SIR
SOCIETY OF INSURANCE RECEIVERS
QUARTERLY NEWSLETTER

Vol. III, No. 1 March 1994

THE BOARD OF DIRECTORS
of the
SOCIETY OF INSURANCE RECEIVERS
Invites you to attend a
RECEPTION
at the
DENVER SUITES 5 AND 6
of the
DENVER MARRIOTT CITY CENTER
1701 California Street • Denver, Colorado
on
Monday, March 7, 1994
from
5:00 p.m. to 7:00 p.m.

Hors d'oeuvres Cash Bar

HEREIN

AN OPPORTUNITY

State of New Jersey
Department of Insurance

New Jersey Department of Insurance is seeking applicants for the Position of Director of Rehabilitations and Liquidations. Applicants should have substantial experience with the liquidation division of a state insurance department or with a company in liquidation. Applicants should forward their resumes and salary requirements to:

Gale Simon
Assistant Commissioner
New Jersey Department
of Insurance
20 West State Street
Trenton, New Jersey 08625
(609) 292-2933 - phone
(609) 292-6765 - fax

MEMO FROM THE PRESIDENT

TO ALL MEMBERS

HIGHLIGHTS OF RECENT ACTIVITIES:

A successful Annual Workshop was held in La Jolla, California during January. Attendance topped 225 and all sessions including the Friday afternoon get away session were well attended. The speakers were top drawer and they touched on almost every current topic of interest to domestic insurance receivers.

Your society – **SIR** – held its Annual Meeting on Wednesday, January 26 preceding the Workshop. SIR membership now is over the 300 mark. Our treasury shows a surplus of about $30,000 at the end of year 2 with $25,000 invested in a time deposit. Our primary goal is to run programs for members, not pile up cash and our prime efforts will be in that direction. Results of our elections and appointments to committees appear elsewhere in this Newsletter.

UPCOMING EVENTS

At each of the four quarterly NAIC Meetings, SIR plans:

- Either a Retreat or Roundtable on the Saturday preceding the NAIC Meeting.
- A reception on late Monday afternoon, thus providing members and their friends an opportunity to meet each other.
- To have the SIR display with membership applications and recent Newsletter. Arrange to meet your colleagues at the SIR display.

SIR's 1994 training program will be held in conjunction with guaranty associations and is scheduled for November in San Antonio, Texas, following the NCIGF Workshop.

The SIR Directory will provide not only name, address and telephone data on members but it will feature their professional fields. The Directory Information Form will be in the next issue of the SIR Quarterly Newsletter. We are targeting distribution of the Directory by the NAIC Fall Meeting in Minneapolis, so be sure to return your form promptly.

Several other exciting plans which are underway will be announced as they develop.

Remember, this is your Society and suggestions are seriously solicited on any action that can be taken to make this Society more valuable to you.

Sincerely,
Michael Miron,
President

IMPORTANT – NAIC EX5 CHARGE

INSOLVENCY (EX5) SUBCOMMITTEE

The duties of this subcommittee shall be administrative and substantive as they relate to issues concerning insurer insolvencies and insolvency guarantees. Such duties include, without limitation, monitoring the effectiveness and performance of state administration of receiverships and the state guaranty fund system; coordinating cooperation and communication among regulators, receivers, and guaranty funds; monitoring ongoing receiverships and reporting on such receiverships to members of the NAIC, developing and providing educational and training programs in the area of insurer insolvencies and insolvency guarantees to regulators, professionals and consumers; developing and monitoring revelant model laws, guidelines, and products, and providing resources for regulators and professionals to promote efficient operations or receiverships and guaranty funds.

1. Continue development, testing and implementation of Uniform Data Standards for both property/casulty and life/health insolvencies to facilitate exchange and use of information concerning receivership administration between receivers and guaranty funds.
2. Continue review of the Insurers Rehabilitation and Liquidation Model Act and develop appropriate amendments or revisions.
3. Produce annual supplement to the *Receivers Handbook for Insurance Company Insolvencies*.
4. Proceed with the development of a national database of vital information concerning receiveships, with data submitted from receivers and guaranty funds, and submit a fiscal impact statement to the Internal Administration (EX1) Subcommittee on the same. Such a database should include not only the information in the current Contact Person Report, but also financial information (e.g., marshaling of assets and deposits, claims and costs) and status of major pending matters.
5. Develop minimum standards for the administration of receiverships, to encompass, but not be limited to statutory elements, procedures, organization and structure, and interstate relations and cooperation. Address the issue of whether the standards should be mandatory, and if mandatory, how the standards should be implemented, i.e., the existing Financial Regulation Standards and Accreditation Program, a separate program, or one or more interstate compacts. Make recommendations by the fall National Meeting.
6. Review the Post-Assessment Property and Liability Insurance Guaranty Association Model Act, consider amendments and adopt appropriate amendments.
7. Consider amendments to the Life and Health Insurance Guaranty Association Model Act recommended by the (EX) Special Comittee on Blue Cross Plans which would extend guaranty association coverage to non-profit hospital and medical service organizations and health maintenance organizations.
8. Monitor guaranty fund assessments in relation to system capacity.
9. Complete the review of the structure and performance of the system for guaranty funds and receiverships and recommend amendments to the relevant model acts or other measures to improve the system's efficiency and the protection for policyholders, claimants and beneficiaries. Make recommendations by the fall National Meeting.
10. Recommend provisions of the guaranty association model acts to be added to the Financial Regulation Standards or other measurers to accomplish greater uniformity, consistency and coordination in guaranty fund coverage among states and ensure that an adequate minimum level of coverage is provided for all insurance policyholders, claimants and beneficiaries. Make recommendations by the fall National Meeting.
11. Evaluate issues arising with respect to the reporting of premium data utilized allocating guaranty fund assessments among insurers and recommend guidelines to the various states in resolving such issues and an overall framework for assessment data collection and distribution.
12. Monitor and discuss issues arising with respect to receiverships of "nationally significant" multi-state insurers and guaranty fund activities involved with these receiverships.

FINANCIAL REGULATION STANDARDS AND ACCREDITATION (EX6) SUBCOMMITTEE

The duties of this subcommittee shall be both administrative and substantive as they relate to administration and enforcement of the NAIC Accreditation Program, including without limitation, consideration of standards and revisions of standards for accreditation, interpretation of standards, evaluation and intepretation of states' laws and regulations, and departments' practices, procedures and organizations as they relate to compliance with standards, examination of members for compliance with standards, development and oversight of procedures for examination of members for compliance with standards, qualification and selection of individuals to perform the examination of members for compliance with standards, and decisions redgarding whether to accredit members.

1. Maintain and stregthen the NAIC financial regulation standards and the NAIC accreditation program.

(continued on page 8)

A GAME OF DOMINOES?

By Paul Evans

There can be few insurance companies of Lloyd's syndicates that do not have settled or future claims under their own reinsurance programmes against several of the ever-increasing list of Insolvent London Market companies. When taken with the number of other companies that have ceased underwriting but are continuing to pay, there is a significant level of actual or potential reinsurer default and increasing concern over the possible "domino effect" in the market, whereby the failure of one company hastens or even causes the failure of another. How real is this issue, how important is it in understanding the reasons for the level of failures and are there more to come?

The problems that beset the Lloyd's market have been well publicised, but many of the factors that have contributed to those problems, especially in the claims area, have also contributed to similar substantial pressures in the company market. Of course the burden in Lloyds falls on the investors, who are experiencing erosion of their personal capital, and policyholders are protected by the Central Fund. In the company market, directors and management have to concerned with the company's capital surplus and when that is eroded, the policyholders suffer, subject to protection under the Policyholders Protection Act.

The causes of the pain are all too well known: the massive environmental pollution and industrial disease claims from the United States; the rising level of Court awards for professional indemnity claims; the unprecedented number of catastrophes in the late 1980's and early 1990's. Behind all of this, in addition, is the residual philosophy that the insurance industry remains a deep pocket, although the stitches seem to be coming apart at the edges.

Recognizing with hindsight the inadequacy of reserving, which in the end has led to most if not all of the failures, is another way of exposing continued underpricing of the product. While the ebb and flow of underwriting cycles have their effect, management decisions to underwrite for cashflow and rely on investment income to cover underwriting losses may come back to haunt as interest rates fall. Perhaps some sympathy should be extended to managements who wrote general liability policies for modest premiums twenty or thirty years ago, when words such as "superfund" and "pollution exclusion" were not remotely in anyone's contemplation. Insurance archaeology specialists are seeking out old policy wordings in the hope of attaching huge liability claims to them many years after the policies were written. Is it any wonder what the historic levels of premium on such occurrence based policies quite often bear no relation to the sort of risk that, with hindsight, the insurance companies were taking? However, in contrast, managements that "give the pen away" to underwriting agencies are often inviting trouble.

Many of these primary causes of failure involve some form of company mismanagement — this should be no surprise. Management should be the first line of defense in the prevention of failure in any company in any business, including the insurance industry. Regrettably the incidence of fraudulent activities by managment is sometimes a further factor.

So, perhaps the "domino effect" is only one cause among many, and in reality the greatest threat is still the past catching up. As rates harden and give some cause for optimism as regards future underwriting results, what hope is there that there are no more dominoes to fall over?

For brokers' security committees, this is a continuing question and many of them, in the past few years, will have answered it by reducing the amount of business placed with smaller companies or withdrawing support completely. This flight to capital is leaving many companies vulnerable and having to contemplate enforced run- off. Investment returns will continue to fall as the general level of interest rates comes down and the need for underwriting profits will come more into focus. The reduction in reinsurance capacity will lead to companies making higher net retentions and can anyone see a willingness to seek to cap or otherwise limit the scope of the Superfund legislation in the United States? Will professional indemnity claims continue rising until a major accounting or legal practice is forced out of business? What is the next liability problem and is Europe facing a surge in pollution claims in the American style? What will be the effect of the new Insurance Premium Tax and will the Policyholders Protection Board levy (probably at the maximum rate of 1% for next year) simply pile on the agony?

There are no simple answers to these questions but together they suggest that the past is far from dealt with. Furthermore, one effect of the reinsurance and retrocession markets is to spread the problems and who knows how many European dominoes there are?

The number of London Market failures since 1990 has at least prompted the corporate recovery specialists to recognize the drawbacks of the liquidation process. The history of previous cases has led to the estate being looked up for many years, with the consequent removal of liquidity from the market. The abundance of Schemes of Arrangement in the insurance and other industries just goes to show that little-used pieces of legislation should not be excised

(continued on page 7)

THE ROLE OF INSURANCE GUARANTY ASSOCIATIONS

By: John F. Del Campo, JD Counsel
National Organization of Life and Health Insurance Guaranty Associations

Introduction

The legal process associated with the rehabilitation or liquidation of life insurance companies is not like the process associated with the reorganization or liquidation of business enterprises under the federal bankruptcy code. Whether or not insurance regulators and receivers are intimately acquainted with the provisions of the bankruptcy code, instinctively they know that the "business of insurance" — whether it is property-casualty or life business — is different from other businesses, and is treated differently by the states in the rehabilitation or liquidation process. But what some insurance regulators, and even receivers, sometimes are not sensitive to is that, because life company operations are different from property-casualty company operations, life company rehabilitation or liquidation processes must also be different from comparable property-casualty company processes.

The life insurance, health insurance, and annuity obligations of life companies are *continuing* obligations — obligations as to which the mere payment of claims by an estate does not provide satisfactory protection against the risk of insolvency. Risks assumed by life insurance companies, i.e., mortality and morbidity, are dependent upon the insurability of a human life and the insurance obligation may extend for the life of the individual. This differs from property-casualty insurance in which risks are based on other factors which permit cancellation and replacement of insurance coverage more readily. And this feature critically affects the relationship between the life company rehabilitator or liquidator, and the life and health insurance guaranty associations.

This article addresses some of the key differences in life company rehabilitations and liquidations from the point of view of life and health insurance guaranty associations, and seeks to promote cooperation.

The Purposes and Functions of NOLHGA and Life Company Guaranty Associations

NOLHGA is the not-for-profit association whose members are the life and health insurance guaranty associations of the 50 states, the District of Columbia, and Puerto Rico. Except for the Arizona Life and Disability Insurance Guaranty Fund, which is a subdivision of the Arizona Department of Insurance, life and health insurance guaranty associations are not-for-profit, unincorporated associations chartered by state law to protect life insurance policyholders, health insurance policyholders, annuity contract holders, and certain other persons against the failure of their insurance company. Most state laws conform to the National Association of Insurance Commissioners (NAIC) Life and Health Insurance Guaranty Association Model Act of 1987 (the "Model Act"), or one of its antecedents.[1]

The scope of protection provided by life and health insurance guaranty associations is limited, and there is variation between the states as to the types of insurance obligations covered, and the dollar amounts of those coverages. Given the autonomy of state life and health insurance guaranty associations, and the variation in state insurer insolvency and guaranty association laws, **NOLHGA** endeavors to act as the coordinator, and clearinghouse through which joint solutions to multi-state insurer insolvencies can be arranged. Backed by the financial strength of the industry, **NOLHGA**, and its member life and health insurance guaranty associations, are positioned to respond to multi-state insolvencies.

Of course, life company regulators, and receivers are also charged by law with protecting the interests of life and health insurance policyholders, beneficiaries, annuitants, and the like. And in the case of receivers, that charge extends to marshaling the assets of the estate for the benefit of policyholders, and other creditors. But marshalled assets, if they are used only to pay liquidated claims or cash surrender values, do not provide life policyholders, health policyholders and annuitants with continuing insurance or annuity coverage. Life and health insurance guaranty associations, by contrast, have no charge other than protecting policyholders by continuing their coverage. The protections they provide are tailored to fit the special characteristics of the "covered obligations" which they must "guaranty, assume or reinsure".

Distinguishing Characteristics

All insurance companies chartered by or admitted into a state, which write the lines of business covered by the guaranty association, are defined as members subject to life and health insurance guaranty association assessments. Assessments are used by all guaranty associations to pay covered claims, and administrative expenses incurred because of the failure of a member insurer. In this, the organization of life and health insurance guaranty associations resembles

(continued on page 9)

1. Insurance regulators, and receivers sometimes see life and health insurance guaranty associations as extensions of the industry. However, the official commentary to the Model Act states that the basic purpose of life and health insurance guaranty associations is "to protect policyowners, insureds, beneficiaries, annuitants, payees and assignees against losses (both in terms of paying claims and continuing coverage) which might otherwise occur due to an impairment or insolvency of an insurer."

REALITY IN REAL ESTATE

. . . A Continuing Series
by Randy Harper

At the recent (January 27-28, 1994) Insolvency Workshop co- sponsored in San Diego by the National Association of Insurance Commissioners and the Society of Insurance Receivers, I had the pleasure to discuss with several members the prospects of the insurance industry, interaction between insurance commissioners and insurance companies regarding management and sale of real estate assets, and the approach of insurance commissioners, or their designated representatives, as receivers to the liquidation of real estate assets, to include loan portfolios, both performing and non- performing.

The insurance industry is undertaking a journey familiar to those of us who have been involved in the workout arena for many years. It would appear there is considerable synergy, and complimentary interests, which are worth exploring in more detail. The recent article by James A. Guillot in the December, 1993 SIR quarterly newsletter addressed "... the need to marshal the assets of the insolvent estate. A careful review of all transactions made by the insolvent company before regulatory action must be made by the receiver." In that same edition of the newsletter, Steven L. Del Sesto addressed "... how to best manage the investment assets of an institution as competing interests lay claim to the asset pie during the liquidation process." Mr. Del Sesto continues on to appropriately describe several techniques relative to maximizing the present value of a recovery specific to a securities portfolio.

The purpose of this continuing series of articles is in the same spirit as Messrs. Guillot and Del Sesto, to provide insurance receivers a practical set of guidelines to follow when the assets, or indeed liabilities, of an insolvent insurance company include real estate and its related entities, some familiar, some not so familiar and some the reluctant "beneficiary" of fraud, bad decision making or their dyslexic combination.

During the early eighties, a significant amount of real estate investment was dictated by the leverage available and the purported tax ramifications offered. The underlying economics of the real estate were often secondary to tax benefits and loan fees. Too much reliance was placed on appraisals that were historical rather than anticipatory; feasibility studies were often used for advocacy more than as an instrument of actual analysis. As overbuilding and new tax law ramifications began to have an effect on both institutional and private real estate portfolios, a sound analysis of the underlying real estate still remained secondary, as various accounting techniques were often utilized to deflect the impact of market reality. These techniques whereby borrowers and lenders could minimize the risk of loss to themselves, combined with a surplus of capital, led to careless underwriting.

Real estate appraisal is an art, and the foundation of valuation is a balance of judgment and practical application of real estate skill. While acknowledging historical data, the approach to estimating value should also be anticipatory in nature, and consider the effects of both speculative investment and supply and demand. For example, reliance on projected income for an apartment complex should be based on effective rents. A good undeveloped land valuation should include a review of local real estate markets relative to highest and best use, and a residual analysis if appropriate.

Discretion and professional judgment should be carefully applied. The cushions that often guaranteed good results for well located property have been usurped by market conditions in many cases. Financing, timing and highest and best use are as equally important as the location merits of a real estate asset.

Solving real estate problems is not easy, partly because absolute answers are seldom found. Success is often determined by the ability to properly define problems and address certain regulatory requirements, albeit that a regulation, by itself, will not insure quality. The best receivers pursue answers to often difficult questions and identify project characteristics that lead to an adequate return.

A receiver is tasked with the responsibility to ensure the due diligence necessary to arrive at an effective and realistic asset management and disposition strategy. Without a correct understanding of the real estate, the effort to maximize recovery will usually be cost ineffective.

How are most valuations communicated? Primarily by an appraisal. But as is well known, appraisals of real property can vary markedly when conducted by different appraisers or under differing assumptions. Given a number of real estate assets under the valuation process, and the time pressures placed upon special deputy receivers, there can be more emphasis placed on "filling out an appraisal review checklist" instead of a review to determine if the value estimate is reasonable. The bottom line for the majority of real estate appraisals should be "If it were my money, or my company's money, that was being invested in this property, would I pay this much; and if so, could I support my purchase price?" Reviews should be made with the intent of verifying the value estimate; they should not be a forum for minutiae. Obviously, if an appraisal is not a professional rendering, or the reviewer is not comfortable with the value estimate, corrective action is necessary, in line with the minimum review standards of the Appraisal Foundation.

Understanding the value of the collateral is essential to the recovery task. That understanding, however, should not become secondary to strictly meeting regulatory requirements. All parties concerned, both in the public and private sector, should be conscious of the

(continued on page 7)

Dominoes?

(continued from page 4)

from the Statute Book — you never know when they might be needed. (I doubt whether the industry feels the same about the Policyholders Protection Act!)

There is a growing acceptance of such Schemes for insurance companies, typically enabling each company to run off the remaining business in an orderly way without some of the costs and inflexibilities of liquidation, and giving real opportunities to pay creditors some money earlier.

The mechanism is not perfect, of course, and it takes quite a time to prepare a Scheme and get it approved by the creditors and the Court. The Department of Trade and Industry has recently issued a Consultative Document on Company Voluntary Arrangements ("CVA") and Administration Orders, which considers some possible changes to the current law, so as to encourage greater use of these rehabilitation procedures. At present, it is not believed possible to bind unknown creditors into a CVA and accordingly the procedure is unworkable for insolvent insurance companies, who without exception, cannot identify all their policyholders.

If CVA's were to bind unknown creditors and permit a stay against creditors whilst proposals were formulated (even if that stay had to be extended by a Creditors' Committee), then the process could be used for insurance companies and appropriate proposals for an orderly run-off could be presented to creditors more quickly, and at even less cost.

So, the signs are that the game of dominoes is not over yet, and, as a new underwriting year commences, many people are, like a latter day Janus, looking forward to future prospects, and back at the past which still threatens.

Reality

(continued from page 6)

fact that while certain basic requirements must be met, the estimate of value should remain the priority. A well written, professionally prepared and accurate real estate appraisal is not the only ingredient to successful resolution of our problems, but to paraphrase Will Rogers, "...trying to manage something you don't understand is like trying to come back from a place you haven't been." Or as Yogi Berra so eloquently stated, "If you don't know where you're going, you will wind up somewhere else."

The objectives of the evaluation process should be twofold:

1) to determine liquidated and going concern values as appropriate, based on economic models using assumptions commonly applied by buyers in today's market environment; and,
2) to compare the cost to the Institution or Guarantee Fund to liquidate the asset versus the potential gain, as offset by any yield maintenance requirement during the projected hold period.

Liquidated Value – is determined by the net proceeds expected from the sale of an asset within usually three to six months of the evaluation date. This method assumes that the receiver will liquidate the interest in the underlying collateral at current market value. Additionally, improvement and completion expense, costs of sale, holding period exposure, litigation and other costs, as applicable, should be deducted from gross sale proceeds in arriving at a liquidated value.

Market value is defined as the most probable price in cash for which the property will sell in a competitive market under all conditions requisite to fair sale, with the buyer and seller each acting prudently and assuming that neither is under undue duress. This definition expresses value as a result that should prevail if buyers and sellers are under no undue influences, motivations, or conditions atypical of the market as addressed in traditional appraisal theory. Another accepted definition, however, is that market value is the most probable selling price and that no idealized market conditions are required. If a seller must sell under duress, and even if financing is not available at typical market terms, the price that is expected to occur is the market value. Foreclosure has often been a prevalent occurrence compared to arms length transactions in several markets.

"Going Concern" Value – is defined as the net proceeds expected from the orderly disposition of the asset in the ordinary course of business. This approach assumes that where required, a workout program will be implemented for an appropriate time period to maximize the present value of the recovery.

Elementary to value as a going concern is finding a solution for a troubled asset satisfactory to all the parties concerned. Proper management of the recovery process is important, given local economic conditions beyond the control of the receiver, the capital improvements often necessary, and the ongoing business risk of an improved property. The process requires a multitude of disciplines, to identify and understand how particular assets became a problem, to evaluate the risks attributed to maintain value, and proper management of the individual assets and the overall portfolio. In some cases the best workout strategy may be prompt and timely disposition. Strategies are not standardized, as they depend upon present and projected market conditions, the physical condition of the asset, and the property's competitive position. It is equally important to recognize both diminishment of losses, and where appropriate, realizable gains, as there is real equity when the long term benefits of underlying collateral could have been

(continued on page 8)

SIR UPDATE

At the annual membership meeting in La Jolla, California two new directors Deanna Delmar and Douglas A. Hartz replaced retiring directors Nelson Burnette and Joyce Wainscott. The directors then elected a new set of officers. The Society owes a debt of gratitude for those officers and directors who returned to the ranks of membership; an active one, I am sure.

The following committees were formed:

Executive: Michael Miron(CH), Jeanne B. Bryant, Robert A. Deck, John A. Massengale and Thomas G. Wrigley.

By-Laws: Vincent B. Vaccarello(CH), Francesca G. Bliss, Robert L. Green, Douglas A. Hartz, Kathleen Neiweem and Joyce Wainscott.

Nominations, Elections & Meeting:
Vincent B. Vaccarello(CH), George Piccoli and Karen Weldin Stewart.

Finance: John Massengale(CH), Richard Darling, Douglas A. Hartz and Stephen Phillips.

Accreditation and Ethics: Ronald Rosen(CH) and Thomas G. Wrigley

Memberships: Robert A. Deck(CH)
Membership Recruiting: Paul Walther(CH)
Domestic Applications: Jacqueline Reese(CH) and Roger H. Hahn
International Applications: Philip J. Singer(CH)

Education: Joyce Wainscott(CH)
SIR/NAIC Workshop: Thomas G. Wrigley(CH)
Training: Kristine J. Bean(CH)

Publications: Deanna Delmar(CH)
SIR Quarterly Newsletter: Morton Mann, Editor
Michael Cass, Associate Editor
Membership Directory: Lawrence J. Warfield(CH) and Morton Mann
Membership Benefits: Frank L. MacArtor(CH)

An active member is a rewarding member. If you have an interest in participating in any committee, please contact the editor or the president or the chairperson of the committee. Articles for publication are always in order.

Reality

(continued from page 7)

overlooked in determination of current market value.

Understanding the value of the underlying collateral is only the first step in the process. A good grasp of fundamentals will enable the receiver to properly address the portfolio be it loans of varying complexity, identifying when a workout is feasible or foreclosure preferable, understanding the considerations of any participants, identifying the risks and a host of other considerations. For example, what is the strength of in-house real estate personnel, if any? Do they have the flexibility and willingness to accept nontraditional solutions? What about the quality of the assets, or the borrower? What is the opinion of counsel? Workout strategies can entail modification of interest payments, deferred or reduction of interest, loan extension, supplemental financing, equity participation, liquidation of a portion of a project, or after analyzing holding costs and risks, liquidation of the entire property.

Future articles will address valuation issues applicable to multifamily, commercial (office and retail), industrial, lodging and undeveloped land properties, as well as subdivisions and resorts. Additionally, we'll examine what to look for in the evaluation of loan portfolios, both single family residential and commercial. Hopefully, the discussions will afford you, the receiver, a better understanding of real estate and loans, to enable you to know what expertise will be required to effect a timely resolution. We will also address several of these topics from a buyer's perspective, for a more complete picture. With this knowledge in hand, you should be better equipped to deal with an often misunderstood group of assets, and have more time to focus on the needs of regulators and policyholders, who will be the ultimate beneficiaries of this expertise.

NAIC EX5 CHARGE

(Continued from page 3)

2. Assist states, accredited and unaccredited as requested and as appropriate in implementing laws, practices and procedures and personnel required for compliance with the standards.
3. Conduct a yearly review of accredited states.
4. Consider new model laws and amendments to existing model laws required for accreditation and to deteminine appropriateness of addition of such new model laws and such amendments to the NAIC financial regulation standards.
5. Render advisory opinions and interpretations of model laws required for accreditation and substantial similarity of corresponding state laws.
6. Develop policies and procedures for 5-year follow-up reviews.

SSO Staff Support: Ed Dinkel/Mark Noller /Susan Martin/Patrick Watts

Insurance Guaranty Associations

(continued from page 5)

their property-casualty counterparts.

Unlike their property-casualty counterparts, whose principal responsibility is to pay covered claims, life and health insurance guaranty associations seek to continue the long-term life insurance, health insurance, and annuity obligations of a failed insurer; generally by reinsuring those obligations to a financially sound reinsurer. This is an important, and distinguishing characteristic of life and health insurance guaranty associations - specifically recognized in the official commentary to the Model Act.[2]

The Model Act provides that life and health insurance guaranty associations shall provide coverage of policyholder obligations of up to $100,000 in health insurance benefits, $100,000 in cash values on life insurance, $100,000 in present value of annuities, and up to $300,000 in life policy death benefits. Simple on its face, the application of life and health insurance guaranty association coverage limits to covered insurance obligations connected to any particular insolvency can be surprisingly complex.

Since their primary responsibility is to provide continuing coverage to policyholders, as opposed to the payment of covered claims, life and health insurance guaranty associations typically seek to reinsure policyholder obligations to an assumption reinsurer. Because they receive continuing coverage, policyholders are not forced to accept termination of their insurance, or the surrender values that would be payable upon termination. But what is the measure of the continuing coverage to which a policyholder is lawfully entitled? Should continuing coverage be limited so as not to exceed a $300,000 face amount, or a $100,000 cash value, or both? Neither the official commentary, nor the Model Act, is instructive on this point.

Life and health insurance guaranty associations have responded to the problem, and fashioned answers that focus on the reserves needed to support a given policyholder obligation. In a simple liquidation scenario, each life and health insurance guaranty association will agree to fund the assets necessary to support the statutory reserves for covered policy obligations, limited by the amounts corresponding to the respective cash surrender values of the policies to be reinsured. This treatment is sensible when one recalls that "cash surrender value", limited to $100,000, is the amount a policyholder would be entitled to receive from the guaranty association had the policy been terminated upon liquidation of the company.[3] And by supporting reserve transfers of up to $100,000, guaranty associations can generally provide continuing ordinary whole life insurance coverage with face amounts far in excess of $300,000, the limit pertaining to death benefits under the Model Act.

Cooperation with Regulators and Receivers

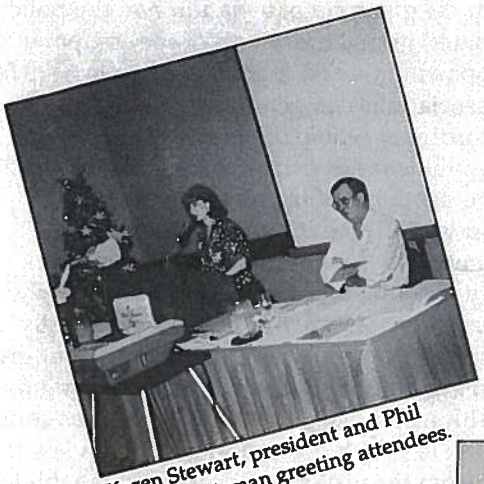
Life and health insurance guaranty associations work closely with the regulators and receivers who must conserve, rehabilitate or liquidate financially impaired or insolvent insurance companies. But given their specialized role, it should not be surprising that life and health insurance guaranty associations come to each insolvency with goals, and points of view that often differ from those of the conservator, rehabilitator or liquidator.

Historically, most insurer insolvencies in this country have involved property-casualty companies. As a result, the insolvency divisions of many departments of insurance have been staffed by personnel whose regulatory experience is property-casualty oriented. And for the same reason, there are generally more contract receivers with experience in property-casualty insurer rehabilitations and liquidations than life company rehabilitations and liquidations — although that situation may be changing due to the increased number of life companies that have become insolvent over the past several years.

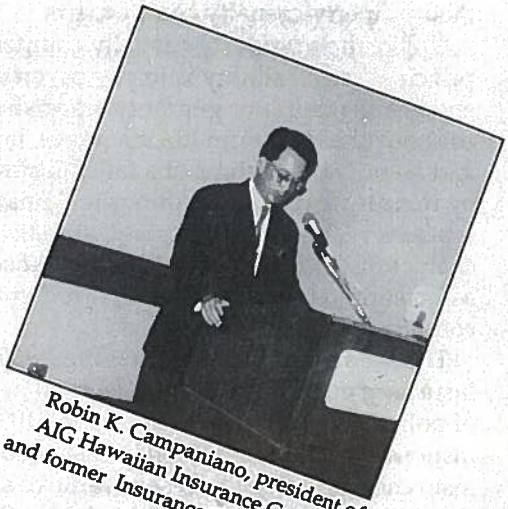
The point is that, because some regulators, and receivers may not be attuned to the very different characteristics of a life company rehabilitation or liquidation — and the different role that life and health insurance guaranty associations have to play in such proceedings — they may be predisposed to solutions that are not ideally suited to the continuation of policyholder obligations. Regulators, receivers, and guaranty associations must all work together with mutual respect, and concern for the different characteristics of life company impairments, and insolvencies so that policyholders do not suffer unnecessarily.

2. "Unlike the property and liability situations, life and annuity contracts in particular are long term arrangements for security. An insured may have impaired health or be at an advanced age so as to be unable to obtain new and similar coverage from other insurers. *The payment of cash values alone does not adequately meet such needs. Thus it is essential that coverage be continued.*" NAIC Model Act of 1987 (emphasis added).
3. In appropriate circumstances, life and health insurance guaranty associations have developed an alternative solution, which is to fund the assets necessary to support the present value of covered death benefits. However, the actuarial assumptions and legal rationale underlying either of these treatments — or the treatment of sophisticated interest sensitive products — are beyond the scope of this article.

SIR FIRST WORLD CONFERENCE — HAWAII

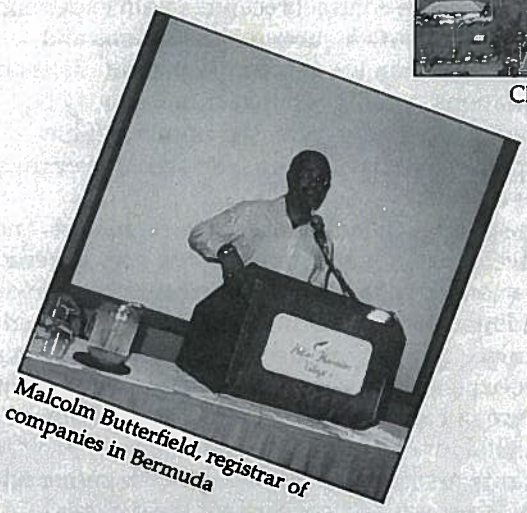


Karen Stewart, president and Phil Singer, chairman greeting attendees.



Robin K. Campaniano, president of AIG Hawaiian Insurance Company and former Insurance Commissioner.

Christmas in Hawaii



Malcolm Butterfield, registrar of companies in Bermuda

New member Allen Breisblatt and John Massengale at SIR cocktail party.

SIR Annual Membership Meeting in La Jolla, California

Current officers and immediate past president.

New board members Deanna Delmar and Doug Hartz.

WELCOME TO NEW MEMBERS

Christopher Barrett
Senate Management Services Ltd. – London

Allen Breisblatt
Insurance & Reinsurance Associates

Roy Burrows
Clifford Change – London

Leah Campbell
Donovan, Leisure, Newton & Irvine

James Corcoran
Donovan, Leisure, Newton & Irvine

David Cralle
Premier Asset Services

Martha Davis
Tennessee Receiver's Office

Dirk deRoos
Fargre & Benson

Anthony Grippa
William Mercer, Inc.

James Johnson
Leboeuf, Lamb, Leiby & Macrae

Anthony McMahon
KPMG Peat Marwick – London

William Mills
Alabama Department of Insurance

Carl Modecki
National Association of Insurance Brokers

George Piccoli
INS Consultants, Inc.

Martin Rosenberg
Consulting Actuary

Maryellen Sebold
Neilson, Elggren, Durkin & Co.

Margaret Spencer
Arthur Andersen & Co.

David Steinberg
Clifford Chance – London

David Sullivan
Clifford Chance – London

Rosemary Sutherland
Clifford Chance – London

Jack Webb
Jack Webb & Associates, Inc.

Justin Westhead
Reynolds, Porter, Chamberlain – London

Jonathan Wood
Clyde & Company – Surrey

MARK YOUR CALENDAR

March 5, 1994

SIR Roundtable
Location to be announced
Denver, Colorado
12:30 to 2:30 Life Receiverships (Principals Only)
2:45 to 5:30 General (Principals and Associates)

March 6, 1994

SIR Board of Directors
Marriott – Penrose Room
1 pm to 3 pm

March 7, 1994

SIR Cocktail Reception
Marriott – Denver Room
Suites 5 and 6
5 pm to 7 pm

March 6-8, 1994

NAIC Spring Zone Meeting
Denver Marriott City Center
Denver, Colorado

March 6, 1994

Insolvency (EX5) Subcommittee
Model Act Issues Working Group
8 am to Noon
Colorado 6, Lower Level 2
(Regulators Only)

NAIC Executive (Ex) Committee followed by Plenary
1 pm to 3 pm
Colorado E/F, Lower Level 2
(Regulators Only)

(EX) Special Committee on Antifraud
1 pm to 2 pm
2 pm to 3 pm (Regulators Only)
Colorado G, Lower Level 2

Insolvency (EX5) Subcommittee
Uniform Data Standard Working Group
3 pm to 4 pm
Colorado C/D Lower Level 2

Renissance (E) Task Force
Model Law on Credit for Renissance Working Group
3 pm to 4 pm
Colorado A/B Lower Level 2

Insolvency (EX5) Subcommittee
Receiver Handbook Working Group
4 pm to 5 pm
Colorado C/D, Lower Level 2

March 7, 1994

Insolvency (EX5) Subcommittee
Assessment Data Working Group
8 am to 10 am
Matchless, Lower Level 1

Update on Mutual Fire, Marine and Inland Insurance Company
8 am to 9 am
Penrose, 3rd Floor

Insolvency (EX5) Subcommittee
Coverage and Uniformity Working Group
10 am to Noon
Matchless, Lower Level 1

(EX) Special Committee on Interstate Compact
11 am to Noon
Colorado B/C/D, Lower Level 2

Insolvency (EX5) Subcommittee
Minimum Standard Working Group
1 pm to 3 pm
Matchless, Lower Level 1

(EX) Special Committee on Antifraud
Antifraud Working Group
3 pm to 4 pm
Matchless, Lower Level 1

Insolvency (EX5) Subcommittee
Kentucky Central Life Working Group
4 pm to 6 pm
Matchless, Lower Level 1
(Regulators Only)

March 8, 1994

Special Insurance Issues (E) Committee
11 am to 12:30 pm
Colorado B/C/D, Lower Level 2

Insolvency (EX5) Subcommittee
12:30 pm to 2 pm
Colorado F, Lower Level 2

June 11, 1994

SIR Board of Directors
Baltimore, Maryland

June 12-15, 1994

NAIC Summer Meeting
Stouffer Harborplace Hotel
Baltimore, Maryland

November, 1994

SIR Training Program
San Antonio, Texas

SOCIETY OF INSURANCE RECEIVERS

Volume III, No. 1 March 1994

Morton L. Mann
Newsletter Editor

AUTHOR BIOGRAPHY

John F. Del Campo is counsel to the National Organization of Life and Health Insurance Guaranty Associations. He previously served as in-house counsel to Transamerica Financial Group, its Arcadia National Life and Arcadia General Insurance Companies, and to Chicago-based North American Company for Life and Health Insurance. He is a graduate of Brown University and of the John Marshall Law School.

Paul Evans is with Price Waterhouse in its London Corporate Recovery practice. He has been working full time in the insurance sector since 1990 and is currently involved in the restructuring of a number of insurance companies in the London market, including Trinity, Bryanston, Monument and Andrew Weir. He is also handling the administrations of London United Investment plc, the holding company of H.S. Weavers, and of English & American Group plc. He is a licensed insolvency practitioner and a member of the U.S. Society of Insurance Receivers.

Randy Harper is a graduate of the U.S. Naval Academy, Masters from the University of Southern California, Senior Vice President with Real Estate Recovery, Inc. and President of its affiliate, RER Appraisal Company. A member of SIR, he also holds the MAI designation from the Appraisal Institute.

Michael Miron, President
Society of Insurance Receivers
801 West 20th Street
Wilmington, DE 19802
Telephone and Fax: 302 • 654 • 8387

First Class

Morton L. Mann, Editor
SIR Quarterly Newsletter