

**CHAPTER 148a. SAFEGUARDING INSURER SECURITIES**

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**Authority**

The provisions of this Chapter 148a issued under sections 206, 506, 1501 and 1502 of The Administrative Code of 1929 (71 P. S. §§ 66, 186, 411 and 412); The Insurance Department Act of 1921 (40 P. S. §§ 1—324); The Insurance Company Law of 1921 (40 P. S. §§ 341—991); 40 Pa.C.S. §§ 6101—6127 and 6301—6335; the Voluntary Nonprofit Health Service Act of 1972 (40 P. S. §§ 1551—1568); the Fraternal Benefit Society Code (40 P. S. §§ 1142-101—1142-701); the Health Maintenance Organization Act (40 P. S. §§ 1551—1567); The Pennsylvania Fair Plan Act (40 P. S. §§ 1600.101—1600.502); and Article VIII of the Health Care Services Malpractice Act (40 P. S. §§ 1301.801—1301.811), unless otherwise noted.

**Source**

The provisions of this Chapter 148a adopted November 1, 2002, effective November 2, 2002, 32 Pa.B. 5409, unless otherwise noted.

**§ 148a.1. Definitions.**

The following words and terms, when used in this chapter, have the following meanings, unless the context clearly indicates otherwise:

*Agent*—

(i) A National bank, state bank or trust company that does any of the following:

(A) Maintains an account in its name in a clearing corporation.

(B) Is a member of the Federal Reserve System through which a custodian participates in a clearing corporation or the Federal Reserve book-entry system.

(ii) With respect to securities issued by institutions organized or existing under the laws of a foreign country or securities used to meet the deposit requirements under the laws of a foreign country as a condition of doing business in that country, the term may include a corporation organized or existing under the laws of a foreign country and legally qualified under those laws to accept custody of securities.

*Authorized person*—A person authorized in writing by an insurer's board of directors to issue instructions relating to the insurer's securities held by a custodian.

*Clearing corporation*—

(i) A clearing corporation as defined in 13 Pa.C.S. § 8102 (relating to definitions) and organized for the purpose of effecting transactions in securities by computerized book-entry.

(ii) With respect to securities issued by institutions organized or existing under the laws of a foreign country or securities used to meet the deposit requirements under the laws of a foreign country as a condition of doing business in that country, the term may include a corporation organized or existing under the laws of a foreign country and legally qualified under those laws to effect transactions in securities by computerized book-entry.

*Custodian—*

(i) A National bank, Federal savings bank, state bank or trust company that is:

(A) Capitalized as required by the standards adopted by United States banking regulators.

(B) Either regulated by Federal or state banking laws or a member of the Federal Reserve System.

(C) Legally qualified to accept custody of securities as required under § 148a.3 (relating to requirements for custodial agreements).

(ii) With respect to securities issued by institutions organized or existing under the laws of a foreign country or securities used to meet deposit requirements under the laws of a foreign country as a condition of doing business in that country, the term may include a bank that is:

(A) Incorporated or organized under the laws of a foreign country.

(B) Regulated as a bank by that country's government, or an agency thereof.

(C) Capitalized as required by the standards adopted by international banking authorities.

(D) Legally qualified to accept custody of securities as required under § 148a.3.

*Department—*The Insurance Department of the Commonwealth.

*Federal Reserve book-entry system—*The computerized systems sponsored by the United States Department of the Treasury and certain agencies and instrumentalities of the United States for holding and transferring securities of the United States Government and its agencies and instrumentalities in Federal Reserve Banks through banks that are members of the Federal Reserve System or that otherwise have access to the computerized systems.

*Foreign country—*A nation, province or territory other than the United States or a state thereof.

*Instructions—*

(i) A written statement that:

(A) States the specific purpose of the requested action.

(B) Identifies the specific transaction or type of transaction to which the requested action relates.

(C) Contains the signature of at least one authorized person.

(D) Is received by letter, facsimile or other form of electronic transmission whereby a custodian is able to verify with a reasonable degree of certainty the identity of the sender.

(ii) The verbal instructions of an authorized person if:

(A) The custodian is able to verify with a reasonable degree of certainty the identity of the sender.

(B) The verbal instructions are confirmed within 24 hours by written instructions.

*Insurer*—The following entities domiciled and licensed to transact business in this Commonwealth:

(i) An insurance company, association or exchange.

(ii) A reciprocal or interinsurance exchange.

(iii) An employers' mutual liability insurance association.

(iv) A nonprofit health plan corporation, whether operating a hospital plan or a professional health services plan, or both.

(v) A fraternal benefit society or beneficial association.

(vi) A health maintenance organization.

(vii) A preferred provider organization.

(viii) The Industry Placement Facility under The Pennsylvania Fair Plan Act (40 P. S. §§ 1600.101—1600.502).

(ix) A joint underwriting association under Article VII of the Health Care Services Malpractice Act (40 P. S. §§ 1301.801—1301.811).

*Investment company*—An entity registered and regulated as an investment company under the Investment Company Act of 1940 (15 U.S.C.A. §§ 80a-1—80a-64).

*Investment company securities*—Stocks or shares issued by an investment company.

*Registered form*—A form of certificated security as defined in 13 Pa.C.S. § 8102.

*Securities*—

(i) Certificated securities and uncertificated securities as defined in 13 Pa.C.S. § 8102.

(ii) The term includes short-term and long-term investments but does not include investment company securities.

*State*—A state, territory or possession of the United States.

### § 148a.2. Permissible methods of holding securities.

(a) An insurer may hold its securities in definitive certificates.

(b) An insurer may provide for its securities to be held by a custodian under a custodial agreement as required under § 148a.3 (relating to requirements for custodial agreements). Securities held under a custodial agreement shall be held by:

(1) The custodian.

- (2) The custodian's agent.
  - (3) A clearing corporation.
  - (4) The Federal Reserve book-entry system.
- (c) An insurer's investment company securities may be held by the investment company that issued the investment company securities as required under § 148a.4 (relating to requirements for investment company securities).
- (d) An insurer may provide for its securities to be held as required by a state treasurer or other state regulatory authority to meet deposit requirements as a condition of doing business in that state.

#### Cross References

This section cited in 31 Pa. Code § 148a.3 (relating to requirements for custodial agreements).

### § 148a.3. Requirements for custodial agreements.

- (a) An agreement between an insurer and a custodian providing for the custody of the insurer's securities under § 148a.2(b) (relating to permissible methods of holding securities) shall be:
- (1) In writing.
  - (2) Authorized by a resolution of either the insurer's board of directors or an authorized committee of its board of directors.
  - (3) Signed by at least one officer of the insurer and one officer of the custodian.
- (b) A custodial agreement shall contain at least the following provisions:
- (1) The custodian shall hold the securities subject to the insurer's instructions. In the event of a discrepancy or dispute, verbal instructions shall be superseded by written instructions. The securities shall be withdrawable immediately upon receipt of the insurer's written instructions.
  - (2) The custodian may not have a security interest or lien in any securities held under the agreement.
  - (3) The custodian may utilize an agent to gain entry in a clearing corporation or in the Federal Reserve book-entry system or for other services if the custodian enters into a written agreement with the agent whereby:
    - (i) The securities of one or more insurers will be held as required under this chapter.
    - (ii) The custodian retains responsibility for the safekeeping of the insurer's securities and for compliance with the terms and conditions of the custodial agreement as required under this chapter.
    - (iii) The custodian provides the insurer with notice within 5 business days of the utilization of an agent. The notice shall include, at a minimum:
      - (A) The identity of the agent.
      - (B) The date of the custodian's written agreement with the agent.
      - (C) An acknowledgement that the custodian has retained responsibility for the insurer's securities as required under subparagraph (ii).

(4) Securities in registered form shall be registered in the name of the insurer, the insurer's nominee, the custodian's nominee or, if held by a clearing corporation, in the name of the clearing corporation or its nominee.

(5) Certificated securities shall be held by the custodian in a separate account established to hold only the insurer's securities under the custodial agreement.

(6) Securities held in a clearing corporation or in the Federal Reserve book-entry system shall be separately identified on the custodian's records as being owned by the insurer.

(7) The custodian's records shall identify which securities are held by the custodian or by its agent and which securities are in a clearing corporation or in the Federal Reserve book-entry system.

(8) The custodian's records shall identify the location of securities held in a clearing corporation or in the Federal Reserve book-entry system and, if applicable, the name of the clearing corporation and the name of the agent.

(9) The custodian shall provide a statement that it has secured and will maintain adequate insurance protection as required by the custodian's banking regulator to cover its duties and activities as custodian of the insurer's assets.

(10) The custodian shall be obligated to indemnify the insurer for any loss of securities occasioned by the negligence or dishonesty of the custodian's officers or employees, or by burglary, robbery, holdup, theft or mysterious disappearance, including loss by damage or destruction. The agreement may provide that the custodian will not be liable for failure to take an action required under the agreement in the event and to the extent that the taking of the action is prevented or delayed by war (whether declared or not and including existing wars), revolution, insurrection, riot, civil commotion, act of God, accident, fire, explosion, stoppage of labor, strikes or other differences with employees, laws, regulations, orders or other acts of any governmental authority, or any other cause whatever beyond its reasonable control.

(11) In the event of a loss of securities for which the custodian is obligated to indemnify the insurer under paragraph (10), the custodian shall immediately replace the following:

(i) The securities or the value thereof.

(ii) The value of any loss of rights or privileges resulting from the loss of the securities.

(12) The custodian shall provide the Department with written notice if the agreement is terminated or if 100% of the assets are withdrawn from one or more custodial accounts established under the agreement. The notice shall be directed to the attention of the Deputy Insurance Commissioner for the Office of Regulation of Companies and provided within 24 hours of the custodian's receipt of the insurer's notice terminating the agreement or within 24 hours of the withdrawal of 100% of the assets in one or more custodial accounts estab-

lished under the agreement. The notice shall include the date of termination or 100% withdrawal and a list of the securities held on that date.

(13) The custodian shall provide the insurer with the following:

(i) Written reports on at least a monthly basis of holdings of the insurer's securities, including written confirmations of all transfers of securities to or from the insurer's account.

(ii) Annual reports of the review of the insurer's trust accounts by the custodian's trust committee.

(14) If requested in writing by an authorized person, the custodian shall provide the following information within 30 days of the custodian's receipt of the written request:

(i) Reports from a clearing corporation or the Federal Reserve book-entry system.

(ii) Internal or external reports on the custodian's system of internal control.

(15) Reports and confirmations provided by the custodian may be transmitted in electronic or paper form.

(16) The custodian shall maintain records and information sufficient to enable the insurer to:

(i) Comply with accounting and reporting requirements for financial statements and supporting schedules filed with the Department, to the extent that information maintained by the custodian is relied upon by the insurer to prepare its financial statements.

(ii) Provide information required in a financial examination of the insurer under Article IX of The Insurance Department Act of 1921 (40 P. S. §§ 323.1—323.8) or an audit, including, the identifying numbers assigned to the securities by the Committee on Uniform Securities Identification Procedures (CUSIP).

(17) Upon receipt of a written request signed by an authorized person, the custodian shall:

(i) Allow officers or employees of the insurer, independent accountants retained by the insurer, and representatives of regulatory agencies to examine the custodian's records relating to the insurer's account on the custodian's premises and during the custodian's normal business hours.

(ii) Provide copies of its records relating to the insurer's account.

(iii) Provide, within 30 days of receipt of the written request, an affidavit sworn to and subscribed by an authorized officer of the custodian and containing language substantially similar to the following:

## CUSTODIAN AFFIDAVIT

\_\_\_\_\_, being duly sworn deposes and says that he/she is \_\_\_\_\_ of \_\_\_\_\_, a banking corporation organized under and pursuant to the laws of the \_\_\_\_\_ with the principal place of business at \_\_\_\_\_ (hereinafter called the “bank”);

That his/her duties involve supervision of activities of the bank as custodian and records relating thereto;

That the bank is custodian for certain securities of \_\_\_\_\_, having a place of business at \_\_\_\_\_ (hereinafter called the “insurer”) pursuant to an agreement between the bank and the insurer;

That the schedules attached hereto are true and complete statements of securities that, as of the close of business on \_\_\_\_\_ were:

*(check all that apply)*

\_\_\_\_ (1) In the custody of the bank for the account of the insurer; that, unless otherwise indicated on the schedule, the next maturing and all subsequent coupons were either attached to coupon bonds or in the process of collection; and that, unless otherwise indicated on the schedule, all such securities were in bearer form or in registered form in the name of the insurer, the insurer’s nominee, the custodian’s nominee or, if held by a clearing corporation, in the name of the clearing corporation or its nominee, or were in the process of being registered in such form.

\_\_\_\_ (2) Credited to a book-entry account with a Federal Reserve Bank under the Federal Reserve book-entry system and in a book-entry account maintained in the name of \_\_\_\_\_ on the books and records of a Federal Reserve bank at such date.

\_\_\_\_ (3) Deposited with \_\_\_\_\_ (a clearing corporation).

That the custodian has the responsibility for the safekeeping of such securities whether in the possession of the bank, credited to a book-entry account with a Federal Reserve Bank under the Federal Reserve book-entry system or deposited with a clearing corporation, as that responsibility is specifically set forth in the agreement between the bank as custodian and the insurer; and

That, to the best of his/her knowledge and belief, unless otherwise shown on the schedule, said securities were the property of said insurer and were free of all liens, claims or encumbrances whatsoever.

**Cross References**

This section cited in 31 Pa. Code § 148a.1 (relating to definitions); and 31 Pa. Code § 148a.2 (relating to permissible methods of holding securities).

**§ 148a.4. Requirements for investment company securities.**

An insurer’s investment company securities may be held by the investment company that issued the investment company securities if the investment company:

(1) Provides the insurer with written reports on at least a monthly basis of the insurer's investment, including written confirmations of all transfers of investments to or from the insurer's account. The reports and confirmations may be transmitted in electronic or paper form.

(2) Maintains records and information sufficient to enable the insurer to:

(i) Comply with accounting and reporting requirements for financial statements and supporting schedules filed with the Department, to the extent that information maintained by the investment company is relied upon by the insurer to prepare its financial statements.

(ii) Provide information required in a financial examination of the insurer under Article IX of The Insurance Department Act of 1921 (40 P. S. §§ 323.1—323.8) or an audit, including the identifying numbers assigned to the securities by the Committee on Uniform Securities Identification Procedures (CUSIP).

**§ 148a.5. Penalty and existing custodial agreements.**

(a) Failure to comply with this chapter will result in the treatment of an insurer's securities or investment company securities as nonadmitted assets for purposes of financial reports filed with the Department.

(b) With respect to custody agreements entered into prior to November 2, 2002, and in compliance with laws or regulations in existence immediately preceding November 2, 2002, insurers have until November 3, 2003, to achieve compliance with this chapter.

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