

## CHAPTER 7

### INSURANCE OF MUNICIPAL BONDS

#### Authority

N.J.S.A. 17:1-8.1 and 17:1-15e.

#### Source and Effective Date

R.1997 d.445, effective September 25, 1997.  
See: 29 N.J.R. 3591(a), 29 N.J.R. 4461(a).

#### Executive Order No. 66(1978) Expiration Date

Chapter 7, Insurance of Municipal Bonds, expires on September 25, 2002.

#### Chapter Historical Note

Chapter 7, Insurance of Municipal Bonds, was adopted as R.1975 d.212, effective July 23, 1975. See: 7 N.J.R. 272(b), 7 N.J.R. 370(b). Chapter 7 was amended by R.1987 d.426 and was assigned an expiration date of October 19, 1992. See: 19 N.J.R. 1409(a), 19 N.J.R. 1908(a).

Pursuant to Executive Order No. 66(1978), Chapter 7 was readopted as R.1992 d.425, effective September 25, 1992. See: 24 N.J.R. 1958(a), 24 N.J.R. 3729(b).

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#### SUBCHAPTER 1. GENERAL PROVISIONS

##### 11:7-1.1 Definitions

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

“Contingency reserve” means an additional premium reserve established for the protection of policyholders covered by policies insuring municipal bonds against the effect of excessive losses usually occurring during adverse economic cycles.

“Insurance of municipal bonds” means insurance against financial loss by reason of nonpayment of principal and interest obligations pursuant to the terms of municipal bonds as defined in “municipal bonds” below.

“Municipal bonds” means obligations issued by a state, territory or possession of the United States of America, or by any municipality, political subdivision (including but not limited to cities, counties, towns, villages, school districts and special districts for fire prevention, water, sewer, irrigation and other municipal public purposes provided for by law) or by any public agency or instrumentality (such as an authority or commission) of one or more of the foregoing.

##### 11:7-1.2 Capital, surplus and contingency reserve requirements

(a) An insurer shall not issue a contract insuring municipal bonds unless it is authorized to write the kinds of insurance defined in paragraph (g) of N.J.S.A. 17:17-1, and unless the insurer's license has been amended to indicate that the insurer is authorized to write municipal bond insurance under paragraph (g), further provided that:

1. If it is a stock insurance company, it has a paid-in capital and surplus, or if it is a mutual insurance company, it has a minimum initial surplus, in an amount deemed by the Commissioner to be reasonable in relation to the insurer's outstanding liabilities and adequate to its financial needs, but in no case shall such amount be less than that prescribed by applicable provisions of the Insurance Law. Such stock or mutual insurer shall at all times maintain a surplus to policyholders or minimum surplus, as the case may be, in an amount at least equal to the minimum prescribed by the stated provisions for the aforementioned class of business and for such other kinds of insurance defined in N.J.S.A. 17:17-1, as it may be authorized to transact; and

2. It shall establish a contingency reserve which shall consist of allocations of sums representing 50 percent of the earned premiums on policies insuring municipal bonds. Allocations to such reserve made during each calendar year shall be maintained for a period of at least 120 months, except that withdrawals may be made by the company in any year in which the actual paid losses on the said type of policy exceeded 35 percent of the earned premiums thereon, but no such releases shall be made without the prior written approval of the Commissioner of Insurance.

(b) In no event shall an insurer have outstanding a cumulative net liability, under policies in force insuring municipal bonds, in an amount which exceeds the sum of its capital and surplus, plus the contingent reserve as defined in (a)2 above. For the purpose of this subsection, the term cumulative net liability shall mean one third of one percent of the insured unpaid principal and insured unpaid interest covered by policies in force insuring municipal bonds. In the event that any such insurer has outstanding a cumulative net liability in excess of the amount as so computed, it shall not transact any new insurance of municipal bonds unless

and until its cumulative net liability no longer exceeds such amount.

(c) An insurer transacting the insurance of municipal bonds may invest the contingency reserve in tax and loss bonds purchased pursuant to Section 832(c) of the Internal Revenue Code, only to the extent of the tax savings resulting from the deduction for Federal income tax purposes of a sum equal to the annual contributions to the contingency reserve. The contingency reserve shall otherwise be invested in classes of securities or types of investments specified in paragraphs (a), (c), (d) and (f) of N.J.S.A. 17:24-1.

Amended by R.1987 d.426, effective October 19, 1987.

See: 19 N.J.R. 1409(a), 19 N.J.R. 1908(a).

Added text in (b) "For the purpose ... insuring municipal bonds." Recodified (b)2 to (c).

#### Case Notes

Rules held valid as promulgated in substantial compliance with statutory and regulatory rulemaking requirements, and as neither arbitrary, capricious nor unreasonable. *Insurance Brokers Ass'n of New Jersey, Inc. v. Sheeran*, 162 N.J.Super. 34, 392 A.2d 203 (App.Div. 1978), certification denied 78 N.J. 408, 396 A.2d 594 (1978).

#### 11:7-1.3 Limitations and restrictions

(a) Policies insuring municipal bonds shall be issued to cover only bonds of the type defined in N.J.A.C. 11:7-1.1.

(b) For the purpose of complying with the provisions of N.J.S.A. 17:18-9, the total net liability of an insurer in respect to any one issue of municipal bonds insured shall be the average annual amount due for principal and interest on insured securities of such issue, net of appropriate allowance for reinsurance.

(c) In no event, shall the total net liability exceed an amount representing 10 percent of the surplus to policyholders of the insurer.

Amended by R.1987 d.426, effective October 19, 1987.

See: 19 N.J.R. 1409(a), 19 N.J.R. 1908(a).

Deleted text from (b) through (b)1.iii "shall be such ... under its policy." and added text "insured shall be ... allowance for reinsurance."

#### 11:7-1.4 Financial statements

(a) The reserve for unearned premiums shall be computed as required by the provisions of N.J.S.A. 17:23-1 or by such other method as the Commissioner may prescribe.

(b) In addition to the contingency reserve required by N.J.A.C. 11:7-1.2(a)2, each insurer engaging in the issuance of policies insuring municipal bonds shall provide a reserve for unpaid losses and loss adjustment expenses on such policies in all financial statements filed by it with this Department. Such reserve shall be computed in a manner consistent with the provisions of N.J.S.A. 17:23-1 and shall be based upon either the case basis method or such other method as the Commissioner may prescribe.

#### 11:7-1.5 Conflicts of interest prohibited

No insurer authorized to transact the business of insuring municipal bonds shall pay any commission or make any gift of money, property or other valuable thing to any employee, agent or representative of any issuer of municipal bonds or to any employee, agent or representative of any underwriter of any issue of such bonds as an inducement to the purchase of, or at any time there is in force, a policy insuring such bonds, and no such employee, agent or representative of such issuer or underwriter shall receive any such payment or gift. However, violation of the provisions of this Section shall not have the effect of rendering void the insurance policy issued by the insurer.