

CUSTODIAL ARRANGEMENTS

June 19, 1996

The commissioner is aware that some Iowa insurers have utilized the services of a broker-dealer to custody assets in lieu of holding the securities themselves or with a banking institution. As a result, it is important to understand the ramifications, as to recovery of insurer assets, in the event of the liquidation of either a bank or broker-dealer that custodies assets. So long as both entities remain solvent, the differences may appear to be insignificant. However, in the event of a liquidation, the protections afforded to customers are dramatically different. In the event of a bank liquidation it is well established that trusted assets held by the trust department of a bank do not become assets of the bank and will be returned to the owner. Upon the liquidation of a broker-dealer the same assurances are not present.

Section 515.35, Code of Iowa (1995) provides that investment programs developed by companies take into account the safety of the company's principal, investment yield and growth, stability in the value of the investment, liquidity and investment diversification. In furtherance of these parameters, all domestic insurers are requested to review their investment practices including custody arrangements. Your attention is directed to assets custodied with an outside party. If funds are held outside the trust department of a bank, potential peril for policyholder funds exists and therefore action is necessary to obviate this exposure.

In the event that assets are held by a third party outside the trust department of a bank, the company is directed to expediently move the assets to an appropriate custodian to insure that in the event of a liquidation, assets will be readily retrievable.

Any questions regarding this bulletin should be directed to Kimberlee L. Cross, Financial Regulation Counsel at 515-281-4163.

Therese M. Vaughan
COMMISSIONER OF INSURANCE

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