of any governmental unit in the United States or Canada, if they are adequately secured by mortgage or lien on property or by specific pledge or revenues, and lawful authorizing resolutions or ordinance of the governing body of the unit require that during the life of the bond or evidence of indebtedness the rates, fees, tolls or charges together with any other revenues pledged shall at all times produce revenues sufficient to pay all expenses of operation and maintenance, interest as promised and the principal sum when due; ~~or.~~

4. ~~They are~~ The bonds or evidences of indebtedness are of public utilities in the United States or Canada and are either adequately secured by mortgage, pledge or other collateral, or have had net earnings available for fixed charges that for the previous 3 fiscal years have averaged per year not less than 1 1/2 times the average annual fixed charges; ~~or.~~

5. ~~They are~~ The bonds or evidences of indebtedness are of a United States or Canadian private corporation, and they are either adequately secured by mortgage, pledge or other collateral, or are issued by a corporation which has had net earnings available for fixed charges that have averaged for the previous 5 years and equaled for each of the previous 2 years an

annual amount which exceeded average annual fixed charges by at least 50%, or 25% in the case of corporations engaged primarily in wholesale or retail merchandising, installment, commercial and consumer financing, factoring or small loan business.

SECTION 13. Ins 6.20 (6) (b) (intro.) and 1. to 5. are amended to read:

Ins 6.20 (6) (b) (intro.) *Permitted investments.* Except as permitted by pars. (c), (d) and (e), a town mutual insurer may only invest in one or more of the following:

1. Treasury bonds, treasury notes, treasury bills or any other direct obligations of the United States government or agencies or instrumentalities of the United States government with a final maturity 15 years or less, except that no part of the amount determined under this paragraph shall be invested in zero coupon bonds or collateralized mortgage obligations;

2. Demand deposit, interest bearing accounts and certificates of deposit in financial institutions, including banks, savings and loan associations and credit unions, except that the amount of an insurer's investment with each such financial institution shall be limited to the total amount eligible for insurance under the financial institution's depositor insurance program;

3. Bonds of any United States or Canadian corporation that at the time of purchase have a "BBB" or better rating from Standard and Poor's Corporation or Moody's Investment Service or bonds rated "1" or 2 rating designation by the National Association of Insurance Commissioners Securities Valuation Office national association of insurance commissioners, or equivalent ratings by an NRSRO, except that no part of the amount determined under this paragraph shall be invested in zero coupon bonds, collateralized mortgage obligations, payment in kind bonds or bonds with a final maturity of more than 15 years;

4. Bonds of any United States municipality that at the time of purchase have a "BBB" or better rating from Standard and Pooers Corporation or Moody's Investment Service or bonds rated "1" or 2 designation by the National Association of Insurance Commissioners Securities Valuation Office national association of insurance commissioners, or equivalent ratings by an

NRSRO, with a final maturity of 15 years or less, except that no amount shall be invested in zero coupon bonds;

5. No more than an aggregate of ~~10~~5% of assets in cumulative dividend preferred stock of any United States or Canadian corporation that at the time of purchase has a “~~BBB~~” or better rating from ~~Standard and Poor’s Corporation or Moody’s Investment Service~~ or bonds rated “1” or 2 designation by the ~~National Association of Insurance Commissioners Securities Valuation Office~~; national association of insurance commissioners, or equivalent ratings by an NRSRO.

SECTION 14. Ins 6.20 (6) (b) 5g. and 5r. are created to read:

Ins 6.20 (6) (b) 5g. Shares in no-load mutual funds provided that all of the following requirements are met:

a. Each no-load mutual fund shall have an expense ratio, including any fees for marketing or distribution, of 0.75% or less.

b. Each no-load mutual fund shall have as a stated investment objective, as disclosed in its prospectus, an intent to invest 80% or more of its assets under management in bonds of any direct obligations of the United States government or agencies or instrumentalities of the United States government, any United States or Canadian corporation, or any United States municipality.

c. At the time of purchase, the shares of each no-load mutual fund shall have a 1 or 2 designation by the national association of insurance commissioners, or an equivalent rating by an NRSRO.

d. Each no-load mutual fund shall have an intent, as stated in its prospectus, to maintain a weighted average maturity of 8 years or less.

e. Investments in no-load mutual fund must be carried at the fair market value on the annual statement filed with the commissioner.

f. A town mutual insurer shall file a prospectus of each fund purchased in accordance with this paragraph with this office no later than February 15 of the year immediately following the year the purchase was made.

5r. Shares of exchange-traded funds provided that all of the following requirements are met:

a. Each exchange-traded fund shall have an expense ratio, including any fees for marketing or distribution, of 0.75%.

b. Each exchange-traded fund shall have as a stated investment objective, as disclosed in its prospectus, an intent to invest 80% or more of its assets under management in bonds of any direct obligations of the United States government or agencies or instrumentalities of the United States government, any United States or Canadian corporation or any United States municipality.

c. At the time of purchase, the shares of each exchange-traded fund shall have a 1 or 2 designation by the national association of insurance commissioners, or equivalent ratings by an NRSRO.

d. Each exchange-traded fund shall have an intent, as stated in its prospectus, to maintain a weighted average maturity of 8 years or less.

e. Investments in exchange-traded funds shall be carried at the fair market value on the annual statement filed with the commissioner.

f. A town mutual insurer shall file a prospectus of each fund purchased in accordance with this paragraph with this office no later no later than February 15 of the year immediately following the year the purchase was made.

SECTION 15. Ins 6.20 (6) (b) 6. is amended to read:

Ins 6.20 (6) (b) 6. ~~No more than an aggregate of 10% of assets in~~ Shares in money market mutual funds.

SECTION 16. Ins 6.20 (6) (c) (intro.) 1. and 2. are amended to read:

Ins 6.20 (6) (c) A town mutual insurer may invest in assets permitted under par. (d) only if, on December 31 of the preceding year, its assets invested in accordance with par. (b) ~~are~~ were in an amount at least equal to the sum of its liabilities plus the ~~greater~~ greatest of the following:

1. ~~50-100%~~ 100% of the net written premiums and assessments for the 12-month period ending December 31;

2. 33% of the ~~gross-direct~~ gross written premiums and assessments for the 12-month period ending December 31; ~~or~~

3. \$300,000.

SECTION 17. Ins 6.20 (6) (d) 3. (intro.) is repealed.

SECTION 18. Ins 6.20 (6) (d) 3. a. to c. are renumbered Ins (6) (d) 3c., 3g., and 3L. and as renumbered 3g. and 3L. are amended to read:

Ins 6.20 (6) (d) 3g. Common or preferred stock or convertible securities of any United States, Canadian or foreign corporation not included in par. (b) that are traded on a federally regulated securities exchange in the United States.

~~3L. Any mutual fund that invests~~ Shares in no-load mutual funds, which have an expense ratio, including any fees for marketing or distribution, of 0.75% or less and have as their stated investment objective, as disclosed in their prospectus, an intent to invest 80% or more of their assets under management in common or preferred stock or convertible securities of any United States, Canadian or foreign corporation not included in par. (b) ~~that has a minimum four-star rating from Morningstar Mutual Funds Inc.~~ A town mutual insurer shall not exceed 10% of assets in any single family of mutual funds.

SECTION 19. Ins 6.20 (6) (d) 3p., 3t., and 3x. are created to read:

Ins 6.20 (6) (d) 3p. Shares of exchange-traded funds, which have an expense ratio, including any fees for marketing or distribution, of 0.75% or less and have as their stated investment objective, as disclosed in their prospectus, an intent to invest 80% or more of their

assets under management in common or preferred stock or convertible securities of any United States, Canadian or foreign corporation not included in par. (b).

3t. Shares in no-load mutual funds with a weighted average maturity of more than 8 years that would otherwise be permitted under par. (b) 5g.

3x. Shares in exchange-traded funds with a weighted average maturity of more than 8 years that would otherwise be permitted under par. (b) 5r.

SECTION 20. Ins 6.20 (6) (d) 5. and 8. are repealed.

SECTION 21. Ins 6.20 (6) (d) 8m. is created to read:

Ins 6.20 (6) (d) 8m. The cash surrender values of life insurance policies and annuities of companies authorized to do business in this state.

SECTION 22. Ins 6.20 (6) (e) (intro.), 1. and 2. are consolidated, renumbered Ins 6.20 (6) (e) and amended to read:

Ins 6.20 (6) (e) *Town mutual insurer reinsurer stock; grandfathered provision.* A town mutual insurer is not required to divest of any stock described in par. (d) ~~3. a. 3c. which is held by the town mutual insurer on December 31, 1995. Any such~~ This type of stock:

~~1. is~~ is an authorized investment; and

~~2. is~~ is not an asset invested in accordance with par. (b) ~~for the purpose of determining under par. (c) whether an investment is authorized under par. (d); and~~

SECTION 23. Ins 6.20 (6) (e) 3. is repealed.

SECTION 24. Ins 6.20 (6) (f) (intro.), 1. and 2. are amended to read:

Ins 6.20 (6) (f) *Limitation on amount of investment.* A town mutual insurer may not invest ~~in any of the following, unless otherwise permitted:~~

1. Except as permitted under subd. 2., more than 3% of assets in securities of any single issuer unless it obtains the prior written permission of the commissioner or unless the investment is in securities of the government of the United States or its instrumentalities or in securities guaranteed by the full faith and credit of the United States; ~~or.~~

2. More than 10% of assets in the securities of one state, of one instrumentality of a state, or of one governmental unit of a state.

SECTION 25. Ins 6.20 (6) (f) 3. to 6. are created to read:

Ins 6.20 (6) (f) 3. More than 10% of assets in any single mutual fund.

4. More than 10% of assets in any single exchange-traded fund.

5. More than 20% of assets in investments sponsored or managed by any single issuer or its affiliates with respect to mutual funds and exchange-traded funds.

6. The cash surrender value of life insurance policies and annuities of companies authorized to do business in Wisconsin shall be included in par. (d) 9. to determine the aggregate allowable investment.

SECTION 26. Ins 6.20 (6) (g) is repealed and recreated to read:

Ins 6.20 (6) (g) *Transition and divestment.* Except as provided under par. (e), town mutual insurers shall comply with all of the following:

1. A town mutual insurer that holds investments permitted under par. (d) but no longer meets the minimum asset test of par. (c) may continue to hold such investments so long as the town mutual insurer holds investments in accordance with par. (b) in an amount that is no less than the sum of its liabilities plus the greater greatest of any of the following:

a. 75% of the net written premiums and assessments for the 12-month period ending December 31.

b. 33% of the direct written premiums and assessments for the 12-month period ending December 31.

c. \$300,000.

2. Town mutual insurers shall divest of any investment which does not meet the requirements of pars. (b) to (f) due to decline in the rating of a bond, the insurer's size, limitations on investments or any other reason, within three years of its noncompliance, unless otherwise permitted or required by the commissioner.

3. Town mutual insurers shall divest of any investment which does not meet the requirements of pars. (b) to (f) at the time of the purchase immediately unless otherwise permitted by the commissioner.

SECTION 27. Ins 6.20 (6) (h) 4. a. to c. and (i) are created to read:

Ins 6.20 (6) (h) 4. a. If a town mutual insurer utilizes the services of an investment advisor, the town mutual shall have, and maintain, a written agreement with the investment advisor, that shall be approved by the board of directors. A separate agreement shall be entered into for each specific arrangement.

b. Each written agreement with an investment advisor shall include, at a minimum, all of the following: a description of the scope and nature of the services to be provided; the standard of care to be provided; how or whether the investment strategy (including asset allocations, and any applicable limitations) incorporates the board approved investment policy; the level of authority the advisor exercises over the insurer's portfolio (discretionary or non-discretionary); a description of all types of compensation to the investment advisor; and a description as to how investment transactions, holdings, and portfolio performance will be communicated to the company's board of directors, including the frequency, content and means of reporting.

c. An agreement under subd. par. (h) 4. b. shall clearly state whether or not the investment advisor is acting as a fiduciary with respect to the town mutual insurer. A fiduciary is someone whose conduct is subject to the fiduciary duty standard, as defined under applicable rules, regulations, or standards of conduct promulgated by the U.S. securities and exchange commission.

(i) Custody. In addition to the requirements of s. 610.23, Stats., the shares of any mutual fund in which a town mutual insurer invests may be held in the direct custody of the town mutual insurer, and the shares must be maintained either in book entry form with the mutual fund's registrar and transfer agent, or in certificate form. If the town mutual insurer does not

have direct custody of the shares, the shares shall be held in the custody of a bank or bank and trust company.

SECTION 28. Ins 6.20 (8) (j), (k), (m), and (o) are repealed:

SECTION 29. Ins 6.20 (8g) and (8r) are created to read:

Ins 6.20 (8g) FOREIGN INVESTMENTS. An insurer, and in the case of insurers that are subject to special restrictions under s. 620.03, Stats., in accordance with any other rules applicable to them, may invest in foreign investments, in addition to investments authorized by s. 620.22 (1) to (7), Stats., that meet the following criteria and limitations:

(a) Insurers with assets less than \$500,000,000 as of the financial statement filing date may invest up to 1% of assets in direct obligations of foreign governments.

(b) Insurers with assets equal to at least \$500,000,000 as of the financial statement filing date may invest up to 4% of assets in direct obligations of foreign governments that at the time of purchase have a 1 or 2 designation from the national association of insurance commissioners, or equivalent ratings by an NRSRO and, in addition, up to 1% of assets in the direct obligations of foreign governments without regard to ratings.

(c) Insurers with assets less than \$500,000,000 as of the financial statement filing date may invest up to 2% of assets in loans, securities or investments of foreign issuers which are of substantially the same kinds, classes and investment grades as those eligible for investment under ch. 620, Stats., and supplementary rules.

(d) Insurers with assets equal to at least \$500,000,000 as of the financial statement filing date may invest up to 8% of assets in loans, securities or investments of foreign issuers which are substantially the same kinds, classes and investment grades as those eligible for investment under ch. 620, Stats., and supplementary rules.

(e) All investments in a foreign country, foreign government, and foreign issuers are subject to all of the following aggregate limits:

1. All investments in a single foreign country, 4% of assets.

2. All investments of a single foreign issuer and its foreign issuer affiliates, 3% of assets.

3. All investments denominated in a single foreign currency, 5% of assets excluding investments under par. (f).

(f) Insurers doing business in a foreign country may invest in assets in that foreign country, or in that country's currency, that are needed to meet the insurer's obligations, provided the investment would be permitted if made in this state.

(g) Insurers are responsible for monitoring their compliance with individual and aggregate limitations on all investments in a foreign country, foreign government, and foreign issuer, including such investments held indirectly through mutual funds, and must maintain a record of all such investments, which shall be reconciled at least quarterly and be available for production upon the request of the commissioner.

Ins 6.20 (8r) DERIVATIVE INSTRUMENTS. An insurer, and in the case of insurers that are subject to special restrictions under s. 620.03, Stats., to the extent other rules are applicable to them, may invest in derivative instruments in addition to investments authorized by s. 620.22 (1) to (7), Stats., provided all of the following requirements are met:

(a) Derivative instrument contracts shall be entered into to protect the investment portfolio of an insurer against the risk of changing asset values or interest rates, to enhance its liquidity, to aid in cash flow management, as a substitute for cash market transactions, and for any other purpose consistent with the investment objectives for the assets of insurers stated in s. 620.01, Stats.

(b) The aggregate market value of all derivative instruments outstanding may not exceed 10% of the insurer's assets.

(c) An insurer may purchase put options or sell call options only with regard to derivative instruments or financial instruments owned by the insurer, or which may be obtained through the exercise of warrants or conversion rights held by the insurer.

(d) An insurer may purchase call options or sell put options on derivative instruments or financial instruments only if the amount of the instrument, which may be acquired upon exercise of the option, when aggregated with current holdings, would be an authorized investment under s. 620.22 (1) to (7), Stats., or this subsection, and would not exceed the limitations specified in s. 620.23, Stats., or this section.

(e) The board of directors or its authorized committee shall first approve the insurer's plan relating to such investments, which plan must contain specific policy objectives and strategies, establish aggregate maximum limits in such investments and internal control procedures, and identify the duties, expertise and limits of authority of personnel authorized by the board of directors to engage in such transactions on behalf of the insurer.

(f) A copy of the insurer's plan shall be filed with the commissioner 30 days prior to its effective date. The commissioner may disapprove the plan within the 30-day period after receipt.

SECTION 30. INITIAL APPLICABILITY. This rule first applies to insurers authorized to do business in this state on the first day of January 2021, as provided in s. 227.22 (2) (intro.), Stats.

SECTION 31. EFFECTIVE DATE. These changes will take effect on the first day of the month following publication in the Wisconsin Administrative Register, as provided in s. 227.22 (2) (intro.), Stats.

Dated at Madison, Wisconsin, this 9th day of January 2020.

Nathan D. Houdek
Deputy Commissioner