



State of Wisconsin / OFFICE OF THE COMMISSIONER OF INSURANCE

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TO: Legislative Reference Bureau
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Madison, WI 53701-2037

FROM: Richard Wicka, Chief Legal Counsel
Office of the Commissioner of Insurance

DATE: March 25, 2020

SUBJECT: Sections Ins 2.02, 2.04, 6.20, 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.

Clearinghouse Rule No. 20-002

This rule is in final draft form and has been submitted to the chief clerk of each house of the legislature. Please publish a statement to this effect in the Wisconsin Administrative Register, pursuant to Wis. Stat. § 227.19 (2). We have e-mailed you an electronic copy of the text of the rule.

For additional information or if you do not receive the e-mail, please contact Karyn Culver at karyn.culver@wisconsin.gov.

**PROPOSED ORDER TO REPEAL; RENUMBER AND AMEND; CONSOLIDATE,
RENUMBER, AND AMEND; AMEND; REPEAL AND RECREATE; AND CREATE 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), (6) (d) 3. (intro.), 5. and 8., (6) (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) (title), (intro.), (a) (title), (intro.), and 2. to 5., (6) (b) (intro.), and 1. to 6., (6) (c) (title), (intro.), 1. and 2., (6) (d) 9., (6) (f) (intro.), and 1.; **to repeal and recreate** Ins 6.20 (5) (a) 1., (6) (g); **to create** Ins 6.20 (3) (am), (ee), (em), (es), (hg), (hr), (6) (a) (title), (6) (b) 5g. and 5r., (6) (d) (title), 3p., 3t., and 3x., (6) (f) 3. to 5., (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 a town mutual insurer 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. The proposed rule was approved by the Governor on March 12, 2020 to submit to the legislature and was submitted to the legislature on March 25, 2020.

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 a town mutual insurer, 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, that 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 mutual insurers 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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Mail: PO Box 7873, Madison, WI 53707-7873

Place where comments are to be submitted and deadline for submission:

The deadline for submitting comments is 4:00 p.m. on the February 17, 2020.

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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) is 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) (b) and (d) are repealed.

SECTION 6. Ins 6.20 (3) (ee), (em), (es), (hg) and (hr) 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 governmental unit or instrumentality that is 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 domiciled in the United States or Canada 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.

(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 7. Ins 6.20 (3) (j) is repealed.

SECTION 8. Ins 6.20 (4), (5) (title), (intro.), and (a) (title), and (intro.) are 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 unless prior permission of is granted by~~ 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.

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

(a) Evidences Bonds or evidences of indebtedness. ~~In~~ An insurer 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 have at least one of the following characteristics:

SECTION 9. Ins 6.20 (5) (a) 1. is repealed and recreated 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 an equivalent rating by a NRSRO.

SECTION 10. 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 11. Ins 6.20 (6) (a) (title) is created to read:

Ins 6.20 (6) (a) (title) *Status as a restricted insurer.*

SECTION 12. Ins 6.20 (6) (b) (intro.), and 1. to 5. are amended to read:

Ins 6.20 (6) (b) 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 an equivalent rating by a 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 an equivalent rating by a

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 ~~40%~~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”~~ 1 or 2 designation by the ~~National Association of Insurance Commissioners Securities Valuation Office;~~ national association of insurance commissioners, or an equivalent rating by a NRSRO.

SECTION 13. 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 1.20% 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, that, at the time of purchase, have a 1 or 2 designation by the national association of insurance commissioners, or an equivalent rating by a NRSRO.

c. 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.

d. Each no-load mutual fund investment must be carried at the fair market value on the annual statement filed with the commissioner.

e. Each town mutual insurer shall file a prospectus of each fund purchased in accordance with this paragraph with the commissioner 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 1.20% or less.

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, that, at the time of purchase, have a 1 or 2 designation by the national association of insurance commissioners, or equivalent ratings by a NRSRO.

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

d. Each exchange-traded fund investment shall be carried at the fair market value on the annual statement filed with the commissioner.

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

SECTION 14. Ins 6.20 (6) (b) 6., (6) (c) (title), (intro.), 1. and 2. are 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.~~

(6) (c) Minimum expected assets. 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~~ written premiums and assessments for the 12-month period ending December 31; ~~or~~

SECTION 15. Ins 6.20 (6) (d) (title) is created.

Ins 6.20 (6) (d) (title) *Permitted investments for assets in excess of minimum expected assets.*

SECTION 16. Ins 6.20 (6) (d) 3. (intro.) is repealed.

SECTION 17. Ins 6.20 (6) (d) 3. a. to c. are renumbered Ins 6.20 (6) (d) 3c., 3g., and 3L. and Ins 6.20 (6) (d) 3g. and 3L. as renumbered, 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 1.20% 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 18. 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 1.20% 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 19. Ins 6.20 (6) (d) 5. and 8. are repealed.

SECTION 20. Ins 6.20 (6) (d) 9. is amended to read:

Ins 6.20 (6) (d) 9. Investments not otherwise permitted by this paragraph, and not specifically prohibited by statute or rule, to the extent of not more than 5% of the insurer's assets. This includes the cash surrender value of life insurance policies and annuities of insurers authorized to do business in Wisconsin.

SECTION 21. Ins 6.20 (6) (e) (title), (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 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~~ is an authorized investment; and

~~2. Is 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 22. Ins 6.20 (6) (e) 3. is repealed.

SECTION 23. Ins 6.20 (6) (f) (intro.), and 1. is amended to read:

Ins 6.20 (6) (f) *Limitations on amount of investment.* A town mutual insurer may not invest: in any of the following:

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,~~

SECTION 24. Ins 6.20 (6) (f) 3. to 5. 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.

SECTION 25. 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), a town mutual insurer 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 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. A town mutual insurer 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.

3. If at the time of purchase a town mutual insurer investment did not meet the requirements of pars. (b) to (f), then the town mutual insurer shall immediately divest of the investment.

SECTION 26. 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 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, whether 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 subpar. b. shall clearly state whether the investment advisor is, or is not, 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 27. Ins 6.20 (8) (j), (k), (m), and (o) are repealed:

SECTION 28. 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) An insurer 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) An insurer 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 a NRSRO and, in addition, up to 1% of assets in the direct obligations of foreign governments without regard to ratings.

(c) An insurer 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) An insurer 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) An insurer 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) An insurer 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.

(8r) DERIVATIVE INSTRUMENTS. An insurer, and in the case of an insurer that is 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 an insurer 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 29. 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 25th day of March 2020.



Mark V. Afable
Commissioner

EXISTING ADMINISTRATIVE RULES Fiscal Estimate & Economic Impact Analysis

1. Type of Estimate and Analysis

Repeal Modification

2. Administrative Rule Chapter, Title and Number

145 Ch Ins 2 Life Insurance, s. Ins 2.02 and 2.04; Ch. Ins 6 General, s. Ins 6.20

3. Date Rule promulgated and/or revised; Date of most recent Evaluation

Sections Ins 2.02 and 2.04 were last revised in 1979, s. Ins 6.20 was last revised in 1997

4. Plain Language Analysis of the Rule, its Impact on the Policy Problem that Justified its Creation and Changes in Technology, Economic Conditions or Other Factors Since Promulgation that alter the need for or effectiveness of the Rule.

The objective for ss. Ins 2.20 and 2.04 are to repeal out-dated regulations.

The objectives for s. Ins 6.20 are to modernize the rules and requirements regarding the permissible investments that may be counted toward compulsory and security surplus and will more closely align the regulation with the requirements of the National Association of Insurance Commissioners (NAIC) Derivative Instrument Model Regulation, as well as the regulations of other states, and modernize investment practices and investment regulations while eliminating the need to revise the rule frequently as financial products experience innovations. The proposed rule uses broader terms to permit more timeless and consistent regulation both in Wisconsin and across states for insurers that operate in multiple 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 while balancing risk especially for smaller insurers.

The proposed rule addresses issues currently faced by town mutuals that are experiencing reduced access to investment custody services at high annual fees in relation to the investment. 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.

5. Describe the Rule's Enforcement Provisions and Mechanisms

The rule interprets ss. 620.01, 620.03, and 620.21 to 620.23, Stats., and are enforced by s. 601.41 (4) and 601.64, Stats.

6. Repealing or Modifying the Rule Will Impact the Following
(Check All That Apply)

State's Economy

Local Government Units

Specific Businesses/Sectors

Public Utility Rate Payers

Small Businesses

7. Summary of the Impacts, including Compliance Costs, identifying any Unnecessary Burdens the Rule places on the ability of Small Business to conduct their Affairs.

This rule will have a beneficial effect on small businesses, specifically, approximately 54 town mutual insurance companies by saving potentially \$6,000.00 to \$10,000.00 in custody fees per year by being permitted to invest in a diversified pool of mutual funds. 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.

8. List of Small Businesses, Organizations and Members of the Public that commented on the Rule and its Enforcement and a Summary of their Comments.

EXISTING ADMINISTRATIVE RULES Fiscal Estimate & Economic Impact Analysis

The request for comment on the proposed rule was sent to 50 organizations and individuals. Additionally the OCI posted the Request for Comment on its public website. The OCI received eight comments on the rule primarily from Town Mutual insurers and their investment advisors and from the Wisconsin Council of Life Insurers. The comments contained some similar requests to increase limitations on Type 1 preferred stock, permit non-bank custodians to hold investments and either eliminate the internal expense ratio as a criterion for funds or increase the expense ratio as the proposed limit of 50-basis points is too restrictive. The OCI has revised the rule to increase the the expense ratio limit to 120-basis points.

9. Did the Agency consider any of the following Rule Modifications to reduce the Impact of the Rule on Small Businesses in lieu of repeal?

- Less Stringent Compliance or Reporting Requirements
- Less Stringent Schedules or Deadlines for Compliance or Reporting
- Consolidation or Simplification of Reporting Requirements
- Establishment of performance standards in lieu of Design or Operational Standards
- Exemption of Small Businesses from some or all requirements
- Other, describe: The rules change minimum necessary to retain financial regulatory oversight, financial solvency and consistency with regulation across states.

10. Fund Sources Affected

- GPR FED PRO PRS SEG SEG-S

11. Chapter 20, Stats. Appropriations Affected

None

12. Fiscal Effect of Repealing or Modifying the Rule

- | | | |
|---|---|--|
| <input type="checkbox"/> No Fiscal Effect | <input type="checkbox"/> Increase Existing Revenues | <input type="checkbox"/> Increase Costs |
| <input checked="" type="checkbox"/> Indeterminate | <input type="checkbox"/> Decrease Existing Revenues | <input type="checkbox"/> Could Absorb Within Agency's Budget |
| | | <input type="checkbox"/> Decrease Cost |

13. Summary of Costs and Benefits of Repealing or Modifying the Rule

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. OCI based the definition of derivative instruments on the model definition developed by the NAIC. 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. Larger insurers will find the guidelines consistent with NAIC and other states without increased costs for implementation.

14. Did the Agency prepare a Cost Benefit Analysis (if Yes, attach to form)

- Yes No

15. Long Range Implications of Repealing or Modifying the Rule

In the long term, the proposed rule will allow greater flexibility with financial derivative instruments and other financial investment options optimizing financial returns while limiting financial risk to ensure Wisconsin insurers remain solvent.

16. Compare With Approaches Being Used by Federal Government

There is no comparable federal regulation.

17. Compare With Approaches Being Used by Neighboring States (Illinois, Iowa, Michigan and Minnesota)

As the proposed changes are built from an NAIC model, all neighboring states have similar provisions for derivative instruments. Each state uniquely regulates town mutuals in accordance with state statutory authority. Wisconsin is substantially more permissive in its current investment laws and rules than Illinois, Iowa or Minnesota. Michigan does not have an equivilent class of insurers.

18. Contact Name

Julie E. Walsh

19. Contact Phone Number

608-264-8101



Tony Evers

Office of the Governor | State of Wisconsin

March 12, 2020

By Electronic Mail Only

Dear Secretaries and Agency Heads:

On this day, I approved the following proposed administrative rules pursuant to Wis. Stat. § 227.185:

- A proposed rule by the Department of Revenue, submitted on February 17, 2020, relating to requests for predeterminations regarding license eligibility due to conviction records (Wis. Admin. Code ch. Tax 1); and
- A proposed emergency rule by the Department of Natural Resources, submitted on February 26, 2020, relating to Minocqua Chain walleye harvest regulations (Wis. Admin. Code ch. NR 20); and
- A proposed rule by the Department of Natural Resources, submitted October 24, 2019, relating to Closed areas and refuges (Wis. Admin. Code chs. NR 11 and 15); and
- A proposed rule by the Department of Health Services, submitted March 3, 2020, relating to Youth Crisis Stabilization Facilities (Wis. Admin. Code ch. DHS 50); and
- A proposed rule by the Office of the Commissioner of Insurance, submitted March 5, 2020, 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 substantial risks, and revisions to the definition of investment terms, limitations on the investments of a town mutual insurer and the permissible scope of foreign investments and affecting small business (Wis. Admin. Code chs. INS 2 and 6).

Please direct any questions about this letter to my policy director, Jenni Dye.

Sincerely,

Tony Evers
Governor

Cc: Ryan Nilsestuen, chief legal counsel (ryan.nilsestuen1@wisconsin.gov)
Jenni Dye, policy director (jenni.dye@wisconsin.gov)
DOA State Budget Office (SBOAdminRules@spmail.enterprise.wistate.us)
Jennifer Chadwick, DOR (Jennifer.Chadwick@wisconsin.gov)
Cortney Mesdjian, DHS (Cortney.Mesdjian@dhs.wisconsin.gov)
Emma Esch, DNR (emma.esch@wisconsin.gov)
Nathan Houdek, OCI (nathan.houdek@wisconsin.gov)



WISCONSIN LEGISLATIVE COUNCIL
RULES CLEARINGHOUSE

Scott Grosz
Clearinghouse Director

Anne Sappenfield
Legislative Council Director

Margit S. Kelley
Clearinghouse Assistant Director

CLEARINGHOUSE REPORT TO AGENCY

[THIS REPORT HAS BEEN PREPARED PURSUANT TO S. 227.15, STATS. THIS IS A REPORT ON A RULE AS ORIGINALLY PROPOSED BY THE AGENCY; THE REPORT MAY NOT REFLECT THE FINAL CONTENT OF THE RULE IN FINAL DRAFT FORM AS IT WILL BE SUBMITTED TO THE LEGISLATURE. THIS REPORT CONSTITUTES A REVIEW OF, BUT NOT APPROVAL OR DISAPPROVAL OF, THE SUBSTANTIVE CONTENT AND TECHNICAL ACCURACY OF THE RULE.]

CLEARINGHOUSE RULE 20-002

AN ORDER to repeal Ins 2.02, 2.04, 6.20 (3) (a), (b), (d), and (j), (6) (d) 3. (intro.), 5. and 8., (e) 3., and (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., and (6) (c) (intro.) and 1. and 2., and (f) (intro.) and 1. and 2.; to repeal and recreate Ins 6.20 (5) (a) 1., and (6) (g); and to create Ins 6.20 (3) (ee), (em), (es), (hg), (hr), (jm), (6) (am), (b) 5g. and 5r., (d) 3p., 3t., and 3x., and 8m., (f) 3. to 6., and (h) 4. a. to c., and (i), (8g) and (8r), 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.

Submitted by **OFFICE OF THE COMMISSIONER OF INSURANCE**

01-09-2020 RECEIVED BY LEGISLATIVE COUNCIL.

02-06-2020 REPORT SENT TO AGENCY.

MSK:DM

LEGISLATIVE COUNCIL RULES CLEARINGHOUSE REPORT

This rule has been reviewed by the Rules Clearinghouse. Based on that review, comments are reported as noted below:

1. STATUTORY AUTHORITY [s. 227.15 (2) (a)]
Comment Attached YES NO

2. FORM, STYLE AND PLACEMENT IN ADMINISTRATIVE CODE [s. 227.15 (2) (c)]
Comment Attached YES NO

3. CONFLICT WITH OR DUPLICATION OF EXISTING RULES [s. 227.15 (2) (d)]
Comment Attached YES NO

4. ADEQUACY OF REFERENCES TO RELATED STATUTES, RULES AND FORMS [s. 227.15 (2) (e)]
Comment Attached YES NO

5. CLARITY, GRAMMAR, PUNCTUATION AND USE OF PLAIN LANGUAGE [s. 227.15 (2) (f)]
Comment Attached YES NO

6. POTENTIAL CONFLICTS WITH, AND COMPARABILITY TO, RELATED FEDERAL REGULATIONS [s. 227.15 (2) (g)]
Comment Attached YES NO

7. COMPLIANCE WITH PERMIT ACTION DEADLINE REQUIREMENTS [s. 227.15 (2) (h)]
Comment Attached YES NO



WISCONSIN LEGISLATIVE COUNCIL RULES CLEARINGHOUSE

Scott Grusz
Clearinghouse Director

Anne Sappenfield
Legislative Council Director

Margit Kelley
Clearinghouse Assistant Director

CLEARINGHOUSE RULE 20-002

Comments

[NOTE: All citations to "Manual" in the comments below are to the Administrative Rules Procedures Manual, prepared by the Legislative Reference Bureau and the Legislative Council Staff, dated December 2014.]

2. Form, Style and Placement in Administrative Code

- a. The agency should review and revise the rule caption's listing of affected provisions to ensure that it accurately enumerates each provision treated by the proposed rule and the nature of treatment.
- b. A date should be inserted for the deadline to submit comments on the proposed rule.
- c. The treatment of s. Ins 6.20 (3) (b) in SECTION 3 of the proposed rule should be moved to appear sequentially following the treatment of s. Ins 6.20 (3) (am) in SECTION 4 of the proposed rule. The treatment of s. Ins 6.20 (3) (b) could be included with the treatment of s. Ins 6.20 (3) (d) in SECTION 5 of the proposed rule.
- d. In the treatment clause for SECTION 10 of the proposed rule, the designation "(intro.)" should be inserted after the identification of par. (a). Also, in the text of par. (a) (intro.), the colon at the end of the provision should be shown without underscoring.
- e. In the treatment clause for SECTION 11 of the proposed rule, the word "replaced" should be revised to "recreated".
- f. In the current text of the rule, s. Ins 6.20 (6) has inconsistent use of paragraph titles. For example, pars. (a), (c), and (d) do not have titles, while pars. (b) and (e) to (h) do have titles. The agency should consider using the opportunity of this proposed rule to revise the paragraphs under sub. (6), for consistent use of paragraph titles. Some of the paragraphs are already amended under the proposed rule.

g. In s. Ins 6.20 (6) (b) 3., 4., and 5., the agency has stricken quotation marks on either side of the number "1". To improve the readability of the proposed rule changes, the agency could consider striking through each instance of the number "1" within the stricken quotation marks and then inserting a "1" in the underscored language that follows the strike-throughs.

h. In SECTION 16 of the proposed rule, the current text of s. Ins 6.20 (6) (c) 3. should be removed as the provision is not amended. If an amendment or other treatment is intended, the provision should be identified in the treatment clause for the SECTION and the text should be shown with a strike-through and underscoring for any revisions.

i. In s. Ins 6.20 (6) (f) (title), the current title has not been transcribed into the rule accurately; "Limitation" should be "Limitations". The agency should ensure the current text of the rule has been accurately transcribed into the proposed rule.

j. In s. Ins 6.20 (6) (f) (intro.), the colon that is shown with a strike-through should be removed, and the final colon should be shown without underscoring.

k. The treatment clause for SECTION 24 of the proposed rule identifies s. Ins 6.20 (6) (f) 2. as being amended, and the current text of the provision is shown, but there do not appear to be any amendments to the text. The text should either be shown with any intended amendment appearing with a strike-through and underscoring, or the text of the provision should be removed and the treatment clause should be updated to remove this cite.

l. In s. Ins 6.20 (6) (h) 4. b., the use of the internal colon and list without subunit designations is improper. As division into further subunits is also improper, consider revising the provision to remove the phrase ", at a minimum, all of the following:". Also, the parenthetical phrases should be removed and, instead, should be set apart with commas.

m. In s. Ins 6.20 (6) (h) 4. c., the format for the reference to "subd. par. (h) 4. b." should be revised to "subpar. b.".

n. It appears that the initial applicability clause in SECTION 30 of the proposed rule is unnecessary and should be removed, as it does not describe a point in a process at which the rule would first become applicable (such as occurs in licensing procedures). If the date that is listed is intended to be the effective date of the proposed rule, the effective date clause in SECTION 31 of the proposed rule should be revised to state that "This rule takes effect on January 1, 2021.".

4. Adequacy of References to Related Statutes, Rules and Forms

a. In s. Ins 6.20 (6) (f) (intro.), the addition of the words "unless otherwise permitted" is unnecessary and confusing. The phrase should either be removed or a citation should be inserted to identify the standards under which the investment may otherwise be permitted. Compare, for example, the citation provided in par. (b) (intro.).

b. In s. Ins 6.20 (6) (g) 2., the agency requires divestment "unless otherwise permitted or required by the commissioner". The next subunit, subd. 3., likewise requires divestment "unless otherwise permitted by the commissioner". These provisions appear to grant the agency authority to allow a town mutual insurer to deviate from rules promulgated as part of this rulemaking. Are there provisions in the current or proposed rule that provide guidance with respect to the circumstances under which the commissioner may exempt a town mutual insurer from these

requirements? A citation should be inserted to identify the governing provisions or applicable circumstances under which a deviation would be allowed. If there are no governing standards, the agency should explain its reasoning in allowing individualized determinations in circumstances that appear to have general applicability and would accordingly otherwise require rulemaking.

5. Clarity, Grammar, Punctuation and Use of Plain Language

a. Throughout the proposed rule, to be consistent with the style used in other parts of the rule and current drafting conventions, the agency should ensure that the singular form of a word is used when referring to whom a requirement applies. For example, in s. Ins 6.20 (5) (a) (intro.), the word “insurers” should be revised to “an insurer”, and in s. Ins 6.20 (6) (g) (intro.) and 2. and 3., each instance of the phrase “town mutual insurers” should be revised to “a town mutual insurer”. [s. 1.01 (9) (e), Manual.]

b. In s. Ins 6.20 (3) (em), the agency should consider rewriting the definition of “foreign government”. The term “foreign” is used within the definition to define itself, and the use of the word “therein” within the definition is confusing.

c. In s. Ins 6.20 (6) (b) (intro.), a comma could be inserted between “(d)” and “and”.

d. In s. Ins 6.20 (6) (b) 5g. (intro.) and 5r. (intro.), consider inserting a comma after both instances of the word “funds”.

e. In s. Ins 6.20 (6) (b) 5g. e., the sentence appears to be incomplete. It should form a complete sentence when read with the introductory statement in subd. 5g. (intro.), and have a parallel grammatical structure to the other subdivision paragraphs.

f. In s. Ins 6.20 (6) (b) 5g. f., the agency should revise the phrase “this office” to “the commissioner”.

g. In s. Ins 6.20 (6) (e) (intro.), the rule is modified to allow a town mutual insurer to hold certain stock, regardless of when it was acquired. Currently, this stock may only be held if it was held on December 31, 1995. Because this modification appears to eliminate the grandfathered status of these stocks, the agency should consider removing the phrase “grandfathered provision” from the title of this paragraph.

h. Also in s. Ins 6.20 (6) (e) (intro.), is the insertion of the phrase “of any” necessary?

i. In s. Ins 6.20 (6) (f) 6., the sentence structure is not grammatically consistent with the introductory language in par. (f) (intro.). As written, it is difficult to understand the intent of this provision.

j. In s. Ins 6.20 (6) (g) 3., the provision requires a town mutual insurer to divest of any investment that does not meet the identified requirements “at the time of purchase immediately”. This provision is confusing because it suggests an insurer may purchase an investment that it is required to immediately divest itself of. Consider rephrasing this provision to more plainly state the applicable circumstance and the required action, such as in an “If..., then...” format.

k. In s. Ins 6.20 (6) (h) 4. c., the words “or not” following “whether” are unnecessary and should be removed.



State of Wisconsin / OFFICE OF THE COMMISSIONER OF INSURANCE

Tony Evers, Governor
Mark V. Afable, Commissioner

Wisconsin.gov

March 3, 2020

Legal Unit
125 South Webster Street • P.O. Box 7873
Madison, Wisconsin 53707-7873
Phone: (608) 267-9586 • Fax: (608) 264-6228
oci.wi.gov

Report on Sections Ins 2.02, 2.04 and 6.20, 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.

Clearinghouse Rule No. 20-002
Submitted Under s. 227.19 (3), Stats.

(The proposed rule-making order is attached.)

(a) A detailed statement of basis for the proposed rule and how the rule advances relevant statutory goals or purposes:

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 a town mutual insurer, 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 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, that 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.

(b) Summary of the public comments and the agency's responses to those comments:

Comment: Clarify the definition of "foreign issuer" to be more consistent with the NAIC model Act.

Response: The office intended the definition to be stronger than the NAIC model Act and did not make the change suggested.

Comment: Broaden the types of investments that can be considered toward compulsory and security surplus by increasing the types of investments in partnerships, limited liability companies, trust certificates from any trust or any other equity interest in a private equity.

Response: The office believes this is not something that we have authority to modify by rule but that it will require a statutory change.

(c) An explanation of any modifications made in proposed rule as a result of public comments or testimony received at a public hearing:

The office revised the proposed rule to incorporate the suggestions made when seeking input on the economic impact analysis. The office modified the rule draft to permit town mutual insurance companies the option to use traditional investment custody accounts for mutual funds and increased the ratio from 0.50% to 1.20% or less to include any fees for marketing or distribution.

(d) Persons who appeared or registered regarding the proposed rule:

Appearances for:

Connie O'Connell, Wisconsin Council of Life Insurers

Appearances against:

None

Appearances for information:

Registrations for:

Tony Langenohl, State Farm Insurance
Andy Franken, Wisconsin Insurance Alliance
Jess Alanis, American Family Insurance

Registrations against:

None

Registrations neither for nor against:

Wes Webendoffer, Professional Insurance Agents of Wisconsin

Letters received:

Connie O'Connell, Wisconsin Council of Life Insurers

Monica Groves, American Family Insurance

22 spam-type incoherent responses unrelated to the subject matter.

(e) An explanation of any changes made to the plain language analysis of the rule under s. 227.14 (2), Stats., or to any fiscal estimate prepared under s. 227.14 (4), Stats.

The plain language was reviewed to ensure consistency with the modification made to the rule in light of the Legislative Council recommendation and public comment received.

(f) The response to the Legislative Council staff recommendations indicating acceptance of the recommendations and a specific reason for rejecting any recommendation:

All comments were complied with and corrected.

(g) The response to the report prepared by the small business regulatory review board:

The small business regulatory review board did not prepare a report.

(h) Final Regulatory Flexibility Analysis

A Final Regulatory Flexibility Analysis is Not Required because the rule will not have a significant economic impact on a substantial number of small businesses.

(i) Fiscal Effect

See fiscal estimate attached to proposed rule.

Attachment: Legislative Council Staff Recommendations