Opinion **US**

# Tackle false rumours about insurance companies

Eric Dinallo JULY 31 2008

Rumours that can destroy the stock price of banks and investment banks have been the focus of the media and have now attracted the attention of regulators. But what about rumours that cast doubt on the solvency of insurance companies that are equally important to the New York economy and global capital markets? All financial services companies – banks, investment banks and insurance companies – rely on market confidence. Just as a depository institution's continued existence depends on the confidence of depositors, so an insurance company's existence depends on the confidence of policyholders.

This is why New York State enacted a law in the 1930's providing for civil and criminal sanctions for spreading false rumours or making statements "untrue in fact" about an insurance company's solvency.

This law recognises that insurance companies can be destroyed by false claims that they are insolvent – that is, unable to pay their claims. Because insurers provide long-term promises of protection, falsely attacking an insurance company undermines all those promises and the economic activities that depend on them. Thus, these attacks can produce systemic harm that may extend beyond the policyholders of that company to the economy as a whole.

A prime example of the potential for widespread damage is the current case of the bond insurers, which are experiencing problems because of the subprime crisis. These companies guarantee that issuers will pay principal and interest on bonds, including municipal bonds, which are widely held by households and institutions. If the issuer of a bond cannot pay, the bond insurer steps in and pays the holder.

Recently, some individuals have asserted that some of the bond insurers are insolvent – a far more serious, far reaching and risky allegation than claims that the insurer's holding company stock is overvalued. Publicly questioning the solvency of these companies is of a completely different order. If the bond insurers, also known as financial guaranty companies, cannot pay claims, major US commercial and investment banks will likely suffer additional writedowns, the current credit crisis may get worse, and the current economic downturn could become deeper. Also, the cost of borrowing for some state and local governments may increase, resulting in reduced services or higher taxes.

This is of particular importance to New York for two reasons. First, New York is home to most of the large commercial and investment banks. Further damage to them will hurt our local economy and runs contrary to Governor David Paterson's efforts to protect New York's status as the financial center of the globe. Indeed, the financial sector downturn has already produced serious job-losses and other negative effects on the New York economy. Second, all of the major bond insurers and many other large insurance companies are located in New York State.

The New York State Insurance Department has been working with the bond insurers to resolve their problems. Our goal is not to protect managers or stockholders of the these companies, but rather to promote a healthy competitive market, to ensure that bond insurance is available for municipalities that need it to lower borrowing costs, and to protect the policyholders of existing companies.

To protect policyholders, we facilitated the injection of more than $7bn into existing bond insurers, licensed new entrants in record time, continue to facilitate additional capital infusions and are preparing for the rational wind-down, that is, run-off, of any impaired companies. We have been successful despite attacks on the stock prices of the insurance holding companies, which have made those tasks more complicated and challenging. Rumour mongering and inaccurately disparaging insurance company solvency, however, crosses a line.

Indeed, solvency determination is one of the Insurance Department's most important roles. For insurance, solvency is a regulatory concept that is complicated because premiums and claims are often paid over a long period of time. Insurance has its own system of Statutory Accounting Principles that differs from Generally Accepted Accounting Principles in meaningful and logical ways. Solvency essentially means that an insurance company can pay its claims when they become due. That is a determination generally made only by the regulator based on examinations or confidential insurance company filings.

We take all these responsibilities very seriously. But our efforts could be stymied –and policy holders and all New Yorkers irreparably damaged – by false accusations as to an insurer's solvency and that is why the law does not permit it.
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