

SENATE BILL REPORT

HB 3011

As Reported By Senate Committee On:
Financial Institutions & Insurance, February 27, 2008

Title: An act relating to safeguarding securities owned by insurers.

Brief Description: Safeguarding securities owned by insurers.

Sponsors: Representatives Loomis, Rodne and Kelley.

Brief History: Passed House: 2/04/08, 93-0.

Committee Activity: Financial Institutions & Insurance: 2/20/08, 2/27/08 [DP].

SENATE COMMITTEE ON FINANCIAL INSTITUTIONS & INSURANCE

Majority Report: Do pass.

Signed by Senators Berkey, Chair; Hobbs, Vice Chair; Benton, Ranking Minority Member; Franklin, Parlette, Prentice and Schoesler.

Staff: Diane Smith (786-7410)

Background: Insurers must meet requirements for the investments they make if those investments are to count as assets for purposes of determining the insurers' financial condition. The Office of Insurance Commissioner (OIC) monitors and regulates the insurers' financial condition. Investments and securities are included in the definition of assets.

In 2000 requirements for safeguarding securities were added to the insurance code. Under these provisions, there are only three methods by which an insurer may hold securities. One of these methods is by designation of a financial institution as its custodian. This custodian then transacts and maintains book-entry securities on behalf of the insurer.

Another method for holding securities is through participation in depository systems of clearing corporations either directly or through a custodian bank. A qualified custodian does not include a securities broker.

Clearing corporations are depository corporations that maintain book-entry accounting systems that accomplish the transfer of securities from one owner to the next.

On the federal level, all United States Treasury bills, notes, and bonds are issued only in book-entry form, meaning that physical stock certificates are not issued. Investors have three options for holding U.S. Treasury securities as follows: Legacy Treasury Direct; TreasuryDirect; and the Treasury/Reserve Automated Debt Entry System, TRADES, also known as the commercial book-entry system.

This analysis was prepared by non-partisan legislative staff for the use of legislative members in their deliberations. This analysis is not a part of the legislation nor does it constitute a statement of legislative intent.

In the Legacy Treasury Direct and TreasuryDirect options, investors hold their Treasury securities directly with the U.S. Treasury.

In the TRADES option, the investor's ownership of securities is reflected only on the records of the broker-dealer in securities where the investor maintains his or her securities account. The broker-dealer maintains its account at a depository institution or a Federal Reserve Bank. The third method for holding securities is to hold the stock certificates themselves.

The National Association of Insurance Commissioners (NAIC) adopted a model for safeguarding securities in 1980. The model was amended in 1981 and 2004.

Summary of Bill: Broker/dealers in securities and banks organized under the laws of a country, other than the United States, may act as custodians for purposes of accepting custody of securities owned by insurers.

To qualify as a custodian, the broker/dealer must be registered with the Securities and Exchange Commission, maintain membership in the securities investor protection corporation and have a tangible net worth of at least \$250 million.

Corporations organized under the laws of any foreign country to effect transactions in securities by computerized book-entry, TRADES, and TreasuryDirect book-entry securities systems may also meet the definition of a clearing corporation.

An insurer may provide for the custody of its securities with a custodian. The custodian, its agent, or a clearing corporation may hold those securities.

The written agreement providing the terms of the relationship between the insurer and the custodian must meet certain specified requirements. One of these requirements is for the securities owned by the insurer to be separately identified on the custodians's official records. Another requirement is for custodial accounts to be insured.

The OIC has rule-making authority to implement the act, including the establishment of standards for custodians.

Appropriation: None.

Fiscal Note: Not requested.

Committee/Commission/Task Force Created: No.

Effective Date: Ninety days after adjournment of session in which bill is passed.

Staff Summary of Public Testimony: PRO: This bill allows companies to have enough assets to cover liabilities. It updates existing state law to the current model so that insurers can manage their portfolios as do other investors, using modern technology. It makes it clearer in real-time where the securities are.

Persons Testifying: PRO: Representative Liz Loomis, prime sponsor; Bill Stauffacher, Securities Industry and Financial Association.