

INSURANCE
DEPARTMENT OF BANKING AND INSURANCE
OFFICE OF SOLVENCY REGULATION

Insurance of Municipal Bonds, Asset-Backed Securities and Consumer Debt Obligations

Adopted New Rules: N.J.A.C. 11:7-1.1 and 1.5

Adopted Amendments: N.J.A.C. 11:7-1.1, 1.2, 1.3 and 1.4

Proposed: May 21, 2007 at 39 N.J.R. 1985(a)

Adopted: January 23, 2008 by Steven M. Goldman, Commissioner, Department of Banking and Insurance

Filed: January 24, 2008 as R. 2008 d. 37, with a substantive change not requiring additional public notice or comment (see N.J.A.C. 1:30-6.3).

Authority: N.J.S.A. 17:1-8.1, 17:1-15e, 17:17-1 and 17:18-9

Effective Date: February 19, 2008

Expiration Date: February 20, 2008

Summary of Public Comments and Agency Responses:

The Department of Banking and Insurance (Department) timely received written comments from the following:

1. Allen Reiser (on behalf of CMDC Guaranty Company Inc.);
2. The Surety and Fidelity Association of America; and
3. The Association of Financial Guaranty Insurers

COMMENT: All of the commenters generally supported the proposed amendments and new rules, but raised specific issues as set forth below.

RESPONSE: The Department appreciates the support of its proposal.

COMMENT: One commenter noted that the definition of “investment grade” in N.J.A.C. 11:7-1.2 refers to a rating agency designated as a nationally recognized securities rating organization by the Securities and Exchange Commission (SEC). The commenter stated that most of the countries where it will do business have rating agencies that are affiliated with one of the “big three U.S. rating agencies,” but these local affiliates are usually separate locally-incorporated entities and thus not the same legal entity that will have been approved by the SEC. The commenter stated that there are other countries, such as Malaysia, where local law requires that all rating agencies be locally-owned. The commenter requested that paragraph 1 of the definition of “investment grade,” after the reference to the SEC, be revised to add as a parenthetical “(or, in the case of obligations or parity obligations issued outside the United States, by a securities rating agency acceptable to the Commissioner)”.

RESPONSE: The Department initially notes that the language suggested by the commenter does not provide sufficient standards for determining the acceptability of rating agencies as required under the Administrative Procedure Act, N.J.S.A. 52:14B-1 et seq. However, the Department recognizes that one of the purposes of the proposed amendments is to provide standards with respect to insuring securities issued outside of the United States. Consistent with and to further this purpose, the Department believes that it is appropriate to revise paragraph 1 of the definition of “investment grade” to provide the following: “..., or in the case of obligations or parity obligations issued outside of the United States, by an affiliate of such a designated securities rating agency.”

COMMENT: One commenter stated that the reference in the proposal Summary indicating that the coverages in N.J.S.A. 17:17-1g are commonly known as “financial guaranty insurance” is incorrect. The commenter stated that N.J.S.A. 17:17-1 does not have a separate definition of financial guaranty insurance, as does New York law. Accordingly, financial guaranty insurance would be a specialized subset of surety insurance. The commenter recommended that the Summary be corrected by deleting this sentence.

RESPONSE: The Department initially notes that proposal Summaries may not be altered once published. The Department does not believe that the colloquial reference set forth in the proposal Summary should cause any confusion. However, the Department notes that the commenter’s clarification will appear as part of this notice of adoption. Accordingly, as part of the rulemaking history and file for these rules, the proposal and adoption notices will provide the additional clarification sought by the commenter.

COMMENT: One commenter, while supporting the proposed new rules and amendments, suggested that the rules be expanded to modernize single risk limits for municipal bond insurance and other types of financial guaranty insurance. The commenter noted that the current standards governing single risk limits for municipal bond insurance in N.J.A.C. 11:7-1.3 (recodified as 1.4) were originally adopted in 1975 and last amended in 1987. The commenter stated that the regulatory structure for municipal bond insurance and financial guaranty insurance in general has been updated considerably in the interim in New York and other states, as well as at the National Association of Insurance Commissioners. The commenter requested that the Department adopt all of the single risk limits applicable to municipal bond coverage. The

commenter stated that these changes would be consistent with Article 69 of the New York Insurance Law. The commenter provided as an attachment to its comments specific proposed amendments. These would include:

1. N.J.A.C. 11:7-1.1 - changes to expand the purpose and scope of the subchapter to include requirements for insurers issuing contracts ensuring utility first mortgage obligations, obligations issued by a single entity and secured by commercial real estate, and other policies providing insurance for obligations issued by a single entity and backed by a single revenue source.

2. N.J.A.C. 11:7-1.2 - proposed definitions of “commercial real estate,” “governmental unit,” “municipal bonds,” “municipal obligation bond,” “special revenue bond,” and “utility first mortgage obligation” consistent with Section 6901 of the New York Insurance Law. In addition, the commenter suggested that the definition of “contingency reserve” should be amended to apply to utility first mortgage obligations, obligations issued by a single entity and secured by commercial real estate, and other policies providing insurance for obligations issued by a single entity and backed by a single revenue source. The commenter also suggested that the existing definition of “municipal bonds” be replaced with the related definition set forth above.

3. N.J.A.C. 11:7-1.3 - the commenter suggested this section be expanded to apply to insurers issuing contracts insuring utility first mortgage obligations and obligations issued by a single entity and secured by commercial real estate, and other policies providing insurance for obligations issued by a single entity and backed by a single revenue source.

4. N.J.A.C. 11:7-1.4 - modify the standards for determining the limitation of an insurer’s exposure to loss on any one risk or hazard for purposes of complying with the limits on

exposure to any one risk set forth in N.J.S.A. 17:18-9 for policies insuring municipal bonds. The commenter stated that these standards would be consistent with Section 6904(d)(1) of the New York Insurance Law, and would be consistent with the approach of nationally recognized statistical rating organizations such as Standard & Poor's, Moody's, and Fitch.

5. N.J.A.C. 11:7-1.5 - the commenter suggested changes for determining the limitation of an insurer's exposure to loss on any one risk or hazard for purposes of complying with the limits on exposure to any one risk set forth in N.J.S.A. 17:18-9 similar to that set forth in paragraph 5 above.

6. N.J.A.C. 11:7-1.6 - the commenter suggested this section be expanded to apply to insurers issuing contracts insuring utility first mortgage obligations, obligations issued by a single entity and secured by commercial real estate, and other policies providing insurance for obligations issued by a single entity and backed by a single revenue source.

RESPONSE: These comments are outside the scope of the proposal. However, the Department will review the suggested changes to determine whether additional amendments should be made to address the insurance of municipal bonds as suggested by the commenter. The Department will consider these suggested changes for possible future amendment.

Federal Standards Statement

A Federal standards analysis is not required because the adopted new rules and amendments are not subject to any Federal requirements or standards.

Full text of the adoption follows (addition to proposal indicated in boldface with asterisks

thus):

11:7-1.2 Definitions

The following words and terms, when used in this subchapter, shall have the following meanings unless the context clearly indicates otherwise.

...

“Investment grade” means that:

1. The obligation or parity obligation of the same issuer has been determined to be in one of the top four generic lettered rating classifications by a securities rating agency designated as a Nationally Recognized Securities Rating Organization by the Securities and Exchange Commission*, **or in the case of obligations or parity obligations issued outside of the United States, by an affiliate of such a designated securities rating agency***;

2. - 3. (No change from proposal.)

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