

CR 84-109

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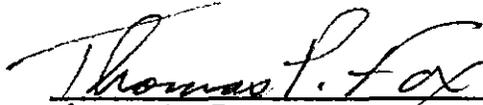
STATE OF WISCONSIN)
OFFICE OF THE COMMISSIONER OF INSURANCE)

TO ALL TO WHOM THESE PRESENTS SHALL COME, GREETINGS:

I, Thomas P. Fox, Commissioner of Insurance and custodian of the official records of said office, do hereby certify that the annexed order amending a rule and creating a rule was issued by this office on September 17, 1984.

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 17th day of September, 1984.


Thomas P. Fox
Commissioner of Insurance

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DOUGLAS LA FOLLETTE
SECRETARY OF STATE

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STATE OF WISCONSIN
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DOUGLAS LA FOLLET
SECRETARY OF STATE

ORDER OF THE COMMISSIONER OF INSURANCE

AMENDING A RULE AND CREATING A RULE

To amend Ins 6.74, and to create Ins 3.08, relating to surety obligations and to municipal bond insurance.

ANALYSIS BY THE COMMISSIONER OF INSURANCE

A Wisconsin-domiciled insurer has indicated its intention to expand substantially its issuance of policies of insurance against financial loss by reason of nonpayment of principal and interest obligations on municipal bonds. Because municipal bond insurance is a highly specialized line of business to which the normal standards of insurance regulation do not apply, the commissioner believes that a special administrative rule is necessary to regulate municipal bond insurance. It is worth noting that the state of New York has adopted a special regulation, New York Regulation 61, for the proper monitoring of municipal bond insurance.

This rule interprets minimum capitalization standards as provided in s. 611.19 (1), Stats., limitations on policies written under s. 627.05, Stats., financial reporting standards under 601.42, Stats., and the establishment of a contingency reserve to meet excessive losses under s. 623.04, Stats., among other items, all of which are areas of concern in the proper regulation of municipal bond insurance. This rule establishes needed regulations over these areas.

The commissioner also amends Wis. Adm. Code s. Ins 6.74 relating to suretyship and risk limitations of surety obligations so that it does not apply to insurers writing municipal bond insurance and no other type of surety insurance. This amendment was made so that a municipal bond insurer is not required to comply with two different sets of rules relating to the writing of surety insurance.

Pursuant to the authority vested in the commissioner of insurance by s. 601.41 (3), Stats., the commissioner hereby creates a rule and amends a rule interpreting ss. 601.42, 611.19 (1), 618.21, 623.03, 623.04, 627.05, 628.34 (2), 632.14, and 632.17, Stats., as follows:

SECTION 1. Ins 3.08 is created to read:

Ins 3.08 MUNICIPAL BOND INSURANCE. (1) PURPOSE. This section implements and interprets ss. 601.42, 611.19 (1), 618.21, 623.03, 623.04, 627.05, 628.34 (2), 632.14, and 632.17, Stats., for the purpose of establishing minimum requirements for the transaction of a type of surety insurance known as municipal bond insurance.

(2) SCOPE. This section shall apply to the underwriting, marketing, rating, accounting and reserving activities of insurers which write municipal bond insurance.

(3) DEFINITIONS. (a) "Annual statement" means the fire and casualty annual statement form specified in s. Ins 7.01 (5) (a).

(b) "Contingency reserve" means a reserve established for the protection of policyholders covered by policies insuring municipal bonds against the effect of excessive losses occurring during adverse economic cycles.

(c) "Cumulative net liability" means one-third of one percent of the insured unpaid principal and insured unpaid interest covered by in-force policies of municipal bond insurance.

(d) "Municipal bonds" means securities, including revenue obligations, the interest on which is exempt from Federal income taxes, including those which are issued by or on behalf of:

1. Any state, territory or possession of the United States of America;

2. Any political subdivision of any such state, territory or possession; or

3. Any agency, authority or corporate or other instrumentality of any one or more of the foregoing, or which are guaranteed by any of the foregoing.

(e) "Municipal bond insurance" means a type of surety insurance authorized by s. Ins 6.75 (2) (g) which is limited to the guaranteeing of the performance and obligations of municipal bonds.

(f) "Municipal bond insurer" means an insurer which issues municipal bond insurance.

(g) "Total net liability" means the average annual amount due, net of reinsurance, for principal and interest on the insured amount of any one issue of municipal bonds.

(h) "Person" means any individual, corporation for profit or not for profit, association, partnership or any other legal entity.

(i) "Policyholders' surplus" means an insurer's net worth, the difference between its assets and liabilities, as reported in its annual statement.

(4) MINIMUM CAPITAL OR PERMANENT SURPLUS. The minimum capital or permanent surplus of a municipal bond insurer shall be \$2 million for an insurer first authorized to do business in Wisconsin on or before January 1, 1984, or the amount required by statute or administrative order after that date for other municipal bond insurers.

(5) LIMITATIONS AND RESTRICTIONS. (a) Policies of municipal bond insurance shall be issued only to provide coverage on bonds of the type defined in sub. (3) (d).

(b) A municipal bond insurer may not have total net liability in respect to any one issue of municipal bonds in excess of an amount representing 10% of its policyholders' surplus.

(c) A municipal bond insurer may not have outstanding cumulative net liability, under in-force policies of municipal bond insurance, in an amount which exceeds the sum of:

1. Its capital and surplus, plus
2. The contingency reserve under sub. (9) plus
3. Fifty percent of the unearned premiums on the stated class of business.

(d) A municipal bond insurer may not have more than 25% of the principal amount which it has insured represented by the principal amount of municipal bonds issued primarily to finance property for use in a trade or business carried on by any person other than a governmental unit, and secured by a pledge of payments to be made by the person or of revenues to be derived from the trade or business.

(6) PREMIUM. The total consideration charged for municipal bond insurance policies, including policy and other fees or similar charges, shall be considered premium and shall be subject to the reserve requirements of subs. (8) and (9).

(7) FINANCIAL STATEMENTS AND REPORTING. (a) The financial condition and operations of a municipal bond insurer shall be reported on the annual statement.

(b) The total contingency reserve required by sub. (9) shall be reported as a liability in the annual statement. This liability may be reported as unpaid losses or other appropriately labeled write-in item. Appropriate entries shall be made in the underwriting and investment exhibit - statement of income of the annual statement. The change in contingency reserve for the year shall be reported in the annual statement as a reduction of or a deduction from underwriting income. If the contingency reserve is recorded as a loss liability, the change in the reserve shall be excluded from loss development similar to fidelity and surety losses incurred but not reported.

(c) A municipal bond insurer shall compute and maintain adequate case basis loss reserves to be reported in the underwriting and investment exhibit, unpaid losses and loss adjustment expenses, of the annual statement. The method used to determine the loss reserve shall accurately reflect loss frequency and loss severity and shall include components for claims reported and unpaid, and for claims incurred but not reported, provided:

1. No deduction may be made for anticipated salvage in computing case basis loss reserves.

2. If the amount of insured principal and interest on a defaulted issue of municipal bonds which is due and payable over the period of the next three years exceeds 10% of a municipal bond insurer's capital, surplus and contingency reserve, its case basis reserve so established shall be supported by a report from a qualified independent source.

(8) UNEARNED PREMIUM RESERVE. A municipal bond insurer shall compute and maintain an unearned premium reserve on an annual or on a monthly pro rata basis on all unexpired coverage, except that in the case of premiums paid more than one year in advance, the premium shall be earned proportionally with the expiration of exposure except as provided under sub. (12).

(9) CONTINGENCY RESERVE. (a) A municipal bond insurer shall establish a contingency reserve which shall consist of allocations of sums representing 50% of the earned premium on policies of municipal bond insurance except as provided under sub. (12).

(b) The contingency reserve established by this subsection shall be maintained for 240 months. That portion of the contingency reserve established and maintained for more than 240 months shall be released and may no longer constitute part of the contingency reserve except as provided under sub. (12).

(c) Subject to the approval of the commissioner, withdrawals may be made from the contingency reserve in any year in which the actual paid losses on municipal bond insurance policies exceed 35% of the earned premiums on municipal bond insurance policies except as provided under sub. (12).

(d) A municipal bond insurer may invest the contingency reserve in tax and loss bonds purchased pursuant to 26 U. S. C. s. 832(e). The contingency reserve shall otherwise be invested only in classes of securities or types of investments specified in s. 620.22 (1), Stats., except as provided under sub. (12)

(10) CONFLICTS OF INTEREST PROHIBITED. No municipal bond insurer may pay any commission or make any gift of money, property or other valuable thing to any employee, agent, or representative of any issuer of municipal bonds or to any employee, agent or representative of any underwriter of any issue of the bonds as an inducement to the purchase of, or at any time there is in force, a policy insuring bonds, and no employee, agent or representative of the insurer or underwriter shall receive any payment or gift. However, violation of the provisions of this subsection does not render void the municipal bond insurance policy.

(11) TRANSITION. Unearned premium reserves and contingency loss reserves shall be computed and maintained on risks insured after the effective date of this section as required by subs. (8) and (9).

(12) LAWS OR REGULATIONS OF OTHER JURISDICTIONS. Whenever the laws or regulations of another jurisdiction in which a municipal bond insurer is licensed, require a larger unearned premium reserve or a larger contingency reserve in the aggregate than that set forth in this section, the establishment and maintenance of the larger aggregated, unearned premium reserve and contingency reserve complies with this rule.

SECTION 2. Ins 6.74 (2) is amended to read:

(2) SCOPE. This section shall apply to the limitations on bond penal amounts imposed on insurers engaged in the business of suretyship. This section shall not apply to insurers issuing only that type of surety insurance known as municipal bond insurance.

This rule shall become effective on the first day of the month following its publication in the Wisconsin Administrative Register as provided in s. 227.026 (1) (Intro.), Stats.

Dated at Madison, Wisconsin, this 17th day of September, 1984.


Thomas P. Fox
Commissioner of Insurance

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The State of Wisconsin
Office of the Commissioner of Insurance

Thomas P. Fox
Commissioner
(608) 266-3585

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DATE: September 17, 1984
TO: Gary Poulson
FROM: M. E. Van Cleave
Assistant Deputy Commissioner of Insurance
SUBJECT: Ins 6.74 and Ins 3.08 - Clearinghouse No. 84-109

A handwritten signature in dark ink, appearing to be "M. E. Van Cleave", is written over the "FROM" line of the memorandum.

Enclosed are two copies of an Order of the Commissioner of Insurance amending Ins 6.74 and creating Ins 3.08, Clearinghouse No. 84-109, relating to surety obligations and to municipal bond insurance.

MEV:LH:mle
Enclosure
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