

CR 81-227

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STATE OF WISCONSIN
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Vel Phillips
VEL PHILLIPS
SECRETARY OF STATE

STATE OF WISCONSIN)
OFFICE OF THE COMMISSIONER OF INSURANCE)

TO ALL TO WHOM THESE PRESENTS SHALL COME, GREETINGS:

I, Susan Mitchell, Commissioner of Insurance and custodian of the official records of said office, do hereby certify that the annexed order adopting a rule relating to compulsory surplus and security surplus was issued by this office June 11, 1982.

I further certify that said copy has been compared by me with the original on file in this office and that the same is a true copy thereof, and of the whole of such original.

IN TESTIMONY WHEREOF, I have hereunto subscribed my name in the City of Madison, State of Wisconsin, this 11th day of June, 1982.

Susan Mitchell

Susan Mitchell
Commissioner of Insurance

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SECRETARY OF STATE

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ORDER OF THE COMMISSIONER OF INSURANCE

ADOPTING A RULE

Relating to compulsory surplus and security surplus.

ANALYSIS PREPARED BY THE OFFICE OF THE COMMISSIONER OF INSURANCE

Section 623.11, Stats., authorizes the Commissioner to determine the amount of compulsory surplus that insurance companies are required to have in order not to be financially hazardous under s. 645.41 (4), Stats. Compulsory surplus is to be an amount that will provide reasonable security against contingencies affecting the insurer's financial position that are not fully covered by reserves or by reinsurance. Security surplus is to be set by the Commissioner between 110% and 140% of the compulsory surplus per s. 623.12, Stats. In setting the figure various factors including the size of the insurer may be considered.

In addition to providing a measure of financial reliability to use in potential liquidation situations, the concepts of compulsory

surplus and of security surplus are an essential part of the standards of ss. 620.21 and 620.22 relating to investment restrictions and permitted classes of investments. Assets may be counted toward satisfaction of the compulsory or security surplus requirements only so far as they are invested in compliance with Chapter 620. Section 620.22 lists classes of investments which may be counted for satisfaction of compulsory surplus and security surplus requirements.

Section 611.26, Stats., limits the amount of investment by an insurer in subsidiaries by prescribing that for the purpose of determining the compulsory surplus and security surplus of the insurer the total value of the outstanding shares of a subsidiary shall be the amount of the surplus of the subsidiary in excess of its security surplus.

A subcommittee of the Financial Advisory Council reviewed the concepts of compulsory surplus and security surplus and recommended a rule which the Commissioner may adopt under the authority of s. 623.11 (2) to establish minimum ratios for the compulsory surplus in relation to premiums written by an insurer. The recommendations of that subcommittee were used as a basis for the rule which was considered at the hearing. That subcommittee and the Financial Advisory Council have reviewed the suggested changes and recommended the substance of this proposal.

Subsection (1) explains that the purpose of the rule is to interpret the statutes mentioned above.

Subsection (2) provides that section Ins 14.04 shall apply to all lines of insurance except title and mortgage guarantee insurance and to all insurers authorized to do business except insurers licensed under Chapter 612, town mutuals; Chapter 613, service insurance corporations; Chapter 615, gift annuities; or Chapter 616, miscellaneous insurers, including school benefits plans and motor clubs. Life insurers domiciled in foreign countries are also excepted.

Subsection (3) establishes that the compulsory surplus of an insurer shall be the greater of: (a) the sum of 15% of premiums for individual life and disability insurance, 10% of premiums for group life and disability insurance, the greater of 2% of reserves or 7 1/2% of premiums for annuities, and 20% of premiums for all other covered lines of insurance; or (b) \$2 million.

Subsection (4) establishes the security surplus of an insurer to be the compulsory surplus plus 10% to 40%, depending on the amount of premiums of the insurer. Subsection (5) explains that compulsory surplus and security surplus are determined separately.

Subsection (6) describes how premiums are to be determined for the purposes of subsections (3) and (4).

Subsection (7) emphasizes that the Commissioner may adjust the factors in this section to calculate the compulsory or security surplus depending on special circumstances of an individual insurer.

Subsection (8) authorizes the combination of two or more insurers for application of the rule and subsection (9) provides that every insurer shall compute its compulsory surplus and security surplus as of December 31 and file it as a part of its annual statement filing.

The note to the rule explains that it is not intended to determine the optimum level of surplus an insurer should have but instead is to establish a basic minimum level which most insurers can easily comply with. The note also emphasizes that the Commissioner may require a higher or lower level of surplus based on special circumstances.

Pursuant to the authority vested in the Commissioner of Insurance by sections 601.41 (3) and 623.11 (2), Wis. Stats., the Commissioner hereby adopts section Ins 14.02 of the Wisconsin Administrative Code interpreting sections 623.11 and 623.12, Stats., as follows:

SECTION 1: Section Ins 14.02 of the Wisconsin Administrative Code is adopted to read:

Ins 14.02 COMPULSORY AND SECURITY SURPLUS. (1) PURPOSE. This section implements and interprets ss. 600.03 (45), 618.21 (1) (a), 623.11 and 623.12, Stats., for the purpose of establishing the amount of compulsory surplus an insurer is required to maintain to provide reasonable security against contingencies affecting its financial position that are not fully covered by reserves or by reinsurance, and the amount of security surplus that an insurer should maintain in order to provide an ample margin of safety and clearly assure a sound operation.

(2) SCOPE. This section shall apply to all lines of insurance except title insurance and mortgage guarantee insurance as defined in s. Ins 6.75 (2) (h) and (i), Wis. Adm. Code, and to each insurer subject to ss. 623.11 and 645.41, Stats., except insurers licensed under chs. 612, 613, 615 or 616, Stats., and life insurers domiciled in foreign countries.

(3) COMPULSORY SURPLUS. Except for the adjustments to the circumstances of individual insurers provided in s. 623.11 (1) (b), Stats., and sub. (6), the amount of compulsory surplus of an insurer shall be the greater of:

(a) The sum of: 1. 15% of premiums for individual life and disability insurance;

2. 10% of premiums for group life and disability insurance;

3. The greater of 2% of reserves or 7 1/2% of premiums for annuities and deposit administration funds;

4. 20% of premiums for all other covered lines of insurance; or

(b) \$2 million for an insurer first authorized to do business in Wisconsin on or after January 1, 1982, or the amount required by statute or administrative order before that date for other insurers.

(4) SECURITY SURPLUS. The security surplus of an insurer shall be the compulsory surplus plus:

(a) 40% of compulsory surplus for insurers restricted under s. 620.04, Stats.

(b) 40% of compulsory surplus for other insurers with premiums of \$10 million or less reduced by 1% of compulsory surplus for each \$33 million of additional premiums in excess of \$10 million, but not less than 10% of compulsory surplus.

(5) SEPARATE DETERMINATION. Compulsory surplus and security surplus are computed separately and are not added together for purposes of determining compliance with this rule.

(6) PREMIUMS. For purposes of subs. (3) and (4), premiums are gross premiums and other considerations received for insurance and

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annuities in the 12-month period ending on or not more than 60 days before the date as of which the calculation is made with the following deductions and exclusions:

(a) Exclude annual and initial reinsurance premiums for contracts of modified coinsurance and premium deposits.

(b) Deduct return premiums; premiums ceded to authorized reinsurers other than premiums of contracts of modified coinsurance; and retrospective premium refunds and dividends paid or credited to policyholders.

(7) INDIVIDUAL CIRCUMSTANCES. In the event of special circumstances of an individual insurer, the Commissioner may by order adjust the factors in this section to calculate the compulsory or security surplus as a higher or lower amount than the amount determined under sub. (3) or (4), or may establish additional factors in relation to any relevant variables in determining the amount of compulsory surplus required for such insurer.

(8) COMBINING INSURERS. The Commissioner may require the combination of two or more insurers for application of this section or may permit such combination upon request by such insurers.

(9) REPORTING. Every insurer to which this section applies shall compute its compulsory surplus and security surplus, as of the preceeding December 31, and include a copy of such computation as a part of its annual statement filed with the commissioner under s. 601.42, Stats., and s. Ins 7.01 (5) and (6), Wis. Adm. Code.

(10) EXISTING ORDERS. This section shall not affect orders of the Commissioner requiring a different level of surplus existing on August 1, 1982.

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(11) DATE OF FIRST REPORT. The first report required by sub (9) shall be computed as of December 31, 1982 and filed with the insurer's annual statement due March 1, 1983.

NOTE: Compulsory surplus is the amount of surplus that an insurer is required to have in order not to be financially hazardous under s. 645.41 (4), Stats. An insurer must comply with investment restrictions and permitted classes of investments in meeting required reserves and compulsory and security surplus. Security surplus is not required beyond its use as a standard in investment regulation.

The rule is not intended to determine the optimum level of surplus an insurer should have. That level should be decided by the officials of each insurer to reflect the individual circumstances and goals of the insurer. The rule is intended instead to establish a basic minimum level with which most insurers can easily comply.

The Commissioner may see fit to require a higher level of surplus, or permit a lower level, based on special circumstances.

For example, a specific order might establish a higher surplus requirement for a small insurer writing primarily surety business or a lower requirement for certain kinds of annuity business or for contracts providing benefits payable in variable dollar amounts within the meaning of s. 611.25, Stats., and s. Ins 2.13, Wis. Adm. Code. Other contingencies, factors and variables which may be considered are set forth in s. 623.11, Stats.

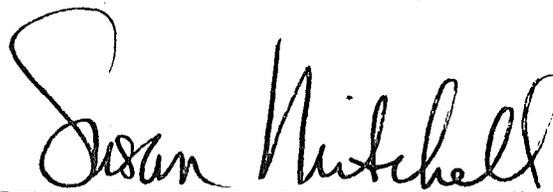
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Since the rule does not apply to some lines of insurance and certain types of insurers, other requirements may be necessary for those companies. This might entail separate rules or specific orders. However, the proposed rule will apply to a high percentage of the insurance business written in Wisconsin.

The treatment of reinsurance premiums in the rule may not be clear. In the case of all reinsurance other than modified coinsurance, it is intended that premiums on direct business be initially included by the originating company under sub (6) (intro.) and that reinsurance premiums ceded to a reinsurer be deducted under sub (6) (b). The reinsurance premiums ceded would be included as premiums of the reinsurer under sub (6) (intro.). In the case of modified coinsurance, the direct premiums are included by the originating company under sub (6) (intro.) and the reinsurance premiums are excluded for purposes of the rule by both the originating company and the reinsurer.

The adoption of section Ins 14.02, Wisconsin Administrative Code, contained in this order, shall take effect as provided in s. 227.026 (1) (intro.), Stats.

Dated at Madison, Wisconsin this 11th day of June, 1982.

A handwritten signature in cursive script that reads "Susan Mitchell". The signature is written in dark ink and is positioned above a horizontal line.

Susan Mitchell
Commissioner of Insurance

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