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By: **Senator Astle**  
Introduced and read first time: February 12, 2003  
Assigned to: Rules

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A BILL ENTITLED

1 AN ACT concerning

2 **Insurers - Assets and Investments - Location**

3 FOR the purpose of altering the exceptions to the types of assets that certain domestic  
4 insurers are required to keep in the State; repealing a certain limitation on the  
5 amount of admitted assets that a domestic insurer may keep outside of the  
6 State; altering the conditions under which the reserve investments of a life  
7 insurer may include derivative transactions; and generally relating to the assets  
8 and investments of insurers.

9 BY repealing and reenacting, with amendments,  
10 Article - Insurance  
11 Section 4-115(c), (d), and (e) and 5-511(o)  
12 Annotated Code of Maryland  
13 (1997 Volume and 2002 Supplement)

14 BY repealing and reenacting, without amendments,  
15 Article - Insurance  
16 Section 5-511(n)  
17 Annotated Code of Maryland  
18 (1997 Volume and 2002 Supplement)

19 SECTION 1. BE IT ENACTED BY THE GENERAL ASSEMBLY OF  
20 MARYLAND, That the Laws of Maryland read as follows:

21 **Article - Insurance**

22 4-115.

23 (c) (1) A domestic insurer, including a reciprocal insurer, fraternal benefit  
24 society, or nonprofit health service plan, with its home or executive office in the State  
25 shall keep in the State:

26 (i) its general ledger accounting records; and

27 (ii) [subject to subsection (d) of this section,] all of its assets except:

1                                   1.       real property lawfully owned by the insurer and located  
2 outside of the State, personal property appurtenant to the real property, or mortgages  
3 on the real property;

4                                   2.       property of the insurer that is customary and necessary to  
5 the operation of the insurer's branch offices outside of the State;

6                                   3.       securities deposited in a jurisdiction outside of the State as  
7 a condition of authority to transact business in that jurisdiction or securities  
8 deposited in connection with obtaining surety bonds; [and

9                                   4.       securities held for safekeeping by a bank or other  
10 institution that:

11                                  A.       is approved by the Commissioner;

12                                  B.       is located in the United States or Canada, or in any  
13 jurisdiction in which the insurer is licensed to do business; and

14                                  C.       has a custodial agreement with the insurer approved by  
15 the Commissioner]

16                                  4.       SECURITIES HELD EITHER BY THE INSURER OR IN  
17 COMPLIANCE WITH REGULATIONS ADOPTED BY THE COMMISSIONER; AND

18                                  5.       TRANSACTIONS OR SECURITIES INVOLVED IN  
19 TRANSACTIONS AUTHORIZED BY § 5-511(N) AND (O) OF THIS ARTICLE OR ANY OTHER  
20 TRANSACTIONS OR SECURITIES INVOLVED IN TRANSACTIONS EXEMPTED BY THE  
21 COMMISSIONER FROM THIS PARAGRAPH.

22                   (2)       A financial guaranty reinsurance company or financial guaranty  
23 insurance company that became domiciled in the State on or before December 31,  
24 1993, and that does not have its home or executive office in the State:

25                                  (i)       shall keep in the State its entire assets as required by  
26 paragraph (1)(ii) of this subsection; and

27                                  (ii)       may keep its general ledger accounting records outside the  
28 State if it makes those records available in the State to the Commissioner within 2  
29 business days after being requested to do so by the Commissioner.

30       (d)       [Unless approved by the Commissioner, a domestic insurer may not keep  
31 more than 15% of the domestic insurer's admitted assets outside of the State under  
32 this section.

33       (e)]       This section does not prohibit the holding of funds or transmission of  
34 securities outside of the State to:

35                                  (1)       secure or record title to the securities; or

1 (2) sell, lend, buy, redeem, or exchange the securities or alter the  
2 provisions of the securities.

3 5-511.

4 (n) (1) The reserve investments of a life insurer may include securities  
5 lending, repurchase, reverse repurchase, and dollar roll transactions with business  
6 entities, subject to the requirements of paragraphs (2) through (9) of this subsection.

7 (2) The insurer's board of directors shall adopt a written plan that  
8 specifies guidelines and objectives to be followed, such as:

9 (i) a description of how cash received will be invested or used for  
10 general corporate purposes of the insurer;

11 (ii) operational procedures to manage interest rate risk,  
12 counterparty default risk, the conditions under which proceeds from reverse  
13 repurchase transactions may be used in the ordinary course of business, and the use  
14 of acceptable collateral in a manner that reflects the liquidity needs of the  
15 transaction; and

16 (iii) the extent to which the insurer may engage in these  
17 transactions.

18 (3) (i) The insurer shall enter into a written agreement for all  
19 transactions authorized under this subsection other than dollar roll transactions.

20 (ii) The written agreement shall require that each transaction  
21 terminate no more than 1 year from its inception or on the earlier demand of the  
22 insurer.

23 (iii) The agreement shall be with the business entity counterparty,  
24 but for securities lending transactions, the agreement may be with an agent acting on  
25 behalf of the insurer, if the agent is a qualified business entity, and if the agreement:

26 1. requires the agent to enter into separate agreements with  
27 each counterparty that are consistent with the requirements of this section; and

28 2. prohibits securities lending transactions under the  
29 agreement with the agent or its affiliates.

30 (4) (i) Cash received in a transaction under this subsection shall be  
31 invested in accordance with this subtitle and in a manner that recognizes the  
32 liquidity needs of the transaction or used by the insurer for its general corporate  
33 purposes.

34 (ii) For so long as the transaction remains outstanding, the insurer,  
35 its agent, or custodian shall maintain, as to acceptable collateral received in a  
36 transaction under this subsection, either physically or through the book entry

1 systems of the Federal Reserve, Depository Trust Company, Participants Trust  
2 Company, or other securities depositories approved by the Commissioner:

- 3 1. possession of the acceptable collateral;
- 4 2. a perfected security interest in the acceptable collateral; or
- 5 3. in the case of a jurisdiction outside the United States, title  
6 to, or rights of a secured creditor to, the acceptable collateral.

7 (5) (i) The limitations of § 5-507 of this subtitle do not apply to the  
8 business entity counterparty exposure created by transactions under this subsection.

9 (ii) For purposes of calculations made to determine compliance with  
10 this subsection, no effect will be given to the insurer's future obligation to resell  
11 securities, in the case of a repurchase transaction, or to repurchase securities, in the  
12 case of a reverse repurchase transaction.

13 (iii) An insurer may not enter into a transaction under this  
14 subsection if, as a result of and after giving effect to the transaction:

15 1. A. the aggregate amount of securities then loaned, sold  
16 to, or purchased from any one business entity counterparty under this subsection  
17 would exceed 5% of its admitted assets; and

18 B. in calculating the amount sold to or purchased from a  
19 business entity counterparty under repurchase or reverse repurchase transactions,  
20 effect may be given to netting provisions under a master written agreement; or

21 2. the aggregate amount of all securities then loaned, sold to,  
22 or purchased from all business entities under this subsection would exceed 40% of its  
23 admitted assets.

24 (6) (i) In a securities lending transaction, the insurer shall receive  
25 acceptable collateral having a market value as of the transaction date at least equal  
26 to 102% of the market value of the securities loaned by the insurer in the transaction  
27 as of that date.

28 (ii) If at any time the market value of the acceptable collateral is  
29 less than the market value of the loaned securities, the business entity counterparty  
30 shall be obligated to deliver additional acceptable collateral, the market value of  
31 which, together with the market value of all acceptable collateral then held in  
32 connection with the transaction, at least equals 102% of the market value of the  
33 loaned securities.

34 (7) (i) In a reverse repurchase transaction, other than a dollar roll  
35 transaction, the insurer shall receive acceptable collateral having a market value as  
36 of the transaction date at least equal to 95% of the market value of the securities  
37 transferred by the insurer in the transaction as of that date.

1 (ii) If at any time the market value of the acceptable collateral is  
2 less than 95% of the market value of the securities so transferred, the business entity  
3 counterparty shall be obligated to deliver additional acceptable collateral, the market  
4 value of which, together with the market value of all acceptable collateral then held in  
5 connection with the transaction, at least equals 95% of the market value of the  
6 transferred securities.

7 (8) In a dollar roll transaction, the insurer shall receive cash in an  
8 amount at least equal to the market value of the securities transferred by the insurer  
9 in the transaction as of the transaction date.

10 (9) (i) In a repurchase transaction, the insurer shall receive as  
11 acceptable collateral transferred securities having a market value at least equal to  
12 102% of the purchase price paid by the insurer for the securities.

13 (ii) If at any time the market value of the acceptable collateral is  
14 less than 100% of the purchase price paid by the insurer, the business entity  
15 counterparty shall be obligated to provide additional acceptable collateral, the market  
16 value of which, together with the market value of all acceptable collateral then held in  
17 connection with the transaction, at least equals 102% of the purchase price.

18 (iii) Securities acquired by an insurer in a repurchase transaction  
19 may not be sold in a reverse repurchase transaction, loaned in a securities lending  
20 transaction, or otherwise pledged.

21 (o) (1) The reserve investments of a life insurer may include derivative  
22 transactions under this subsection, whether entered into directly or indirectly  
23 through an investment subsidiary, under the conditions of paragraphs (2) through (7)  
24 of this subsection.

25 (2) (i) An insurer may use derivative instruments under this  
26 subsection to engage in hedging transactions.

27 (ii) Prior to entering into any derivative transaction, the board of  
28 directors of the insurer shall approve a derivative use plan that:

29 1. describes investment objectives and risk constraints, such  
30 as counterparty exposure amounts AND COLLATERAL ARRANGEMENTS SUPPORTING  
31 DERIVATIVE TRANSACTIONS;

32 2. defines permissible transactions identifying the risks to be  
33 hedged, the assets or liabilities being replicated; and

34 3. requires compliance with internal control procedures that  
35 demonstrate the intended hedging characteristics and the ongoing effectiveness of the  
36 derivative transaction or combination of the transactions through cash flow testing or  
37 other appropriate analyses.

38 (iii) Whenever the derivative transactions entered into under this  
39 subsection are not in compliance with this subsection or, if continued, may now or

1 subsequently, create a hazardous financial condition to the insurer that affects its  
2 policyholders, creditors, or the general public, the Commissioner may, after notice and  
3 an opportunity for a hearing, order the insurer to take any action as may be  
4 reasonably necessary to:

- 5                                   1.       rectify a hazardous financial condition; or
- 6                                   2.       prevent an impending hazardous financial condition from  
7 occurring.

8                   (3)       An insurer may enter into hedging transactions under this subsection  
9 if, as a result of and after giving effect to the transaction:

10                   (i)       the aggregate statement value of options, caps, floors, and  
11 warrants not attached to another financial instrument purchased and used in  
12 hedging transactions does not exceed 7.5% of its admitted assets;

13                   (ii)       the aggregate statement value of options, caps, and floors  
14 written in hedging transactions does not exceed 3% of its admitted assets; and

15                   (iii)       the aggregate potential exposure of collars, swaps, forwards,  
16 and futures used in hedging transactions does not exceed 6.5% of its admitted assets.

17                   (4)       An insurer shall include all counterparty exposure amounts in  
18 determining compliance with the limitations of § 5-507 of this subtitle.

19                   (5)       Each derivative instrument shall be:

20                   (i)       traded on a securities exchange;

21                   (ii)       entered into with, or guaranteed by, a business entity;

22                   (iii)       issued or written by or entered into with the issuer of the  
23 underlying interest on which the derivative instrument is based; or

24                   (iv)       in the case of futures, traded through a broker that is registered  
25 as a futures commission merchant under the Commodity Exchange Act or that has  
26 received exemptive relief from registration under Rule 30.10 adopted under the  
27 Commodity Exchange Act.

28       SECTION 2. AND BE IT FURTHER ENACTED, That this Act shall take effect  
29 October 1, 2003.