

INSURANCE
DEPARTMENT OF BANKING AND INSURANCE
OFFICE OF SOLVENCY REGULATION

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

Proposed Readoption: N.J.A.C. 11:7

Authorized By: Steven M. Goldman, Commissioner, Department of Banking and Insurance

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

Calendar Reference: See Summary below for explanation of exception to calendar requirement.

Proposal Number: PRN 2008-93

Submit written comments by June 6, 2008 to:

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The agency proposal follows:

Summary

The Department of Banking and Insurance (Department) proposes to readopt N.J.A.C. 11:7, which is scheduled to expire on February 20, 2008, in accordance with N.J.S.A. 52:14B-5.1b. In accordance with N.J.S.A. 52:14B-5.1c, the submission of this notice of proposal to the Office of Administrative Law extends the expiration date 180 days, to August 18, 2008.

The Department has reviewed these rules pertaining to insurance of municipal bonds, asset-backed securities and consumer debt obligations and has determined them to be reasonable, necessary and proper for the purpose for which they were originally promulgated, as required by

Executive Order No. 66 (1978). These rules are being proposed for readoption without amendment.

In accordance with Title 17 of the New Jersey Statutes, the Department is charged with regulating financial guaranty insurance that is issued by an insurer pursuant to the authority of N.J.S.A. 17:17-1g. In order to provide for the regulation of such insurance, N.J.A.C. 11:7-1 was originally adopted and became effective July 23, 1975.

The rules in this chapter originally applied solely to the insurance of municipal bonds. The Department recently adopted new rules and amendments to N.J.A.C. 11:7-1 to provide specific standards for the issuing of insurance contracts covering asset-backed securities and related credit enhancement products by financial guaranty insurers. See 39 N.J.R. 1985(a) and 40 N.J.R. 881(a). As noted in the notice of adoption of those new rules and amendments, one commenter suggested substantial revisions to the existing rules governing the insurance of municipal bonds to reflect the requirements of Article 69 of the New York insurance laws with respect to these products. The Department has no objection to those changes in principle and is in the process of evaluating all of the suggestions for possible future amendments. Given the complexity of the suggested changes and the timeframes involved in the re-adoption process, the Department believes that it is appropriate to address the above-referenced suggested changes through a separate proposal. Moreover, the Department is in the process of reevaluating the rules applicable to the insurance of asset-backed securities in light of recent problems in the market for such insurance. Any changes that are determined to be necessary upon the conclusion of that analysis will be reflected in amendments to be proposed at a future date. In the interim, to ensure that the existing rules do not expire, the chapter is being proposed for re-adoption without change at this time.

The rules set forth in this chapter provide that insurers shall be properly authorized and licensed in order to engage in the business of writing insurance on municipal bonds, asset-backed securities and consumer debt obligations. The rules also provide measures aimed at protecting the public by establishing minimum capital and surplus, as well as contingency reserve standards for these coverages. The rules further provide standards for the investment of contingency reserves and limitations and restrictions on the types of insurance that may be issued and on the total net liability of an insurer with respect to any risk or hazard insured. Moreover, reserves for unearned premiums, unpaid losses and loss adjustment expenses are required by the rules. The rules state that all reserves required shall be reflected in all financial statements filed with the Department by the insurer. Finally, the rules prohibit specific activities that are deemed to be a conflict of interest.

The Department continues to believe that the rules are reasonable and necessary to effectively regulate municipal bond, asset-backed securities and consumer debt obligations insurance.

A 60-day comment period is provided for this notice of proposal, and, therefore, pursuant to N.J.A.C. 1:30-3.3(a)5, the proposal is not subject to the provisions of N.J.A.C. 1:30-3.1 and 3.2 governing rulemaking calendars.

Social Impact

The rules proposed for readoption will continue to provide guidance with respect to requirements for financial guaranty insurers issuing the products to which the rules apply. Thus, compliance efforts of all insurers of municipal bonds, asset-backed securities and consumer debt obligations will continue to be facilitated by the rules set forth in the chapter. The specific

standards prescribed fulfill the Department's regulatory purpose by preventing abuses and assuring that only authorized insurance companies engage in this type of business. The public has benefited, and will continue to benefit, from the oversight and regulation of the propriety of the financial arrangements and the soundness of the financial practices utilized with respect to these coverages. Moreover, without these rules, insurers would lack guidance with respect to this coverage, which, in turn, could result in disruptions in the market and resulting risks upon the public.

Economic Impact

Insurers will continue to be required to incur any costs associated with continued compliance with the rules, including capital and surplus, contingency reserves, meeting standards for collateral, limits on an insurer's exposure on any one risk or hazard, and filing requirements. However, the Department does not believe that these requirements should impose an undue burden on insurers, which are generally consistent with those established under New York law. These rules do not impose any new requirements, fees or charges upon insurers of municipal bonds, asset-backed securities and consumer debt obligations. These rules will continue the existing regulatory framework through which the Department monitors the affected insurers to help ensure that they do not lapse into a hazardous financial condition and are otherwise in a position to pay claims when they become due. This, in turn, should continue to benefit the public and insurers.

Federal Standards Statement

A Federal standards analysis is not required because the rules proposed for readoption are not subject to any Federal requirements or standards.

Jobs Impact

The Department does not anticipate that any jobs will be generated or lost as a result of the rules proposed for re adoption.

The Department invites commenters to submit any data or studies on the potential jobs impact of the rules proposed for re adoption with their comments on other aspects of the proposal.

Agriculture Industry Impact

The rules proposed for re adoption will not have any impact on the agriculture industry in New Jersey.

Regulatory Flexibility Analysis

The rules proposed for re adoption should apply to few, if any, “small businesses” as that term is defined in the Regulatory Flexibility Act, N.J.S.A. 52:14B-16 et seq. To the extent that the rules apply to small businesses, they will apply to insurers licensed to transact financial guaranty insurance in this State seeking to provide or providing coverage on municipal bonds, asset-backed securities and consumer debt obligations. The compliance, recordkeeping and financial reporting requirements imposed by the rules are clearly defined in the rules themselves as outlined in the Summary above. Compliance with various provisions of this chapter must be reflected in all financial statements filed by insurers engaged in the business to which these rules apply.

The Department has determined that the rules proposed for re adoption continue to be reasonable and necessary to help assure the financial stability and integrity of financial guaranty insurance. Financial guaranty insurance is imbued with a significant public interest because it

also provides unique benefits for public entities. For example, municipal bond insurance permits these public entities to obtain funding at a lower interest rate, which saves costs in financing public projects. The requirements set forth in the rules promote the long-term financial integrity of the insurers that transact this line of business. Therefore, the rules properly apply to all insurers without regard to size. Future annual costs of compliance with these rules are not expected to differ from current annual costs. (See Economic Impact statement above.) The use of professional services of actuaries and accountants as currently required by the rules will continue to be necessary. These professional services should continue to be available either on the staff of insurers or from independent firms.

Therefore, to ensure the continued consistency and uniformity in the regulation and supervision of insurers transacting financial guaranty insurance, the rules proposed for readoption provide no differentiation in compliance requirements based on insurer size.

Smart Growth Statement

The rules proposed for readoption will not have impact on the achievement of smart growth or implementation of the State Development and Redevelopment Plan.

Full text of the rules proposed for readoption may be found in the New Jersey Administrative Code at N.J.A.C. 11:7.