» Insolvency
TRENDS
Summer 2013

National Conference of Insurance Guaranty Funds NCIGF

A biannual publication providing updates on recent property and casualty insolvencies and public policy developments

GUARANTY FUNDS WORK

in partnership with insurance regulators to protect policyholders.

A state court finds an insurance company insolvent and orders it liquidated.

Policyholder claim files are transferred to the guaranty funds for servicing.

Covered claims are paid from a pool of money drawn from three sources made available at the time of the insolvency: a) the insolvent insurance company's remaining assets, b) statutory deposits collected in certain states, and c) assessments on insurers licensed to write business in a state.

Payments are made promptly.

HOW THE GUARANTY FUND SYSTEM IS FUNDED

Recoveries

To the extent possible to fulfill guaranty fund statutory duties, monies are obtained from remaining estate assets.

- The insurance company's remaining assets (including reinsurance)
- Statutorily mandated deposits collected in certain states while the company is still writing business

Assessments from Insurers

Charged to insurance companies licensed to write business in a state

- Typical cap is 2% of "net direct written premium"
- Assessment is determined by the amount of money needed by the guaranty fund to supplement the funding pool described above
- Some guaranty funds have separate "assessment accounts" allowing them to segregate assessment billing and payments into various lines of business—a typical structure would be workers' compensation, auto, and all other property & casualty lines covered by the funds

Welcome to the 2013 summer issue of the National Conference of Insurance Guaranty Funds' (NCIGF) *Insolvency Trends*. Authored by the legal and public policy staff of the NCIGF, this paper provides an update on recent events in insolvency law and practice and a look ahead at what is on the horizon.

See inside for…

- Insurance insolvency developments; new liquidations this year and status of estates
- Developments from the federal front on issues such as Dodd-Frank implementation
- International developments
- Developments in state laws
- Run-offs of troubled companies

Property and Casualty Guaranty Funds: Continuing to Evolve to Protect Policyholders

The guaranty fund system was established in 1969 by the property and casualty insurance industry, insurance regulators, and states to provide a safety net that protects insurance consumers if an insurance company fails. The guaranty fund system, an innovative and common-sense mechanism, draws first on the assets of the failed insurance company before turning to assessments of healthy insurers in each state. Since its inception, the system has paid out more than $27 billion to policyholders, beneficiaries, and claimants related to more than 550 insolvencies.

Following liquidation, the statutorily created guaranty funds seamlessly step into the shoes of a defunct company and pay the covered claims of policyholders and claimants whose claims otherwise would go unpaid by an insolvent insurance company.

Today, the guaranty fund system remains true to its original intent: delivering protection to those least able to weather the impact of insurance company insolvencies.

NEW INSOLVENCIES THIS YEAR: THE PROPERTY CASUALTY GUARANTY FUNDS CONTINUE TO PROTECT CLAIMANTS

Two writers of substantial blocks of workers' compensation business, the Lumbermens companies, and the ULLICO Casualty Company, were liquidated in May. Guaranty funds began servicing a substantial block of workers' compensation claims along with other lines of business on both insolvencies. Both companies wrote business on a large deductible basis. In both cases, guaranty fund representatives worked with the receivers of the insolvent companies to ensure that periodic benefits such as workers' compensation disability payments and pharmacy benefits were not disrupted. While the Lumbermens companies had been in run-off for an extended period, the ULLICO matter came up with little advance notice. This recent activity clearly shows the benefits of maintaining guaranty fund readiness and underscores the importance of pre-liquidation planning.

Overall, five insolvencies occurred in 2012: Autoglass Insurance Company, a single-state New York private passenger auto company; First Sealord Surety, Inc., a small bond and surety company domiciled in Pennsylvania and licensed in 38 states with claims in six states; Garden State Indemnity Company, Inc., a single-state New Jersey professional liability and surety company; Northern Plains Insurance Company, an automobile insurance company domiciled and writing business primarily in South Dakota; and Frontier Insurance Company.

Seven insolvencies occurred during the second quarter 2013: Lumbermens companies (Lumbermens Mutual Casualty Company, American Manufacturers Mutual Insurance Company and American Motorists

Insurance Company) domiciled in Illinois and licensed in all states; and ULLICO, domiciled in Delaware and licensed in all states except Maine, New Hampshire and Rhode Island; Santa Fe Auto Insurance Company, a small automobile insurance company domiciled in Texas, licensed and with claims in eight states (Arizona, Arkansas, Georgia, Nevada, New Mexico, Oklahoma, Texas and Utah); Drivers Insurance Company, a small automobile insurance company domiciled in Oklahoma, licensed in 11 states and with claims in Georgia, Oklahoma and Texas; and American Fellowship Mutual Insurance Company, a Michigan single-state personal auto and homeowners company. The NCIGF staff assisted in various capacities in these new liquidations. From 2011 through the second quarter 2013, 25 property and casualty companies went into liquidation. The Florida guaranty funds were particularly heavily hit in 2011 with many single-state or regional companies being liquidated in this hurricane-prone area.

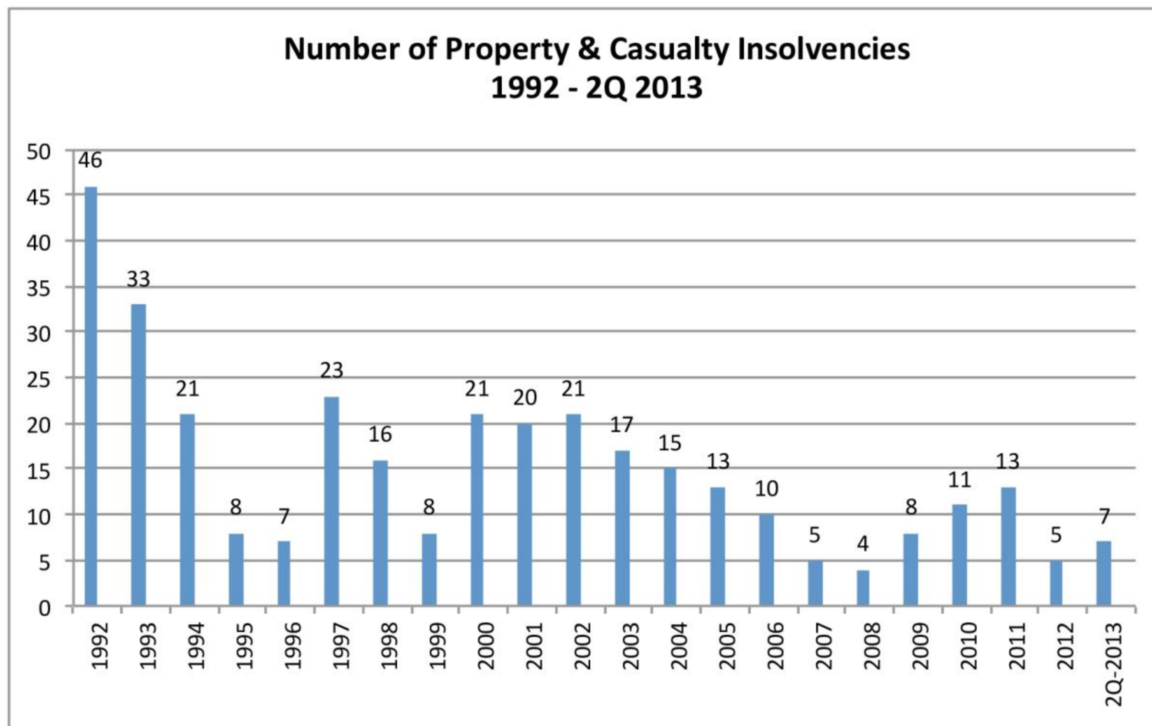
The list of liquidations from 2008 through the second quarter 2013 can be found in the following table.

Property & Casualty Insurance Companies in Liquidation 2008 - 2nd Quarter 2013				
Name of Company	**Liquidation Date**	**State of Domicile**	**Type of Company**	**States Licensed**
New Jersey Exchange Insurance Company	2/11/08	NJ	Auto, Commercial	NJ only
Guarantee Title and Trust Company	10/27/08	MI	Title	MI only
Austin Indemnity Lloyds Insurance Company	12/29/08	TX	Homeowners multiperil, private passenger auto, auto physical damage	TX only
MIIX Insurance Co	4/9/08	NJ	Fire, Allied, CMP, ITO, Ocean, IM, Medical Malpractice, WC	NJ, PA, NY, TX, OH, MI, MD
Valor Insurance Company, Inc.	5/27/09	MT	Workers compensation	MT only
Colonial Indemnity Insurance Company	7/7/09	NY	Other liability, private passenger auto, commercial auto, and auto physical damage	KY, NY, SC (All claims in NY)
Consumer First Insurance Company	7/21/09	NJ	Auto	NJ only
First Commercial Insurance Co.	8/24/09	FL	WC, commercial, auto, general liab, commercial multiperil	FL, Georgia
First Commercial Transportation and Property Insurance Co.	8/24/09	FL	Commercial auto	FL only
American Keystone Insurance Co.	10/9/09	FL	Homeowners	FL only
Southeastern U.S. Insurance Inc.	10/27/09	GA	WC	Georgia
Park Avenue Property and Casualty Insurance Co.	11/18/09	OK	WC	28 states (claims primarily in FL and GA)
Insurance Corporation of NY	3/10/10	NY	Fire and casualty	26 states (all claims in NY)
Imperial Casualty and Indemnity Insurance Co.	3/18/10	OK	WC	All states except FL, ME, MA, NY
Magnolia Insurance Co.	4/20/10	FL	Homeowners	FL only
Northern Capital Insurance Company	5/1/10	FL	Homeowners, automobile and inland marine	FL only
Financial Advisors Assurance Select RRG	5/20/10	NV	Errors and omissions	NV only
Gibraltar National Insurance Company	5/21/10	AR	WC	AR only
Titledge Insurance Company of New York	6/16/10	NY	Title	NY only
Coral Insurance Co.	7/26/10	FL	Homeowners	FL only
Pegasus Insurance Co.	8/12/10	OK	WC, minimal private passenger auto liability physical damage	27 states
Georgia Restaurant Mutual Captive Insurance Company	9/21/10	GA	WC	GA only
Colonial Cooperative Insurance Company	9/30/10	NY	Fire	NY only
Constitutional Casualty Co.	1/3/11	IL	Private passenger auto and homeowners multiple peril insurer; some commercial liability	IL only
Aequicap Insurance Co.	3/7/11	FL	Commercial auto	FL, GA, OK, SC, TX
Seminole Casualty Insurance Company	3/15/11	FL	Personal and commercial auto	8 states (claims primarily in FL and MD)
Atlantic Mutual Insurance Company	4/27/11	NY	WC, commercial multiperil, private passenger auto, homeowners, suretly, aircraft	All states
Western Insurance Company	9/13/11	UT	Surety	35 states
National Group Insurance Company	10/10/11	FL	Commercial auto, commercial property	FL and GA (all claims are in FL)
National Insurance Company	10/25/11	PR	Commercial auto	PR and FL
American Sterling Insurance Company	10/26/11	CA	Private passenger auto, auto physical damage	AZ, NV, KS
Homewise Preferred Insurance Company	11/4/11	FL	Primarily homeowners insurance	FL, TX, SC
Homewise Insurance Company	11/18/11	FL	Primarily homeowners insurance	FL and LA
Southern Eagle Insurance Company	12/16/11	FL	WC	FL only

Property & Casualty Insurance Companies in Liquidation

2008 - 2nd Quarter 2013 *(continued)*

Name of Company	Liquidation Date	State of Domicile	Type of Company	States Licensed
Autoglass Insurance Company	1/9/12	NY	Private passenger auto	NY only
First Sealord Surety, Inc.	2/8/12	PA	Bond and surety	38 states
Garden State Indemnity Company, Inc.	6/22/12	NJ	Professional liability, surety	NJ only
Northern Plains Insurance Company, Inc.	9/18/12	SD	Automobile	SD only
Frontier Insurance Company	11/9/12	NY	Fire, allied, homeowners and commercial multiperil, inland marine, medical malpractice, WC, other liability, products liability, private passenger auto liability, auto physical damage, fidelity, surety, burglary and theft, warranty	All states
Santa Fe Auto Insurance Company	4/5/13	TX	Private passenger auto, auto physical damage	AZ, AR, GA, NV, NM, OK, TX, UT
Lumbermens Mutual Casualty Company	5/10/13	IL	Workers' compensation, fire, homeowners and commercial multiperil, ocean marine, inland marine, medical professional liability, group accident and health, other accident and health, other liability, products liability, private passenger auto, commercial auto, auto physical damage, aircraft, fidelity and surety	All states
American Manufacturers Mutual Insurance Company	5/10/13	IL	Workers' compensation, homeowners and commercial multiperil, inland marine, other liability, products liability, private passenger auto, commercial auto, auto physical damage, fidelity and surety	All states
American Motorists Insurance Company	5/10/13	IL	Workers' compensation, homeowners and commercial multiperil, ocean marine, inland marine, medical professional, other liability, products liability, private passenger auto, commercial auto, auto physical damage, aircraft, fidelity, surety and warranty	All states
Drivers Insurance Company	5/13/13	OK	Private passenger auto, commercial auto	AR, GA, IA, KS, KY, LA, MS, MO, NB, OK, TX
ULLICO Casualty Company	5/30/13	DE	Workers' compensation, fidelity, surety, fiduciary liability, professional liability, commercial auto and commercial multiperil	All states except ME, NH and RI
American Fellowship Mutual Insurance Company	6/12/13	MI	Personal auto and homeowners	MI only



This chart shows the overall number of property and casualty insolvencies from 1992–2Q 2013.

For comprehensive information on the companies the guaranty funds are handling with payout information, please see our Web site at www.ncigf.org.

ESTATE DISTRIBUTION AND CLOSING EFFORTS

A critical component of the guaranty funds' ability to pay claims of insolvent insurance companies in a timely manner is the distribution of remaining assets of the insolvent estates. Guaranty funds work together with estate liquidators to ensure that guaranty fund loss and expense payments are reported on a timely basis and legal documentation is in place to permit available funds to flow to the guaranty associations on an expedited basis. In 2011 and 2012 the guaranty funds recovered from the insolvent companies' estate assets more than $475 million and $456 million, respectively. To date, in 2013 distributions have been recieved or proposed for distribution to guaranty associations totaling more than $66.5 million.

ESTATES NEARING CLOSURE

Closing efforts continue in several jurisdictions. The liquidator for the two Credit General estates in Ohio (Credit General Insurance Company and Credit General Indemnity) expects to file motions by the end of 2013 to propose a plan for estate closure. The American Mutual insolvencies are also moving toward

closure, with $110 million distributed in 2011. The court approved an additional $50 million in the fall of 2012, which was sent out to the guaranty funds in October. In both cases the receivers needed to settle up on values with the guaranty funds on remaining blocks of open claims, in particular long-term workers' compensation cases. These are cases that the guaranty funds may be servicing for an extended period after the estate closes. We are also seeing indications that one Illinois insolvency, the Coronet Insurance Company, is moving toward closure.

TRANSIT CASUALTY COMPANY - CLOSED

Transit Casualty Company, a Missouri domiciled, was placed into liquidation in December 1985. The receiver for Transit Casualty Company filed a petition with the receivership court seeking approval to make a final distribution from the Transit estate. The guaranty associations and other policyholder-level claimants have received prior distributions of 86 percent of their allowed claims. Following approval of the liquidation court, the receiver made the final distribution to policy-level claimants, bringing the final dividend to 87.3 percent. A hearing on the receiver's petition to close the estate was held on December 20, 2012. The estate is closed; however, certain essential records will be held for a period of five years.

RECIPROCAL OF AMERICA

Reciprocal of America (ROA) was placed into liquidation in June 2003 in Virginia. The company wrote workers' compensation, professional liability, and general commercial liability policies. As of 2012, the estate has made distributions of 95 percent to policyholder-level claimants, with an additional 5 percent to the guaranty associations as early access. In 2012, the receiver announced its intention to sell the estate's entire block of workers' compensation insurance to an outside insurer in an effort to accelerate closure of the estate. It is expected that the proposed Loss Portfolio Transfer will be submitted to the liquidation court for approval in the summer of 2013.

FRONTIER INSURANCE COMPANY

Frontier Insurance Company, a New York domestic, was placed into rehabilitation in October 2001. Following a court ruling that held that certain bond claims were entitled to the same priority as the company's other policy claims, thereby complicating the rehabilitation, the receiver decided to place the company into liquidation in October 2012.

RUN-OFF PROPOSALS

In some cases a state regulator will attempt to resolve a troubled company's claims by means other than a statutory liquidation. In these cases the guaranty funds are not activated. Proponents of alternative approaches cite orderly claims processing, low cost, and greater flexibility to achieve commercially acceptable results. However, the efficiency and cost-effectiveness of a liquidation alternative – compared to a statutory liquidation – to our knowledge has never been established. In fact, there are many questions about how a prolonged run-off, versus a statutory liquidation, would impact the various stakeholders, including policy claimants.

HIGHLANDS

Highlands was placed into receivership in Travis County, Texas, in November 2003. In 2007 the court approved the Second Amended Plan of Rehabilitation. Under the terms of the plan, the receiver was ordered to administer a Monitoring Plan to ensure the estate will continue to have sufficient funds to pay the company's claims as they come due. As of April 22, 2013, the estate held total assets of $194 million against total liabilities of $353 million.

LINCOLN GENERAL

On February 9, 2009, Lincoln General discontinued the writing of new business and began a process that would result in a voluntary, solvent run-off of all business. Year-end 2012 financials indicate a policyholder surplus of approximately $1.8 million after augmentation for permitted practices that increased reserves by a total of almost $9 million. The acquisition of control by Tawa plc ("Tawa") of Lincoln General Insurance Company was approved by the Pennsylvania Insurance Department on October 5, 2011. Tawa is an entity that manages the run-off of non-life insurance companies and portfolios of policies.

Dodd-Frank, Resolution of Systemically Important Financial Institutions, and the 2012 Elections

Enacted in 2010, the Dodd-Frank Wall Street Reform and Consumer Protection Act creates a new system for regulating large, interconnected bank holding companies and nonbank financial companies whose distress or failure could threaten the financial stability of the United States.

The law calls for large, interconnected financial companies that are systemically important to be identified by the Financial Stability Oversight Council (FSOC) chaired by Treasury Secretary Timothy Geithner. Systemically important financial institutions could include insurance companies and insurance holding

companies, although most observers contend that few, if any, insurers are systemically significant. Once identified, these companies will be subject to stringent regulation by the Federal Reserve Board.

The legislation also creates a new mechanism for liquidating systemically important financial institutions whose failure could destabilize the economy. **While the Federal Deposit Insurance Corporation (FDIC) will be appointed receiver of – and will liquidate – most types of financial companies, insolvent insurers (including any deemed systemically important) will remain subject to state receivership and guaranty association processes.**

Resolution of Systemically Important Financial Institutions (SIFIs) will be funded by a post-liquidation resolution fund. If any insurers are tapped to contribute to such a fund, the amount of their contributions will take into account guaranty fund assessments already paid.

Even though insurer insolvencies will be conducted under state law, under certain circumstances the FDIC could be appointed receiver of certain subsidiaries of insurance companies if those companies are in default, are in danger of default, or if their failure would have a significant adverse effect on the U.S. economy. Any value remaining after claims are paid would be paid to the parent company.

THE FUTURE OF DODD-FRANK AND THE 2012 ELECTION

The 2012 elections brought about little changes to the political environment in which Dodd-Frank implementation will continue. The Democrat-controlled Senate is expected to continue to protect Dodd-Frank in its current form and ramp up projects to implement its provisions. The Republican-controlled House is expected to have interest in alternative resolution ideas.

Federal Insurance Office: Anticipating the Report

We continue to anticipate the release of the Federal Insurance Office (FIO) report, which has been delayed from its scheduled January 2012 delivery. The FIO did recently issue its first annual report. This is not the insurance modernization report that was due in January 2012, but rather a factual overview of the U.S. insurance industry. FIO Director Michael McGraith has said that the modernization report is going to finally be released before the end of July. At that point we will do a thorough analysis of the report and the ramifications for the state-based P/C guaranty fund system. To review the FIO annual report, click here.

Both the NCIGF and National Organization of Life and Health Guaranty Associations (NOLHGA) provided input to the FIO as the agency drafted the report. For property and casualty guaranty associations, the comments focused on:

- The operation of state insurance guaranty fund systems, including the loss of guaranty fund coverage if an insurance company is subject to a federal resolution authority; and
- Policyholder protection, including the loss of the priority status of policyholder claims over other unsecured general creditor claims.

To view the joint comments, filed on December 16, 2011 click here.

The Financial Stability Oversight Council (FSOC)

The Financial Stability Oversight Council (FSOC) was established by Dodd-Frank. It is charged with three primary responsibilities:

- To identify risks to the financial stability of the United States that could arise from the material financial distress or failure, or ongoing activities, of large interconnected bank holding companies or nonbank financial companies, or that could arise outside the financial services marketplace.
- To promote market discipline by eliminating expectations on the part of shareholders, creditors, and counterparties of such companies that the U.S. government will shield them from losses in the event of failure.
- To respond to emerging threats to the stability of the U.S. financial system.

Pursuant to Dodd-Frank, the council consists of 10 voting members and five nonvoting members. It brings together the expertise of federal financial regulators, state regulators, and an insurance expert appointed by the President.

Insurance representatives include former Kentucky insurance commissioner Roy Woodall (a voting member), Missouri Insurance Director John Huff, and FIO Director Michael McRaith.

The FSOC voted in June to identify Systemically Important Financial Institutions (SIFIs). We understand that American International Group, GE Capital, and Prudential acknowledged that they were among those designated. They will have 30 days to appeal this decision. One aspect of the additional regulation is the requirement that the company write a “living will” that details the steps they would take if the company ever had to wind down its operations. This analysis will almost certainly include a description of the guaranty fund system.

Insurance Capital and Accounting Standards Act of 2013

In May, Representatives Gary Miller (R-CA) and Carolyn McCarthy (D-NY), both members of the Housing and Insurance Subcommittee, introduced HR 2140, the Insurance Capital and Accounting Standards Act of 2013.

The bill seeks to have state law capital requirements apply to insurance companies that are depository holding companies, or are subsidiaries of such. It seeks to do so by amending Dodd-Frank. Similarly, state-law accounting standards for nonbank financial companies supervised by the Federal Reserve would be applicable.

Of interest is Section 5, which would amend the FDIC Act by limiting the ability of a federal banking regulator to treat an insurance company as a source of strength for an affiliated depository institution (including savings and loans institutions). Under the bill, the insurance company could not be used as a source of strength without the consent of its domestic regulator, and the domestic regulator would have to certify that he or she considered the insurance company's safety and soundness prior to giving the consent.

Medicare Secondary Payer

On January 10, 2013, President Obama signed the Strengthening Medicare and Repaying Taxpayers Act of 2011 (SMART Act). The law will amend provisions of the current Medicare Secondary Payer statute, greatly streamlining the processes attendant to Medicare secondary payer reporting.

The International Scene: Dealing with Insolvency in a World Economy

The IAIS studies "Guarantee Schemes"

The International Association of Insurance Supervisors (IAIS) has undertaken a study of guaranty associations, which they call "guarantee schemes." The Organization for Economic Cooperation and Development (OECD) is also developing a white paper on guarantee schemes in OECD-member countries and selected non-OECD countries. The OECD paper "examines the rationale for a policyholder protection scheme; the relationship between certain design features and moral hazard; the role of a policyholder protection scheme within the overall resolution framework; and some cross-border features of these schemes. While the paper focuses on protection schemes for policyholders, it seeks to draw lessons from compensation schemes in the banking and occupational pension fund sectors, while

recognizing sectoral differences."[1] Both papers feature information on the state-based system in the United States along with a wealth of information on various guaranty schemes throughout the world. Currently neither of the organizations has finalized a work product.

NAIC's Solvency Modernization Initiative (SMI)

SOLVENCY MODERNIZATION INITIATIVE

The financial crisis has brought about increased efforts to globalize regulation and accounting principles. Many changes have already occured in major insurance markets, including those in the U.S. and Europe. These insurance regulatory and accounting changes potentially impact the ability to detect insolvencies.

The NAIC consolidated its regulatory improvement and update efforts under its Solvency Modernization Initiative. According to the NAIC's Web site: "SMI is a critical self-examination to update the United States' insurance solvency regulation framework and includes a review of international developments regarding insurance supervision, banking supervision, and international accounting standards and their potential use in U.S. regulation." SMI has been described as the NAIC looking at all the "tools in its tool box" and deciding what stays, what goes, and what needs to be changed. The current plan calls for all major policy decisions completed by the end of 2012.

There are three topics the NAIC's Solvency Modernization Initiative is studying that could potentially have an impact on the property and casualty guaranty associations.

NAIC'S ORSA: The first is the NAIC's Own Risk Solvency Assessment (ORSA). On September 12, 2012, the NAIC adopted the ORSA Model Act, which will be a regulator resource to assess and monitor insurers' and groups' risk management processes, and to align regulatory requirements with business practices and the insurers' ability to withstand stresses. The NAIC's ORSA is expected to increase the chances that the U.S. insurance regulatory system will be viewed as "equivalent" to Europe's regulatory system under Solvency II. As encouraged by the industry, the ORSA will be less burdensome than Europe's to complete.

The Model Act provides for an effective date of January 1, 2015.

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[1] *"Policyholder protection schemes: Selected considerations" OECD discussion draft, May 2012.*

An annual ORSA report will be required by large insurers (at least $500 million in annual premiums that are part of an insurance group with at least $1 billion in annual premiums). Under certain circumstances, the report could be requested by state regulators, federal agencies, or international insurance supervisors.

The NAIC adopted the ORSA Guidance Manual in March 2011. The manual provides general guidance to an insurer or insurance group for completing the annual ORSA report.

FUTURE OF GAAP AND STATUTORY ACCOUNTING: The second item of interest is the international and U.S. accounting board (IASB and FASB) project that seeks to converge to a single set of global accounting standards. Because Statutory Accounting evaluates GAAP accounting and makes adjustments when called for, Statutory Accounting will be affected by whichever method (U.S. GAAP vs. International Financial Reporting Standards, or IFRS) is adopted by the U.S. Some maintain it may be more difficult to assess solvency if the U.S. moves toward IFRS because it is principles-based, and therefore more subjective than the U.S. rules-based method.

The NAIC will make policy decisions regarding IFRS after the SEC's decision. An SEC convergence decision is pending completion of priority projects: financial instruments, leases, revenue recognition, and insurance contracts. The SEC's final staff report released in 2012 was expected to make a recommendation regarding using IFRS. The report identifed areas and factors relevant as to whether, when, and how the U.S. system is transitioned to IFRS. The report also noted that IFRS is not supported by the vast majority of participants in U.S. capital markets and is not consistent with methods employed by other major capital markets.

INSURANCE CONTRACTS: The third item of interest is the U.S.-based Financial Accounting Standards Board and London-based International Accounting Standards Board's convergence project on insurance contracts. Despite pressures from the G20, convergence on insurance contracts is unlikely. The NAIC cited a statement by FASB Chairman Leslie Seidman: "I'm disappointed to report that after a couple of different attempts, we're simply not reaching converged conclusions on insurance in what I would call fundamental aspects of the proposals." The IASB's initial exposure draft did not distinguish the differences in practices between life and property and casualty insurers, especially with regard to short-term contracts. The IASB issued a revised exposure draft late June 2013 that built on previous consultations from 2007 and 2010. During the same week in June 2013, the FASB issued a proposed updated GAAP standard for insurance contracts. Both the IASB and FASB proposals are open for comment until October 25, 2013. The IFRS Web site's "Snapshot: Insurance Contracts" compares the two proposals, stating "most of the conclusions reached by the IASB and FASB are consistent, although important differences remain in how the IASB and FASB each propose to portray the pattern of profit recognition and in how the entity reflects changes in the estimates of the profit that is earned from insurance contracts.

In the States…

ARIZONA SB 1013 – TRANSFER OF "SPECIAL FUND" TO PROPERTY AND CASUALTY GUARANTY FUND. There is discussion of transferring the operation of the Arizona "Special Fund," which pays workers' compensation claims for Arizona, into the property and casualty guaranty fund. SB 1013 is a first step in this possible transition process. It calls for a report, supported by an actuarial opinion, on the funds available in the Special Fund for payment of workers' compensation claims. We understand this legislation has been enacted. Any additional action in this regard would probably take place in 2014.

STATE WORKERS' COMPENSATION FUNDS. In Oklahoma a bill was enacted this year (SB 1026) to privatize the state-run fund, CompSource, and make it a member of the property and casualty guaranty fund effective in 2015. The bill states that pre-2015 obligations will not be obligations of the guaranty fund. Similar legislation was discussed last year in Colorado with regard to its state fund, Pinnacol. However, no push to implement a change in Colorado is being made in 2013.

Also in Oklahoma, legislation has been enacted to permit employers to opt out of the workers' compensation system either by purchase of alternative insurance or by self-insuring (SB 1062). The legislation charges the Oklahoma Insurance Guaranty Association to administer guaranty funds created for the alternative insurance and for opt-out self-insurers.

FLORIDA SB 324 AND HB 211 FIGA ASSESSMENTS. Legislation was introduced in Florida to call for assessments to be collected from policyholders before remittance to the guaranty fund. The measure is dead for this year.

FLORIDA PEOS AND LARGE DEDUDCTIBLE POLICIES. The Florida Workers' Compensation Insurance Guaranty Association (FWCIGA) conducted a study of Professional Employment Organizations' (PEOs') use of large deductible programs. Problems arise when the programs are undercapitalized and when the insurance company is closely affiliated with a PEO. Recent insolvencies with a large deductible and PEO component include Park Avenue, Pegasus, and Southern Eagle Insurance Company. A working group was formed by FWCIGA to study this matter. The working group deliberations led to the suggestion that legislation be enacted to 1) strengthen collateral requirements, 2) protect collateral, 3) strengthen eligibility requirements for carriers, and 4) strengthen eligibility requirements for insureds using large deductible programs. No legislative action was taken this year.

ILLINOIS HOUSE BILL NO. 981 PUBLIC GUARANTY FUND BOARD MEMBERS. This bill adds one public member to the Illinois Guaranty Fund board. It has passed the legislature and is awaiting the governor's approval.

ILLINOIS SB 1873 TRANSFER OF GROUP WORKERS' COMPENSATION POOLS TO ILLINOIS GUARANTY FUND. Legislation was introduced in 2013 to make group workers' compensation pools in Illinois members

of the Illinois Guaranty Fund. Assets and liabilities of these pools (regardless of time of occurrence) would be transferred to the fund. This bill failed to pass during the 2013 session but will be studied further this summer.

INDIANA GUARANTY FUND ACT (SB 431). A comprehensive proposal was enacted to raise the covered claim cap to $300,000 with unlimited benefits for workers' compensation (the norm in most states). The bill also eliminates an exclusion for "special" damages, which has been the source of much litigation in Indiana.

MASSACHUSETTS SB 480 TO INCREASE COVERED CLAIM CAP TO $600,000. Legislation was introduced in 2013 to increase the covered claim cap in Massachusetts to $600,000. This bill has been introduced in previous sessions and typically does not gain traction.

MISSOURI SB 59 increases the assessment cap to 2 percent from the current 1 percent; excludes workers' compensation coverage from the $300,000 deductible exclusion; and increases the board from seven to nine members. The Governor has signed the bill. The new provisions will go into effect August 28, 2013.

BUSINESS TRANSFERS. *(Vermont – H. 198)* In Vermont, legislation was introduced to "regulate the receipt and management by Vermont companies of closed blocks of non-admitted commercial insurance policies and reinsurance agreements." This legislation would call for closed blocks of business to be transferred to Vermont insurance carriers. The transaction would amount to a novation under Vermont law and all obligations of the transferring entity would be extinguished. While guaranty funds typically do not cover reinsurance and surplus lines products, there may be some confusion on the status of coverage when a non-admitted block of business is transferred to an entity that is a licensed insurer. Further, whether the transaction would amount to a novation outside of Vermont may be questionable. The state of Vermont would garner significant fees once a transaction were approved – a $30,000 administrative fee and 1 percent of the first $100,000,000 of business transferred and .5 percent for additional amounts. The bill was amended to call for transferred blocks of business to be exempt from the requirements of the Vermont guaranty fund act. The bill passed the House and was pending action in Senate. The Vermont legislature adjourned on May 14.

WASHINGTON SB 5675. COMPETITIVE WORKERS' COMPENSATION MARKET. Legislation has been introduced in Washington State to make the state's workers' compensation fund a competitive rather than monopolistic fund. Claims from private carrier insolvencies would flow to the Washington Insurance Guaranty Association. No action has been taken on this measure to date.

WYOMING SB 113 AMENDMENTS TO GUARANTY ASSOCIATION ACT. SB 113 has been enacted. The new law: 1) increases the covered claim cap to $300,000; 2) eliminates the $250 per claim deductible; 3) establishes an independent bar date 25 months after the date of liquidation (or has the guaranty association bar date coincide with the liquidator's bar date, if it occurs sooner); 4) excludes incurred-but-

not-reported (IBNR) claims; and 5) excludes claims for punitive and exemplary damages (unless they are covered by the policy).

DODD-FRANK AMENDMENTS. The NAIC has adopted a guideline to assist states in modifying their insurance liquidation acts to deal with an insolvency of an insurance company that may be part of a Systemically Important Financial Institution (SIFI). Two states have enacted these measures so far: California and Texas. In Illinois a similar measure has passed the legislature.

SWAPS AND DERIVATIVES. We understand that 21 states have adopted swaps language based on Section 711 of the Insurer Receivership Model Act. This continues to be a matter of interest to property and casualty and life and health insurance companies, both which use these devices to some extent. In light of the high interest in the states, the NAIC took another look at the provision, inviting experts on the topic to address the working group. While it appears that Section 711 will remain intact, there is a "guideline" being exposed to address liquidation stay provisions related to these devices. There was more 711 activity in 2013. Kansas (SB 166) enacted a law in the 2013 session. The state of Washington introduced a bill (SB 5065) during the 2013 session.

FEDERAL HOME LOAN BANKS. Recently there has been interest in clarifying the status of federal home loan banks in insurance liquidation. While claims of such entities are generally treated as "secured" in an insolvency, promoters are floating proposals to further strengthen their status by exempting them from the preference and stay provisions embodied in the NAIC model liquidation act (IRMA).

The NAIC has not taken a particular position on these proposals at this time. However, legislation has been introduced in Connecticut (SB 1092) and enacted in Nebraska (L. 337).

To learn more…

More information about the property and casualty guaranty fund system is available on our Web site at **www.ncigf.org.**

Look for a new issue of NCIGF's *Insolvency Trends* in January 2014.

The NCIGF is a nonprofit association incorporated in December 1989 and designed to provide national assistance and support to the property and casualty guaranty funds located in each of the fifty states and the District of Columbia.

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