

**R590. Insurance, Administration.**

**R590-178. Securities Custody.**

**R590-178-1. Authority.**

This rule is promulgated by the Insurance Commissioner pursuant to Utah Insurance Code Sections 31A-2-201, 31A-2-206, and 31A-4-108.

**R590-178-2. Purpose and Scope.**

This rule authorizes domestic insurance companies to utilize modern systems for holding and transferring securities without physical delivery of securities certificates. This rule establishes standards for national banks, state banks, trust companies and broker/dealers to qualify and operate as custodians for insurance company securities.

**R590-178-3. Definitions.**

As used in this rule:

A. "Agent" means a national bank, state bank, trust company or broker/dealer that maintains an account in its name in a clearing corporation or that is a member of the Federal Reserve System and through which a custodian participates in a clearing corporation or the Federal Reserve book-entry system.

B. "Clearing corporation" means a corporation, as defined in Subsection 70A-8-101(1), that is organized for the purpose of effecting transactions in securities by computerized book-entry. Clearing corporation also includes "Treasury/Reserve Automated Debt Entry Securities System" and "Treasury Direct" book-entry securities systems established pursuant to 31 U.S.C. Section 3100 et seq., 12 U.S.C. pt. 391 and 5 U.S.C. pt. 301.

C. "Custodian" means:

1. a national bank, state bank, or trust company that shall at all times during which it acts as a custodian pursuant to this rule, be no less than adequately capitalized as determined by the standards adopted by United States banking regulators and that is regulated by either state banking laws or is a member of the Federal Reserve System and that is legally qualified to accept custody of securities in accordance with the standards set forth below; or

2. a trust company with minimum net worth of \$1,500,000 at all times during which it acts as a custodian, is licensed by the United States or any state thereof as a trust company, and is in compliance with the regulatory authority as verified through regular examination by the regulatory authority; or

3. A broker/dealer that shall be registered with and subject to jurisdiction of the Securities and Exchange Commission, maintains membership in the Securities Investor Protection Corporation, and has a tangible net worth equal to or greater than

two hundred fifty million dollars (\$250,000,000).

D. "Custodied securities" means securities held by the custodian or its agent, or that are being cleared or transferred through a clearing corporation.

E. "Federal Reserve book-entry system" means the computerized systems sponsored by the United States Department of the Treasury and other agencies and instrumentalities of the United States for holding and transferring securities of the United States government and the agencies and instrumentalities.

F. "Security" has the same meaning as that defined in 70A-8-101(1).

G. "Securities' certificate" has the same meaning as that defined in 70A-8-101(1).

H. "Tangible net worth" means shareholders equity, less intangible assets, as reported in the broker/dealer's most recent Annual or Transition Report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 (S.E.C. Form 10-K) filed with the Securities and Exchange Commission.

I. "Treasury/Reserve Automated Debt Entry Securities System" (TRADES) and "Treasury Direct" mean the book entry securities systems established pursuant to 31 U.S.C. Section 3100 et seq., 12 U.S.C. pt. 391 and 5 U.S.C. pt. 301. The operation of TRADES and Treasury Direct are subject to 31 C.F.R. pt. 357 et seq.

#### **R590-178-4. Use of Book-Entry Systems.**

A custodian may utilize a clearing corporation to clear and transfer securities when depositing or arranging for the deposit of securities held in or purchased for a domestic insurance company's general account or its separate accounts. When a clearing corporation is used to clear and transfer securities, securities of the same class of the same issuer may be merged and held in bulk in the name of the nominee of such clearing corporation regardless of the ownership of such securities and securities of small denominations may be merged into larger denominations. The records of any custodian utilizing a clearing corporation to clear and transfer securities shall at all times show that such securities are held for such insurance company and for which accounts thereof. Ownership of, and other interest in, such securities may be transferred by bookkeeping entry on the books of such clearing corporation without physical delivery of certificates representing such securities.

#### **R590-178-5. Requirements for Custodial Agreements.**

A. An insurance company may, by written agreement with a custodian, provide for the custody of its securities with that custodian. The securities that are the subject of the agreement may be held by the custodian or its agent, by the Federal Reserve

book-entry system, or may be cleared or transferred through a clearing corporation.

B. Agreements shall be in writing and shall be authorized by a resolution of the Board of Directors of the insurance company or of an authorized committee of the board pursuant to 31A-5-412. The terms of the agreement shall comply with the following:

1. Securities' certificates held by the custodian shall be held separate from the securities' certificates of the custodian and of all of its other customers.

2. Securities held indirectly by the custodian or its agent, by the Federal Reserve book-entry system, and securities being cleared or transferred through a clearing corporation shall be separately identified on the custodian's official records as being owned by the insurance company. The records shall identify which securities are held by the custodian or its agent, by the Federal Reserve book-entry system, and which securities are being cleared or transferred through a clearing corporation. If the securities are with the Federal Reserve book-entry system or are being cleared or transferred through a clearing corporation, the records shall also identify where the securities are and the name of the clearing corporation. If the securities are held by an agent of the custodian, the records shall contain the name of the agent.

3. All custodied securities shall be registered in the name of the insurance company or in the name of a nominee of the insurance company or in the name of the custodian or its nominee or, if in a clearing corporation, in the name of the clearing corporation or its nominee.

4. Custodied securities shall be held subject to the instructions of the insurance company and shall be withdrawable upon the demand of the insurance company, except that custodied securities used to meet the deposit requirements set forth in Subsection 31A-2-206(2) shall, to the extent required by Subsection 31A-2-206(2), be under the control of the insurance commissioner and shall not be withdrawn by the insurance company without the prior written approval of the insurance commissioner. Broker/dealers are not authorized to hold custodied securities that are used to meet the deposit requirements set forth in Subsection 31A-2-206(2). To the extent that national banks, state banks, and trust companies hold custodied securities that are used to meet the deposit requirements set forth in Subsection 31A-2-206(2), these custodied securities must be held in an account separate from other custodied securities of the insurance company.

5. The custodian shall be required to send or cause to be sent to the insurance company a confirmation of all transfers of custodied securities to or from the account of the insurance company. In addition, the custodian shall be required to furnish no less than monthly the insurance company with reports of

holdings of custodied securities at times and containing information reasonably requested by the insurance company. The custodian's annual report of the insurance company's accounts shall also be provided to the insurance company. Reports and verifications may be transmitted in electronic or paper form.

6. During the course of the custodian's regular business hours, an officer or employee of the insurance company, an independent accountant selected by the insurance company or a representative of the Insurance Department shall be entitled to examine, on the premises of the custodian, the custodian's records relating to custodied securities, but only upon furnishing the custodian with written instructions to that effect from an appropriate officer of the insurance company.

7. Upon written request from the insurance company, the custodian and its agents shall be required to send to the insurance company:

(a) all reports they receive from a clearing corporation on their respective systems of internal accounting control, and

(b) reports prepared by outside auditors on the custodian's or its agent's internal accounting control of custodied securities that the insurance company may reasonably request.

8. The custodian shall maintain records sufficient to determine and verify information relating to custodied securities that may be reported in the insurance company's annual statement and supporting schedules and information required in an audit of the financial statements of the insurance company.

9. The custodian shall provide, upon written request from an appropriate officer of the insurance company, the appropriate affidavits with respect to custodied securities. These shall be substantially in the form of Custodian Affidavits, Form A, 298-6, Form B, 298-7, and Form C, 298-8, published by NAIC Model Regulation Service.

a. "Form A" is to be used by a custodian where securities entrusted to its care have not been redeposited elsewhere;

b. "Form B" is to be used in instances where a custodian corporation maintains securities on deposit with The Depository Trust Company or like entity; and

c. "Form C" is to be used where ownership is evidenced by book entry at a Federal Reserve Bank.

10. A national bank, state bank or trust company shall secure and maintain insurance protection in an adequate amount covering the bank's or trust company's duties and activities as custodian for the insurance company's assets, and shall state in the custody agreement that protection is in compliance with the requirements of the custodian's banking regulator or other regulator of a trust company. A broker/dealer shall secure and maintain insurance protection for each insurance company's

custodied securities in excess of that provided by the Securities Investor Protection Corporation in an amount equal to or greater than the market value of each respective insurance company's custodied securities. The commissioner may determine whether the type of insurance is appropriate and the amount of coverage is adequate.

11. The custodian shall be obligated to indemnify the insurance company for any loss of custodied securities occasioned by the negligence or dishonesty of the custodian's officers or employees, and for burglary, robbery, holdup, theft and mysterious disappearance, including loss by damage or destruction.

12. In the event that there is loss of custodied securities, for which the custodian shall be obligated to indemnify the insurance company as provided in paragraph (11) above, the custodian shall promptly replace the securities or the fair value thereof and the value of any loss of rights or privileges resulting from the loss of securities.

13. 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 such 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, other acts of any governmental authority, or any other cause beyond its reasonable control.

14. In the event that the custodian gains entry in a clearing corporation through an agent, there shall be an agreement between the custodian and the agent under which the agent shall be subject to the same liability for loss of custodied securities as the custodian. However, if the agent shall be subject to regulation under the laws of a jurisdiction that is different from the jurisdiction the laws of which regulate the custodian, the Commissioner of Insurance of the state of domicile of the insurance company may accept a standard of liability applicable to the agent that is different from the standard of liability applicable to the custodian.

15. The custodian shall provide written notification to the insurance company's domiciliary commissioner if the custodial agreement with the insurance company has been terminated or if 100% of the account assets in any one custody account have been withdrawn. This notification shall be remitted to the insurance commissioner within three (3) business days of the receipt by the custodian of the insurance company's written notice of termination or within three (3) business days of the withdrawal of 100% of the account assets.

**R590-178-6. Requirements for Deposits with Affiliates.**

A. Nothing in this rule shall prevent an insurance company from depositing securities with another insurance company with which the depositing insurance company is affiliated, provided that the securities are deposited pursuant to a written agreement authorized by the board of directors of the depositing insurance company or an authorized committee thereof and that the receiving insurance company is organized under the laws of one of the states of the United States of America or of the District of Columbia. If the respective states of domicile of the depositing and receiving insurance companies are not the same, the depositing insurance company shall have given notice of the deposit to the insurance commissioner in the state of its domicile and the insurance commissioner shall not have objected to it within thirty (30) days of the receipt of the notice.

B. The terms of the agreement shall comply with the following:

1. The insurance company receiving the deposit shall maintain records adequate to identify and verify the securities belonging to the depositing insurance company.

2. The receiving insurance company shall allow representatives of an appropriate regulatory body to examine records relating to securities held subject to the agreement.

3. The depositing insurance company may authorize the receiving insurance company:

a. To hold the securities of the depositing insurance company in bulk, in certificates issued in the name of the receiving insurance company or its nominee, and to commingle them with securities owned by other affiliates of the receiving insurance company, and

b. To provide for the securities to be held by a custodian, including the custodian of securities of the receiving insurance company or in a clearing corporation.

**R590-178-7. Penalties and Prohibitions.**

A. Insurance companies found to be or to have been in violation of this rule shall be subject to fine, suspension, and revocation of license or other penalties permitted by Section 31A-2-308.

B. Insurance companies are not authorized to provide for the custody of their securities except as granted in this rule. Custodial securities held in violation of this rule shall be disregarded in determining and reporting the financial condition of an insurer.

**R590-178-8. Enforcement Date.**

The commissioner will begin enforcing this rule 90 days from

the rule's effective date.

**R590-178-9. Separability.**

If any provision of this rule or the application to any person or circumstance is for any reason held to be invalid, the remainder of the rule and the application of such provisions may not be affected.

**KEY: insurance law**

**Date of Enactment or Last Substantive Amendment: September 19, 2006**

**Notice of Continuation: August 2, 2016**

**Authorizing, and Implemented or Interpreted Law: 31A-4-108**