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**IDAPA 18
TITLE 01
CHAPTER 33**

**18.01.33 - DOMESTIC INSURER PURCHASING AND SELLING OF
EXCHANGE-TRADED CALL AND PUT OPTIONS**

000. LEGAL AUTHORITY.

Title 41, Chapter 6, Section 601, Idaho Code; Title 41, Chapter 7, Section 703, Idaho Code; and Title 67, Chapter 52, Idaho Code. (7-1-93)

001. TITLE AND SCOPE.

01. Purpose. It is the purpose of this rule to regulate the manner and circumstance under which Idaho domestic insurance companies may purchase and sell exchange-traded call and put options and by establishing recordkeeping requirements concerning such transactions. (7-1-93)

02. Securities Options Trading. With the introduction of securities options trading on national regulated securities exchanges, securities options can now be bought and sold in much the same way that securities are bought and sold on major stock exchanges. With the regulation and standardization of option contracts and trading practices, investments in options have become less risky and present a reasonable and alternate investment opportunity for insurers. (7-1-93)

002. -- 003. (RESERVED)

004. DEFINITIONS.

For the purpose of this rule: (7-1-93)

01. Call Option. "Call option" means an option contract under which the holder of the contract has the right, in accordance with the terms of the contract, to purchase (or to make a cash settlement in lieu thereof) the amount of the underlying financial instruments covered by the contract. (7-1-93)

02. Exchange-Traded. "Exchange-traded" means traded under the terms and conditions required by (or substantially similar to) a national securities exchange registered under the Securities and Exchange Act of 1934 (15 U.S.C.789 et seq.) which has been authorized to provide a market for option contracts pursuant to Rule 9b-1 of the Securities and Exchange Act of 1934, as amended or traded on a commodity exchange designated as a contract market regulated by the Commodity Futures Trading Commission. (7-1-93)

03. Closing Sale Transaction. "Closing sale transaction" means the writing (sale) of a call or put option, the effect of which is to reduce or eliminate the obligations of an insurer as a call or put option purchaser with respect to an option contract or contracts. (7-1-93)

04. Commodity Futures Trading Commission. "Commodity Futures Trading Commission" means the federal regulatory agency charged and empowered under the Commodities Futures Trading Commission Act of 1974 (7 U.S.C.A.1 et seq.) with the regulation of the commodity exchanges or any other agency of the federal government which thereafter succeeds to or shares such power. (7-1-93)

05. Escrowed Securities. "Escrowed securities" means a financial instrument owned by an insurance company with respect to which a custodial agreement has been entered. (7-1-93)

06. Closing Purchase Transaction. "Closing purchase transaction" means the purchase of a call or put option the effect of which is to reduce or eliminate the obligations of a call or put option writer with respect to an option contract or contracts. (7-1-93)

07. Financial Futures Contract. "Financial futures contract" means an exchange-traded agreement to make or take delivery of (or to make cash settlement in lieu thereof) a specified amount of financial instruments on or before a specified date or period of time under terms and conditions regulated by the Commodities Futures Trading Commission. (7-1-93)

08. Financial Instrument. “Financial instrument” means a security, currency, financial futures contract or index of a group of securities or currencies authorized or permitted under Title 41, Chapter 7, Sections 702, 703, 707, 708, 709, 710, 711, 713, 714, 715, 716, 717, and 727, Idaho Code. (7-1-93)

09. Guaranteed Funds. “Guaranteed funds” means cash or cash equivalents as may be defined from time to time under Federal Reserve Regulation T (12 CFR.220.1 et seq.) or its equivalent successor federal regulation, which are owned by an insurer and with respect to which a guarantee letter has been issued. (7-1-93)

10. Margin. “Margin” means any type of deposit or settlement, made or to be made with a futures commission merchant, security broker, clearinghouse, or safekeeping agent to ensure performance of the terms of the option contract. (7-1-93)

11. Put Option. “Put option” means an option contract under which the holder of the contract has the right in accordance with the terms of the contract to sell (or to make a cash settlement in lieu thereof) the amount of the underlying financial instrument covered by the put option contract. (7-1-93)

005. -- 010. (RESERVED)

011. PURCHASE AND EXERCISE OF EXCHANGE - TRADED CALL AND PUT OPTIONS.
Any purchase of exchange-traded call or put options, except in closing purchase transactions, shall be: (7-1-93)

01. Limitations. Limited in the aggregate by purchase of such options as set forth in Title 41, Chapter 7, Section 735, Idaho Code. (7-1-93)

02. Continuation. Evidenced by a trade confirmation or other confirmation of ownership issued to the insurer by an entity duly authorized to do so. (7-1-93)

012. SALE AND ASSIGNMENT OF CALL AND PUT OPTIONS.

01. Selling Requirements of Call Options. Any insurer which sells (writes) call options with respect to financial instruments it owns shall: (7-1-93)

a. Maintain custodial agreements which call for its escrowed securities to be kept segregated by the bank or other custodial agent from other financial instruments owned by the insurer or others, which are deposited with the same bank or custodial agent or in a margin account; (7-1-93)

b. Obtain and retain in its possession complete documentation for all transactions relating to the escrowed securities. (7-1-93)

02. Selling Requirements of Exchange-Traded Put Options. Any insurer which sells (writes) exchange-traded put options guaranteed by funds it owns shall: (7-1-93)

a. Maintain custodial agreements which call for its guaranteed funds to be kept segregated by the bank or other custodian from other financial instruments owned by the insurer or others which are deposited with the same bank or custodial agent or in a margin account; and (7-1-93)

b. Obtain and retain in its possession a copy of a guarantee letter identifying with particularity its guaranteed funds so escrowed; and (7-1-93)

c. Not become potentially obligated through the sale of such put options for the purchase of financial instruments in amounts which, when aggregated with current holdings exceed the applicable limitations contained in Title 41, Chapter 7, Section 735, Idaho Code, whether or not such put options are acquired at the delivery date. (7-1-93)

013. ACCOUNTING FOR TRANSACTIONS IN EXCHANGE-TRADED CALL AND PUT OPTIONS.

01. Accounting for Sale of Call or Put Option. The consideration received for selling a call or put option shall not be included in income at the time of receipt, but shall be carried in a deferred account until one of the following occurs: (7-1-93)

- a. The call or put option expires through the passage of time; (7-1-93)
- b. The insurer sells the underlying financial instrument pursuant to an exercise of the call option; or (7-1-93)
- c. The insurer purchases the underlying financial instrument pursuant to the exercise of the put option; or (7-1-93)
- d. The insurer engages in a closing purchase transaction. (7-1-93)

02. Accounting for Expiration Through Passage of Time. If the obligation under a call or put option expires through the passage of time, the consideration for the option shall be treated as income received at the time of such expiration. (7-1-93)

03. Accounting When Underlying Financial Instruments Sold. If the underlying financial instrument is sold pursuant to the exercise of a call option, the consideration received for the option shall be treated as increasing the amount realized upon the sale of the underlying financial instrument and shall be included in determining capital gain or loss. (7-1-93)

04. Accounting When Underlying Financial Instrument Purchased. If the underlying financial instrument is purchased pursuant to the exercise of the put option, the consideration received for the option shall be treated as reducing the cost basis of the financial instrument so purchased. (7-1-93)

05. Accounting When Obligation is Terminated. If the obligation under a call or put option is terminated through a closing purchase transaction, the difference between the consideration received from the sale of the call or put option and the consideration paid in the closing purchase transaction shall be treated, at the time of such closing purchase transaction, as a capital gain or loss, as the case may be. (7-1-93)

014. VALUATION.

01. Current Market Price. Each exchange-traded call or put financial instrument option purchased by an insurance company shall be valued at the current market price. This "marking-to-market" will result in an unrealized gain or loss. (7-1-93)

02. Stock. Stock owned by an insurance company with respect to which a call option has been sold shall be valued, so long as the option exists, at the current market price of the stock. (7-1-93)

03. Deferred Account Valued at Market Value. The amount held in a deferred account for call or put stock options sold shall be valued at the current market price. The adjustment will result in an unrealized gain or loss. (7-1-93)

04. Deferred Account Valued at Cost. The amount held in a deferred account for a call or put option may be valued at cost if the underlying financial instrument: (7-1-93)

- a. Would be carried at amortized value if acquired by the insurance company; or (7-1-93)
- b. Is a debt financial futures or a debt index contract. (7-1-93)

05. Uncompleted Hedging Transactions. Amounts may be deferred for expired or closed options contracts if the contracts are related to uncompleted hedging transactions as defined in IDAPA 18.01.45, "Domestic Insurers Regarding Financial Futures Contracts." (7-1-93)

06. Debt Instruments. Debt instruments owned by an insurance company with respect to which a call

option has been sold shall continue to be valued in the same manner as any other such instruments owned by said company. (7-1-93)

015. ADMINISTRATION AND RECORDKEEPING.

01. Policies and Procedures. Prior to engaging in transactions in call and put options, an insurer shall develop and adequately document policies and procedures regarding investment strategies and objectives, recordkeeping needs, and reporting matters. Such policies and procedures shall address authorized investments, investment limitations, authorization and approval procedures, accounting and reporting procedures and controls, and shall provide for review of activity in call and put options by the insurer's board of directors or its designee. (7-1-93)

02. Recordkeeping Systems. Recordkeeping systems must be sufficiently detailed to permit internal auditors and insurance department examiners to determine whether operating personnel have acted in accordance with established policies and procedures. Insurer records must identify for each hedging transaction the related call and put options and the hedged items. (7-1-93)

016. PROHIBITION AGAINST SPECULATING IN OPTIONS.

The authority granted to insurers herein to engage in option transactions shall be used solely in a manner consistent with the insurer's obligation to exercise prudent judgement in the conservative management of its assets. Each option transaction shall reflect such prudent judgement and shall have a rationale related to such conservative management of assets rather than speculation. Nothing herein shall be construed to authorize an insurer to engage in options transactions to an extent or to a degree which would, under the relevant circumstances, be inordinate or speculative. Subject to the foregoing limitation, nothing in this rule shall prohibit a domestic insurer from participating in the exchange-traded financial futures markets as provided in IDAPA 18.01.45, "Domestic Insurers Regarding Financial Futures Contracts." (7-1-93)

017. SEVERABILITY.

If any provision of this rule or the application thereof to any persons or circumstances is held invalid, the remainder of the rule and application of such provision to the other persons or circumstances shall not be affected thereby. (7-1-93)

018. -- 999. (RESERVED)

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