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HOW INSURANCE LAWS ARE MADE: THE NAIC AND STATE ADOPTION OF NAIC MODEL LAWS

HEARING

BEFORE THE

SUBCOMMITTEE ON ANTITRUST, MONOPOLIES AND BUSINESS RIGHTS

OF THE

COMMITTEE ON THE JUDICIARY

UNITED STATES SENATE

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FIRST SESSION

ON

HOW OUR STATE INSURANCE LAWS ARE MADE

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TUESDAY, APRIL 9, 1991

U.S. SENATE,
SUBCOMMITTEE ON ANTITRUST, MONOPOLIES AND BUSINESS RIGHTS,
COMMITTEE ON THE JUDICIARY,
Washington, DC.

The subcommittee met, pursuant to notice, at 10:09 a.m., in room SD-628, Dirksen Senate Office Building, Hon. Howard Metzenbaum, chairman of the subcommittee, presiding.

Present: Senators Metzenbaum, Thurmond, and Specter.

OPENING STATEMENT OF SENATOR METZENBAUM

Senator METZENBAUM. The subcommittee will come to order.

On December 10 of last year, this subcommittee conducted the first in what I described as a series of hearings on the insurance industry. At that hearing, we examined the vitally important issue of whether States are assuring that insurance company assets, like real estate, real estate mortgages and junk bonds, are accurately valued and whether States know the true financial condition of the companies.

What we found was disturbing. In essence, we have an honor system for reporting asset values because States examine companies infrequently and rarely, if ever, verify the company-assigned asset values. To make matters even more uncertain and confusing, we learned from our 50-State survey that States require a wide variety of asset valuation methods to be used by the companies.

Under these circumstances, State regulatory agencies and policyholders simply cannot be confident that the financial health of insurance companies is accurately reflected in their financial statements.

Today, the subcommittee will continue our series of hearings and initiate for the 102d Congress our ambitious schedule for oversight of the insurance industry. Before I describe today's hearing, I would like to briefly explain the subcommittee's insurance oversight agenda.

There is no Federal protection when the public deals with one of the Nation's largest and most powerful industries, an industry that affects Americans from cradle to grave. No Federal agency is mandated to regulate insurance companies or the insurance marketplace. No Federal agency is mandated to do oversight of insurance company and State regulatory agency practices. To the contrary, one important Federal agency, the Federal Trade Commission, is specifically prohibited from even studying the business of insurance.

Where there is no Federal involvement, there is instead State regulation. However, State insurance departments are woefully understaffed and are struggling to regulate 2,400 life insurance companies and 3,800 property and casualty companies. This glaring absence of regulatory muscle occurred throughout the decade of the 1980's when dramatic changes were remaking the face of insurance, particularly life insurance.

Life insurance was once a stable, predictable, and profitable business based on relatively simply policies that paid a death benefit. Today, life insurance is dominated by tax-guided, wheeler-dealer type investment policies. To make good on these high-interest-rate products, companies have had to abandon conservative investment practices for unpredictable, high-risk investments.

Frankly, the public has too much at stake for the Federal Government and the Congress to sit on the sidelines and hope for the best. In the face of no Federal agency oversight, the Congress has a responsibility to evaluate the industry and the States' regulatory problems.

The goal of this subcommittee is to determine whether the American public is adequately protected by the way States regulate insurance companies and their investments. We will attempt to open every major aspect of the industry and State regulation to the scrutiny that is urgently needed. We will do so in the course of numerous hearings during the next 8 months.

Today, we will examine how our State insurance laws are made. We will begin by looking at the National Association of Insurance Commissioners [NAIC] and the model laws it recommends for adoption by the 50 States.

The NAIC performs the essential function of pooling the knowledge of the States for the development of new insurance laws and regulations. The organization avoids the futility of 50 States independently attempting to address the same regulatory problems. In this quasi-legislative role, with the significant influence it exerts over the States, the NAIC carries the heavy burden of maintaining the public's trust. For this reason, congressional oversight of NAIC operations is critical.

Of course, NAIC model laws are just the beginning of the process because they must be adopted by the States. The States are under no obligation to act and, unfortunately, in far too many instances the States do not adopt important NAIC models.

For example, in 1985 the NAIC adopted an important model regulation that defines "standards commissioner's authority for companies deemed to be in hazardous financial condition"—certainly, a very important subject. No States have adopted the NAIC model, and only four States—Illinois, Kansas, Texas, and Virginia—have passed what the NAIC defines as legislation related to the model law.

Even where a significant number of States adopt a model, it usually takes many years. For example, in 1971 the NAIC adopted the Life and Health Insurance Guaranty Association Model Act in order to protect insurance policyholders when an insurance company becomes insolvent. That was in 1971. Today, 47 States have that model act as a part of their State insurance laws. On the surface, that would appear to be impressive. However, it took 20 years for these 47 States to create their life and health guaranty associations.

This situation begs the question: Why are the States not moving more quickly to adopt the NAIC models? I hope to explore that issue with some of the witnesses we will hear from this morning.

It is not only the States that are slow to act. In some instances, the NAIC has itself been behind some of the more progressive States in adopting model laws in time to deal effectively with problems in the insurance industry.

As an example, at our December 10, 1990, hearing, this subcommittee learned that the NAIC is just now working on a model act on mandatory reserves for investments in real estate and real estate mortgages. The NAIC predicts it will complete the model late this year. Knowing, as we do, of the challenge and the problems existing in the real estate industry at the present time, that is just unbelievable—unbelievable to the point of absurdity and irresponsibility.

Even if that optimistic schedule is met, by the time States consider the model we may well be finished with one of the worst real estate slumps in memory and be faced with a significant number of insurance companies that are severely impaired.

We also want to look at who the 50 commissioners turn to for assistance in the development of the model laws. The primary source of advice comes from advisory committees that are supposed to be made up of representatives of the insurance industry and of consumers. Don't you believe it.

While the NAIC is on record as being committed to equal consumer representation, it has failed miserably, as noted by that chart. The 30 current advisory committees have 383 industry representatives and 14 consumer representatives. Twenty-six of the 30 advisory committees have no consumer representatives. It is obvious that the insurance industry is running the show; they have taken over the NAIC.

And what of the commissioners themselves? Information provided by the NAIC indicates that State insurance commissioners, whether appointed by their Governor or elected by the voters, have strong ties to the insurance industry. Counting all commissioners since 1984, 18 percent have come from the insurance industry, and after serving as their State's top insurance regulator, 29 percent moved to the very companies they regulated, while another 21 percent go into private law practice, much of which involves representing insurance companies. The close connections with the regulated industry brings into question the willingness of State insurance commissioners to be the tough, no-nonsense regulators we so urgently need.

These are some of the issues we will discuss today with what I consider to be three excellent panels. The timeliness of this hearing could not be more appropriate. When we read in the paper this morning that First Executive Life's policyholders may not be able to recover in the event the company goes under, one realizes the serious problems existing not only with respect to this insurance company, but the questions that are out there in the minds of many people as to what is the financial viability and strength of the insurance industry.

We are already aware of what Equitable did just a few weeks ago. We know of other companies that have been talked about prominently and publicly. We don't know about a lot of companies because the ability of the American people to learn all that is going on in the insurance industry is not as helpful as it might be.

We will ask Mr. Earl Pomeroy, commissioner of insurance, State of North Dakota, and past president of the NAIC, to come forward as our first witness. We are happy to have you with us, Mr. Pomeroy.

STATEMENT OF EARL R. POMEROY, COMMISSIONER OF INSURANCE, STATE OF NORTH DAKOTA, AND PAST PRESIDENT, NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS

Mr. POMEROY. Thank you, Mr. Chairman.

Senator METZENBAUM. I think you know we have a 5-minute rule.

Mr. POMEROY. In order to comply with the 5-minute rule, Mr. Chairman, I have heavily abridged my oral presentation, but will be happy to expand on my remarks in the question-answer period.

Senator METZENBAUM. And your entire statement will be included in the record, Mr. Pomeroy.

Mr. POMEROY. Thank you.

Senator METZENBAUM. We are very happy to have you with us this morning.

Mr. POMEROY. Thank you very much. I am the elected insurance commissioner for North Dakota and immediate past president of the NAIC, the NAIC being the association of the insurance regulators of the 50 States and 5 territories. It plays a key role in coordinating the insurance regulatory activity conducted by the States.

We welcome this subcommittee's interest in the regulation of the insurance industry and have sincerely tried to provide your staff, Mr. Chairman, with every assistance in preparing them for today's hearing.

Not long after the various States undertook insurance regulation in the mid-1800's, it became clear that coordination between the jurisdictions was required. The National Association of Insurance Commissioners was established in 1871, a full 18 years before the State of North Dakota even entered the Union. They perform a variety of coordinating functions, but the focus of today's hearing being the model laws, that is where I will confine my remarks.

The NAIC is an exceptionally active association of independent State jurisdictions. Each State is a participating member. Meetings are held quarterly, with interim committee meetings in addition to that. The interaction of regulators produces a vital sharing of experiences, insights, and resources as States regulate this industry.

The primary conduit for multistate issue analysis occurs within the standing committee framework. Committees are assigned charges within their jurisdiction. The committee work product on various assigned charges is often a model law recommendation.

The model law status is attained upon a vote of the general membership.

The NAIC has adopted 199 model laws. They vary widely in breadth, and they vary widely in importance. Most are intended to serve as policy recommendations only to the States, should the States deem appropriate. The nature of the insurance markets in this country varies between States very significantly, depending upon the unique characteristics of each jurisdiction. Accordingly, except for solvency regulation, as I will explain in a moment, it is entirely appropriate for each State department and each State legislature to determine the regulatory strategy appropriate for that jurisdiction.

Mr. Chairman, like yourself, I am a former State legislator, and we recognize the legislative prerogative of each given State in determining the mix of regulations as they approach the regulation of this industry.

The primary input driving the creation of model laws is the regulatory experiences incurred by the commissioners and staff in the State insurance departments of this country on a daily basis. This input includes thousands of calls of inquiries, questions or complaints from consumers, daily observation of company and agent conduct in the marketplace, information received in consumer forums and hearings, as well as vigorous industry advocacy, as might be expected for any closely regulated industry.

One area of model laws we now expect States to adopt, and we expect compliance, and this is in the area of solvency regulation. We have taken this position based upon the fact that a company based in one State will write in other States, and therefore imperil, potentially, the policyholders in those other jurisdictions.

The insurance commissioners have decided that minimum standards are appropriate for gauging the adequacy of a State's solvency regulatory activities, and in a historic vote the association, by a unanimous vote of the States, voted to impose upon themselves minimum standards in 1989. The standards include laws and regulations, regulatory practices and procedures, and organizational and personnel practices.

An audit mechanism was developed in 1990 to assess and confirm that States are complying. Complying jurisdictions will be publicly certified. In 1990, we saw the first two States certified upon successful completion of the audit—Florida and New York.

In 1991, there is a great deal of activity that the standards have spawned. More than 40 jurisdictions have activities underway seemingly to bring themselves into compliance with the standards. Yesterday, the Governor of North Dakota signed into law this 135-page bill, the longest considered by this legislative session in North Dakota, designed to bring North Dakota into compliance. It contains six models we formerly did not have. We passed them specifically to attain compliance. That is indicative of the activity occurring across the country in order to confirm and obtain the certified status.

The upcoming activity is also important. We will be strengthening the sanction on noncomplying jurisdictions. I happen to chair the NAIC committee on the solvency standards. At our meeting next week, we will be recommending a very tough sanction against companies based in States that don't meet the minimum standards.

We will be recommending, and I anticipate that the membership will adopt, a requirement that a company based in a noncomplying State will need to comply fully with all requirements of a complying jurisdiction if it is to write any business in those complying jurisdictions after January 1, 1994.

Mr. Chairman, I appreciate the sincerity of your interest. I vigorously disagree with many of your conclusions regarding the effectiveness of State regulation, which I contend has demonstrated an ability to adapt to an increasingly complex industry.

Thank you very much.

Senator METZENBAUM. Thank you very much, Mr. Pomeroy.

I am very happy to see that a member of our subcommittee has joined us. Do you have an opening statement, Senator Thurmond?

OPENING STATEMENT OF SENATOR THURMOND

Senator THURMOND. Very briefly, Mr. Chairman. Mr. Chairman, you have scheduled today's hearing to examine how insurance laws are made and the role of the NAIC and the States in that process. This hearing is a continuation of the subcommittee's inquiry into the insurance industry generally which was begun last December with a hearing on the financial reporting methods used by insurance companies.

At the outset, Mr. Chairman, I would note that these hearings are not specifically related to your legislation seeking to repeal McCarran-Ferguson. I assume such hearings will be scheduled at some future date. I also note that a number of other Senate committees are looking into the insurance industry. I hope that we do not duplicate their efforts. There is much that this subcommittee has to do, and I would not want to see us going back over what others have already done.

Mr. Chairman, it should come as no surprise to you that I continue to believe it is best for the industry and the consumer that regulation of insurance remain with the States. I have consistently maintained this position every time legislation seeking to repeal the McCarran-Ferguson antitrust exemption is introduced.

Nevertheless, hearings such as today's are useful in keeping us apprised of the nature of State regulation and of the need for States to address particular problem areas. To the extent this hearing provides a forum in which these problems can be aired, then I believe we have provided a useful service to the States.

Mr. Chairman, I note that representatives from several States are here to testify today, as well as the past president of the National Association of Insurance Commissioners. I am sure they will enlighten the subcommittee on the concerns they have about the problems within the insurance industry and the effectiveness of State regulation. I look forward to hearing their testimony and the testimony of other witnesses. I want to thank them for their time and effort in appearing before us this morning.

I have several committees meeting at the same time today, and if I do not get to stay for the full hearing, of course, I will read the testimony. Thank you very much, Mr. Chairman.

Senator METZENBAUM. Thank you. We are happy to have you with us, Senator Thurmond.

We are very happy to have you with us, Commissioner Pomeroy, and I might say that I think it was masterful to have your own State sign a 135-page bill having to do with this subject yesterday. I don't think you can have much better timing than that.

Mr. Pomeroy, a 1985 NAIC resolution states that it is the objective of the NAIC to assist the State regulators in fulfilling their responsibilities to represent the interests of the insurance-consuming public. That resolution goes on to say that:

> The NAIC has continuously encouraged participation by interested representatives of consumer groups in activities of the NAIC for a number of years, including the appointment of consumers to advisory committees, solicitation of consumer presentations at executive committee and key task force meetings, et cetera.

Now, as pointed out in your testimony, the NAIC advisory committees serve as an important vehicle in which those affected by NAIC model laws have an opportunity to develop and make recommendations regarding proposed insurance laws. Is it true that the membership of these advisory committees is decided at the discretion of the Chair of the various committees and that you have no formalized guidelines or rules to direct that selection process?

Mr. POMEROY. Mr. Chairman, first of all, the decision of even whether to appoint an advisory committee and the subsequent membership of the committee is up to the individual chairman of the task force. There are protocols under development generally to assist commissioners in what has informally been passed to them by way of appropriately staffing these advisory committees.

I think it is terribly important to note that, first of all, the advisory committees play purely an advisory role in the process, with most of the insurance department information based upon activity gleaned from the respective State insurance departments.

We have seen a variety of advisory committees appointed in extremely technical areas and, frankly, have not seen much consumer interest—no consumer interest, in fact, demonstrated in many of the areas where the advisory committees assist the task forces.

In the committee that I chair, Mr. Chairman, the Medicare supplement committee, I have made it a point to have an equal number of consumer representatives and insurance representatives. We've scheduled meetings in Washington, DC, to the detriment of insurance departments from the western part of the country, but because this is where the organized consumer groups tend to be based and where they can attend, every effort has been made.

And, generally, I think that it is a fair statement that in those committees where there is a keen interest for consumer participation, the commissioners have made every effort to facilitate that participation.

Senator METZENBAUM. Well, let us talk about the actual membership of these advisory committees because, frankly, Mr. Pomeroy, I have some difficulty in accepting your statement that where consumers wanted to be involved, they could be. That isn't what we hear from the consumer groups, and I doubt very much, when I look at the titles of some of the advisory committees that have been appointed without consumer representation, that that is actually in accord with the facts.

But there is the chart, and that is based upon data provided by the NAIC. The subcommittee has determined that there are 30 NAIC advisory committees currently in existence, with 383 members. Only 14 of those members—14 out of 383—represent consumer organizations, a mere 3 percent. These 14 members serve on only 4 advisory committees—6 out of 31 on the Long-Term Care Advisory Committee, 1 out of 16 on the Long-Term Care Technical Advisory Committee, 6 out of 12 on the Medicare Supplemental Standardization Advisory Committee, and 1 out of 14 on the Assumption Reinsurance Advisory Committee.

Now, many of the other committees that you have have to do with Medicare or supplemental insurance and that field. But, certainly, consumers have an interest in many of the other committees that you have mentioned; 26 of the 30 advisory committees have absolutely no consumer representation.

Now, as far as you know, are the numbers that I have just stated in accordance with the facts?

Mr. POMEROY. Mr. Chairman, I am not in a position to confirm or deny the accuracy of those numbers. I think, to put it in perspective, there are more than 5,000 licensed insurance companies doing business in this country. The number of organized consumer advocacy groups is considerably less than that.

The number of consumer advocacy groups that have an interest in insurance is less than that, and the number that have interest in various aspects of the industry that we regulate, such as commercial liability insurance and the life and health actuarial task force, drops yet further.

There is no accident that the number of consumer representatives is greatest in the health area because this is where you have the greatest area of active consumer groups, and we have made every effort to facilitate their participation in our process.

Again, however, the regulator's experience which that regulator brings to bear in making a decision on a model law is drawn from the regulator's daily contact with the public in their State capitals. On a week-in, week-out basis, Mr. Chairman, I have much more contact with consumers than industry as relates to the variety of issues dealt with by the North Dakota department, and it is this background that I bring as a regulator, or any other regulator brings to the table in making a decision.

In the event an advisory committee recommendation is a shameless, self-serving recommendation from the insurance industry, it is understood to be such and paid very little accord in the ultimate decision reached by the committee.

Senator METZENBAUM. Well, I want to be certain that you and I are not in disagreement. You are not suggesting in any way that the numbers that I have provided, which we obtained from the NAIC, are incorrect?

Mr. POMEROY. As I mentioned, Mr. Chairman, I have not looked at the numbers prior to this hearing and can neither confirm nor deny.

Senator METZENBAUM. Nor are you suggesting, are you, that because there are 5,000 insurance companies and there are a very small number of consumer organizations—let us say 20, to pick a number—therefore, we would expect the ratio to be 250 to 1 as far as membership on the committees is concerned? If not, I don't understand why you pointed out that there are 5,000.

Mr. POMEROY. I am pleased you ask that for clarification, Mr. Chairman. I am certainly not suggesting that, but as a practical matter, it is difficult to identify representatives of consumer advocate groups for purposes of obtaining their participation.

Senator METZENBAUM. Do you know of any instances in which substantial numbers of consumer representatives have refused to serve on these advisory committees? You seem to suggest that they are hard to get to serve.

Mr. POMEROY. Mr. Chairman, you are going to hear from some in a later panel, but they may either refuse to participate in light of their funding limitations or they will agree to serve, but find attendance at the meetings difficult, again, in light of serious funding restrictions.

Senator METZENBAUM. Mr. Pomeroy, my real concern is a concern that the American people have to have. Now, we think of the NAIC—and I have always thought of it as being a body that is trying to provide some balance and helping to bring about better regulation of the insurance industry.

But I really ask you, how can the American people have any confidence in a situation where the committees that are advising the commissioners as they deliberate on model bills—how can they explain 3-percent representation from the consumers of this country and 97 percent from the industry, and expect to get adequately heard?

Mr. POMEROY. Mr. Chairman, the caboose does not drive the train, and you might quite properly refer to the advisory committees as the caboose. The train is driven by the commissioners; 12 of them are elected, directly accountable to the people of their jurisdictions.

Senator METZENBAUM. Mr. Pomeroy, let me say something to you and let me interrupt you. Are you telling me that the consumers, the people who buy insurance in this country, are the caboose, that they are the tail end of the whole ball game, and that the ones you have to be concerned about in drafting legislation are the insurance companies, and they are the ones who are providing the engine and they are the ones we have to protect? Is that the point of your remarks?

Mr. POMEROY. You directly misheard me, I am afraid, Mr. Chairman. I am telling you that the advisory committees are the caboose, the insurance regulators are the engine. Six hundred and fifty thousand insurance consumers elect me in the State of North Dakota; 11 other of my colleagues are elected. The rest are appointed by a Governor that is accountable to the constituency for the administration of their insurance departments. And it is the commissioners, directly responsible to the consumers in their respective States, that drive this train, not the advisory committees.

Senator METZENBAUM. Well, let us talk for a minute about the role that the few consumers who are involved do play in this whole relationship of advisory committees. In an article that appeared in the January 1985 publication of the Insurance Forum, a consumeroriented publication—I am sure you are probably familiar with it. It is called the Insurance Forum which is put out; Joseph Belth is the editor. Are you familiar with that?

Mr. POMEROY. Yes.

Senator METZENBAUM. Now, Professor Belth describes his experience with an NAIC advisory committee. In that article, under the subtitle "The Industry Majority," Professor Belth states:

> When the advisory committee had to make important decisions, industry domination of the committee was evident. Industry representatives outnumbered the independent members and controlled the outcome whenever they chose to do so.

To illustrate his point, Professor Belth goes on to say that:

> In advance of one meeting, I drafted and circulated four motions that I said would be made at the meeting. The purpose of the motions was to stimulate discussion of the disclosure approach. We did not get to the motions until late in the meeting when several members were ready to leave. When the motions were finally made, three of them were voted down by the industry majority without discussion. The chairman ruled that the fourth motion was out of order. I appealed the chairman's ruling, but it was upheld by the industry majority.

Mr. Pomeroy, what kind of consumer input would you consider that to be?

Mr. POMEROY. Mr. Chairman, that sounds like a very poorly run advisory committee. If I were a member of the task force receiving that advisory committee report, I would be inclined to throw it on the floor upon the receipt of it; it would be of no value to me whatsoever.

As you evaluate input you receive on various pieces of legislation, Mr. Chairman, I know you look to determine its objectivity and its accurate read of the situation. Shamelessly self-serving advice is of very little use to a policymaker, and that is precisely what occurs within the NAIC process. If an industry-dominated advisory committee wants to shamelessly advocate its interest, it is not going to get a whole lot of credibility for purposes of the regulatory analysis given their work product.

Senator METZENBAUM. Well, let me go on, then, Mr. Pomeroy. In a more recent example, in a letter dated November 20, 1990, addressed to you as the then president of the NAIC, Consumers Union, a well-respected public interest organization, expressed similar concerns about the manner in which the Medigap and long-term care advisory committees were operating.

Under the heading "Domination of Advisory Committee by Industry," the letter complains that, "Despite our efforts to participate actively in the work of the advisory committees, the industry representatives control the work product."

By way of an example, Consumers Union notes that their offer to help in the drafting of the Consumer Guide for Long-Term Care Insurance for Continuing Care Retirement Communities was rejected. Instead, industry representatives drafted it. Less than 2 weeks before the proposed guide was to be circulated to the NAIC, the consumer representative had not even been able to review the final draft.

With these types of problems, how can the consumer, how can we in Congress, have any confidence that the NAIC is getting consumer input?

Mr. POMEROY. As you know, Mr. Chairman, the course of the path of a piece of legislation—at various times, one becomes anxious about the way the process is working. It is unfortunate that that letter does not reflect the final work product of either the Medigap or the long-term care task forces in 1990.

In fact, the long-term care buyer's guide has very little industry input in the drafting. It was drafted by NAIC staff, with very heavy involvement by an individual who often writes as a reporter for Consumers Reports, one of the publications under the Consumers Union umbrella.

I have chaired last year, and continue to chair this year, the Medicare supplement task force, and I vigorously resist any suggestion that the consumer input is not given full accord.

Senator METZENBAUM. Well, unfortunately, Mr. Pomeroy, from the consumers' standpoint, it is they who are saying that they are not being heard.

Mr. POMEROY. Mr. Chairman, just to clarify, that letter says that the advisory committees don't take full account of their positions. It does not suggest that the task force does not take full account of their positions, and I think that the distinction is terribly important.

Senator METZENBAUM. I agree with you that the distinction is a valid one to make, but I think that one has to assume that, in the main, these advisory committees do have an impact. I am in no position to judge as to what impact it had upon the deliberations of your own committee, but the fact is that those advisory committees feel that when they are working at their responsibility, they are going to have an impact.

The fact that you say that it didn't have an impact, that it was written by staff and such other matters, I think may be relevant in connection with this particular advisory committee; it may not be. I don't know the facts, but I know this, that, assumedly, advisory committees are created for the purpose of giving advice, and, assumedly, such an advisory committee ought to be balanced.

Unfortunately, 26 of the advisory committees of the NAIC have had no consumer representatives on them. Now, whether or not the advisory committee does or doesn't have an impact, I don't know, but my guess is that, in the main, they do, even if they didn't have in connection with your particular committee's activities.

Now, Professor Belth and Consumers Union have stated—and it will be attested to by one of our witnesses here today—it would appear that the current NAIC advisory committee system is not only seriously flawed, but also makes a mockery of the whole concept of consumer participation. The viewpoints and interests of independent parties and the insurance-consuming public is being stifled and, in some cases, ignored.

Mr. Pomeroy, my question to you is what assurances, what guarantees, what promises can you make, representing the NAIC, that the presently standing advisory committees, as well as any future ones, will indeed have a fair proportion of consumer representatives involved, and if they are not involved it will be because they have declined to serve, not because they weren't asked?

Mr. POMEROY. Mr. Chairman, there is an established NAIC committee on consumer participation. It includes the president, the vice president, and me, as the immediate past president, of the NAIC. It is a priority issue for us. We have among our bylaws the charge to this committee, which includes "directed to enhance consumer participation."

Basically, to the degree that we can identify interested and representative consumer advocacy groups, we will invite them to participate. You have my full assurance of that. There is an ongoing reality that, on occasion, they have funding difficulties that hinder the involvement of their staff to the full degree they would like, but I don't believe that that represents an NAIC shortfall.

Senator METZENBAUM. Well, as long as you are talking about the inability of consumer groups to be present by reason of financial shortcomings, is there not some reason for the NAIC, which is representing the public—I mean, it is a group of insurance commissioners. Does it not then make sense to provide some funding to cover expenses of those who want to serve, who have something to contribute, but don't have the wherewithal to do it, since in the last sense the money that are being spent represent the money of all of the policyholders because, indirectly, that is where it comes from, and the consumers and the consumer groups are those policyholders?

Mr. POMEROY. Your question is a very fairly put one, Mr. Chairman. Two points in response. First, the regulators themselves represent consumers, and it should not be forgotten that regulators are directly accountable to the policyholders of their jurisdictions and do have a consumer representation to the very heart of their responsibility.

Second, we have looked at funding consumer participation, and ultimately found it cleaner in concept, more difficult to implement. How do you pick one consumer group from another? What is a representative consumer group? Who wants to participate?

We noted with some interest the FTC endeavor to enlist consumers through a funding of participation, ultimately dropping their program after finding it to be a tremendous administrative headache trying to sort representative consumer groups from nonrepresentative consumer groups.

Senator METZENBAUM. Well, you mentioned that the insurance commissioners themselves do represent the public. I think you recognize that in my opening statement I raised a question about a proinsurance-company prejudice on the part of some of the insurance commissioners—certainly, not all—by reason of the fact that a substantial proportion comes directly from the industry and a far greater proportion goes back into the industry, as well as being legal counsel for the industry.

So part of the thrust of our concern relates to a matter we will get into at a later point in these hearings, not today. It relates to this whole question of whether or not the insurance commissioners are indeed the unbiased, unprejudiced, fair individuals adequately representing the public because, in the last analysis, that is the concern both of this Congress as well as the concern of the people of your State and every other State in the Union.

Mr. POMEROY. Mr. Chairman, I am in my 7th year as insurance commissioner from North Dakota. I came into this position without any involvement in the industry. I was an attorney in private practice with virtually no industry component of my practice.

I have not seen during my years as commissioner any linkage between prior association with the industry and subsequent conduct as a regulator. In a couple of instances that I can think of, I know that the prior association with the industry created some of the toughest, some might say, reactionary regulators we have had that were extremely hard on virtually every component of industry conduct.

Once a commissioner enters office, they take an oath of public office, and I don't believe they are any less able to distance themselves from their prior association and make fair public policy judgments than members of the U.S. Senate that will have to, upon taking an oath of public office, pass on many public policy issues affecting areas where they may have had prior association.

Senator METZENBAUM. Well, the man who sits next to me and I worked very hard to enact legislation so that those who were in the Congress couldn't go out and subsequently represent various nations or people who had an interest before the Congress.

In your situation, in the insurance commissioner's situation, you have 3 out of every 10 going directly into the insurance industry, based upon past statistics, and you have another 2 out of 10 going into private law practice with the general understanding that a substantial portion of their new practice comes from the insurance industry. That makes up a total of 50 percent.

So, Mr. Pomeroy, it is a question that the American people have a right to be concerned about: NAIC advisory committees, almost no consumer representation; insurance commissioners—this whole question of whether or not they start off with any prejudices or whether or not they wind up being a favorite of the insurance industry that just 1 week before they had been regulating.

Mr. POMEROY. Mr. Chairman, I am not aware of restrictions prohibiting former Members of this body or the House of Representatives from engaging in the practice of law, including lobbying activities, relative to various items for consideration before the Senate or the House. In fact, I believe it is a very common occurrence among former Members of this Chamber or the House, and I don't impugn some lack of integrity to the processes of the Congress resulting from the subsequent employment of former Members. I believe that State regulators ought to be afforded the same credibility.

Senator METZENBAUM. Well, I would only say to you that he and I spent many hours on this question of going out representing Germany, France, Saudi Arabia, whatever, immediately upon leaving the Congress.

Mr. POMEROY. Foreign countries, maybe, Mr. Chairman, although I have personal knowledge of many Members that I know of engaged in the practice of law, including lobbying activities, including contact with their former colleagues. I would suggest that, of the commissioners leaving office and going into the industry, very few of them have contact with their former departments in a lobbying capacity, and there is a reason for this.

Often, a commissioner leaves office with a change of administration. If I am defeated when I stand for reelection, clearly I am not going to have much lobbying clout with the Insurance Department in North Dakota. Clearly, if, in those appointed situations, the Governor's office changes, the former commissioner has got no great truck with the new commissioner. I don't believe that this phenomenon you describe is actually occurring.

Senator METZENBAUM. Well, you just said something that, first of all, I am not sure you know whereof you speak when you say that when they leave the department, they don't come back and have any further contact. Second, you made the point that when they leave, quite often it is by reason of political change.

According to the NAIC, your organization, the average tenure of office is 18 months. That obviously would vitiate your argument that there is a change of administration or there is something of that kind occurring. The NAIC tells us the average term of office for commissioners is 18 months.

Mr. POMEROY. Mr. Chairman, there are circumstances that have some tenures shorter than another, and certainly there has been some considerable volatility within some jurisdictions relative to the tenure of their commissioners. Not unlike the executive branch in Washington, in those areas where you see shorter tenures of commissioners, you have an elevated role for the technical staff within those insurance departments, affording continuity.

In addition, we at the NAIC have tried to make sure we bring our new colleagues up to speed as quickly as possible by initiating a commissioners school which we conduct, as well as the association with fellow regulators occurring within the quarterly NAIC meetings. So I believe that, notwithstanding the turnover, there is a good deal of, first of all, technical support, and then extensive orientation to bring the newer commissioners up to speed as quickly as possible.

Senator METZENBAUM. I don't think that answers the question, but I won't belabor the point.

Mr. Pomeroy, I am pleased to learn from your submission that in an effort to increase consumer input into the NAIC legislative process, the NAIC has established a consumer participation working group. You made that statement in your submissions to us.

Let me ask you, when was the last time that working group met, and what has the group accomplished in the last 3 years, and how often does the group meet?

Mr. POMEROY. Mr. Chairman, the group has as part of its authority consumer affairs and market conduct activity. It meets on an ongoing basis throughout the year. A meeting is normally scheduled at every NAIC meeting. And, again, those activities will regard market conduct activities, as well as consumer outreach.

Within the last 3 years, a new level of dialog has occurred between the leadership of the NAIC and the consumer advocates groups and we initiated regular meetings of the officers of the NAIC with these groups at the outset of every new term of NAIC officers. And I believe that consultation with the consumer groups themselves would indicate that the level of dialog is at a higher level than it formerly was.

Senator METZENBAUM. Either you are totally wrong or the consumer groups are totally wrong; there is no middle ground. Our subcommittee staff contacted 2 insurance consumer groups located in Washington. One group, Consumers Union, which has probably been in existence 50 to 100 years, said that the only working group they were invited to was held 2 years ago, and the other, United Health Seniors Co-op, never heard of the working group.

You say that we have got these meetings going, we are doing this and we are doing that. I guess I would have to ask you to submit to us in writing the actual facts.

Mr. POMEROY. I will do that, Mr. Chairman, but I can briefly clarify. Consumers Union and Seniors Co-op both participate actively in the health advisory committees. The other meetings I spoke of have involved Consumer Federation of America, the National—Bob Hunter's outfit, whatever the name of his outfit is, and the consumer insurance information group, all of these three groups having primarily a property-casualty outlook rather than the health outlook. The consumer organizations focused on health insurance that you mentioned are deeply involved in the advisory committee process, and I don't think they would deny that.

Senator METZENBAUM. Senator Thurmond.

Senator THURMOND. Thank you, Mr. Chairman. I have another committee meeting. I just have a few questions that I want to ask you before I go.

Mr. Pomeroy, you have described the procedures used by the NAIC to enact a model law. Are all of these proceedings public proceedings, and if not would you explain why not?

Mr. POMEROY. Senator Thurmond, they are public proceedings. On occasion, the regulators themselves will go into executive session, but all advisory committee meetings are open.

Senator THURMOND. Mr. Pomeroy, you have testified that only Florida and New York have been accredited by the NAIC. How long does each accreditation take, and what other States, if any, are in the accreditation process?

Mr. POMEROY. Senator, I am proud to report that the audit mechanism to verify compliance for purposes of arriving at a certification was only established in June 1990. By the end of the year, the first two States had been certified. Presently, over 40 States have some level of activity which we believe is geared toward obtaining certification in progress, and we believe that by 1994 most States ought to be certified. For that reason, we are keying January 1, 1994, as the date where the sanctions for noncompliance really begin to kick in.

Senator THURMOND. Mr. Pomeroy, do you believe it will be necessary for the Federal Government to become involved in solvency regulation or any other kind of regulation of the insurance industry, or do you believe the States can continue to effectively regulate?

Mr. POMEROY. Senator Thurmond, I believe the States can continue to effectively regulate, working closely together through the NAIC. I think that they have shown an ability to adapt to an increased complexity within the insurance industry. I think they are much closer to the industry in terms of observing daily market activity and new solvency strains.

They have the historical expertise, the laws, and the personnel to do the job, and I think it would be a tragic mistake to begin to divide the regulatory responsibilities for this industry, leaving marketplace activities with the States and putting solvency regulation in the Federal Government. I think it would be a harbinger to a savings and loan disaster.

Senator THURMOND. Mr. Pomeroy, there has been some criticism that the financial information collected by the States is too stale by the time it becomes available. What is your response to this problem?

Mr. POMEROY. Senator, I believe that that is not a fair criticism. In addition to the annual statements filed with the NAIC, we are now requiring quarterly statements to be filed. We have moved into the reporting blank a requirement to affect all insurance companies filing the required financial statement requiring actuarial verification of loss reserves and CPA audit verification of the numbers reported.

There are times, of course, where the solvency fortunes of a company can slip very quickly, but on a general basis I believe the financial information reported to the commissioners is timely.

Senator THURMOND. Mr. Pomeroy, Mr. Johnston, who is a State senator from California, and whose prepared testimony will be presented in the next panel, suggests that the NAIC must be accountable to either Congress or the State legislatures. Would you share with the subcommittee your reaction to that suggestion?

Mr. POMEROY. Senator Thurmond, I think that view reflects somewhat of a misunderstanding of the NAIC. The NAIC is not an entity unto itself; it is the collective entity of the insurance regulators of this country. As I have mentioned previously, 12 of those regulators are directly elected. The others are appointed by elected Governors. I believe that this instills a direct accountability of their cooperative association, the NAIC, to the people of this country.

Senator THURMOND. Those are all the questions I have. I just want to make this comment. I get very frustrated—I have been here 36 years—to see people keep on chipping away, chipping away, at the rights of the States. The original intent of the Constitution was that the States were to be the dominant agencies of government in this country. The Federal Government was given only certain powers in the Constitution, and no more, and until they amend the Constitution, that is the way it should be.

I don't know of any instance in which the field of insurance has been delegated to the Federal Government. As I have said before, the Supreme Court got the Government into it in the 1940's, and Congress passed a law and took it out. That is when the Congress was more dominant and didn't necessarily listen to the Supreme Court on things where it felt it was right.

At any rate, I think we have got to maintain the rights of the States. One reason we have got such a big deficit now, over $3 trillion—interest alone is about $200 billion, the second largest item in the budget—is that we keep going into fields of activity where we don't have authority to do it. This Federal Government was intended to be a limited government, and it has become the dominant government. That is the reason we have such a big debt today.

Again, I say the rights of the States should be preserved because that is part of the Constitution of the United States. And I hope you insurance commissioners will continue to stand for your rights under the States, which you have a right to do.

Thank you.

Senator METZENBAUM. Well, I won't engage my colleague in a discussion of whether it ought to be State or Federal.

Senator THURMOND. We have been talking about that for years. [Laughter.]

Senator METZENBAUM. I will say that our prime concern is the American public. It is not a question of who has got the power.

In our next panel, Mr. Pomeroy, we are going to talk about why it takes States so long to enact insurance laws. However, I am also concerned about whether the NAIC develops its model laws in a timely manner.

Last December, we learned that while the country was deep into a real estate recession, the NAIC was just getting around to developing a model law dealing with real estate reserves. In fact, we recently learned that the model law is still being drafted and will not be ready for consideration until late this year.

My question to you is why does it take the NAIC so long to develop model laws, and I guess the subsequent question, why does it take the States so long to implement the model laws once they are proposed by the NAIC?

Mr. POMEROY. Mr. Chairman, as to the first question, the NAIC is developing risk-based reserving requirements. This is a very important new endeavor for insurance regulators. It will have very serious implications for company solvency or surplus positions, and, accordingly, it is an extremely technically demanding endeavor, one that cannot be rushed.

I know of no company that has become insolvent or financially impaired as a sole result of the declining real estate market so particularly evident here in the Northeast.

Senator METZENBAUM. You wouldn't necessarily know about it. There would be no way of knowing about it. You get a financial statement submitted to you by any one of 5,000 companies. You look at the statement and they say real estate mortgages, $350 million. You have no way of knowing until there is a default or until they change it on their balance sheet from being a current asset to being an asset in default, and therefore noted by the accountant. But other than that, you wouldn't know it.

Mr. POMEROY. Mr. Chairman, that is not accurate. The primary solvency regulation occurring in this country is through the work of financial examiners in the bowels of the insurance companies of this country verifying the assets, item by item, reported by those companies.

For example, in my own State a financial examination will include a review of the mortgage loans reported and whether they are accurately stated, whether they are held at appropriate values.

Senator METZENBAUM. Now, how would you know that? Now, let us just take an example. Let us assume it is the Pru, or the Equitable, or the Metropolitan, or whatever the case may be, and let us assume that on their books they show a particular office building in Dallas, TX, and that that building was taken originally at a valuation of $300 million and they provided a loan of $280 million. And the payments are current, but the reality is that that piece of real estate in Dallas, TX, is today worth $160 million. How would you possibly know that?

Mr. POMEROY. Mr. Chairman, that is another issue. That is marking to market as opposed to determining whether a real estate holding is in a performing status. Companies do not engage in real estate lending for purposes of short-term trading. They engage in real estate lending for purposes of long-term performance on the note obligation.

Senator METZENBAUM. I understand.

Mr. POMEROY. As long as it is in a performing status, the relative resale value is not of concern to the regulator, particularly when the company is in a very liquid position and that asset can indeed be held to maturity.

Senator METZENBAUM. As an insurance commissioner, you wouldn't even know if that loan was in default unless the company brought it to your attention, would you?

Mr. POMEROY. Mr. Chairman, that would be information from the internal company records that my examiners could verify, regardless of whether the company disclosed it or not.

Senator METZENBAUM. How many companies do your examiners examine in a year—actually examine?

Mr. POMEROY. Each State is primarily responsible for the domestic companies within that State. In the case of North Dakota, we do not have a particularly large domestic industry. I would say we have 12 companies of any size, and maybe a dozen county mutuals in addition to that. They are examined on a triennial basis. The examinations——

Senator METZENBAUM. Does triennial mean once every 3 years?

Mr. POMEROY. Yes. There are annual desk audits of the annual statement information, and then the complete triennial examination. Within the context of North Dakota, I have an appropriate examination staff for the purposes of conducting the examinations of our fairly limited domestic industry.

Last year, in order to improve the examination process, the NAIC embarked upon an ambitious undertaking outlined in my written testimony resulting in reforms which will, we believe, enhance the conduct of financial examinations within this country.

Senator METZENBAUM. Mr. Pomeroy, that isn't the thrust of our inquiry this morning, but let me ask you, do you have any concern as to the economic viability of the insurance industry at this point in time?

Mr. POMEROY. Mr. Chairman, undoubtedly, the business of running an insurance company has grown more complex. Line by line of insurance coverage has solvency perils that they did not have 10 or 15 years ago. It, therefore, requires more rigorous regulatory oversight. We have moved that into place and are continuing to tighten the screws of financial regulation. I believe that is one of the key distinctions from the savings and loan industry where, at a point of new solvency perils, they pulled the financial examiners out of the field.

Senator METZENBAUM. I didn't ask you that.

Mr. POMEROY. We have tightened solvency examination, and I think, therefore, State regulators have met the primary thrust of staying abreast of this industry.

Senator METZENBAUM. Mr. Pomeroy, that is a fine speech, but you didn't answer my question. My question was do you have some concern as to the economic viability of a substantial portion of the insurance industry at the present time.

Mr. POMEROY. Mr. Chairman, I am going to specifically answer your question, and the answer is no. I do not have a great concern about the economic viability of a substantial portion of the industry. I refer specifically to a study presented last year by the IDS Life Insurance Co. that showed that, in a major economic downturn, up to 20 percent of life insurance companies could become insolvent.

That figure has been thoroughly analyzed and is generally believed to represent not just a worst case scenario, but a truly cataclysmic event occurring within this country. Generally speaking, while there is greater solvency peril, which may lead to greater numbers of insolvency over the one-half of 1 percent average over the last 5 years, I do not believe a substantial portion of this industry is imperiled as we meet today.

Senator METZENBAUM. Do you think that a substantially higher percentage of the industry is in more peril today than it was in yesteryear?

Mr. POMEROY. Mr. Chairman, that really is a question that requires some relativity. Over the last 5 years, we have averaged about one-half of 1 percent of licensed insurance companies becoming insolvent. I believe that we probably will have greater incidence in the future, in light of the new solvency strains on the insurance industry. It may go up to, you know, a substantial portion of—it could double and be 1 percent.

Senator METZENBAUM. Could it be higher, in your opinion?

Mr. POMEROY. I believe that the number of insolvencies will rise. I still believe they will represent the smallest portion of insurance companies doing business in this country.

There is one other thing I would like to point out. If you have competitive pricing occurring within the market, you are going to have an occasional company missing the boat in the pricing of their premium and they are going to become insolvent.

The tradeoff for a guaranteed solvent situation is a noncompetitive market with no competition in pricing and higher premiums to the consumers. And I believe that the U.S. insurance consumer will take the present risk of insolvency, buttressed with guaranty fund protection, in exchange for the competitive pricing environment.

Senator METZENBAUM. Mr. Pomeroy, to go back to the thrust of my earlier questions, with respect to junk bonds, we also recently learned that the NAIC has yet to adopt a final model regulation that would place a limit on junk bond holdings.

Now, I don't have to tell you of the concern that this has caused the American people. We have seen what has happened in the savings and loan industry. We have heard of what is happening in certain parts of the insurance industry. Why didn't the NAIC address this issue in the early 1980's when the junk bond market was becoming a significant force, with billions of dollars' worth of junk bonds being purchased by the insurance industry?

Mr. POMEROY. Mr. Chairman, the NAIC last year moved a new valuation scheme into place that allows for a more accurate tracking and a greater reserving of riskier investments in the processes administered through the Securities Valuations Office. To presently move limitations in place——

Senator METZENBAUM. I am asking why you didn't do it in the 1980's. You saw all these junk bonds being bought by insurance companies; your own auditors had to see that. It was public information in some instances. Why didn't you do something about it?

Mr. POMEROY. Well, Mr. Chairman, a couple of States did take action. Florida and New York took action in that activity. I don't believe that at the NAIC there was wide consensus that this activity was imperiling the financial solvency of the insurance industry, in toto, or individual companies.

Senator METZENBAUM. Mr. Pomeroy, to the extent the NAIC is late in developing insurance laws, States are even later, since they rely so heavily on NAIC model laws when crafting their own laws. Wouldn't you agree that if the NAIC acted faster in developing its insurance laws, we would stand a better chance of avoiding a possible insurance calamity?

Mr. POMEROY. Mr. Chairman, regulation and legislation within a State capital respond to the obvious needs and demands of a given moment. You have noted this morning the delayed implementation of the life and health guaranty fund laws. You have not noted that the property-casualty guaranty fund laws were implemented across the States at a much quicker rate. The reason for that is obvious.

At the time the guaranty fund laws were constructed, there was a much greater incidence of insolvency occurring on the property-casualty side of the market. Therefore, State insurance departments and State legislators responded to that. As insolvencies of life insurance companies became more familiar in the 1980's, States have moved the life and health guaranty funds into place.

As a State regulator, I cannot go into my legislative session with virtually every model enacted by the NAIC. You remember from your own days in the legislature that an administrative agency gets so many shots; you basically get a set number of items which a legislature will consider.

Our legislative agenda in any given session is responding to the most pressing needs of insurance regulation at that point in time, and I believe, therefore, is reasonably responsive to the needs of the marketplace.

Senator METZENBAUM. Well, let me say, when you say it is reasonably responsive, you had a Post-Assessment Property and Liability Insurance Guaranty Association Model Act that was adopted in 1970. You had one in 1963 and four in 1969 before the act was adopted, and you had a number in 1970 and 1971 and then it drags on—1972, 1974, 1976, 1981, all the way down into 1988. Wouldn't you agree that is too long in order to put a model NAIC-recommended law into effect in all the States?

Mr. POMEROY. Mr. Chairman, I would not necessarily agree. It would depend upon the incidence of insolvencies occurring within jurisdictions. I would wager that the rate of enactment tracks very closely a given State's experience with an insolvent insurance carrier unable to meet its obligations. I believe those States most belatedly adopting the model may not have had the imperative to bring it into place at an earlier point in time.

Senator METZENBAUM. Well, I notice, I might say, that your own State took 15 years to adopt that model law.

Mr. POMEROY. That is not accurate.

Senator METZENBAUM. Aren't you in North Dakota?

Mr. POMEROY. I am in North Dakota, Mr. Chairman. That figure is not accurate.

Senator METZENBAUM. That is not accurate?

Mr. POMEROY. No.

Senator METZENBAUM. Will you be good enough to supply for the record the correct figure, then?

Mr. POMEROY. Yes.

Senator METZENBAUM. We got the information from the NAIC; we didn't go out and find it ourselves.

Mr. POMEROY. In 1985, the State of North Dakota recodified its insurance code. It appears that that is the date listed. We had a guaranty fund law some time prior to that.

Senator METZENBAUM. Well, will you tell the NAIC that so that the NAIC can then correct their records?

Mr. POMEROY. I will tell both the NAIC and committee staff, Mr. Chairman.

Senator METZENBAUM. Very good. Now, just a couple more questions. We have found that many of your models have not been adopted by a significant number of States, and I have already stated that. One example I mentioned earlier is your model regulation that defines standards and commissioner authority for companies deemed to be in hazardous financial condition. Obviously, that is an important concern; it is a very relevant one.

That was adopted in 1985, 6 years ago, but not one State has adopted it since then. Only four States have adopted what you referred to as related legislation. Your own State of North Dakota is not among them.

Another example is your model bill on criminal sanctions for failure to report impairment. You adopted that in 1973, 18 years ago. In those 18 years, only one State, West Virginia, has adopted your model.

Let us look at your model regulation on life reinsurance agreements. Only five States have adopted that in the last 6 years. North Dakota has not adopted it. In 1983, you adopted a State insurance department funding model. Only four States, including your State of North Dakota, have adopted it. A number of other States adopted what you call related legislation, but nearly half the States have taken no action.

Frankly, Mr. Pomeroy, an adequately funded insurance department is the key to effective State regulation. It seems to me that the States are not following the NAIC's lead on this legislation, and what we have is the American people thinking that the NAIC is helping to provide some overview of the insurance industry. Then we have a situation where, in creating these model laws, there is a failure to involve the public consumers into the development of those model laws.

Then we have a situation where very few States really move very rapidly, even people who are instrumental in drafting the legislation and are in a leadership role in NAIC, in implementing and seeing to it that their State legislatures do enact the law.

I must say to you, you made some reference to the fact that I know, as a former legislator, which goes back, certainly, a great number of years, in the State body, that there is a certain amount of legislation that you can take to the legislature from the insurance department. I never heard of such a rule or any such contemplation.

So I have to say to you that many people have hoped that the NAIC would provide some leadership, and I think that a good many of the Members are well-intentioned in an effort to do that. But I think that the NAIC doesn't sit impartially and doesn't evaluate proposals objectively, with consumer involvement. Third, when it does, the implementation of the NAIC recommendations is often too long in becoming a reality.

Mr. POMEROY. Mr. Chairman, I would love to respond to some of that. First of all, as to the funding model, the funding of State government is something that a State legislature will vigorously hold within its own prerogative. Frankly, philosophies are very divided on whether off-budget funding or special funding is appropriate.

I believe that there is a trend in State legislatures presently to avoid special funding and to have all agencies general-funded. That doesn't mean there are not adequate general funds provided. But, clearly, a State legislature and a Governor will determine how the agencies of a given State are funded, and a recommendation from a national body may or may not be influential in that recommendation.

You have mentioned certain other models that I would like to just briefly respond to in indicating that only a few States have adopted the authority of commissioners for companies in hazardous financial condition. There are other models that relate to this key area of authority. Two that I might mention are the model law on supervision and the model law on rehabilitation and liquidation.

The model law on rehabilitation and liquidation is contained within the NAIC financial solvency standards. All States are expected to meet the standards. We are auditing States in terms of whether they comply. We will have tough sanctions for States that do not comply by 1994.

So, as a general matter about models, I believe that it is up to the individual State to establish its own regulatory mix, except for the core solvency regulatory areas, and in that area the policyholders of this country have a right to expect minimum performance. The NAIC has moved minimum standards into place. They have moved an arms-length audit mechanism into place to verify State compliance. We are moving into place tough sanctions for noncompliance.

So, in the areas where the models are truly imperative, I believe the NAIC does not disagree with your assumption that States ought to have these models, and we now have an enforcement mechanism for ensuring that they are brought on board.

Senator METZENBAUM. Well, I want to thank you, Mr. Pomeroy. I did give some figures as to what the extent of participation of consumer groups is in the advisory committees, and I will at this point put into the record a list which was compiled on the basis of information submitted to us by the NAIC, which shows, out of a total of 30 advisory committees, 383 industry representatives and 14 consumer representatives.

[The information referred to can be found in the appendix.]

Senator METZENBAUM. When I asked you whether or not those facts were correct, you had some reservations; you weren't certain. I would ask you to confirm for us by letter whether or not they are correct, and if they aren't correct, indicate which are correct.

Mr. POMEROY. Yes. Mr. Chairman, I had indicated I could neither confirm nor deny. I will be happy to confirm in subsequent writing.

Senator METZENBAUM. Thank you very much, and I appreciate your cooperation in being with us, Mr. Pomeroy.

Mr. POMEROY. Thank you.

[The prepared statement and attachments of Mr. Pomeroy follow]:

TESTIMONY BY

the

NATIONAL ASSOCIATION OF

INSURANCE COMMISSIONERS

before the

SUBCOMMITTEE ON ANTITRUST,

MONOPOLIES, AND BUSINESS RIGHTS

of the

JUDICIARY COMMITTEE

UNITED STATES SENATE

on the

NAIC MODEL LAW PROCESS

The Honorable Earl R. Pomeroy
Past President, NAIC
Commissioner of Insurance
State of North Dakota
April 9, 1991

I. INTRODUCTION TO THE NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS

Mr. Chairman, Members of the Subcommittee, my name is Earl Pomeroy. I am the Insurance Commissioner for the State of North Dakota, and the Immediate Past President of the National Association of Insurance Commissioners (NAIC). The NAIC thanks you for the opportunity to discuss NAIC Model Laws and Regulations.

The role that the NAIC has played in the regulation of the insurance industry is truly unique. As Past President of the NAIC, I am most proud of that role, and am happy to discuss it with you today. Throughout the 120 years that the NAIC has coordinated the efforts of state regulators, it has been called upon on numerous occasions to step forward on behalf of insurance consumers and the general public and provide valuable national leadership in the regulation of the insurance industry.

In the 1870s, when hundreds of companies were going insolvent and the nascent community of state regulators was struggling to establish some degree of uniformity in the reporting of insurer financial condition, the NAIC developed the predecessor to the Annual Statement Blank which, since then, has served as the uniform financial reporting form for all insurance companies. In 1909, when securities fraud threatened to rock the industry, the NAIC established the Securities Valuation Office (SVO) to provide uniform valuation of insurers' securities. In 1932, when the entire financial services industry was in the midst of crisis, the power of the SVO to alter the valuation of securities on a countrywide basis in periods of national emergency obviated the need for President Roosevelt to take drastic federal regulatory action when he and the Congress were forced to do so in dealing with the nation's banks.

In the late 1940s, after the Congress had challenged the states to regulate the insurance industry or face federal preemption, the NAIC led state regulators in the development of an effective system to protect consumers from both insolvencies and anti-competitive practices. Most recently, with the rise in public concern over increasing insurance insolvencies, the NAIC has moved aggressively to push for a national program of minimum financial regulation standards.

II. UNIFORMITY OF STATE REGULATION AND THE NAIC

One of the key methods by which the NAIC seeks to maintain and improve state insurance regulation is to facilitate a certain degree of uniformity of regulation among the states. The achievement of this level of uniformity is accomplished through four primary vehicles:

- By providing a vehicle for the drafting and adoption of Model Bills and Regulations, the NAIC serves a valuable function for the development of uniform legislative and regulatory approaches to solvency regulation. The NAIC currently has 199 Model Acts, Regulations and Guidelines.

- The vast majority of insurance companies, primarily multi-state insurers, are required in each state to file an Annual Statement, designed by the NAIC, with the insurance department of each state in which they do business, as well as with the NAIC. This uniform system of reporting the financial information about insurance companies is a powerful tool for the promotion of the uniform regulation of insurers.

- To promote consistency in the examination of multi-state insurance companies, the NAIC provides a centralized machinery for conducting examinations of insurance companies. Under the Zone Examination System, the NAIC coordinates multi-state examinations conducted under the procedures of the NAIC Examiners Handbook.

- Through its Securities Valuation Office in New York, the NAIC values on a uniform basis the securities held in portfolios of virtually every insurance company in the United States.

Thus, NAIC's r le of developing Model Acts and Regulations is but one of an array of tools in the effort to bring an appropriate level of uniformity to state insurance regulation. It is, however, an important role, one which I am all too happy to discuss with this Subcommittee.

III. THE NAIC'S PROCEDURES FOR THE ADOPTION OF MODEL LAWS

Uniformity of regulation is desirable in some instances and undesirable in others. The broad economic and social diversity of the various states necessitates a flexible regulatory approach that is responsive to the differences among the states.

In some areas of the regulation of the business of insurance, national uniformity does offer advantages. Typical of this sort are the Model Acts and Regulations included as part of the NAIC's Financial Regulation Standards, adopted in 1989 to establish a national set of standards for insurer solvency regulation.

In other areas, uniformity is not necessary and may in fact damper innovation both of products and new regulatory approaches. In areas such as rate approval procedures, consumer disclosure, and funding of insurance departments, state variations are appropriate and healthy for the regulatory process. Quite often one or two states can move quicker and further in consumer protection than a single, rational regulatory body.

In these areas, the adoption by the NAIC of Model Laws or Regulations can nevertheless provide a benefit to state insurance regulators. The collective experience and expertise of insurance commissioners from a number of states can provide valuable assistance to the insurance department and legislature of a particular state seeking to address a regulatory question that may not call for a national program. Examples of Model Acts of this sort include those addressing property/casualty insurance rating systems. The NAIC has developed Models for both competitive pricing and prior approval property/casualty rating systems.

In both situations, the procedure for adoption by the NAIC of models is the same, and, in some ways, is similar to the procedures of many legislative bodies, including the Congress. When a regulatory need is recognized and characterized as one for which a model would be appropriate, the NAIC committee or subcommittee with pertinent jurisdiction over the area may begin study of the issue. That committee or subcommittee may assign the issue to the NAIC equivalent of a legislative subcommittee, a Task Force, which may, in turn, assign study of all or a portion of the issue to one or more Working Groups. An organization chart of the NAIC is included with this testimony as Attachment A. A list of all of the current NAIC Committees is included as Attachment B.

These bodies are composed of state regulators, who, like their legislative counterparts, may hold hearings and conduct primary and secondary research, all in an effort to generate a sufficient body of information to draft a sound model. Public input into this deliberative process may come in the form of testimony from interested individuals, groups, and more formal groupings of interested parties known as Advisory Groups. An advisory group may be established by a Task Force or Working Group in order to provide technical assistance and public input from academics, consumers, industry organizations, and others.

Furthermore, as reflected in the NAIC Bylaws, all of the NAIC Members are interested in increasing the level of consumer input into the NAIC process. We have carried out our intentions in several ways, including the creation of a Consumer Participation Working Group, which is chaired by the NAIC Vice President, William McCartney, the Director of Insurance of the State of Nebraska. The NAIC President, Jim Long, Insurance Commissioner of North Carolina, and I also sit on this Working Group. We meet periodically with representatives from national consumer groups here in Washington, D.C., and seek their advice. In addition, we encourage NAIC staff to undertake outreach efforts to include consumers in the model law process and in other programs the NAIC undertakes.

Once a proposal has been developed at the Task Force or Working Group level, the parent Committee or Subcommittee may elect to expose the draft model for comment. This exposure period, which is usually 30 to 90 days, allows interested parties to supplement their previously-given input with comments directed at the specific draft proposal.

At any stage in the drafting process, a Working Group, Task Force, Subcommittee or Committee may amend the draft model. The draft is then reported to the NAIC Executive (EX) Committee for approval, which approval results in the referral of the proposed model to the Plenary Session of the NAIC. Upon a majority vote of the Plenary, a Model is adopted by the NAIC. Then, the Model Law or Regulation may be taken up in the individual states where, prior to adoption, it is subject to the more formal requirements of a legislative or administrative process -- both of which allow for a variety of methods of public input and scrutiny.

One further point with respect to solvency regulation is worth noting. Should a Model Act or Regulation be considered by the NAIC to be essential to stringent solvency regulation, that model may be adopted as a component of the NAIC's Financial Regulation Standards. States seeking to become or remain accredited by the NAIC have two years from the addition of the model to the Financial Regulation Standards to adopt either the model or a functional equivalent of the model.

IV. A CLOSER LOOK AT SOME SPECIFIC NAIC MODELS

NAIC Model Laws, Regulations and Guidelines fall into two broad categories: those that have been adopted as a part of the NAIC's Financial Regulation Standards, and those that have not been made a part of the Standards. Before I explore the adoption process for typical models of each of these categories, I will first outline the Financial Regulation Standards.

A. The Financial Regulation Standards

While the regulation of insurance companies for solvency has, from the beginning, been the primary concern of the NAIC, the bulk of the modern regulatory approach to solvency regulation has been assembled over the last twenty years, beginning with the adoption of model laws addressing guaranty funds and culminating most recently with the adoption of the Examination Model Law, which I will describe below.

By 1989, state insurance regulators had reached consensus on what it was that comprised appropriate legal and administrative framework for solvency regulation. In an historic decision, state regulators voted to codify this framework in the form of the NAIC's Financial Regulation Standards. The standards are divided into three categories: laws and regulations; regulatory practices and procedures; and organizational and personnel practices.

The "laws and regulations" component of the NAIC standards originally included 18 laws and regulations, 12 of which are embodied in NAIC Models, considered by the NAIC to be the legal and administrative authority necessary for solvency regulation. The "regulatory practices and procedures" component of the standards establishes requirements for the handling by state insurance departments of financial analysis, financial examinations, and troubled insurance companies. Finally, the "organizational and personnel practices" component of the NAIC standards establishes requirements for professional development, organizational structure, staff performance evaluation, minimum educational and experience requirements, pay structure, and funding.

To furnish direction to the states regarding the minimum standards and an inducement to put them in place, the NAIC adopted last year a formal accreditation system. Under this program, each state's insurance department is reviewed by an independent review team which determines whether that department is in compliance with the NAIC's Financial Regulation Standards.

Critics of the Accreditation Program, particularly those who support the involvement of the federal government in solvency regulation, have claimed that the voluntary nature of the NAIC constitutes a weakness in the program. This criticism is based, however, upon a misunderstanding of the potency of the incentives that are a part of the program.

Originally, the only incentive states had for complying with the Financial Regulation Standards was the public acknowledgement accorded to accredited states. However, at the NAIC's Winter

National Meeting in December 1990 the NAIC began what is expected to be an ongoing process of adding more concrete incentives to the Accreditation Program. At that meeting, the NAIC adopted a Model Act on Examinations which provides that, beginning in January 1994, accredited states will not accept reports of zone examinations from unaccredited states. At the time of this writing, the NAIC Financial Regulation Standards Committee is considering the adoption by the NAIC of additional sanctions to be imposed on non-accredited states, including a proposal under which an accredited state would impose restrictions on the issuance of a license to a company domiciled in a non-accredited state.

The effectiveness of the existing incentives and those under consideration can be seen in the reaction of state legislatures and insurance departments. So far, two states, New York and Florida, have undergone the formal certification process and have been accredited as being in compliance with the Financial Regulation Standards. More importantly, as of late March 1991, 38 state legislatures were considering proposals to enhance their solvency regulation statutes through the adoption of NAIC Models that are included in the NAIC Financial Regulation Standards (see Attachment C).

Prospects for this widespread legislative activity are excellent. As of this writing, the General Assembly of South Carolina had approved a comprehensive legislative package designed to bring the state in compliance with the "laws and regulations" component of the NAIC standards, and similar packages in other states were receiving favorable legislative treatment. By March 25, six states had approved such proposals. Most informed observers see 1991 as a banner year for the passage by state legislatures of bills to enhance solvency regulation, due in largest part to the NAIC's Accreditation Program.

B. An Example of the Model Law Adoption Process of a Model in the Financial Regulation Standards: The Model Law on Examination

While the path taken to final adoption of one model may differ from that taken for another, it may be instructive to follow in detail the adoption of one model that has been included in the NAIC's Financial Regulation Standards in order to give the Subcommittee a flavor for the process. To that end, I have selected the Model Law on Examination as my example, both because it is recent and because it involves a key component of solvency regulation.

The Committee on Examination Processes, which reports to the NAIC's Executive Committee, was created in 1990 to address directly the charge of the Solvency Policing Agenda to assess and improve the insurance company examination process. During 1990, the Committee held public hearings in Salt Lake City, Utah, Scottsdale, Arizona, Orlando, Florida, Chicago, Illinois, and Boston, Massachusetts. During the course of these hearings, the Committee received testimony from 9 insurance commissioners, 16 insurance department staff members, 9 insurance industry trade associations, 16 insurance companies or groups, and 3 "Big 6" accounting firms.

In the course of its work, the Committee also reviewed five major reports which, at least in part, address the question of the adequacy of the state regulatory process with regard to the examination of insurance companies:

- Strengthening the Surveillance System, McKinsey & Company (1974);
- A 1982 report by the NAIC Special Joint COmmittee on Examinations (Bell-Budd);
- Insurance Regulation: Problems in the State Monitoring of Property/Casualty Insurer Insolvency, U.S. General Accounting Office (1989);
- Insurer Solvency: Public Policy Recommendations for Improvement, National Association of Independent Insurers (NAII) Task Force on Solvency (1989);
- Failed Promises, Subcommittee on Oversight and Investigations of the House Energy and Commerce Committee (1990).

During the course of the hearings, it became clear to the Committee that there were a number of areas of agreement among all the witness about needed improvements in the examination process. These areas, while touching upon nearly every phase of the process, addressed rather narrow issues of each phase. In short, the necessary improvements included:

- The scheduling of examinations of companies should be made more flexible, in order to allow regulators to focus resources more flexible, in order to allow regulators to focus resources on companies most in need of regulatory attention.

- Improving the examination planning process in order to insure timely responses by insurer personnel to requests for information and to increase the efficient use of time by examiners.
- Enhancing the conduct of examinations in order to more efficiently focus regulatory resources on material information, particularly the management and operational aspects of insurers.
- Tightening the administrative process involved in examinations in order to improve the timeliness of various aspects of the examination process, particularly the preparation of the report of examination.
- Establishing a process that is better designed to attract and retain competent examiners.
- Improving coordination of examinations through efforts at the state insurance department level and by increasing the role of the NAIC in such coordination.

By September, the Committee had enough information to generate a lengthy report outlining the concerns expressed during the hearing process. That report led to the development of a Model Law in December 1990, and the inclusion of the Model Law in the Financial Regulation Standards.

Even though, under the Accreditation Program I have outlined, this Model will not be required for certification under the NAIC's minimum solvency regulation standards until December 1993, it already has been introduced in seven states, and adopted by one of those states.

C. An Example of the Model Law Adoption Process of a Model Not in the Financial Regulation Standards: the Model State Insurance Department Funding Bill

As I have already mentioned, NAIC Model Laws and Regulations that have not been designated as part of the Financial Regulation Standards promote uniformity by providing suggested language for legislation. On such model is the Model State Insurance Department Funding Bill.

As the 1980s dawned, the NAIC began the process of taking a fresh look at itself, particularly from the perspective of establishing organizational priorities. After nearly two years of work, the Executive (EX) Committee adopted, in February 1981, a list of 47 NAIC projects. Topping that prioritized list was the development of approaches to enhanced funding of state insurance departments. The NAIC adopted this list of priorities, with enhanced funding still at the top of the list, in June of that year.

In the Spring of 1982, a survey of the state insurance departments confirmed that a major concern of regulators was the adequacy of departmental funding. In June 1982, a subgroup of the newly-created Inter-Departmental Resources (EX1) Task Force was created to look into alternative methods of funding insurance departments with the intent of drafting a model bill. The minutes of the Task Force reflect at this point that the model was not intended for universal adoption by the states. This subgroup conducted a thorough examination of state insurance department resources and existing funding systems, which was presented in September 1982. That examination revealed a wide diversity in funding mechanisms and financial need of the various departments.

By March 1983, a draft model bill had been prepared, and was presented to the Task Force for discussion. The Task Force heard statements from a wide range of trade associations, most of which objected to a number of components of the Model. Nevertheless, the Model was approved by the Task Force, and subsequently adopted by the NAIC in June of that year, over those objections.

The Model creates a special trust fund, dedicated to the functioning of the insurance department, into which all monies from a variety of regulatory activities, to be specified by the individual states, would be deposited. While only four states have adopted the Model, the basic concept of dedicated funding, embodied in the model, is quite widespread, with 21 states operating with dedicated funding and another 15 with quasi-dedicated funding.

V. CONCLUSION

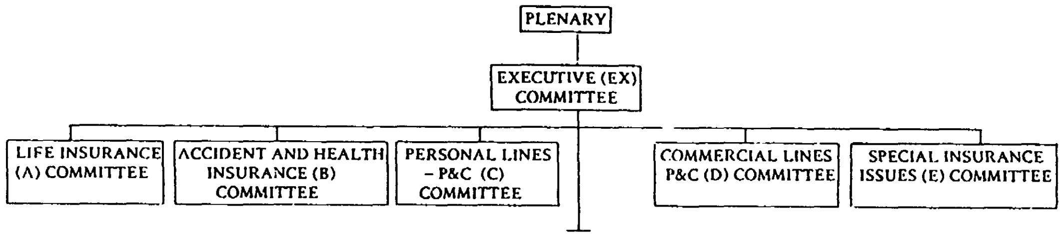
In short, NAIC Model Laws and Regulations have served a variety of valuable functions in state insurance regulation, answering two basic questions:

- "If this state were to regulate in this area, what should that regulation look like?" and
- "What should minimum national regulatory standards be, and how can we put them in place?"

As I have said, I am proud of the role of the NAIC in the development of sound regulatory policy. We appreciate the Subcommittee's interest in this area, and will be happy to provide any information you desire as you continue your study of this and other insurance regulation issues.

ATTACHMENT A

NAIC ORGANIZATIONAL STRUCTURE



(EX1) Internal Administration

(EX2) Zone Coordination

(EX3) Market Conduct and Consumer Affairs

(EX4) Financial Condition

ATTACHMENT B

DRAFT: 4/1/91

NAIC 1991 COMMITTEE, SUBCOMMITTEE & TASK FORCES

EXECUTIVE (EX) COMMITTEE

William H. McCartney, Chair	Nebraska
Earl R. Pomeroy, Vice Chair	North Dakota
Jim Long, President	North Carolina
Robin Campaniano, Recording Secretary	Hawaii

NORTHEASTERN ZONE

Constance B. Foster, Chair	Pennsylvania
Jeffrey Johnson, Vice Chair	Vermont
Salvatore R. Curiale, Secretary	New York

SOUTHEASTERN ZONE

Steven T. Foster, Chair	Virginia
Elaine A. McReynolds, Vice Chair	Tennessee
Tom Gallagher, Secretary	Florida

MIDWESTERN ZONE

Mary Jane Cleary, Chair	South Dakota
John J. Dillon, III, Vice Chair	Indiana
David J. Lyons, Secretary	Iowa

WESTERN ZONE

Harold C. Yancey, Chair	Utah
Andrea Bennett, Vice Chair	Montana
(Vacant) Secretary	

SSO Support Staff: David B. Simmons/Sandra L. Gilfillan

Mission Statement:

The Executive Committee shall have the responsibility to make recommendations to achieve the goals of the NAIC based upon either its own initiative or the recommendations of the Standing Committee or Subcommittees reporting to it; manage the affairs of the NAIC in a manner consistent with the Constitution and By-Laws; create and terminate one or more Task Forces reporting to it to the extent needed; to approve, disapprove, appoint or terminate an advisory committee or board reporting to it; establish and allocate functions and responsibilities to be performed by each Zone; oversee in accordance with the By-Laws, a Support and Services Office to assist the NAIC and the individual members in achieving the goals of the NAIC; submit to the NAIC at each National Meeting its report and recommendations concerning the reports of the Standing Committees; plan implement and coordinate communications and activities with other state, federal and local government organizations in order to advance the goals of the NAIC and promote understanding of state insurance regulation.

Working Groups

Consumer Participation Working Group

William H. McCartney	Nebraska
Jim Long	North Carolina
Earl R. Pomeroy	North Dakota

1991 Charge:

1. Meet periodically with consumer groups to facilitate dialogue and to encourage input and participation in the NAIC process by such group.

Advisory Organization Activities Working Group

William H. McCartney, Chair	Nebraska
Tom Gallagher, Vice Chair	Florida
Joseph A. Edwards	Maine
Gary Weeks	Oregon
Mary Jane Cleary	South Dakota
Harold C. Yancey	Utah

SSO Support Staff: Robert Klein

1991 Charge:

1. Monitor and coordinate implementation of loss cost system by states in property/casualty lines including workers' compensation.

2. Provide oversight for the examination of the National Council on Compensation Insurance.

(EX) Committee on Financial Regulation and Accreditation

Earl R. Pomeroy, Chair	North Dakota
Jim Long, Vice Chair	North Carolina
John Garamendi	California
Tom Gallagher	Florida
Jim Schacht	Illinois
William H. McCartney	Nebraska
Louis E. Bergeron	New Hampshire
Salvatore Curiale	New York
Steven T. Foster	Virginia

EXECUTIVE (EX) COMMITTEE (CONT'D)

(EX) Committee on Financial Regulation and Accreditation (Cont'd)

1991 Charge:

1. Continue and strengthen the financial regulation standards and the accreditation program.
2. Assist states in implementation of regulations and statutes required for compliance with the standards.

SSO Support Staff: Bruce Schowengerdt

(EX) Committee on McCarran Ferguson Act

Robin Campaniano, Chair	Hawaii
David Walsh	Alaska
Tom Gallagher	Florida
Tim Ryles	Georgia
Salvatore R. Curiale	New York
Jim Long	North Carolina
Earl R. Pomeroy	North Dakota
Constance B. Foster	Pennsylvania

SSO Support Staff: Kevin Cronin/Sandra L. Gilfillan

(EX) Committee on Credit Insurance

Jeffrey Johnson, Chair	Vermont
Steven T. Foster, Vice Chair	Virginia
John Garamendi	California
Tom Gallagher	Florida
Tim Ryles	Georgia
Jim Schacht	Illinois
Dominic A. D'Annunzio	Michigan
Lewis Melahn	Missouri
Terry Rankin	Nevada
Louis E. Bergeron	New Hampshire
Salvatore R. Curiale	New York
Harold C. Yancey	Utah

SSO Support Staff: Robert Klein/David B. Simmons

1991 Charge:

1. Review data reported by insurers on the Credit Life and Accident and Health Experience Exhibit and filed with state insurance departments and the NAIC to assure the accuracy of the data and assess trends in the industry at the state and national level. Consider improvements to the credit insurance exhibit, with input from the actuarial task forces, and recommend revisions to the Blanks (EX4) Task Force for adoption.

(EX) Committee on Credit Insurance (Cont'd)

2. Propose mechanisms for state insurance departments to assess the loss ratio performance of credit insurers and maintain that performance at adequate levels, review existing loss ratio standards to determine whether higher standards are required, and appropriate, develop measures to ensure compliance with the standards.

3. Evaluate and report on the market conduct of credit insurers, with particular emphasis on: adequacy of disclosure to consumers; tying arrangements; marketing of credit insurance by unlicensed agents; post-claim underwriting practices; and other significant marketing issues.

4. Examine all credit insurance products offered by insurers with an emphasis on evaluating the products' suitability for consumers. Evaluate and consider regulatory provisions for credit property insurance.

5. Conduct other research to accomplish the goal of establishing a fair and rational marketplace for credit insurance products.

6. Develop an implementation and technical assistance program outlining regulatory provisions for state departments to assist them in improving credit insurance.

Working Groups

Pricing and Data Reporting Working Group
of the (EX) Committee on Credit

Jeffrey Johnson, Chair	Vermont
John Garamendi	California
Tom Gallagher	Florida
Tim Ryles	Georgia
Jim Schacht	Illinois
Dominic A. D'Annunzio	Michigan
Fabian Chavez	New Mexico
Salvatore R. Curiale	New York
Harold T. Duryee	Ohio
Harold C. Yancey	Utah
Steven T. Foster	Virginia

Market Practices Working Group
of the (EX) Committee on Credit

Lewis Melahn, Chair	Missouri
John Garamendi	California
Dominic A. D'Annunzio	Michigan
Terry Rankin	Nevada
Louis E. Bergeron	New Hampshire
Earl R. Pomeroy	North Dakota

EXECUTIVE (EX) COMMITTEE (CONT'D)

War Time Exclusion Working Group

Steven T. Foster, Chair	Virginia
David Walsh	Alaska
Jim Long	North Carolina
John G. Richards	South Carolina
Harold C. Yancey	Utah

SSO Support Staff: David B. Simmons

<u>1991 Charge</u>:

1. Continue to monitor practices of companies in regard to wartime exclusions on life insurance policies.

2. Review and monitor practices of companies regarding reinstatement of property and casualty coverages which have lapsed while individuals are on active military duty.

3. Address health insurance issues confronting those who return from active duty.

(EX) Special Committee on Alien Insurance

Jim Schacht, Chair	Illinois
David N. Levinson	Delaware
Tom Gallagher	Florida
John J. Dillon III	Indiana
Fabian Chavez	New Mexico
Salvatore R. Curiale	New York
Steven T. Foster	Virginia

(EX) Special Committee on Guaranty Funds and Liquidations

John J. Dillon III, Co-Chair	Indiana
Jim Long, Co-Chair	North Carolina
John Garamendi	California
Tom Gallagher	Florida
Jim Schacht	Illinois
Willma H. McCartney	Nebraska
Earl R. Pomeroy	North Dakota
Salvatore R. Curiale	New York
Steven T. Foster	Virginia

(EX) Ad Hoc Committee on Solvency

Susan Gallinger	Arizona
David N. Levinson	Delaware
Tom Gallagher	Florida
Tim Ryles	Georgia

EXECUTIVE (EX) COMMITTEE (CONT'D)

(EX) Ad Hoc Committee on Solvency Cont'd)

Robin Campaniano	Hawaii
Ron Todd	Kansas
George Neumayer	Idaho
Jim Schacht	Illinois
John J. Dillon III	Indiana
John A. Donaho	Maryland
Andrea Bennett	Montana
Earl R. Pomeroy	North Dakota
Fabian Chavez	New Mexico
Salvatore R. Curiale	New York
Constance Foster	Pennsylvania
John G. Richards	South Carolina
Philip W. Barnes	Texas
Steven T. Foster	Virginia
Robert D. Haase	Wisconsin
Kenneth Erickson	Wyoming

FINANCIAL SERVICES AND INSURANCE REGULATION (EX) TASK FORCE

David J. Lyons, Chair	Iowa
Elaine A. McReynolds, Vice Chair	Tennessee
Susan Gallinger	Arizona
Joaquin G. Blaz	Guam
Ron Todd	Kansas
John A. Donaho	Maryland
Susan K. Scott	Massachusetts
Jim Long	North Carolina
Philip W. Barnes	Texas
Jeffrey Johnson	Vermont
Robert D. Haase	Wisconsin

SSO Support Staff: Ellen Dollase/Carolyn J. Johnson

Mission Statement:

The Financial Services and Insurance Regulation (EX) Task Force shall study the impact on the NAIC of the current trends towards the integration of financial services and determine the most effective method of state regulation of insurance in light of a changing environment and pressures for the integration of financial services institutions and products. Additionally, the Task Force will monitor the relationship and activities between federal state securities laws and insurance regulation.

1991 Charge:

1. Monitor changes in federal regulation of financial planners and the effects on state regulation of insurance.

2. Draft memorandum on conflicts between federal and state law regarding financial services.

3. Analyze and consider possible amendment of NAIC models on annuities in light of recent changes in law and practice.

4. Explore the need for dialogue with federal and state banking regulators in areas of solvency regulation, access to records, and impact on guaranty fund if banks continue to expand into the insurance arena.

Liaison Committee

Lee Polson	North American Securities Administrators Assoc., Inc.
Bob Richard	Conference of State Bank Supervisors
A. John Taylor	National Assoc. of Securities Dealers, Inc.
John D. Seymour	American Council of State Savings Supervisors

INTERNAL ADMINISTRATION (EX1) SUBCOMMITTEE

Jim Long, Chair	North Carolina
William H. McCartney, Vice Chair	Nebraska
Susan Gallinger	Arizona
Robin Campaniano	Hawaii
Salvatore R. Curiale	New York
Earl R. Pomeroy	North Dakota
Steven T. Foster	Virginia

SSO Support Staff: Sandra L. Gilfillan/Judith P. Lee

Mission Statement:

The subcommittee shall periodically monitor operations of the SSO including preparing a budget for Executive Committee review, approving emergency expenditures, evaluating the Executive Vice President and assisting the Executive Vice President in resolving competing demands for staff resources.

1991 Charge:

1. Oversee the completion and release of the Property & Casualty Cycle.

2. Establish priorities for the NAIC's Management Information System (MIS) resources. As part of this process the subcommittee should review and approve current iteration of the MIS strategic plan. The MIS strategic plan should be prepared with consideration of technical input from the Data/Systems Management (EX4) Task Force and other affected NAIC entities.

3. Consider funding for recommendations of Solvency Policing Agenda.

EDUCATION, RESEARCH AND TRAINING (EX1) TASK FORCE

Steven T. Foster, Chair	Virginia
Harold C. Yancey, Vice Chair	Utah
Margurite C. Stokes	District of Columbia
Tom Gallagher	Florida
Joaquin G. Blaz	Guam
George Neumayer	Idaho
John A. Donaho	Maryland
William H. McCartney	Nebraska
Constance B. Foster	Pennsylvania
Philip W. Barnes	Texas
Kenneth Erickson	Wyoming

SSO Support Staff: Iris Elfenbein/Judith P. Lee

Mission Statement:

The Education, Research and Training (EX1) Task Force shall propose, develop and implement appropriate training and educational opportunities for insurance commissioners and their staffs, including monitoring and refining the Commissioners Education Program, the Staff Education Program, and the Financial Examiners Program. They shall also propose, develop and implement special seminar and forum offerings on significant insurance issues.

1991 Charge:

1. Oversee the revision and delivery of the Commissioners Education Program and the Financial Examiners Program.

2. Monitor the delivery of all insurance regulator's educational programs.

3. Review and refine an outline of basic knowledge and skills essential for all regulators, which will serve as the basis for a generic insurance regulators curriculum. The curriculum will lead to the development of independent study courses and/or an insurance regulators' designation.

Supplemental Charge From the Recommendations of the Committee on Exam Processes:

4. Direct the NAIC Education Manager, under the auspices of the Task Force to prioritize future financial condition examination training needs, including the development of classes for more experienced examiners and the offering of training classes on a regional basis, and to recommend a schedule for implementation.

Supplemental charge from the NAIC Solvency Agenda for 1991:

5. Develop and implement intermediate to higher level training courses for financial analysts, financial auditors and financial regulators with decision making and policy setting responsibilities.

EDUCATION, RESEARCH AND TRAINING (EX1) TASK FORCE (Cont'd)

Supplemental charge from meeting with the Insurance Regulatory Examiners Society:

6. Direct the NAIC Education manager to cooperate and coordinate with the Insurance Regulatory Examiners Society in the development of a training program for market conduct examiners.

Working Group

Commissioners Program Working Group

Steve Foster, Chair	Virginia
Margurite C. Stokes	District of Columbia
George Neumayer	Indiana
Tom Gallagher	Florida
John A. Donaho	Maryland
William H. McCartney	Nebraska
Kenneth Erickson	Wyoming

ZONE COORDINATION (EX2) SUBCOMMITTEE

Jim Long, Chair	North Carolina
Earl R. Pomeroy, Vice Chair	North Dakota
Louis E. Bergeron	New Hampshire
Constance B. Foster	Pennsylvania
Mary Jane Cleary	South Dakota
Harold C. Yancey	Utah
Steven T. Foster	Virginia

SSO Support Staff: Miriam Hennosy/Sandra L. Gilfillan

Mission Statement:

1991 Charge:

1. Schedule and coordinate all Zone meetings where NAIC committees, subcommittees and task forces are invited or permitted to attend.

2. Coordinate interim meetings by designating a set of dates and sites for committees, subcommittees, task forces and/or working groups to meet between Zone and National meetings.

3. Select sites for national and annual meetings of the NAIC.

4. Determine criteria and categories for registrants at NAIC meetings.

MARKET CONDUCT AND CONSUMER AFFAIRS (EX3) SUBCOMMITTEE

Lewis Melahn, Chair	Missouri
Andrea Bennett, Vice Chair	Montana
Mike Weaver	Alabama
John Garamendi	California
Tim Ryles	Georgia
Jim Schacht	Illinois
William H. McCartney	Nebraska
Harold C. Yancey	Utah
Steven T. Foster	Virginia

SSO Support Staff: Art Chartrand

Mission Statement:

The Market Conduct Consumer Affairs (EX3) Subcommittee is to review and make recommendations regarding the market behavior of insurers and producers as that behavior affects insurance consumers. The subcommittee also serves as a forum to challenge, refine or improve concepts concerning the examination of insurance company market activities as developed by the standing Market Conduct Examination Oversight Task Force.

1991 Charge:

1. Consider development of criteria for market conduct standards and review for integration with NAIC accreditation of state insurance departments. (New Charge)

2. Monitor market conduct database developments including RIRS, SAD, and the nationwide complaint database with Data/Systems Management Task Force.

3. Study and make recommendations regarding consumer groups fronting as leads or advertising agencies for insurance companies.

4. Study and make recommendations regarding the automobile extended warranty and service contract industry.

5. Develop NAIC Model Disaster Preparedness Program.

6. Finalize NAIC position regarding the earthquake project in conjunction with the Commercial Lines (D) Committee and Personal Lines (C) Committee.

7. Review the relationship between NAIC Model Unfair Trade Practices Act and existing status of state Unfair Trade Practices Regulations and make recommendations as appropriate.

Working Group

Subgroup on Market Conduct Annual Statement

Dick Rogers, Chair	Illinois

MARKET CONDUCT EXAMINATION OVERSIGHT (EX3) TASK FORCE

Jeffrey Johnson, Chair	Vermont
Jim Long, Vice Chair	North Carolina
John Garamendi	California
Joanne Hill	Colorado
Jim Schacht	Illinois
Ron Todd	Kansas
Lewis Melahn	Missouri
William H. McCartney	Nebraska
Terry Rankin	Nevada
Salvatore R. Curiale	New York
Philip W. Barnes	Texas

SSO Support Staff: Arthur J. Chartrand

Mission Statement:

This task force shall become a standing committee as provided for in the NAIC Bylaws, Section 3. The mission of the task force is to monitor all aspects of the market conduct examination process. This includes the identification, investigation, and development of solutions to problems arising related to market conduct examinations. The task force will propose changes to the market conduct section of the NAIC Examiners' Handbook. The task force will monitor the coordination of examinations and market surveillance and foster multi-state communication. This includes the development of market data, computer applications and other resources for monitoring market conduct behavior. The task force will also establish procedures for the flow of information between both market conduct and financial examiners for the identification of troubled companies and for the coordination of appropriate examination schedules and examination methods.

1991 Charge:

1. Monitor the market conduct examination process and the effectiveness of current practices.
2. Establish a Market Conduct Standards Review Committee for the purpose of promoting adequate and fair market conduct examination practices.
3. Study the utility of a standardized, automated market conduct report for electronic filing with the NAIC.
4. Work with [Financial] Examination Oversight (EX4) Task Force and NAIC staff to update the NAIC Exam Call System.
5. Provide recommendations for NAIC sponsored training programs for market conduct examiners.
6. Conduct regulators only forums on specific companies identified with market conduct concerns.
7. Continue development of market conduct annual statement.
8. Develop a concensus on new examination methodologies.

MARKET CONDUCT EXAMINATION OVERSIGHT (EX3) TASK FORCE (Cont'd)

7. Review, monitor and implement computer audit software in association with examinations and training of examiners including cost reviews and sharing of applications.

8. Provide recommendations on NAIC data base enhancements on troubled companies and sharing of market conduct information.

9. Review annual salary increases for market conduct examiners for amendment to the Market Conduct Examiners Handbook for recommendation to EX3 Subcommittee 30 days prior to December National Meeting each year.

FINANCIAL CONDITION (EX4) SUBCOMMITTEE

William H. McCartney, Chair	Nebraska
Philip W. Barnes, Vice Chair	Texas
John Garamendi	California
David N. Levinson	Delaware
Tom Gallagher	Florida
Jim Schacht	Illinois
David J. Lyons	Iowa
John J. Dillon III	Indiana
Terry Rankin	Nevada
Louis E. Bergeron	New Hampshire
Salvatore R. Curiale	New York
Earl R. Pomeroy	North Dakota
Steven T. Foster	Virginia

SSO Support Staff: Bruce Schowengerdt

Mission Statement:

The mission of this subcommittee is to be the central forum and coordinator of solvency related considerations of the NAIC as it relates to accounting practices and procedures, blanks, valuation of securities, the Insurance Regulatory Information System (IRIS), solvency and profitability, Zone Examinations, financial examinations and examiner training, guaranty funds and rehabilitation and liquidation. In addition, the subcommittee interfaces with the Technical Services Subcommittees.

1991 Charge:

1. Monitor the activity of the Sale of Future Revenue/Securitization of Nonadmitted or Unrecorded Assets Working Group to study and develop statutory position on capital enhancement transactions.

2. Monitor the development of an NAIC position and/or model addressing insurer investments in high yield securities by the High Yield Securities Working Group.

3. Monitor the activity of the High Yield Securities Working Group to conform the ratings of preferred stocks to the method currently used by the SVO to rate bonds.

4. Monitor the activity of the Examination Model Law Working Group to consider enhancements or clarifications necessary regarding the authority to call and conduct special association examinations as outlined in the Examiners Handbook.

5. Develop a Model Law on Investments.

6. Determine whether the SVO has the necessary resources to assist states in analyzing and valuing insurer investments.

7. Survey insurers to determine the extent of investment in real estate related assets and develop a monitoring mechanism for those insurers with a high level of investments in this area.

FINANCIAL CONDITION (EX4) SUBCOMMITTEE (Cont'd)

8. Encourage states to hire a computer audit specialist (the Society of Financial Examiners is currently evaluating administering/sponsoring a new designation for a computer audit specialist in addition to the CFE/AFE designations).

9. Initiate or support and encourage other NAIC efforts to address the critical need for the availability of greater expertise in the form of specialists to enhance regulatory capabilities to examine computer based operations; evaluate loss reserves and underlying data; analyze reinsurance arrangements and measure their value; and perform other specialized solvency policing tasks that require special training and experience.

<u>Working Groups</u>

Sale of Future Revenue/Securitization of Nonadmitted or Unrecorded Assets Working Group

Leon Hank, Chair	Michigan
Norris Clark	California
John Montgomery	California
Larry Gorski	Illinois
James Hanson	Illinois
Windell Clark	Kentucky
James Oetting	Missouri
Robert Solitro	New Hampshire
Robert J. Callahan	New York
Terry Lennon	New York
Ted Becker	Texas

SSO Support Staff: Jean Olson

Sale of Future Revenue/Securitization of Nonadmitted or Unrecorded Assets Advisory Committee

Richard A. Hemmings	Lord, Bissell & Brook
Cecelia Kempler	LeBoeuf, Lamb, Leiby & MacRae
William Carroll	American Council of Life Insurers
Roy Woodall	National Assoc. of Life Companies
Dan Kunesh	Tillinghast
Charles B. Friedstat	Ernst & Young
Ransom B. Jones	Goldman, Sachs & Co.
Donald W. Seely	Lincoln National
Karen McDonald	Transamerica
Kevin S. King	A.L. Williams
Dominick Agostino	Citibank
Harris Bak	Chase Manhattan Bank
Bruce Winterhof	Millman & Robertson
Diane Wallace	DB Wallace Company
William P. Hannon	Peat Marwick
Ralph Milo	Clarendon National Ins. Company
G. William Boyd	Lyndon Insurance Group
T. Lawrence Jones	Hunton & Williams
Peter W. Gillies	LeBoeuf, Lamb, Leiby & MacRae
Robert E. Schaaf	Insurance Management Services, Inc.

ACCOUNTING PRACTICES AND PROCEDURES (EX4) TASK FORCE

John Garamendi, Chair	California
Jim Schacht, Vice Chair	Illinois
David Walsh	Alaska
Susan Gallinger	Arizona
David N. Levinson	Delaware
Tom Gallagher	Florida
David J. Lyons	Iowa
Elizabeth P. Wright	Kentucky
Hunter O. Wagner, Jr.	Louisiana
John A. Donaho	Maryland
Joseph A. Edwards	Maine
Susan K. Scott	Massachusetts
Dominic A. D'Annunzio	Michigan
Lewis A. Melahn	Missouri
Andrea Bennett	Montana
William H. McCartney	Nebraska
Louis E. Bergeron	New Hampshire
Samuel F. Fortunato	New Jersey
Salvatore R. Curiale	New York
Harold T. Duryee	Ohio
Gary Weeks	Oregon
Constance B. Foster	Pennsylvania
Miguel A. Villafane	Puerto Rico
Elaine A. McReynolds	Tennessee
Harold C. Yancey	Utah
Robert D. Haase	Wisconsin

SSO Support Staff: Bruce Schowengerdt

Mission Statement:

The mission of the task force is to identify, investigate, and develop solutions to accounting problems with the ultimate goal of guiding insurers in properly accounting for various aspects of their operations and to modify the accounting manual to reflect changes necessitated by Task Force action or federal tax laws, and to study innovative insurer accounting practices which affect the ability of regulators to determine the true financial condition of insurers.

1991 Charge:

1. Enhance annual statement disclosure by providing for greater information on material transactions.

2. Continue evaluation in the areas of non-transfer of risk, surplus relief, reinsurance contracts and financial reinsurance contracts and develop or refine the appropriate statutory accounting standards for these transactions.

3. Monitor the activity of the life and property and casualty study groups to evaluate existing statutory accounting principles as presently outlined in the Accounting Practices and Procedures Manual for purposes of further development, expansion and codification.

ACCOUNTING PRACTICES AND PROCEDURES (EX4) TASK FORCE (Cont'd)

4. Monitor the activity of the Emerging Accounting Issues Working Group to provide authoritative guidance to insurance regulators on current statutory accounting issues.

5. Monitor the progress of the Accounting and Reporting of Deposit Type Business to determine the proper reporting of certain types of contracts including deferred annuities, deposit administration contracts and guaranteed annuity contracts.

6. Monitor the activity of the study group formed to review the reporting of property and casualty deficiency reserves in the annual statement.

Working Groups

Emerging Issues Working Group

Norris Clark, Chair	California
James Hanson	Illinois
Leon Hank	Michigan
Vincent Laurenzano	New York
Ron Newton	Texas
Randy Blumer	Wisconsin

Emerging Issues Advisory Committee

Patrick Kenny	Aetna Life and Casualty
Daniel Plummer	Alliance of American Insurers - Consultant
John Baily	Coopers & Lybrand
Katherine A. Mason	The Equitable Financial Companies
Wayne Kauth	Ernst & Young
Ransom B. Jones	Goldman, Sachs & Co.
Harris Chorney	KPMG Peat Marwick
Peter Storms	The Travelers Insurance Co.

1991 Charge:

1. To assist Emerging Issues Working Group in identifying and addressing emerging statutory insurance accounting issues.

Premium Deficiency Reserve (EX4) Working Group

Robert Gossrow, Chair	Illinois
Kevin Conley	Iowa
Edwin Jordan	North Carolina
Anne Kelly	New York
Alan E. Wickman	Nebraska

ACCOUNTING PRACTICES AND PROCEDURES (EX4) TASK FORCE (Cont'd)

Premium Deficiency Reserve Advisory Committee

Thomas Ward	NAII
George McGann	Allstate Insurance Company
Michael Olson	State Farm Mutual Ins. Co.
Phillip Schwartz	AIA
Wayne D. Holdredge	Tillinghast/Towers Perrin
James Anastasio	American Re-Insurance Company
Terrence O'Brien	Coopers & Lybrand
Ronald J. Zaleski	Maryland Casualty Companies
Edmond F. Rondpierre	General Reinsurance Corporation
Daniel Plummer	Alliance (Consultant)
Samuel Licitra	Virginia Surety Co., Inc.
Edward Fisher	Munich American Reinsurance Co.

Property & Casualty Reinsurance Advisory Committee

George McGann	Allstate
James Anastasio	American Reinsurance Company
David Holman	Ernst & Whinney
Bob Graham	General Reinsurance
Anne Sharp	Kemper Reinsurance
Edward Fischer	Munich American Reinsurance
James Godorecci	CIGNA
John T. Clark	Alpine Insurance Company
Ed Bader	Arthur Andersen
Carolyn Cobb	ACLI
Phillip Schwartz	AIA
James M. Shamberger	Reinsurance Association of America
Richard Hefferan	Alliance of American Insurers
Thomas Ward	National Assoc. of Independent Insurers
William L. McDonough	American International Group Inc.

1991 Charge:

1. To provide reference and technical expertise on matters before the Study Group.

BLANKS (EX4) TASK FORCE

Louis E. Bergeron, Chair	New Hampshire
Tom Gallagher, Vice Chair	Florida
David Walsh	Alaska
John Garamendi	California
George Neumayer	Idaho
Jim Schacht	Illinois
David J. Lyons	Iowa
Elizabeth P. Wright	Kentucky
Hunter O. Wagner, Jr.	Louisiana
Joseph A. Edwards	Maine
Susan K. Scott	Massachusetts
Dominic A. D'Annunzio	Michigan
Bert J. McKasy	Minnesota
George Dale	Mississippi
Lewis Melahn	Missouri
Andrea Bennett	Montana
William H. McCartney	Nebraska
Samuel F. Fortunato	New Jersey
Terry Rankin	Nevada
Salvatore R. Curiale	New York
Jim Long	North Carolina
Harold T. Duryee	Ohio
Gary Weeks	Oregon
Elaine A. McReynolds	Tennessee
Philip W. Barnes	Texas
Harold C. Yancey	Utah
Jeffrey Johnson	Vermont
Richard G. Marquardt	Washington
Robert D. Haase	Wisconsin

SSO Staff Support: Glenda Channel/Terry Boyer

Mission Statement

The mission of the task force is to consider changes to the various blanks and to conform these blanks to changes made in other areas of the NAIC in order to promote uniformity in reporting of financial information by insurers, to develop reporting formats for other entities subject to the jurisdiction of the state insurance departments; to conform the various NAIC blanks and books of instructions (P/C, L/A&H, Fraternal, HMDI, CCRC, Title, and HMO) to adopted NAIC policy; and, to oversee the development of additional reporting formats within the existing annual statements, as needs are identified.

1991 Charges:

1. Monitor and address changes in the industry related to accounting and reporting requirements for insurance companies through the Financial Reporting Working Group.

2. Develop a separate reporting form to gather additional information related to Universal Life products through the Financial Reporting Working Group.

BLANKS (EX4) TASK FORCE (Cont'd)

3. Explore the feasibility, through the Financial Reporting Working Group, of standardizing reporting formats between states to the extent possible by gathering and analyzing the forms currently utilized.

4. Conform the various NAIC annual statement instructions to current accounting and reporting requirements via the Annual Statement Instructions Working Group.

5. Revise and reformat the Hospital, Medical and Dental Service or Indemnity Corporations blank and develop a separate reporting form to be used by limited health care services, i.e., prepaid dental and vision plans through the HMDI Working Group.

6. Improve annual statement disclosure by adding a new section entitled "Managements Discussion and Analysis of Financial Condition and Results of Operations" through the Management's Discussion of Results of Operations Study Group.

7. Consider the feasibility of using bar codes on annual statements and all related filings for purposes of tracking these filings with the states and the NAIC through the Bar Code Working Group.

8. Develop revisions to Schedule D related to groupings of securities and related issues through the Schedule D Working Group.

9. Develop changes to the IEE and P/C blank, through the Insurance Expense Exhibit Working Group, to improve reporting of statistical information.

10. Develop a separate reporting format, through the Reporting Format for Financial Guaranty and Mortgage Guaranty Study Group, for those companies writing only financial guaranty or mortgage guaranty lines of business.

11. Develop a reporting format for purposes of requiring the restatement of the balance sheet and the income statement on a direct basis and develop abbreviated reinsurance schedules to accompany these.

12. Develop a form for purposes of reporting directors and key officers of insurance companies, through the Biographical Data Form Working Group.

<u>Working Groups</u>

Reinsurance Working Group

Arnold Dutcher, Chair	Illinois
Sheldon Summers	California
Ron Newton	Texas
Randy Blumer	Wisconsin

BLANKS (EX4) TASK FORCE (Cont'd)

Reinsurance Advisory Committee

Phillip Schwartz	American Insurance Association
Rob Graham	General Reinsurance Corp.
James M. Shamberger	Reinsurance Association of America
Peter F. Storms	Statutory Financial Standards
Roy Woodall	National Association of Life Companies
William D. Ward	Aetna Life & Casualty Ins. Co.
John T. Clark	Alpine Insurance Company
William Carroll	American Council of Life Insurance
Charles Wittenberg	Wolfman & Moscovitch, Inc.
Charles McGann	Allstate Insurance Company
James A. Godorecci	Cigna Corporation
Michael Olson	State Farm Mutual
Tom Ward	National Association of Independent Insurers
Jim Mack	National Assoc. of Mutual Ins. Cos.
Burton I. Henry	Constitution Reinsurance Corp.
Linda Dougherty	Prudential Insurance Company
Dan Plummer	Alliance of American Insurers - Consultant

1991 Charge:

1. To assist regulators in drafting proposed changes to the Annual Statement Blank regarding reinsurance disclosure.

Schedule D Working Group

Ron Newton, Chair	Texas
Jim Hanson	Illinois
Terence Lennon	New York

Schedule D Advisory Committee

William Ward	Aetna
Phillip Schwartz	AIA
William Carroll	ACLI
Richard Hefferan	Alliance
Tom Ward	NAII
Linda Dougherty	Prudential
Jim Shamberger	RAA

BLANKS (EX4) TASK FORCE (Cont'd)

Insurance Expense Exhibit Working Group

Windell Clark, Co-Chair	Kentucky
Martin Simons, Co-Chair	South Carolina
Richard Roth	California
Robert Gossrow	Illinois
Donald Wulf	Illinois
Kevin Conley	Iowa
Alan Wickman	Nebraska
Terry Rankin	Nevada
Martin Rosenberg	New Jersey
Anne Kelly	New York
David Eley	Texas
Ron Newton	Texas

SSO Support Staff: Robert Klein/Dan Atkisson/Glenda Channel

1991 Charge:

1. Review the Insurance Expense Exhibit for any changes necessary to promote accurate and useful reporting of statistical information by line of business. Coordinate changes on this form with the appropriate changes to the P&C annual statement blank.

Insurance Expense Exhibit Advisory Committee

Phillip Schwartz	American Ins. Association
Bill Ward	Aetna
Dick Hefferan	Alliance
Carol Banfield	Insurance Services Office
Dave Conrad	National Independent Statistical Service
Michael Dolan	National Council on Compensation
William Ward	Aetna
Michael Dolan	National Council of Compensation Insurance
Newell Hart	IMT Insurance Company
Thomas J. Kozik	Allstate
Dan Plummer	Alliance of American Insurers - Consultant
Tom Ward	National Association of Independent Insurers
Wade E. Harrell	Liberty Mutual Insurance Company
Linda Dougherty	Prudential
Carole Banfield	Insurance Services Office
Edward Fischer	Munich American Reinsurance
Jerry Scheibl	Wasau Insurance Companies

1991 Charge:

1. To provide input to the Working Group as respects its analysis and development of revisions to the Insurance Expenses Exhibit.

BLANKS (EX4) TASK FORCE (Cont'd)

Bar Code Working Group

Robert Stern, Chair	New York
Tom Porter	Florida
Jack Traylor	Florida
Jimmy Blissett	Mississippi
Ron Newton	Texas

Bar Code Advisory Committee

Gary Wicklund	The Freedom Group
Linda S. Dougherty	Prudential
William Carroll	ACLI
Mike Leonard	Booke and Company
Mike Bronston	AM Best Company
Phil Schwartz	AIA
Carolyn Goodale	Bowne Insurance Division

Biographical Data Form Study Group

Tom Burke, Chair	New Hampshire
Windell Clark	Kentucky
Jim Borchardt	Montana
Bill Hosea	Tennessee

Biographical Data Form Advisory Committee

Tom Ward	NAII
George McGann	Allstate
Bill Ward	Aetna
Mike Olson	State Farm
Phil Schwartz	AIA

DATA/SYSTEMS MANAGEMENT (EX4) TASK FORCE

Sal Curiale, Chair	New York
Terry Rankin, Vice Chair	Nevada
John Garamendi	California
Tom Gallagher	Florida
Jim Schacht	Illinois
Hunter O. Wagner, Jr.	Louisiana
John A. Donaho	Maryland
Andrea Bennett	Montana
Samuel F. Fortunato	New Jersey
Jim Long	North Carolina
Constance B. Foster	Pennsylvania
Philip W. Barnes	Texas

SSO Staff Support: Jim Rose/Denise Matthews

Mission Statement:

Promote education and training in the use of automated computer systems to enhance the efficiency and effectiveness of state insurance regulation. This activity will build on the state training programs already underway by the NAIC staff and be targeted to increase state usage of NAIC computer applications.

1991 Charge:

1. Oversee the development of training programs designed to improve: a) understanding of NAIC Information Systems applications; and b) their ability to use these applications. Recommend new programs and enhancements to existing programs as appropriate.

2. Provide a forum for the discussion and dissemination of programs, procedures, and applications that a state may have developed that would be of assistance to other states.

3. Oversee the activities of the Data Capture Working Group. Charges for the working group include the following:

   - Develop recommended standards for the processing of annual and quarterly statement data received on diskette.

   - Develop recommendations for the capture of additional statement blanks on diskette.

   - Resolve coordination issues surrounding annual statement changes made by both the states and the NAIC.

   - Explore other forms of electronic filings such as magnetic tape and communication over telephone lines or satellite networks.

4. Provide assistance to the Internal Administration (EX1) Subcommittee and the NAIC staff in review and deliberations concerning resource allocation (hardware, software, manpower) for new and existing Information Systems projects.

DATA/SYSTEMS MANAGEMENT (EX4) TASK FORCE (Cont'd)

Supplemental Charge From the Recommendations of the Committee on Exam Processes Which Should be Included in the 1991 Charges:

5. Direct the Data Capture Working Group to begin capturing selected Schedule D investment information which can then be merged with the existing Advance Valuation System for use by examiners to test portfolio valuation, MSVR calculation, due and accrued interest calculation, gains and losses on sales of investments, and to perform modeling and trending analysis.

Working Group

Data Capture Working Group

Mission Statement:

Address issues, develop standards, and make appropriate recommendations to assure timely, accurate, and complete capture of regulatory data that resides in the NAIC's database and develop a central repository of regulatory data. This central repository concept assumes the NAIC as a central source for processing of regulatory data, therefore relieving the states of the burden of capturing this data.

1991 Charge:

1. Develop and maintain recommended standards for the processing of annual and quarterly statement data received on diskette.

2. Develop recommendations for the capture of additional annual and quarterly statement blanks on diskette. Coordinate this effort with the Blanks (EX4) and Data/Systems Management (EX4) Task Forces.

3. Address and make recommendations pertaining to issues affecting the successful processing of annual and quarterly statement data captured on diskette.

4. Oversee the development of annual and quarterly statement diskette specifications, including a review of "state specific" diskette specifications to ensure they are generally consistent with procedures and practices used for "nationwide" NAIC diskette specifications.

5. Study a proposal by the Audit Software (EX4) Working Group to capture a subset of Schedule D information, define exactly what data is to be captured, develop recommendations for the capture of that data and determine the impact on NAIC resources.

6. Continue to develop recommendations and address issues surrounding the central processing and capture of regulatory data by the SSO office in Kansas City, in order to maintain a database that is complete, accurate, and timely. One example of an issue is: How will annual and quarterly statement changes made at the states be communicated to the central annual statement database at the SSO office?

7. Explore other forms of electronic filing such as magnetic tape and communication over telephone lines.

EXAMINATION OVERSIGHT (EX4) TASK FORCE

Jim Schacht, Chair	Illinois
Philip W. Barnes, Vice Chair	Texas
Mike Weaver	Alabama
Lee Douglass	Arkansas
Susan Gallinger	Arizona
John Garamendi	California
Joanne Hill	Colorado
David N. Levinson	Delaware
Tom Gallagher	Florida
Joaquin G. Blaz	Guam
Robin Campaniano	Hawaii
George Neumayer	Idaho
David J. Lyons	Iowa
Elizabeth P. Wright	Kentucky
Hunter O. Wagner, Jr.	Louisiana
John A. Donaho	Maryland
Bert J. McKasy	Minnesota
George Dale	Mississippi
Lewis Melahn	Missouri
Andrea Bennett	Montana
William H. McCartney	Nebraska
Terry Rankin	Nevada
Louis E. Bergeron	New Hampshire
Salvatore R. Curiale	New York
Jim Long	North Carolina
Harold T. Duryee	Ohio
Gary Weeks	Oregon
Constance B. Foster	Pennsylvania
Elaine A. McReynolds	Tennessee
Harold C. Yancey	Utah
Jeffrey Johnson	Vermont
Steven T. Foster	Virginia
Richard G. Marquardt	Washington
Robert D. Haase	Wisconsin

SSO Staff Support: Terry Boyer/Jean Olson

<u>Mission Statement</u>

The mission of the task force is to monitor all aspects of the financial examination process and to identify, investigate, and develop solutions to problems arising related to financial examinations, to monitor additions to the NAIC Examiners Handbook, to oversee the IRIS Examiner Team Project including follow-through procedures and quarterly statement filings on immediate [illegible]ation companies, to review details of examination surveillance process, to monitor the development of tests for determining when a financial examination of an insurer is necessary, to establish procedures for flow of information between states on troubled companies, to enhance the quality and timeliness of financial examinations and prepare additional material for the Financial Examiners Handbook covering this area, and to monitor the currently of examination schedules in various states and assist the states in developing methods to maintain current schedules

EXAMINATION OVERSIGHT (EX4) TASK FORCE (Cont'd)

1991 Charge:

1. Monitor the Financial Examiners Handbook Technical Group's revision and enhancement of the NAIC Examiners Handbook to provide greater examination efficiency and effectiveness.

2. Monitor the Financial Examiners Handbook Technical Group's maintenance of the Examiners Handbook.

3. Develop new or revised procedures that will produce examination findings within specific time frames following completion of the examination.

4. Explore the feasibility of mandating the use of Schedule P "expert system" loss reserve analysis on examinations of property and casualty companies.

5. Create a NAIC/SSO financial analysis unit responsible for refining and improving the IRIS ratios; developing computerized analytical models from the NAIC Database to enhance the financial analysis resources and capabilities of state insurance departments; assisting states in developing and improving in-house financial statement analysis, and continuing development of other financial models to support the activities of the Potentially Troubled Companies Working Group.

6. Monitor the Potentially Troubled Companies Working Group in its further development and implementation of additional computer based analytical techniques to assist in effectively monitoring financial condition and prioritizing examination needs.

7. Establish an NAIC/SSO examiner team or "strike force" consisting of NAIC employees who will direct the activities of the annual examiner team project, coordinate the activities of the Potentially Troubled Companies Working Group, perform ongoing financial analysis and be available upon request by states to assist in special association examinations. (Recommendation of Examination Processes Committee)

8. Monitor the Financial Examiners' Qualification, Compensation and Training Technical Group expansion of the minimum qualifications for zone examiners and determine the necessity of strengthening such qualifications.

9. Monitor the technical group overseeing the IRIS Examiner Team Project.

10. Monitor the technical group developing and recommending compensation, expansion of classification and continuing education for examiners.

11. Continue development of risk based capital approach to define required levels of capital and surplus.

12. Continue development of a model law which would provide for a variable capital and surplus requirement based on the nature and volatility of business underwritten and other factors.

EXAMINATION OVERSIGHT (EX4) TASK FORCE (Cont'd)

13. Monitor the activity of the CPA/Actuary Working Group to review the actuarial opinion for consistency with the CPA changes and to address situations in which unaudited information provided by insurers is relied upon.

14. Continue development of new automated examination tools to assist in examining reinsurance, loss reserves and investments.

15. Increase emphasis and coordination of computer audit techniques.

Working Groups

Potentially Troubled Companies Working Group

Robin Campaniano, Chair	Hawaii
Robert D. Haase, Vice Chair	Wisconsin
John Garamendi	California
David N. Levinson	Delaware
Jim Schacht	Illinois
John A. Donaho	Maryland
William H. McCartney	Nebraska
Salvatore R. Curiale	New York
Jim Long	North Carolina

1991 Charge:

1. Monitor the continuing development and implementation of computer based analytical techniques to assist in effectively monitoring financial condition and prioritizing examination needs.

2. Develop annual and quarterly financial analysis reports available for use as requested by domiciliary or any other states to assist in special association examinations and monitoring of domestic and foreign companies doing business in their jurisdiction.

3. Review and amend as needed the selection criteria for identifying potentially troubled companies.

4. Review the synopses of potentially troubled companies prepared by the NAIC Financial Services Staff and determine which companies should be discussed by the Examination Oversight (EX4) Task Force.

5. Continue to monitor companies which have been recommended to Examination Oversight (EX4) Task Force as troubled.

EXAMINATION OVERSIGHT (EX4) TASK FORCE (Cont'd)

Life & Health Financial Ratios (EX4) Working Group

John Montgomery, Chair	California
John Tinsley	Delaware
John Kummer	Florida
Jim Hanson	Illinois
Windell Clark	Kentucky
George LeFalce	New Jersey
Terry Lennon	New York
Lewis P. Roth	New York
Terry Meagher	Oregon
Ronald Chronister	Pennsylvania
Bill Hosea	Tennessee
Ron Newton	Texas
Billy Lovelady	Utah
Gregory Krohm	Wisconsin

1991 Charge:

1. Continue to monitor proposed revisions to the selection criteria of targeted companies.

2. Coordinate the development and content of the public IRIS Ratio Results 1991 book with the Property and Casualty Financial Ratios Working Group of the Examination Oversight (EX4) Task Force.

3. Investigate with the assistance of the NAIC/SSO the possibility of programming the IRIS System to more clearly define the conditions which cause 999 and -99 ratio results.

4. Continue monitoring the "Troubled Life Insurer Predication Study" being performed by the Center for Risk Management and Insurance Research, College of Business Administration, Georgia State University.

5. Monitor the changes to the IRIS System in calculating Life and Health IRIS Ratios for Canadian Companies.

Life & Health Financial Ratios Advisory Committee

Morton Mann	Inter-American
John Christopherson	Omaha Woodmen
Anthony Accardi	Metropolitan
William Ward	Credit Life of Ohio
David Fishbaum	Crown Life
Richard Robertson	Lincoln National
Peter Storms	Travellers
Stan Kozial	Blue Cross/Blue Shield
William Koenig	Northwestern Mutual
William Carroll	ACLI
Richard Baker	State Mutual

EXAMINATION OVERSIGHT (EX4) TASK FORCE (Cont'd)

Life & Health Financial Ratios Advisory Committee (Cont'd)

Joel Gimpel	Blue Cross/Blue Shield
Gary Fagg	Credit Life of Ohio
Carolyn Goodale	Packard Press
Linda Dougherty	Prudential

1991 Charge:

1. To assist the regulatory groups in monitoring the effectiveness of the IRIS Ratios.

Property and Casualty Financial Ratios
Profitability (EX4) Working Group

James Schacht, Chair	Illinois
Richard Roth	California
John Tinsley	Delaware
Robert Howe	Iowa
Vincent Laurenzano	New York
Anne Kelly	New York

1991 Charge:

1. Monitor the progress of the study of the effectiveness of the IRIS ratios which is being performed by Ken Mrozek of the Illinois Insurance Department.

2. Coordinate the development and content of the public IRIS Ratio Results 1991 book with the Life and Health Financial Ratios Working Group of the Examination Oversight (EX4) Task Force.

3. Consider the development of IRIS ratios for title companies and other entities as needed.

Property & Casualty Financial Ratios
Advisory Committee

Phillip Schwartz, Chair	AIA
Robert A. Bailey	E.W. Blanche
Robert Brooks	NAII
Kenneth J. Nails	AAI
Carole Banfield	ISO
Irving Plotkin	Arthur D. Little, Inc.
Michael B. Olson	State Farm Ins. Plaza
Joseph W. Levin	Employers Reinsurance Corp.
Charles L. McClenahan	Coopers & Lybrand
Walter J. Fitzgibbons	Aetna Life and Casualty
James Shamberger	Reinsurance Assoc. of America

EXAMINATION OVERSIGHT (EX4) TASK FOR^E (Cont'd)

Audit Software User Group

Bob Solitro, Chair	New Hampshire
Chad Collier	Colorado
Jim Schacht	Illinois
David L. Krumm	Nebraska
Terry Meagher	Oregon

SSO Support Staff: Gary Gummig

Working Group of Audit Software User Group

Jerry Roberts, Chair	Texas
Howard Wong	California
Billy Kwan	Colorado
Tom Farrell	Illinois
Terry Sindelar	Nebraska
James Dreyer	New Hampshire
Robert Stern	New York
Joy Little	North Carolina
Cynthia Sikorski	Ohio
Terry Meagher	Oregon
Gail Nielsen	Utah
Michael Maffei	New York

SSO Support Staff: Gary Gummig

Non Investment Grade Bonds Working Group

James W. Schacht, Co-Chair	Illinois
Alex Spencer, Co-Chair	North Carolina
Larry Cross	Arizona
Ray Bacon	California
Norris Clark	California
George Donhauser	Delaware
John Kummer	Florida
Phillip J. Sullivan	Massachusetts
James Wennberg	Minnesota
Jim Miller	Minnesota
William H. McCartney	Nebraska
Terry Lennon	New York
Bob Callahan	New York
Bob Crawford	Texas
A.W. Pogue	Texas

SSO Staff Support: Terry Boyer/Bill Smythe

EXAMINATION OVERSIGHT (EX4) TASK FORCE (Cont'd)

Risk Based Capital Working Group

Vincent Laurenzano, Chair	New York
Norris Clark	California
John Kummer	Florida
Jim Schacht	Illinois
Al Iuppa	Nevada
Herschell Dunham	Nevada
Randy Blumer	Wisconsin

SSO Staff Support: Jean Olson

Risk Based Capital Advisory Committee

Christy Armstrong	Coopers & Lybrand
Dick Heffernan	Alliance
James Mack	NAMIC
George McGann	Allstate
William Murray	Chubb
Tony Spano	ACLI
Tom Ward	NAII
William D. Ward	Aetna

CPA/Actuary Working Group

Zack Stamp, Chair	Illinois
Tom Gallagher	Florida
Robin Campaniano	Hawaii
William H. McCartney	Nebraska
Louis E. Bergeron	New Hampshire
Salvatore R. Curiale	New York
Richard F. Reynolds	Texas

Life Risk Based Capital Working Group

Norris Clark	California
Carol Ostapchuk	Florida
Larry Gorski	Illinois
Rochelle Bergin	Minnesota
Chuck Renn	Missouri
Herschell Dunham	Nevada
Terry Lennon	New York
Robert Callahan	New York
Lewis Roth	New York
Randy Blumer	Wisconsin

1991 Charge:

1. Develop a draft of a formula to calculate risk adjusted capital ratios by June 1991.

2. Develop a draft law or regulation defining regulatory review and/or action, based on the level of a company's risk adjusted capital ratio and/or the trend in its ratio by June 1991.

EXAMINATION OVERSIGHT (EX4) TASK FORCE (Cont'd)

Life Risk Based Capital Advisory Committee

Warren R. Adams	The Principal Financial Group
Christy Armstrong	Coopers & Lybrand
Gary Corbett	Equitable Insurance Companies
Michael J. Cowell	Unum Life Insurance Company
Gary Eisenbarth	Security Benefit Life Insurance Co.
Lorin Fife	Broad, Inc.
Douglas M. Hodes	Metropolitan Life Insurance Company
Howard H. Kayton	Security First Life Insurance Co.
Dennis P. Lauzon	Massachusetts Mutual Life Ins. Co.
Michael E. Mateja	Aetna Life & Casualty
Karen McDonald	TransAmerican Occidental Life Insurance Company
James F. Reiskytl	The Northwestern Mutual Life Insurance Company
Michael Slipowitz	MONY Financial Services
Stephen N. Steinig	New York Life Insurance Company
Peter Storms	The Travelers Companies
Bruce Winterhof	Milliman & Robertson

1991 Charge:

1. Develop a forumla to calculate risk adjusted capital ratios.

2. Identify and address various technical issues which arise in designing and applying a single formula to all insurance companies, despite differences in portfolio mix, overall size, etc.

3. Develop law or regulation defining regulatory review and/or action, based on the level of a company's risk adjusted capital ratio and/or the trend in its ratio.

Property and Casualty Risk Based Capital Working Group

Vincent Laurenzano	New York
Norris Clark	California
James W. Schacht	Illinois
John Kummer	Florida
Randy Blumer	Wisconsin
Charles F. Renn	Missouri
Terry Rankin	Nevada
Hershell Dunham	Nevada
Rochelle Bergin	Minnesota
Michael F. Motil	Ohio

EXAMINATION OVERSIGHT (EX4) TASK FORCE (Cont'd)

Property and Casualty Risk Based Capital Advisory Committee

George McGann	Allstate Insurance Company
Tom Ward	NAII
Christy Armstrong	Coopers & Lybrand
Michael Olson	State Farm Mutual Insurance Company
James Mack	Bloomington, Illinois
Dale D. Skupa	NAMIC
Richard Hefferan	Alliance of American Insurers
William D. Ward	Aetna Life & Casualty
William Murray	Chubb Insurance Group
Walter White	Kemper National Insurance Co.
Paul Braithwaite	Home Insurance Company
Robert Butsic	Firemen's Fund Insurance Co.
James M. Shamburger	Reinsurance Association of America
Walter J. Fitzgibbons, Jr.	Aetna Life & Casualty
Allan Kaufman	Milliman & Robertson
Peter F. Storms	The Travelers Insurance Companies

1991 Charge:

1. To furnish input on the development of a draft formula and model legislation.

Technical Committees

Financial Examiners Handbook Technical Group

David Krumm, Chair	Nebraska
Leon Hank	Michigan
Herschell Dunham	Nevada
Robert Solitro	New Hampshire
Joy Little	North Carolina
Dana Rudmose	Ohio
Terry Meagher	Oregon
Bill Hosea	Tennessee
Steve Durish	Texas
Randy Blumer	Wisconsin

1991 Charge:

1. Revise, expand and/or enhance the NAIC Examiners Handbook to include criteria or standards that will directly result in greater examination efficiency and effectiveness. Tailor to a regulatory perspective the AICPA's generally accepted auditing standards and incorporate into the Examiners Handbook where appropriate.

2. Maintain the Examiners Handbook to include appropriate pronouncements by the AICPA as well as other necessary annual updates.

EXAMINATION OVERSIGHT (EX4) TASK FORCE (Cont'd)

Financial Examiners Handbook Technical Group (Cont'd)

3. Integrate or cross-reference the Automated Examination Procedures Manual with the Examiners Handbook.

4. Incorporate provisions in the Examiners Handbook that will produce examination findings which reveal not only the financial condition of a company but also management and/or operational changes and characteristics that may have current or prospective impact on the company's solvency.

Financial Examiners Handbook Advisory Committee

William Heller	HIAA
William Carroll	ACLI
Tom Finnell	Ernst & Young
Dick Hefferan	AAI
George McGann	Allstate
Michael Olson	State Farm
William Scott	Arthur Andersen
Richard Smith	KPMG
Tom Ward	NAII
William Ashley .erlander	NALC
Linda Dougherty	Prudential

1991 Charge:

1. To assist the regulatory group in identifying suggested changes to the NAIC Financial Examiners Handbook.

Financial Examination Scheduling and Planning Technical Group

John Tinsley, Chair	Delaware
Arnold Dutcher, Vice Chair	Illinois
Jerry Reiley	California
A. Windell Clark	Kentucky
Robert Solitro	New Hampshire
William Rossbach	Ohio

1991 Charge:

1. Monitor the activity and effectiveness of the Examiner Team Project.

Financial Examination Suggestions and Grievances Technical Group

Terry Meagher, Chair	Oregon
Norris Clark	California
Daniel Colaiannia	Colorado
David L. Krumm	Nebraska
Stewart A. Keir	New York

EXAMINATION OVERSIGHT (EX4) TASK FORCE (Cont'd)

Financial Examination Suggestions and Grievances Technical Group

1991 Charge:

1. Same charge as previous year. Group has not convened since March 15, 1988.

Financial Examiners' Qualification, Compensation and Training Technical Group

Robert Solitro, Chair	New Hampshire
Gary Torticill	Arizona
Robert Howe	Iowa
William Rossbach	Ohio
Bill Hosea	Tennessee

1991 Charge:

1. Monitor and review the compensation and geographic expense reimbursement plan for insurance examiners.

2. Work in conjunction with the Society of Financial Examiners to expand the minimum qualifications and to include certain CPAs and others meeting prescribed equivalency as qualified to participate in zone examinations.

3. Determine if any changes are necessary to strengthen the qualifications of zone examiners.

4. Establish a new classification of examiner (Supervising Examiner) which would be similar to a "Big 6" audit manager and who would be responsible for overseeing several examinations concurrently.

GUARANTY FUND (EX4) TASK FORCE

John J. Dillon III, Chair	Indiana
Elaine A. McReynolds, Vice Chair	Tennessee
Susan Gallinger	Arizona
John Garamendi	California
David N. Levinson	Delaware
George Neumayer	Idaho
Jim Schacht	Illinois
George Dale	Mississippi
Constance B. Foster	Pennsylvania
Steven T. Foster	Virginia
Robert D. Haase	Wisconsin

SSO Staff Support: David B. Simmons/Arthur J. Chartrand

Mission Statement:

To monitor the NAIC Life and Health Insurance Guaranty Association Model Act and Post-Assessment Property and Liability Guaranty Association Model Act to assure the models are meeting their stated objectives and to conduct further studies as necessary to address appropriate protection of policyholders for non-traditional products.

1991 Charge:

1. Review various proposals for improvement of guaranty associations including the "peer review" concept. Proposals should incorporate features designed to encourage communication from industry to regulators of companies with practices which may indicate or lead to financial difficulties. Funding mechanisms and coordination among funds should also be considered.

2. Continue to monitor guaranty fund assessments and report periodically to Financial Condition (EX4) Subcommittee.

REHABILITATORS AND LIQUIDATORS (EX4) TASK FORCE

Tom Gallagher, Chair	Florida
Constance B. Foster, Vice Chair	Pennsylvania
Mike Weaver	Alabama
Lee Douglass	Arkansas
Susan Gallinger	Arizona
John Garamendi	California
David N. Levinson	Delaware
Joaquin G. Blaz	Guam
George Neumayer	Idaho
Jim Schacht	Illinois
David J. Lyons	Iowa
Elizabeth P. Wright	Kentucky
Hunter O. Wagner, Jr.	Louisiana
Susan K. Scott	Massachusetts
Dominic A. D'Annunzio	Michigan
Lewis Melahn	Missouri
William H. McCartney	Nebraska
Samuel F. Fortunato	New Jersey
Fabian Chavez	New Mexico
Salvatore R. Curiale	New York
Gerald Grimes	Oklahoma
Gary Weeks	Oregon
Maurice Paradis	Rhode Island
Elaine A. McReynolds	Tennessee
Philip W. Barnes	Texas
Harold C. Yancey	Utah
Hanley C. Clark	West Virginia
Robert D. Haase	Wisconsin

SSO Staff Support: Ellen Dollase/David B. Simmons

Mission Statement:

The mission of the task force is to encourage cooperation between the states in order that the affairs of receiverships and liquidations are handled in a manner conducive to the timely settlement of claims and the equitable treatment of claimants; to provide an effective forum for rehabilitators and liquidators for the exchange of ideas, information and technical assistance; to coordinate the rehabilitation or liquidation of multi-state insurers; to educate and train staff with regard to rehabilitations, liquidations and conservatorships, to strive for uniformity and consistency in the legislation and procedures of states regarding rehabilitation and liquidation proceedings, including the updating of the NAIC Manual for Receivers and to identify problems which are detected in receiverships which may demand or suggest a change in regulatory practices and refer to appropriate committee.

1991 Charge:

1. Review membership of all working groups reappointing regulators only to working groups and appointing industry advisory committees as appropriate.

2. Finalize recommendations concerning federal bankruptcy code regarding HMOs by June, 1991.

REHABILITATORS AND LIQUIDATORS (EX4) TASK FORCE (Cont'd)

3. Finalize recommendations on immunity and indemnification amendments to NAIC Rehabilitation and Liquidation Model Act by June, 1991.

4. Solicit comments on "Compendium Taking the Offense on Directors and Officers in the Liquidation Arena" and report back to task force for possible adoption by June, 1991.

5. Monitor progress and development of Brief and Forms Bank Database for rehabilitators and liquidators.

6. Coordinate an NAIC sponsored annual liquidator workshop.

7. Finalize amendments to Sections 54 and 55 of the NAIC Insurers Rehabilitation and Liquidation Model Act regarding filing procedures in ancillary proceedings.

8. Develop final work product on Model Early Access Distribution Plan and Model Early Access Distributi:n Agreement.

9. Study common database concept for receivers and guaranty funds as well as the feasibility of a compilation of companies interested in acquiring books on property/casualty business.

10. Complete revision of the Receivers Handbook.

11. Finalize recommendations regarding the NAIC Model Mediation Guidelines and the NAIC Model Mediation Agreement by June, 1991.

Working Groups

Subgroup Prepaid Health Care Insolvency Worki. roup

David N. Levinson, Chair Delaware

Immunity Indemnification Working Grou

Vincent Vaccarello, Chair Pennsylvania

Directors and Officers Liability Working Group

Robert Deck, Chair Missouri

Brief and Forms Bank Working Group

Debra J. Anderson, Chair Illinois

REHABILITATORS AND LIQUIDATORS (EX4) TASK FORCE (Cont'd)

Guaranty Funds Symposium Working Group

Brian D. Salwowski, Chair   Indiana

Handbook Development Working Group

Vincent Vaccarello, Chair   Pennsylvania

Mediating Disagreements Working Group

Deanna Delmar, Chair   Arizona

VALUATION OF SECURITIES (EX4) TASK FORCE

Jim Schacht, Chair	Illinois
Salvatore R. Curiale, Vice Chair	New York
John Garamendi	California
Hunter O. Wagner, Jr.	Louisiana
William H. McCartney	Nebraska
Louis E. Bergeron	New Hampshire
Harold T. Duryee	Ohio
Philip W. Barnes	Texas

SSO Support Staff: Bill Smythe/Dick Newman

Mission Statement:

The mission of the task force is to act as the forum for proposed changes to or interpretations of the revised "Purposes of the Securities Valuation Office." This document governs how securities are valued by the SVO staff and constitutes the task force's permanent instructions to the staff on valuation matters.

1991 Charge:

1. Monitor the ongoing implementation and application of the Zeta Credit evaluation system to private placement investments by the staff and at industry zeta sites.

2. Monitor the ongoing automation of the SVO's internal valuation procedures including the credit information module and rating standards.

3. Monitor the ongoing work of the Mandatory Securities Valuation Reserve (MSVR) Study Group which is examining alternatives to the present MSVR.

4. Monitor the ongoing work of the Special Valuation Study Group which will examine new investment vehicles from a valuation standpoint.

5. Develop a model law on Invested and Admitted Assets.

6. Establish a working group to monitor insurer changing investment practices and trends including conducting a survey of insurer mortgage loan and real estate investments, study the appropriateness of current statutory valuation requirements for mortgage loans and real estate. Conduct a study of Schedule BA assets, develop a system to monitor the effect of changing global economic trends on insurer investment portfolios and to monitor statutory valuation requirements for invested assets.

7. Establish a standing working group to provide special assistance to the staff of the Securities Valuation Office for unusual or emergency-type situations.

VALUATION OF SECURITIES (EX4) TASK FORCE (Cont'd)

Working Groups

Lending of Securities Working Group

Jim Hanson, Chair Illinois

1991 Charge:

1. Monitor the implementation of the working group's recommendations which were adopted at the December meeting.

MSVR Study Group

Terry Lennon, Chair New York

MSVR Advisory Committee

Bill Ward Aetna

1991 Charge:

1. To furnish input to the Mandatory Securities Valuation Reserve (MSVR) Study Group.

Invested and Admitted Asset Model Law Working Group

Tom Gallagher, Chair Florida

1991 Charge:

1. To develop an NAIC model law on invested and admitted assets.

Invested Asset Working Group

Larry Gorski, Chair Illinois

1991 Charge:

1. To conduct th survey of real estate and mortgage loan reporting, the analysis of Schedule BA assets and to develop, implement and monitor systems to study the investment asset trends of the insurance industry and the changing financial viability of the insurance industry's invested assets in light of changing economic conditions.

2. Study the appropriateness of current statutory valuation requirements for real estate and mortgage loans.

3. Monitor the continuing appropriateness of statutory valuation requirements for all classes of invested assets.

VALUATION OF SECURITIES (EX4) TASK FORCE (Cont'd)

Special Valuation Study Group

Norman Koefed, Chair — Illinois

Valuation Office Support Working Group

Terry Lennon, Chair — New York

<u>1991 Charge:</u>

1. Supervise the activities and operations of the Valuation of Securities Office.

2. Assist the Valuation of Securities staff in special and unusual circumstances which occur and require direct involvement of regulators.

LIFE INSURANCE (A) COMMITTEE

Harold C. Yancey, Chair	Utah
David J. Lyons, Vice Chair	Iowa
Mike Weaver	Alabama
John Garamendi	California
Harold T. Duryee	Ohio
Gary Weeks	Oregon
Philip W. Barnes	Texas
Steven T. Foster	Virginia
Richard G. Marquardt	Washington

SSO Staff Support: Judith P. Lee

Mission Statement:

The mission for this committee is to consider problems relating to life insurance and annuities, review new life products and establish priorities of the Life and Health Actuarial (Technical) Task Force.

1991 Charge:

1. Monitor implementation of the NAIC Accelerated Benefits Model Regulation.

2. Review industry marketing methodologies to determine appropriate point of delivery of the "Financial Review of This Policy" disclosure form.

3. Oversee NAIC staff actuarial analysis of the cost/benefit of policies defined in Section 8I of the Life Insurance Disclosure Model Regulation.

4. Review the annuity market, including: advertising, agent contracts, disclosure, annual reports and two-tiered annuities.

5. Determine whether guaranteed investment contracts and deposit administration contracts are annuities.

6. Consider development of a standardized policy service and information request form and mandate its usage through life insurance replacement regulations.

Working Groups

Annuities Working Group

David J. Lyons, Chair	Iowa
Mike Weaver	Alabama
Harold T. Duryee	Ohio
Philip W. Barnes	Texas
Steve T. Foster	Virginia
Richard G. Marquardt	Washington

LIFE INSURANCE (A) COMMITTEE (Cont'd)

Senior Marketing Working Group

Theodore R. Kulongoski, Chair	Oregon
John A. Garamendi	California
David J. Lyons	Iowa
Steven T. Foster	Virginia

PRODUCT DEVELOPMENT (A) TASK FORCE

John Garamendi, Chair	California
Margurite C. Stokes, Vice Chair	District of Columbia
David N. Levinson	Delaware
Joaquin G. Blaz	Guam
Jim Schacht	Illinois
Gerald Grimes	Oklahoma
Philip W. Barnes	Texas
Kenneth Erickson	Wyoming

SSO Staff Support: Judith P. Lee/Carolyn J. Johnson

Mission Statement

The mission of this task force is to monitor developments in nonstandard life insurance and draft or amend model legislation to respond to regulatory concerns.

1991 Charge:

1. Examine doctrine of insurable interest relative to corporate-owned life insurance.

2. Participate in review of annuity market as directed by parent committee.

3. Review arbitrage life concept and determine appropriate response.

Product Development Advisory Committee
Corporate-Owned Life Insurance

George T. Coleman, Chair	The Prudential Insurance Company of America
William N. Albus	The National Association of Life Underwriters
Jonathan P. Neipris	American International Companies
Michael J. Bartholomew	American Council of Life Insurance
Anthony J. Sara	Metropolitan Life Insurance Company

ACCIDENT AND HEALTH INSURANCE (B) COMMITTEE

Tom Gallagher, Chair	Florida
David N. Levinson, Vice Chair	Delaware
Susan Gallinger	Arizona
John Garamendi	California
John J. Dillon	Indiana
Elizabeth P. Wright	Kentucky
Terry Rankin	Nevada
Gary Weeks	Oregon
Robert D. Haase	Wisconsin

SSO Staff Support: Carole Olson, Gary Claxton

Mission Statement:

The mission of the committee is to consider problems relating to accident and health insurance and to continue liaison with the NAIC/NAHMOR Joint Committee in that committee's consideration of amendments to the HMO Model Act and Regulation.

1991 Charge:

1. Evaluate the role of underwriting in group health insurance.

2. Recommend appropriate revisions in the Discontinuance and Replacement Model Law.

3. Examine potential industry, regulatory or legislative initiatives that might address the serious problems of the 37 million uninsureds and the related problems of uncompensated care or under compensated care facing our nation's health care providers.

4. Recommend appropriate action to address employee leasing, in conjunction with the Workers' Compensation (D) Task Force.

5. Consider issues relating to funding of risk pools.

6. Consider enhancements to the health insurance components of continuing education requirements. (New Charge)

Health Care Insurance Access Working Group

Tom Gallagher, Chair	Florida
Susan Gallinger	Arizona
Roxani Gillespie	California
Zack Stamp	Illinois
David J. Lyons	Iowa
Jim Long	North Carolina
Earl R. Pomeroy	North Dakota
Theodore R. Kulongoski	Oregon
Robert D. Haase	Wisconsin

ACCIDENT AND HEALTH INSURANCE (B) COMMITTEE

Advisory Committee

Health Care Insurance Access Advisory Committee

1991 Charge:

1. To assist the Health Care Access Working Group in developing a mechanism addressing availability of health insurance.

HMO (B) TASK FORCE

Elizabeth P. Wright, Chair	Kentucky
John Garamendi	California
George Neumayer	Idaho
Jim Schacht	Illinois
David J. Lyons	Iowa
Susan K. Scott	Massachusetts
Joseph A. Edwards	Maine
Philip W. Barnes	Texas
Steven T. Foster	Virginia

SSO Staff Support: Carolyn J. Johnson

Mission Statement:

The mission of the committee is to coordinate activities of the NAIC and NAHMOR concerning regulation of health maintenance organizations and related issues. The committee was organized in 1982 to further the development of interstate cooperation in the regulation of health maintenance organizations. The committee consists of 10 members with equal representation from the NAIC and NAHMOR and whose members are appointed by each organization. This joint committee establishes its own agenda.

1991 Charge:

1. Refine and adopt HMO Accounting Manual.

2. Develop a model law or regulation on affiliated transactions, including the purchase/sale/merger of HMOs.

3. Develop and evaluate solvency surveillance indicators for HMOs. Develop language to give Commissioners authority to intervene when an HMO is in hazardous financial condition.

4. Consider reinsurance issues in context of Medicare and the uncovered expenditures insolvency deposit.

5. After the fronting model has been completed, consider fronting in the context of HMOs.

6. Develop resource document describing overlapping state and federal requirements for regulating Medicare contracting HMOs.

LONG-TERM CARE INSURANCE (B) TASK FORCE

Susan Gallinger, Chair	Arizona
Richard G. Marquardt, Vice Chair	Washington
John Garamendi	California
David N. Levinson	Delaware
Tom Gallagher	Florida
Jim Schacht	Illinois
Dominic A. D'Annunzio	Michigan
Earl R. Pomeroy	North Dakota
Gary Weeks	Oregon
Mary Jane Cleary	South Dakota
Steven T. Foster	Virginia

SSO Support Staff: Carole Olson/Gary Claxton

Mission Statement:

The Long-Term Care Insurance Task Force is to evaluate the appropriate regulatory standards for long-term care insurance policies, to protect applicants from unfair or deceptive sales or enrollment practices, and to facilitate flexibility and innovation in the development of long term care insurance. This Task Force is also charged with monitoring and responding to federal legislative activity on long-term care insurance as appropriate.

1991 Charge:

1. Develop appropriate revisions to Long-Term Care Insurance Model Act and Regulation.

2. Recommend whether a mandated offer of nonforfeiture benefits should be required. (New Charge)

3. Develop regulatory framework for continuing care retirement communities; coordinate this issue with the Life and Health Actuarial Task Force.

4. Revise Shopper's Guide to Long Term Care Insurance for 1992 distribution. (New Charge)

5. Finalize applicability of loss ratio requirements to life insurance policies containing long-term care benefits. (New Charge)

6. Evaluate the effectiveness of loss ratio reporting form. (New Charge)

Long Term Care Advisory Committee

Paul Rapo, Chair	Aetna
Bob Steil	HIAA
James T. Farha	Standard Life & Accident
J. Wallace Knobel	Prudential
John Cutler	AARP

LONG-TERM CARE INSURANCE (B) TASK FORCE (Cont'd)

Long Term Care Advisory Committee

Erling Hansen	GHAA
Tony Spano	ACLI
Susan Case	Hartford
Ron Hagen	Amex Life Assurance Company
Valerie Wilbur	American Association of Homes for the Aging
Glenn Joppa	Union Fidelity Life Insurance Company
Linda Lanam	Life of Virginia
John Benton	CNA
Saul Spivack	Metropolitan Life Insurance Co.
Jim Firman	United Seniors Health Cooperative
Kendall Surfass	Equitable Life and Casualty Co.
Trudy Lieberman	Consumer Reports
Bartley Munson	Mercer, Meidinger & Hansen
Steve Kellison	Georgia State University
Brian Quigley	Travelers
Gail Shearer	Consumers Union
Bonnie Burns	Claremont, California
David H. Brenerman	Unum Insurance Company
Merle Pederson	The Principal Group
Barry Skolnick	Merrill Lynch
Brice Oakley	Blue Cross/Blue Shield Association
Bill Odell	Odell & Associates, Actuarial Services
Dorothy Thorson	Golden Rule
Alfred Famiglietti	John Hancock
Gary Sanders	NALU

Long Term Care Technical Actuarial Advisory Committee

Bartley L. Munson, Chair	Mercer Meidinger Hansen
Mark F. Bartorelli	Prudential
Jack R. Dykhouse	Life Investors
Robert A. Hall	Aetna Life & Casualty
Stephen G. Kellison	Georgia State University
Dennis M. O'Brien	Transport Life
W.H. Odell	W.H. Odell & Assoc. (Golden Rule)
Robert Shapland	Mutual of Omaha
Ashok K. Sharma	CNA
Gerald R. Shea	Blue Cross/Blue Shield Assoc.
Stephen L. Smith	UNUM (AAHA)
Morris Snow	Metropolitan
Anthony T. Spano	ACLI
Julie C. Stenlund	Hartford Life
John C. Wilkin	Actuarial Research Corporation
Robert Yee	AMEX Life

MEDICARE SUPPLEMENT & OTHER LIMITED BENEFIT PLANS (B) TASK FORCE

Earl R. Pomeroy, Chair	North Dakota
Robert D. Haase, Vice Chair	Wisconsin
John Garamendi	California
David N. Levinson	Delaware
Jim Schacht	Illinois
Susan K. Scott	Massachusetts
Bert J. McKasy	Minnesota
Andrea Bennett	Montana
William H. McCartney	Nebraska
Harold T. Duryee	Ohio
Richard G. Marquardt	Washington

SSO Staff Support: Gary Claxton/Carole Olson

Mission Statement:

The Medicare Supplement and Other Limited Benefit Plans (B) Task Force is to establish standards as appropriate for Medicare supplement and other limited benefit plans policies, to facilitate public understanding and comparison of such policies, to provide for disclosure in the marketing of such coverages, to protect applicants from unfair or deceptive sales or enrollment practices and to facilitate flexibility and innovation in the development of new products.

1991 Charge:

1. Monitor state implementation of revised Medicare supplement insurance minimum standards and provide assistance as necessary.

2. Evaluate effectiveness of revised Medicare supplement experience exhibit.

3. Develop recommendations for the development of effective loss ratio monitoring program.

4. Monitor on an ongoing basis additional changes made to the federal Medicare program and revise the minimum standards in NAIC model regulation as required to maintain federal certification. Specifically, develop standardization approach for policies and other revisions to conform to OBRA 1990.

5. Recommend revisions to minimum benefits and loss ratios standards for limited benefit policies.

MEDICARE SUPPLEMENT & OTHER LIMITED BENEFIT PLANS (B) TASK FORCE (Cont'd)

<u>Advisory Committee</u>

Medicare Supplement Standardization Advisory Committee

Gail Shearer, Co-Chair	Consumers Union
Galen Ullstrom, Co-Chair	Mutual of Omaha Insurance Company
Bonnie Burns	California Consumer Consultant
Lucia DiVenere	Families USA Foundation
Jim Firman	United Seniors Health Cooperative
Larry Kirsch	Consumer Health Advocates
J. Wallace Knobel	The Prudential-AARP Operations
Cheryl Matheis	AARP
Brice Oakley	Blue Cross/Blue Shield Association
James Sedgwick	Torchmark Corporation
Ron Souders	National Home Life Assurance Co.
Lee VanValkenburgh	Capital Blue Cross

<u>1991 Charge:</u>

1. To furnish comment to the Medicare Supplement and Other Limited Benefit Plans (B) Task Force on the development of standardized Medicare supplement policies pursuant to the Omnibus Budget Reconciliation Act of 1990.

STATE AND FEDERAL HEALTH INSURANCE
LEGISLATIVE POLICY (B) TASK FORCE

Joanne Hill, Chair	Colorado
John Garamendi, Vice Chair	California
Tim Ryles	Georgia
George Neumayer	Idaho
John J. Dillon	Indiana
Lewis Melahn	Missouri
Terry Rankin	Nevada
Constance B. Foster	Pennsylvania
Mary Jane Cleary	South Dakota
Philip W. Barnes	Texas
Steven T. Foster	Virginia

SSO Staff Support: Gary Claxton/Kevin Cronin

Mission Statement:

The State and Federal Health Insurance Legislative Policy (B) Task Force is charged with reviewing and monitoring federal activity and analyzing and developing NAIC strategy with respect to national health care issues including consideration of ERISA preemption, creation and development of state risk pools, comprehensive health insurance plans, availability of health care and cost containment issues.

1991 Charge:

1. Identify and monitor federal legislative proposals on health insurance.

2. Address regulation of METS, MEWAs and other ERISA related issues.

3. Study the Education of the Handicapped Act and consider whether private health insurance is a viable source of financing early intervention services for infants and toddlers. (New Charge)

SENIOR COUNSELING ACTIVITIES (B) TASK FORCE

Jim Long, Chair	North Carolina
Richard G. Marquardt, Vice Chair	Washington
Susan Gallinger	Arizona
David N. Levinson	Delaware
Jim Schacht	Illinois
John J. Dillon	Indiana
Philip W. Barnes	Texas

SSO Staff Support: Carole Olson/Gary Claxton

Mission Statement:

The Senior Counseling Activities (B) Task Force is charged with assisting states in the development and enhancement of counseling programs and other educational activities for senior citizens.

1991 Charges:

1. Identify issues of common concern to state insurance departments.

2. Gather and disseminate information on how to establish a counseling program for senior citizens.

3. Provide assistance to other NAIC health committees in the identification and preparation of buyer's guides for seniors.

PERSONAL LINES--PROPERTY AND CASUALTY (C) COMMITTEE

Robin Campaniano, Chair	Hawaii
John Garamendi, Vice Chair	California
Susan Gallinger	Arizona
Tim Ryles	Georgia
Terry Rankin	Nevada
Harold T. Duryee	Ohio
Gerald Grimes	Oklahoma
John G. Richards	South Carolina
Hanley C. Clark	West Virginia

SSO Staff Support: Robert Klein/Ellen Dollase

Mission Statement:

The Personal Lines - Property and Casualty Insurance (C) Committee is to monitor and respond to problems associated with the products, delivery and cost in the property casualty insurance market as it operates with respect to individual persons.

1991 Charge:

1. Monitor trends in private passenger automobile insurance rates and analyze the factors underlying these trends.

2. Identify possible policy measures that could be implemented to help reduce the cost of automobile insurance.

3. Work with NAIC staff in developing data and methodologies for market analysis in personal lines that could be used by state insurance departments.

4. Coordinate response from the NAIC to the Earthquake Project.

5. Study issue of minimum standards for personal automobile policies.

6. Study and disseminate information on insurer withdrawals from and the restructuring of personal lines markets. (New Charge)

7. Evaluate the adequacy of consumer information in the personal lines and recommend measures to improve that information. (New Charge)

8. Investigate whether NAIC models respond to the issue of redlining.

COMMERCIAL LINES--PROPERTY AND CASUALTY INSURANCE (D) COMMITTEE

Louis E. Bergeron, Chair	New Hampshire
Steven T. Foster, Vice Chair	Virginia
David Walsh	Alaska
Lee Douglass	Arkansas
John Garamendi	California
Jim Schacht	Illinois
David J. Lyons	Iowa
Salvatore R. Curiale	New York
Philip W. Barnes	Texas

SSO Staff Support: David B. Simmons/Robert Klein

Mission Statement:

The mission of this committee is to consider problems of property and casualty insurance which are usually defined as commercial insurance problems.

1991 Charge:

1. Develop procedures and necessary forms for implementation of the loss cost system in workers' compensation.

2. Draft any necessary amendments to model legislation to implement the loss cost system in workers' compensation.

3. Monitor state and federal risk retention acts and respond to proposed changes.

4. Consider and respond to Insurance Services Office proposed endorsement to environmental liability policies and any new proposals relating to CGL policies.

5. Monitor the study of the underwriting cycle and the commercial liability market and consider regulatory strategies that could be developed to mitigate adverse consequences of the cycle.

6. Review and consider the drafting of a model regulation for the regulation of self-insured government entity property/casualty pools.

Working Groups

Risk Retention Working Group

David J. Lyons, Chair	Iowa
David Walsh	Alaska
David N. Levinson	Delaware
Tom Gallagher	Florida
Zack Stamp	Illinois
Samuel F. Fortunato	New Jersey
Salvatore R. Curiale	New York
Jim Long	North Carolina
Steven T. Foster	Virginia

COMMERCIAL LINES--PROPERTY AND CASUALTY INSURANCE (D) COMMITTEE (Cont'd)

Minimum Standards for Extended Reporting Working Group

Alan Wickman, Chair	Nebraska
Richard Hsia	New York
Mike Lamb	Oregon
Bob Miller	Virginia

Uniform Filing Procedures Advisory Committee

Al Iuppa, Liaison	Nevada
Robert W. Lennon	General Reinsurance Corporation
Janet L. Shemanske	Integral Insurance Company
Craig W. Kalck	American Continental Ins. Co.
Richard J. Smelzter, II	United Southern Assurance Co.
Jack Casper	Dodson Insurance Group
Bruce C. Walling	General Accident Insurance
Ernie Taylor	Nationwide General Ins. Co.
Donald L. Coughennower	Employers Mutual Cos.
Bert Gindy	Florida Farm Bureau Ins. Cos.
Tim Wagner	Central National Ins. Group of Omaha
Robert R. Ratch	Allstate Insurance Company
Carole J. Banfield	ISO
Patrick McNally	NAII

STATISTICAL (D) TASK FORCE

Philip W. Barnes, Chair	Texas
Salvatore R. Curiale, Vice Chair	New York
Margurite C. Stokes	District of Columbia
Robin Campaniano	Hawaii
Jim Schacht	Illinois
William H. McCartney	Nebraska
Terry Rankin	Nevada
Samuel F. Fortunato	New Jersey
John G. Richards	South Carolina
Harold C. Yancey	Utah
Steven T. Foster	Virginia

SSO Staff Support: Robert Klein/Dan Atkisson

Mission Statement:

The Statistical (D) Task Force develops and recommends policy regarding the format, structure and implementation of data collection activities by the NAIC, state insurance commissioners and the statistical agents.

1991 Charge:

1. Write additional chapters for the revised NAIC Statistical Handbook.

2. Oversee implementation of biennial closed claim survey.

3. Monitor timely release of accelerated reports.

4. Develop model statistical plans for lines of insurance where no model statistical plans exist.

5. Evaluate different approaches to collecting statistical data on surplus lines, excess and umbrella coverages and risk retention groups.

6. Evaluate and recommend improvements to the reporting of data on expenses.

7. Evaluate and make recommendations with respect to the coordination and reconciliation of financial and statistical reporting.

8. Evaluate and recommend changes to the By Line By State Report on Profitability and explore other data bases and methodologies which might be used to assist rate and market analysis.

STATISTICAL (D) TASK FORCE (Cont'd)

Working Groups

Statistical Plan Working Group

Richard F. Reynolds, Chair	Texas
Robert Gossrow	Illinois
Alan Wickman	Nebraska
Stewart Keir	New York
Peg Ising	Ohio
David Eley	Texas

SSO Support Staff: Dan Atkisson

1991 Charge:

1. Write additional chapters for the Statistical Handbook.

2. Develop model statistical plans lines of insurance where no model statistical plans exist.

3. Develop standard output reports upon completion of model statistical plans.

Closed Claims Information Working Group

Harold C. Yancey, Chair	Utah
Mike Lamb	Oregon
David Eley	Texas

SSO Support Staff: Dan Atkisson

1991 Charge:

1. Oversee implementation of biennial closed claim survey.

Profitability Working Group

Marty Simons, Chair	South Carolina
Bob Loo	California
Robert Gossrow	Illinois
Don Wulf	Illinois
Kevin Conley	Iowa
Ilona Klasons	Maryland
Craig Kliethermes	Missouri
Terry Rankin	Nevada
Anne Kelly	New York
David Eley	Texas

1991 Charge:

1. Evaluate and recommend changes to the By Line/By State Report on Profitability and explore other databases and methodologies which may be used to assist rate and market analysis.

STATISTICAL (D) TASK FORCE (Cont'd)

General Advisory Committee

Carole Banfield	Insurance Services Office (ISO)
Robert Montgomery	American Association of Insurance Services (AAIS)
Stu Yakes	National Association of Independent Insurers (NAII)
David Conrad	National Independent Statistical Services
Lloyd Friedli	State Farm Insurance Companies

WORKERS' COMPENSATION (D) TASK FORCE

Joseph A. Edwards, Chair	Maine
Joanne Hill, Vice Chair	Colorado
Lee Douglass	Arkansas
John Garamendi	California
Tom Gallagher	Florida
Hunter O. Wagner, Jr.	Louisiana
Susan K. Scott	Massachusetts
Gary Weeks	Oregon
Maurice Paradis	Rhode Island
Mary Jane Cleary	South Dakota
Philip W. Barnes	Texas

SSO Staff Support: Robert Klein/David B. Simmons

Mission Statement:

The mission of the task force is to study the nature and effectiveness of state approaches to workers compensation and related issues, including but not limited to, assigned risk plans, safety in the workplace, treatment of investment income in rating, occupational disease and cost containment.

1991 Charge:

1. Study the structure, operation, and responsiveness of NCCI including rate filings, actuarial methodology, the classification systems, the administration of residual markets, and data reporting.

2. Evaluate specific policy measures to control medical costs in workers' compensation including alternative DRG's.

3. Implement system for the reporting of detailed claims information as specified in the Workers' Compensation Insurance Data Reporting Model Regulation.

4. Implement statistical data monitoring system for workers' compensation insurance.

5. Study growth and administration of residual markets and recommend policy measures to address problems identified.

6. Coordinate with Accident and Health Insurance (B) Committee and NAIC/IAIABC Joint Committee on employee leasing issues.

Working Groups

NCCI Activities Working Group

Joseph A. Edwards, Chair	Maine
Tom Gallagher	Florida
Robert J. Janes	Rhode Island

WORKERS' COMPENSATION (D) TASK FORCE (Cont'd)

NCCI Activities Working Group (Cont'd)

1991 Charge:

1. Study the structure, operation, and responsiveness of NCCI including rate filings, actuarial methodology, the classification systems, and data reporting.

2. Implement system for the reporting of detailed claims information as specified in the Worker's Compensation Insurance Data Reporting Model Regulation.

3. Implement statistical data monitoring system for workers' compensation insurance.

Medical Cost Containment Working Group

Theodore R. Kulongoski, Chair	Oregon
Richard F. Reynolds	Texas
Harold C. Yancey	Utah

1991 Charge:

1. Evaluate specific policy measures to control medical costs in workers' compensation including alternative DRG's.

Residual Market Working Group

Ron Taylor, Chair	Arkansas
David Walsh	Alaska
Tom Gallagher	Florida
Douglas D. Green	Louisiana
Lewis Melahn	Missouri

1991 Charge:

1. Study growth and administration of residual markets and recommend policy measures to address problems identified.

SPECIAL INSURANCE ISSUES (E) COMMITTEE

Salvatore R. Curiale, Chair	New York
Philip W. Barnes, Vice Chair	Texas
Tom Gallagher	Florida
Tim Ryles	Georgia
Robin Campaniano	Hawaii
John J. Dillon III	Indiana
William H. McCartney	Nebraska
Jim Long	North Carolina
John G. Richards	South Carolina

SSO Staff Support: David B. Simmons/John Darwood

Mission Statement:

This committee has the responsibility for problems relating to the miscellaneous lines of insurance including, but not limited to title, captive insurers, surety, fidelity, mortgage guaranty and reinsurance.

1991 Charge:

1. Develop a Model Law for reciprocal insurers and inter-insurance exchanges.

2. Review and discuss the loss experience and rates charged by title insurers.

Advisory Committee

MGA/Reciprocals Advisory Committee

1991 Charge:

1. To offer comment genrally to the working group on draft legislation.

Broker Controlled Model Act Working Group

Sal Curiale	New York
William H. McCartney	Nebraska
Jim Long	North Carolina

1991 Charge:

1. To review the Broker Controlled Model Act.

INTERNATIONAL INSURANCE RELATIONS (E) TASK FORCE

Robin Campaniano, Chair	Hawaii
David Walsh, Vice Chair	Alaska
Susan Gallinger	Arizona
David N. Levinson	Delaware
Jim Schacht	Illinois
Dominic D'Annunzio	Michigan
William H. McCartney	Nebraska
Fabian Chavez	New Mexico
Salvatore R. Curiale	New York
Jim Long	North Carolina
Philip W. Barnes	Texas

SSO Staff Support: Kevin Cronin/John Darwood

1991 Mission Statement:

The International Insurance Relations (E) Task Force provides a forum for cooperative efforts between the United States and international regulators on issues of mutual interest.

1991 Charges:

1. Provide support for the annual International Conference by way of participation in the International Conference Planning Group.

2. Participate, to the extent possible, in the GATT negotiation process and its aftermath.

3. Participate, to the extent possible, in the U.S.-Mexico Free Trade Agreement discussions.

4. Increase NAIC participation in OECD proceedings.

REINSURANCE (E) TASK FORCE

Jim Schacht, Chair	Illinois
Louis E. Bergeron, Vice Chair	New Hampshire
David Walsh	Alaska
John Garamendi	California
David J. Lyons	Iowa
Andrea Bennett	Montana
Salvatore R. Curiale	New York
Constance B. Foster	Pennsylvania
Philip W. Barnes	Texas
Steven T. Foster	Virginia
Kenneth Erickson	Wyoming

SSO Staff Support: Pat Lynch/Betty Cordial

Mission Statement:

The mission of the task force is to discuss current issues relating to reinsurance including development of an appropriate database.

1991 Charge:

1. Monitor activity of Fronting Working Group to develop a model law on reinsurance arrangements generally referred to as "fronting arrangements."

2. Monitor progress of Assumption Reinsurance Working Group in researching the area of assumption or bulk reinsurance and developing a model act to address the problems in these transactions.

3. Monitor progress of the Reinsurance Database Working Group and continue development of the reinsurance reporting function including the release, over the State Data Network, of a report which verifies credit taken on reinsurance from company to company.

4. Create a reinsurance office at the SSO to assist state insurance departments in interpreting reinsurance contracts and evaluating reinsurance companies.

Working Groups

Limitations on Reinsurance Working Group (Fronting)

Vincent Laurenzano, Chair	New York
Clyde Galloway, Jr.	Florida
Arnold Dutcher	Illinois
Lewis Melahn	Missouri
William H. McCartney	Nebraska

REINSURANCE (E) TASK FORCE (Cont'd)

Assumption Reinsurance Working Group

James Hanson, Chair	Illinois
Lewis Wharff	Arkansas
Meyer Baruch	New York
Chuck Renn	Missouri
Craig Gardner	Texas

Assumption Reinsurance Advisory Committee

Patrick L. Carmody, Chair	Mutual of Omaha
Joseph M. Belth	The Insurance Forum
Carolyn Cobb	American Council of Life Insurers
Jim Dwyer	Lord, Bissell & Brook
Gerald Fisher	North American Reinsurance Corp.
Donald J. Greene, Esq.	LeBoeuf, Lamb, Leiby & MacRae
Beth Kravetz	Washington, D.C.
Jon C. Ogg	National Assoc. of Life Corporations
Stephen E. Rahn	Lincoln National Corporation
Edmond F. Rondepierre	General Reinsurance Corporation
Eden D. Sarfaty	National Organization of Life & Health Insurance Guaranty Associations
Phil Schwartz	American Insurance Association
Jane Hummel Simmons	Sullivan Payne Company
William Weller	Health Insurance Association of America

1991 Charge:

1. To provide assistance and technical expertise regarding the assumption of reinsurance as the Working Group drafts model law/regulation.

Reinsurance Database Working Group

James Schacht, Chair	Illinois
Terry Rankin	Nevada
Vincent Laurenzano	New York
Randy Blumer	Wisconsin

REINSURANCE (E) TASK FORCE (Cont'd)

Reinsurance Advisory Committee

Edmond F. Rondepierre, Chair	General Reinsurance Corp.
Jack H. Blaine	Reinsurance Association of America
Jonathan F. Bank	Buchalter, Nemer, Fields, Chrystie & Younger
Richard Blum	Guy Carpenter & Co. Inc.
Harry D. Boyd	Harbor Insurance Company
Carolyn Cobb	ACLI
Francis T. Donahue	John P. Woods Company, Inc.
Gerald F. Fisher	North American Reinsurance Corp.
Patrick J. Foley	American International Group
Ronald S. Gass	American Insurance Association
John Gavin, Esq.	Hopkins & Sutter
Donald J. Greene	LeBoeuf, Lamb, Leiby & MacRae
Robert F. Hall, Esq.	American Re-Insurance Company
M.S. Harvey	Mercantile and General Reinsurance
John J. Hayden	Mercantile and General Reinsurance
L. Jane Hummel	Sullivan Payne Company
J. Wesley J. Kinder	La Habra, California
Andrew Klivan	Norman Reitman Company, Inc.
Albert B. Lewis	Bower & Gardner
Janet B. Melchione	Prudential Reinsurance Company
Frank Nutter	Alliance of American Insurers
Nicholas Pearson, Esq.	Carter, Ledyard & Milburn
Louis H. Roushon, Jr.	Ropers, Majeski, Kohn, Bentley, Wagner & Kane
Don Seely	Lincoln National Corporation
T. Darrington Semple, Jr.	Boca Grande, Florida
Jane Hummel Simmons	Sullivan Payne Co.
Gerald J. Sullivan	Gerald J. Sullivan & Assoc., Inc.
Thomas M. Tobin	Skandia America Reinsurance Corp.
Harold Tract	Kroll & Tract
William J. Wall	Ellison, Inc.
Brooks White	The Continental Insurance Co.
Robert L. Zeman	Natioal Assoc. of Independent Insurers

<u>1991 Charge:</u>

1. To provide input on matters involving reinsurance before the Task Force.

SURPLUS LINES (E) TASK FORCE

David Walsh, Chair	Alaska
Salvatore R. Curiale, Vice Chair	New York
Jim Schacht	Illinois
John J. Dillon III	Indiana
David J. Lyons	Iowa
Hunter O. Wagner, Jr.	Louisiana
George Dale	Mississippi
William H. McCartney	Nebraska
Kenneth Erickson	Wyoming

SSO Staff Support: John Darwood/David B. Simmons

Mission Statement:

The mission of the task force is to foster discussions on surplus lines matters and develop or amend model legislation as necessary.

1991 Charge:

1. Continue to review the practice of non-admitted insurers effectively writing business on behalf of related admitted insurers.
2. Investigate the extent to which unauthorized alien insurers are active in the surplus lines marketplace to determine whether changes to the Model Surplus Lines Law are appropriate. (New Charge)
3. Complete the current amendment to the tax provisions of the Model Surplus Lines Law by finalizing the requisite regulations.
4. Review the financial criteria within the NAIIO Plan of Operation to determine whether the trust fund requirement should be linked to such factors as premium volumes, nature of business, and capital and surplus.

CASUALTY ACTUARIAL (TECHNICAL) TASK FORCE

Gary Weeks, Chair	Oregon
John Garamendi, Vice Chair	California
Joanne Hill	Colorado
Margurite C. Stokes	District of Columbia
Jim Schacht	Illinois
William H. McCartney	Nebraska
Samuel F. Fortunato	New Jersey
Fabian Chavez	New Mexico
Salvatore R. Curiale	New York
Jim Long	North Carolina
Richard G. Marquardt	Washington

SSO Staff Support: Jean Olson/Glenda Channel

Mission Statement:

The mission of the task force is to identify, investigate and develop solutions to actuarial problems in the property and casualty insurance industry with the ultimate goal of maintaining the financial health of property and casualty insurers. This is to be done by providing assistance and reporting to the Personal Lines (C) Committee, the Commercial Lines (D) Committee, the Special Insurance Issues (E) Committee and the Financial Condition (EX4) Subcommittee.

1991 Charge:

1. Develop accounting manual language for reserves required for retirement coverage under claims made professional liability contracts.

2. Review present standards and procedures and explore development of new standards and procedures for improving and insuring the adequacy of loss reserves for property and casualty companies.

3. Monitor and refine reporting requirements for property and casualty companies to insure accurate disclosure of loss reserves.

4. Continue to review and improve requirements for actuarial opinions of property and casualty reserves.

5. Consider and develop solutions for other relevant property and casualty actuarial issues.

Casualty Actuarial (Technical) Advisory Committee

Warren P. Cooper, Chair	Huggins Financial Services
Carole J. Banfield	ISO
Michael D. Covney	Re Capital Reinsurance Corp.
Alan C. Curry	State Farm Mutual Automobile Insurance Company
Sholom Feldblum	Liberty Mutual Insurance Co.
Edward W. Ford	Mercer Meidinger Hansen
David G. Hartman	Chubb Group of Insurance Companies

CASUALTY ACTUARIAL (TECHNICAL) TASK FORCE (Cont'd)

Casualty Actuarial (Technical) Advisory Committee (Cont'd)

Tim Kolojoy	Coopers & Lybrand
Thomas J. Kozik	Allstate
Jerome A. Scheibl	Wausau Insurance Companies
Richard H. Snader	United States Fidelity & Guaranty Company
James W. Yow	Aetna Life and Casualty Company

<u>1991 Charge:</u>

1. Determine necessity of revisions to Schedule P reserve lists and loss reserve discounting actuarial opinion.

LIFE AND HEALTH ACTUARIAL (TECHNICAL) TASK FORCE

John Garamendi, Chair	California
Philip W. Barnes, Vice Chair	Texas
Joanne Hill	Colorado
Margurite C. Stokes	District of Columbia
Jim Schacht	Illinois
Joseph A. Edwards	Maine
John A. Donaho	Maryland
William H. McCartney	Nebraska
Samuel F. Fortunato	New Jersey
Fabian Chavez	New Mexico
Salvatore R. Curiale	New York
Jim Long	North Carolina
Gary Weeks	Oregon
Richard G. Marquardt	Washington
Robert D. Haase	Wisconsin

SSO Staff Support: Jean Olson/Glenda Channel

Mission Statement:

The mission of the task force is to identify, investigate and develop solutions to actuarial problems in the life and health insurance industry with the ultimate goal of maintaining the financial health of life and health insurers. This is to be done by providing assistance and reporting to the Life Insurance (A) Committee, the Accident and Health Insurance (B) Committee, the Special Insurance Issues (E) Committee and the Financial Condition (EX4) Subcommittee, and their respective task forces. The task force is to continue to reevaluate the priorities of its projects, make recommendations for additions to or deletions from its projects and report their status to the appropriate committees, subcommittees and task forces.

1991 Charge

1. Complete work on the model "Actuarial Opinion and Memorandum Regulation" in support of the 1990 amendments to the "Standard Valuation Law".

2. Continue work on revisions to the "Standard Nonforfeiture Laws".

3. Monitor progress of the Society of Actuaries work on a new group annuity table.

4. Study long range concerns on the valuation actuary concept.

5. Monitor the progress of the Reinsurance Advisory Committee in its review of a number of actuarially related phases of reinsurance and coordinate actuarial task force activities on this subject with the work of the Sale of Future Revenues/Securitization of Nonadmitted or Unrecorded Assets (EX4) Working Group.

6. Monitor progress of the American Academy of Actuaries group developing non-guaranteed element annual statement interrogatories.

LIFE AND HEALTH ACTUARIAL (TECHNICAL) TASK FORCE (Cont'd)

7. Re-establish advisory group to provide assistance in the implementation of Actuarial Guideline XXV, "Calculation of Minimum Reserves and Minimum Nonforfeiture Values for Policies with Guaranteed Increasing Death Benefits."

8. Monitor the work of the joint ACLI/NALC task force on term policies with increasing premiums which purport to grade into whole life policies and develop an actuarial guideline for adoption.

9. Monitor work of the Society of Actuaries in developing a new mortality table for individual life policies.

10. Consider valuation, reporting forms and nonforfeiture values relating to long term care as well as other uses of life insurance providing for long term care benefits.

11. Monitor progress of proposed actuarial guideline on accelerated benefits.

12. Complete work on proposed NAIC Rate Filing Guidelines for Health Insurance.

13. Meet and make interim decisions on emerging actuarial issues.

14. Consider and develop solutions for other actuarial issues currently on the actuarial task force agenda.

Nonforfeiture Law Working Group

John O. Montgomery, Chair	California
Ted Becker, Vice Chair	Texas
Harry Marble	Maryland
Robert J. Callahan	New York
Larry Gorski	Illinois

Nonforfeiture Law Advisory Committee

Darrell W. Beernink	State Farm Life Ins. Co.
Douglas C. Doll	Tillinghast/Towers Perrin
Michael G. Gallo	New York Life Ins. Co.
Doug Hawley	Hawley Actuarial Software
Wilford A. Leonard	Jefferson-Pilot Life Ins. Co.
Carol A. Marler	Transamerica Occ. Life Ins. Co.
Michael E. Mateja	Aetna Life & Casualty
Esther H. Milnes	Prudential Insurance Co. of America
Ken Nelson	Alfa Life Insurance Co.
William H. Odell	W.H. Odell & Associates, Inc.
W. Keith Sloan	Bryan, Pendleton, Swats, McAllister
Anthony T. Spano	American Council of Life Insurance
Roy Woodall	National Assoc. of Life Companies

LIFE AND HEALTH ACTUARIAL (TECHNICAL) TASK FORCE (Cont'd)

Standard Valuation Law Working Group

John Montgomery, Chair	California
Larry Gorski	Illinois
Robert J. Callahan	New York

Standard Valuation Law Advisory Committee

Donald B. Maier	Metropolitan Life Ins. Co.
Walter S. Rugland	Milliman & Robertson, Inc.
Anthony T. Spano	ACLI
Roy Woodall	NALC

Standing Technical Advisory Committee

Walter Shur, Chair	New York Life Insurance Co.
Martin R. Claire, Secretary	New York Life Insurance Co.
John M. Bragg	John M. Bragg & Associates, Inc.
Gregory J. Carney	VALIC
Kenneth L. Gittings	North American Reassurance Co.
Norman E. Hill	Associated Madison Companies
J. Thomas Liddle	Equitable Life Assurance Society
Mark E. Litow	Milliman & Robertson, Inc.
Donald B. Maier	Metropolitan Life Insurance Co.
Michael E. Mateja	Aetna Life & Casualty
Richard S. Miller	Tillinghast/TPF&C
Esther Milnes	Prudential Insurance Company
William H. Odell	W.H. Odell & Associates
Walter S. Rugland	Milliman & Robertson, Inc.
Donald E. Scanning	The Principal Financial Group
William K. Tyler	Lincoln National Life Ins. Co.
Ronald J. Welch	American National Ins. Co.

Reinsurance Advisory Committee

Diane Wallace, Chair	Atrium Corporation
Frank A. Alvarez	ITT/Lyndon Insurance Group
Wayne Bidelman	Security Life of Denver
Linda Dougherty	The Prudential
Tim Herr	United of Omaha
Norman E. Hill	National Actuarial Consultants, Inc.
Robert P. Johnson	North American Reinsurance Corp.
Tom Kabele	Guardian Life Insurance Company of America
Denis Loring	The Equitable Life Assurance Society of the United States
Karen MacDonald	Transamerica Occidental Life Insurance Company
James D. Maughn	Employers Reinsurance Corporation
Gregory E. Morrison	London Life
Dave Scherr	North American Reassurance Co.
Alan W. Sibigtroth	Sibigtroth & Consultants Inc.

LIFE AND HEALTH ACTUARIAL (TECHNICAL) TASK FORCE (Cont'd)

Reinsurance Advisory Committee (Cont'd)

Pete Storms	The Travelers
James L. Sweeney	Munich America Reassurance Co.
William Tyler	Lincoln National Corporation
William Ward	Aetna Life Insurance Company
Roy Woodall	National Assoc. of Life Companies
Melville J. Young	Tillinghast Financial Centre

NAIC/NCOIL

Robert D. Haase, Chair	Wisconsin
Louis E. Bergeron, Vice Chair	New Hampshire
Lee Douglass	Arkansas
Susan Gallinger	Arizona
George Neumayer	Idaho
Jim Schacht	Illinois
John J. Dillon III	Indiana
Hunter O. Wagner, Jr.	Louisiana
George Dale	Mississippi
Lewis Melahn	Missouri
William H. McCartney	Nebraska
Terry Rankin	Nevada
Harold T. Duryee	Ohio
John G. Richards	South Carolina
Hanley C. Clark	West Virginia

SSO Support Staff: Sandra L. Gilfillan\Judith P. Lee

Mission Statement:

This committee is charged with the responsibility of developing recommendations for exchanging information and pursuing mutual objectives with the Conference of Insurance Legislators, developing strategy for the enactment by the states of the designated model acts and providing NAIC representation on the NAIC/COIL Joint Committee.

NAIC/IAIABC

Joseph A. Edwards, Chair	Maine
Mary Jane Cleary, Vice Chair	South Dakota
David Walsh	Alaska
Lee Douglass	Arkansas
Tom Gallagher	Florida
George Neumayer	Idaho
Hunter O. Wagner, Jr.	Louisiana
Gary Weeks	Oregon
Maurice Paradis	Rhode Island

SSO Support Staff: David B. Simmons

Mission Statement:

This committee is charged with the responsibility of developing recommendations for exchanging information and pursuing mutual objectives with the International Association of Industrial Accident Boards and Commissions and provides NAIC representation on the NAIC/IAIABC Joint Committee.

1991 Charge:

1. Draft legislation or regulation regarding employee leasing companies.

NAIC/JOURNAL OF INSURANCE REGULATION BOARD

Robert D. Haase, Chair	Wisconsin
David Walsh	Alaska
William H. McCartney	Nebraska
Jim Long	North Carolina
Earl R. Pomeroy	North Dakota
Harold C. Yancey	Utah

SSO Staff Support: Judith P. Lee/Cynthia Lafferty

Mission Statement:

The Board of the Journal of Insurance Regulation is a self-standing committee which oversees the publication of the Journal. Although associated with the NAIC, the Board is an independent entity with a separate budget. The Journal's bylaws require that the Board consist of six NAIC members, appointed by the NAIC officers, and five persons from outside the NAIC. The Board Chair and Vice Chair are elected by a vote of the Board members.

j:@cmte@1991@charges.doc

Senator METZENBAUM. Our next panel consists of Mr. James Firman, president and chief executive officer, United Seniors Health Co-op; Mr. John Donaho, insurance commissioner of the State of Maryland; Mr. Don Wesely, State senator from the Nebraska Legislature and co-chair of the NCSL Task Force on Insurance Company Insolvencies; and Mr. Ross Sargent, chief of staff to State Senator Patrick Johnston of the California Senate, on behalf of Senator Johnston.

Mr. Firman, we are very happy to have you with us, and please proceed.

STATEMENTS OF A PANEL CONSISTING OF JAMES P. FIRMAN, PRESIDENT AND CHIEF EXECUTIVE OFFICER, UNITED SENIORS HEALTH COOPERATIVE; JOHN A. DONAHO, INSURANCE COMMISSIONER, STATE OF MARYLAND; DON WESELY, STATE SENATOR, NEBRASKA LEGISLATURE, ON BEHALF OF THE NATIONAL CONFERENCE OF STATE LEGISLATURES; AND ROSS SARGENT, CHIEF OF STAFF TO SENATOR PATRICK JOHNSTON, CALIFORNIA SENATE, ON BEHALF OF SENATOR PATRICK JOHNSTON

Mr. FIRMAN. Thank you. Mr. Chairman, my name is James Firman. I am president and chief executive officer of the United Seniors Health Cooperative. We are a nonprofit consumer organization with 11,000 older members. We counsel on health insurance matters; we have done many studies of health insurance, and written books. We have no ties to any insurance companies and we don't sell any insurance products.

I have a full statement for the record. I would just like to——

Senator METZENBAUM. All of your statements will be included in the record in their entirety.

Mr. FIRMAN. Let me begin by emphasizing how important we believe effective model laws and national standards are for insurance regulation. National standards often lead to the prohibition of insurance policies with clauses and restrictions that are detrimental to consumer interests. National standards help identify and prohibit sales and marketing abuses and consumer fraud practices. Very importantly, national standards also serve a vital leadership function by establishing model laws and regulations that can be adopted by individual States with less expertise, interest or resources to develop good standards on their own.

It should be axiomatic that good consumer protection laws and regulations cannot be developed without substantial and thoughtful input from knowledgeable consumers and their representatives. I noticed from the statistics you cited that 12 out of the 14 consumer representatives in the NAIC advisory process participated in the Medigap and long-term care areas. which are the two that I would like to talk to today.

By my calculation, that means 90 percent of the consumer representatives participate in these two areas, and unfortunately I must report that I believe that consumer participation in the Medigap and long-term care areas is lacking to the point that the public interests are not being as well served as they should be.

For example, in 1990 the NAIC undertook an initiative to strengthen the consumer protection aspects of the model legislation and regulation for long-term care insurance. Despite diligent efforts by the NAIC to identify and encourage consumer participation in the advisory committee, the actual results were dismal.

At most advisory committee meetings, the ratio of industry representatives to consumer representatives was on the order of 20 or 30 to 1. Counting additional industry strategy meetings and preparatory time, the actual ratio of industry input to consumer input was at least 100 to 1.

Particularly troublesome was the fact that the final report to the NAIC that came from the advisory committee implied that the committee's recommendations reflected the views of both consumer and industry groups. In fact, the report accurately reflected the views of only the insurance industry. As a result, the consumer protection amendments approved by the NAIC last year were, in my view, much weaker than they should have been.

One might assume that the situation has been remedied in the area of Medicare supplemental insurance regulation, where Congress has mandated that the NAIC seek advice from both consumer and industry representatives. In addition, that committee is chaired by one of the most proconsumer regulators that I know, Earl Pomeroy, who just spoke to you. However, although this process is somewhat better, it is still far from ideal.

To its credit, the NAIC did appoint an advisory committee composed of six consumer and six industry representatives. However, at a typical advisory committee meeting there will be 3 or 4 consumer representatives, because the other ones can't afford to attend, and 25 to 30 industry representatives. In addition, the industry people usually convene for another full-day meeting prior to the advisory committee meeting to get their ducks in a row.

There is, theoretically, an opportunity for the advisory committee to interact with the actual commissioners at joint meetings of the task forces and advisory committees usually held in conjunction with the NAIC quarterly meeting. Unfortunately, due to time and expense constraints, only one of the six appointed consumer representatives will be attending next week's quarterly meeting in Charleston, West Virginia, where several key issues related to Medigap regulation will be discussed and some decided.

The currently inadequate level of consumer participation in the NAIC advisory committee process is not the fault of the NAIC leadership, in my opinion. Commissioner Earl Pomeroy, who chairs the Medigap task force, and Commissioner Susan Gallinger of Arizona, who chairs the long-term care task force, are both outstanding public servants who have demonstrated that they sincerely want as much consumer input as possible. They are, in my opinion, two of the most proconsumer regulators among the bunch.

Unfortunately, even with this good intention, the results are that they and the NAIC and the American public are not getting the quality of consumer input that is needed to make the best possible decision. Frankly, if there were 50 Pomeroys and Gallingers participating in the process, my concerns about responsiveness would be somewhat mitigated. But as you have shown in your own records, many insurance regulators have much closer ties to the industry and are not as responsive to consumer views.

What, then, is the problem? If these people really want assistance, why aren't they getting it? Fundamentally, it seems to me that consumer groups do not have the resources to take to devote to the process. Industry participants have this responsibility as their primary job. They are well paid and this is what they're supposed to do.

Consumer representatives, with the exception of one, are not paid to do this. They have full-time responsibilities and they don't have the travel budget to come to the meeting. In fact, the only consumer organization that has any paid staff with job responsibilities is one that is an organization that profits $100 million a year from the sale of health insurance.

Senator METZENBAUM. Thank you very much.

Mr. FIRMAN. I realize I am short on time, so let me just——

Senator METZENBAUM. You are not short on time. You are out of time.

Mr. FIRMAN. I am out of time.

Senator METZENBAUM. I will give you one last sentence to wind up.

Mr. FIRMAN. Well, let me just say that I think the fundamental process is flawed. I think that the public interest would best be served by the establishment of a Federal commission comprised of regulators, consumers and industry that would have the responsibility for making these decisions. These decisions are too importantly to leave solely in the hands of the NAIC commissioners.

[The prepared statement of Mr. Firman follows:]

UNITED SENIORS HEALTH COOPERATIVE

TESTIMONY OF JAMES P. FIRMAN
BEFORE THE
SUBCOMMITTEE ON ANTITRUST, MONOPOLIES AND BUSINESS RIGHTS
OF THE U.S. SENATE COMMITTEE ON THE JUDICIARY
APRIL 9, 1991

My name is James Firman. I am President and Chief Executive Officer of the United Seniors Health Cooperative. Thank you for the opportunity to present my views on the issue of consumer participation in the development of national standards for insurance laws and regulations.

I represent a non-profit consumer organization with 11,000 members in the greater Washington area. Each year, United Seniors counsels several thousand older persons on health insurance issues. Our organization has conducted several studies of Medigap and long-term care insurance. We have written a variety of books for consumers and professionals on health insurance. We do not sell or endorse any insurance products and have no ties to any insurance companies.

Effective national standards for insurance regulation are the best way for Congress to ensure that citizens in every state have at least a minimum level of consumer protection. National standards often lead to the prohibition of insurance policies with clauses and restrictions that are unfair or detrimental to consumer interests. National standards can identify and prohibit sales and marketing practices that lead to consumer fraud and abuse. National standards also serve a very important leadership function by establishing model laws and regulations that can be adopted by individual states with less expertise, interest or resources to develop good standards on their own.

Within guidelines established by Congress, the National Association for Insurance Commissioners (NAIC) currently has the sole responsibility for developing national standards for insurance regulation in key areas of national interest such as Medigap and long-term care insurance. With varying degrees of industry and consumer input, a small number of NAIC staff and members develop model laws and regulations which are then approved by a majority vote of the full NAIC membership.

Good consumer protection laws and regulations cannot be developed without substantial and thoughtful input from knowledgeable consumers and their representatives. Unfortunately, in the two areas of insurance regulation in which I am directly involved, Medigap and long-term care insurance, consumer participation is seriously lacking to the point that the public interests are not being served as well as they should be.

A not-for-profit organization of health care consumers helping people to achieve health, independence and financial security
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Consumer participation in the NAIC Advisory process for long-term care insurance regulation has been paltry at best. For example, in 1990 the NAIC undertook an initiative to strengthen the consumer protection aspects of the model legislation and regulations. Despite diligent efforts by the NAIC staff to identify and encourage consumer representatives to participate in Advisory Committee process, the actual results were dismal. At most Advisory Committee meetings, the ratio of industry representatives to consumer representatives was on the order of 20 or 30 to 1. Counting additional industry strategy meetings and preparatory time, the actual ratio of industry input to consumer input was at least 100 to 1.

Particularly troublesome was the fact that the final report to the NAIC that came from the Advisory Committee implied that the Committee's recommendations reflected the views of both consumer and industry groups. In fact, the report accurately reflected only the views of the insurance industry. As a result, the consumer protection amendments approved by the NAIC last year were, in my view, much weaker than they should have been.

One might assume that the situation has been remedied in the area of Medicare supplemental insurance regulation where Congress has mandated that the NAIC to seek advice from both consumer and industry representatives. Although the process is somewhat better, it is still far from ideal. To its credit, the NAIC did appoint an Advisory Committee composed of six consumer and six industry representatives. However, at a typical Medicare Supplemental Insurance Advisory Committee meeting, there will be three or four consumer representatives (those from out of town are unable to attend) and 25 to 30 industry representatives. In addition, the industry representatives usually convene for another full day meeting the day before the actual Advisory Committee meets to develop their positions in advance.

Joint meetings of the NAIC Task Force and the Advisory Committee provide an important opportunity for insurance regulators, consumer and industry representatives to get together to discuss key issues. Unfortunately, most consumer representatives on the Medicare Supplement Advisory Committee are unable to devote the time and expenses necessary to attend these meetings, usually held in conjunction with NAIC quarterly meetings. For example, only one of the six appointed consumer representatives will be attending next week's quarterly NAIC meeting in Charleston West Virginia, during which several key issues regarding the standardized Medigap policies and benefits will be discussed and/or decided.

The currently inadequate level of consumer participation in the development of national standards for Medicare supplemental and long-term care insurance is by no means the fault of the NAIC leadership and staff. Commissioners Earl Pomeroy of North Dakota and Susan Gallinger of Arizona are both outstanding public servants who have demonstrated that they sincerely want as much consumer input as possible. I have found these two individuals to be always willing to listen and respond to the views of consumer representatives. Unfortunately, in my view, they are not getting level and quality of consumer input they need to make the best possible decisions.

Frankly, if there were fifty Pomeroys and Gallingers participating in the NAIC and its Task Forces, my concerns about the responsiveness of the NAIC to consumer views would be somewhat mitigated. Unfortunately, some insurance commissioners have much cozier relationships with the insurance industry and are not as interested in what consumers have to say. Furthermore, some members of the NAIC Task Forces that make the key decisions do not appear to spend very time on the issues, thus leaving the real work to a few assistant commissioners. At least one key NAIC Task Force member has the misguided view that regulators are not doing an effective job unless both consumer and industry representatives disagree with their decisions.

If most of the leadership and staff of the NAIC genuinely wants consumer input, why is there so little of it? I believe that a large part of the problem is that potential consumer representatives have almost no resources to devote to this process, while the insurance industry will literally spare no expense to ensure that their views are well known by the insurance commissioners.

Whereas for most industry representatives participation in the NAIC advisory process is a primary or sole job responsibility, most consumer representatives are required to make the time for NAIC work while still completing a full set of other employment responsibilities. To the best of my knowledge, the only consumer organization that has any paid staff members with job responsibilities that include participation in the NAIC advisory process is a membership association that also nets well over $100 million annually from the sale of health insurance.

The individuals best able to represent the interests of consumers are simply unable to volunteer the time and resources necessary to participate fully in the NAIC process for developing national standards. Full participation as a member of an Advisory Committee requires at least 25 - 30 days per year: 16 days for quarterly NAIC meetings, four or more days for separate advisory committee meetings, plus preparatory work. In addition, each person needs a travel budget of at least $3,000 to $5,000 annually to be able to attend the meetings which are held in various locations throughout the country. It is unrealistic to expect that consumer representatives who work for non-profit organizations are in a position to donate 30 days plus travel expenses each year on a pro bono basis.

However, even if there were sufficient consumer input into NAIC advisory committees, I believe the fundamental process for obtaining and considering advice is flawed and should be changed. Typically, Advisory Committees meet on their own to develop recommendations, many of which are often ignored by the NAIC because they reflect primarily the industry's point of view. Because consumers, regulators and industry representatives are not in the same room developing standards together, the result is too often sub-optimal national standards, regulations and model laws.

My experiences over the past three years lead me to the following recommendations:

1. The American people deserve the best possible national standards, model laws and regulations to ensure adequate consumer protection in Medigap, long-term care and probably other key areas of insurance regulation.

2. The responsibility for development of national standards, model laws and regulations is too important to leave solely to the NAIC. Consumer and industry representatives should also have some say in determining what standards are finally adopted.

3. The public interests would be better served by the establishment of Federal Commissions which determined national standards for at least a few key areas of insurance regulation. For example, Congress could establish a Federal Commission for Long-Term Care Insurance Regulation comprised of seven NAIC representatives, four consumer representatives and four industry representatives. Members of the Commission could be appointed either by Congress, the President or the Secretary of Health and Human Services.

4. Both consumer representatives and regulators on the Federal Commission should be compensated for their time and expenses to ensure that they can put in the time and effort that is needed. Funding should also be available to the NAIC which should provide the necessary staff work.

5. Funding for a Federal Commission would probably cost between $150,000 and $200,000 per year. I recommend that one-half of the funding be provided by Congress and one-half by the NAIC from a levy on the insurance companies. This is a small price to pay to ensure the best possible standards, laws and regulations for areas of insurance where billions of dollars and the national interests are at stake.

The establishment of Federal Commissions, in which consumers industry representatives and regulators participate as equals, would result in fundamental and beneficial changes in the way insurance laws and regulations are developed. It would allow the level and quality of participation, give-and-take and creative thinking that is necessary to develop the best possible national standards, laws and regulations.

Thank you for the opportunity to present these views. I will be glad to respond to any questions you may have.

Senator METZENBAUM. Thank you very much.

Mr. John Donaho, Insurance Commissioner of the State of Maryland. We are happy to have you with us, sir.

STATEMENT OF JOHN A. DONAHO

Mr. DONAHO. Thank you, Mr. Chairman. Maryland has expressed a great interest in the adoption of standards for solvency and for effective regulation, as the governor appointed a blue ribbon task force to examine the State's insurance needs, and that task force has recently made recommendations just prior to the meeting of the General Assembly to the governor.

The governor presented a body of legislation dealing with capital and surplus and other matters of solvency—rehabilitation and liquidation, broker control of insurers, managing general agents, and disclosure of impairment—to the General Assembly. The General Assembly has just finished; they have adopted, I think, all of that legislation, with one possible exception or variation.

This blue ribbon group, along with my organization and the governor, is intimately interested in achieving accreditation by NAIC in accordance with its newly developing processes. We hope to join New York and Florida soon. In the process of achieving these goals, the use of the NAIC model legislation has been of extraordinary importance to us.

The legislation, once in place adopting the model laws that have been referred to—the next problem for us is implementation, and that throws us face to face with a very critical element; namely, how do we achieve the funding for adequate regulation.

I will, in May, have been commissioner for two years, and during my brief tenure the funding for the division as a proportion of the premium tax has been going downward. So, in reality, we have less funding, less resources, proportionately, to do a more extensive job. Sometimes I refer to my outfit as attempting to dig a ditch with a feather duster. But the basic element is we have to get a handle on the problem and we have to get adequate funding with which to do it.

As we seek to achieve both our statutory requirements and oversight, we have to look once again at the possibility of grabbing a larger slice of the premium tax. Now, from my examination of the premium tax throughout the country, there is no State which does not raise enough money through the premium tax, which was initially placed on the policyholders for the sole purpose of financing adequate regulation. The resources are there.

So if we are to move ahead and we are to consider Federal regulation, which I do not think is the answer, we have to find some way of achieving regulation with adequate funding. I say Federal regulation is not the answer for one basic reason. Rate regulation cannot be separated from solvency, and in my judgment the Federal Government cannot efficiently and effectively deal with rate regulation.

If the Federal Government is to perform and act in this area, then its interest should be in assisting in the fixing of minimum standards following the recommendations of the NAIC dealing with financial standards, and it could be that, as the Federal Government has done in other areas, it could then require not only the standards, but appropriate financing, as it does in game and fish where it requires the dedication of revenues for this purpose.

Increasingly, by the way, Federal laws are imposing additional requirements upon State insurance regulators—for example, Medigap and Medicare.

Senator METZENBAUM. Could you wind up, please, Mr. Donaho?

Mr. DONAHO. Surely. I think I have brought forth those basic elements which are included in my written testimony before you.

[The prepared statement of Mr. Donaho follows:]

Testimony before the U.S. Senate Subcommittee on Anti-Trust, Monopolies and Business Rights

John A. Donaho
Maryland Insurance Commissioner

INTRODUCTION

I am pleased to appear before you today to have an opportunity to express my views on the adequacy of State regulation of insurance and its funding.

At the 1991 Maryland Legislative Session, Maryland Governor, William Donald Schaefer, caused to be introduced a package of insurance solvency bills that were based on the recommendations of his blue ribbon Governor's Commission on Insurance and enthusiastically supported by me as the Insurance Commissioner. The highlight of the legislative package is a bill that proposes to raise the minimum capital and surplus requirements in Maryland for the 1st time since 1964. Other bills concern rehabilitation and liquidation, broker controlled insurers, managing general agents, fraud, and disclosure of impairment to bring the statutes into compliance with the NAIC requirements for accreditation.

As the session comes to a close, several of the bills await the Governor's signature while most of the others show promise for passage into law. Thus, I must now address the ongoing issue of securing adequate funding to implement solvency laws and regulations. Although the funding problem has always plagued State insurance regulators, increasing complexity in the insurance industry and its investments, a downward economic trend, and the increase in significant insurance insolvencies all accentuate the funding problem. With the NAIC-led drive towards better solvency regulation gaining speed in the 1990s, insurance regulators nationwide are working to bolster statutory solvency requirements and oversight. However, funding simply has not kept pace.

The source of funds for State Insurance Departments in 25 States is, in part or whole, the premium tax. All other State Insurance Departments, including Maryland, are funded by the State's general fund into which the premium tax is received as revenue. Yet, whether a State derives its funding directly from the premium tax or from the general fund, insurance regulators nationwide receive an average of 7.43% of the premium tax as budget (NAIC, 1989 the most recent data available). Thus the premium tax, which was created in 1872 for the sole purpose of funding the regulation of insurance, now fails to serve its original purpose in many States.

In Maryland, 6.76% of the premium tax or $8.4 million was devoted to insurance regulation in Fiscal Year 1989. (However, $375,000 of the budget was a unique, one-time, supplement for automation equipment.) In FY 1990, the Maryland budget as a percentage of premium tax was 5.61%.

Fiscal years 1991 and 1992 indicate a continuation of the devastating downward trend in budget as a percentage of premium tax. Because of the State administration's austerity program, the FY 1991 Insurance Division budget of $8.8 million was reduced $900,000 to $7.9 million. As a percentage of the 1991 premium tax, the budget equalled 5.52%. For 1992, the Maryland Insurance

Division has an allowance of $8.0 million or 5.24% of the estimated premium tax.

I have sought a supplemental budget of $2.9 million for 1992 over the 1991 allowance to no avail. Our budget for FY 1992 will be $800,000 less than FY 1991. I can tell you beyond a peradventure of a doubt that we need $11 million to do a minimum job. That is $3.1 million more than we will be appropriated for next fiscal year. How are we to cope with greater responsibility with less resources?

Maryland's situation is not isolated from the recent experience of regulators nationwide. If we are to adequately protect the public, each State must face its responsibility to provide both the authority and the tools and resources to do the job. Each State collects enough in premium taxes to do this.

Federal regulation is not the answer. Rate regulation cannot be separated from solvency regulation and rate regulation would be an impossible task for the federal government to perform. If the federal government is to act, it can take a leaf from the other activities in which it is involved. It can fix minimum standards and it can require adequate State funding. It does this for game and inland fish activities by requiring the dedication of license fees collected to the financing of the programs. Increasingly, federal laws and regulations are imposing requirements upon State insurance regulation (Medigap, Medicare, etc.). The increased statutory responsibility cannot translate into proper regulation without adequate funding.

Based upon the latest (1989) data from NAIC, Maryland ranks 11th in budget, 14th in premium tax and 18th in ratio of budget to premium tax among the States. The uninformed might conclude that by comparison Maryland is in a good position. It would be self-delusion to so conclude.

The blue ribbon Commission on Insurance appointed by Governor Schaefer, which was previously referred to, became well aware of the funding problem and in its recommendations emphasized the need for carrying out those very laws it was recommending. In the drafting of those laws, the NAIC and its model laws were exceedingly helpful to the deliberations of the Commission, of which I was a member. In fact, the NAIC is one of those institutions which if it did not exist would have to be invented. As a State regulator, I can testify that we are in regular and frequent contact with the NAIC not only in the drafting of laws but in their implementation. We look upon the NAIC as a reservoir of information on State problems and practices; of course, model laws frequently need to be adapted to local conditions and local practices of draftsmanship and conditions.

States are faced with difficult administrative problems in the implementation of model laws. There are very subtle pressures on the part of both industry and consumer interests which impact upon regulation. To some extent, there is an interest in avoiding regulation on the part of the industry and a like interest in punitive requirements on the part of consumer advocates. The greatest problem however lies in the funding in order to achieve adequate implementation. In my own instance I have described my organization as one attempting to dig a ditch with a feather duster.

In drafting the proposed legislation which is currently being enacted by the Maryland General Assembly, the Governor was very careful to appoint a commission balanced in representation among representatives of the industry, the organized consumers, the public and the legislature. Each had a full opportunity to present its views and influence upon the Commission's deliberations and subsequently in the legislative process.

There is no question that the current insurance regulatory system can be improved. It is essential that the laws be administered without fear or favor. The staff resources and research capabilities must be available so that regulatory agencies can be kept abreast of changes in the needs and the increasing complexity of the market place so that the regulators' laws, regulations and administrative practices can keep pace. The high price of actuarial talent necessary is a critical factor. A vital need is for adequace automation. One of the principle problems with which every State regulator is confronted involves the need for processing large amounts of data and the utilization of such data and information which can only be achieved by proper automation. All of these factors, of course, rest upon the essential adequate funding, without which, the whole effort lapses into mediocrity.

FEDERAL/STATE INSURANCE REGULATORY ISSUES

There are many interrelated aspects of insurance regulation that contribute to the complex nature of the regulatory process -- such as ratemaking oversight and assurance of company solvency. In addition, for all intents and purposes, there are two insurance industries, each with its seprrate issues. Factors relating to the life and health industry in the areas of solvency and products sold are different from those factors in the property and casualty industry.

The complexities of insurance regulation and the insurance industry itself suggest the need for continued State regulation. However, there is an area in which federal oversight could prove beneficial to the regulatory process. That area resides in the establishment of minimum solvency and funding standards for insurance regulation in the States.

FEDERALLY SET MINIMUM REQUIREMENTS

All States should be required to maintain federally established minimum financial standards in the areas of (1) solvency requirements for companies and (2) funding requirements for State insurance regulators.

SOLVENCY REQUIREMENTS

The purpose of minimum solvency requirements would be to set basic levels of capital and surplus that a company must have in order to do business. For life insurance companies those minimums vary today from $400,000 in Vermont and Montana, to $6 million in New York and Rhode Island. In Connecticut the minimum solvency requirements for life insurance companies are established on a company by company basis. In Maryland the minimum capital and surplus requirement is $1 million.

For multi-line property and casualty insurance companies the current minimum capital requirement varies from $750,000 in Delaware, Oklahoma, and West Virginia to $6 million in Alaska. In Maryland there is a $1 million requirement. For mono-line companies the variance is from $350,000 in Utah to $4 million in Vermont. The Maryland figure is $625,000. It should be noted that the numbers cited above are for 1990.

The federal government should establish a minimum requirement for insurance companies in the range of the higher numbers cited above as there is an unquestionable relationship between capital and surplus minimums and solvency. Of course, there should be a period of time allotted to enable companies who do not meet those standards to adhere.

STATE FUNDING

An even more pressing need than minimum solvency requirements for insurance companies is minimum funding for State Insurance Departments. In 1989, the latest year available, the national average percentage of funds allocated to Insurance Departments from premium taxes collected was 7.43%. In Maryland, the percentage has fallen over t'.e last three years from 6.76% in 1989 to an estimates 5.24% for 1992.

Although Maryland is not an especially large State, it does possess a rich insurance market and therefore serves as a good example of the need for federally regulated minimum funding requirements. In 1989, Maryland saw 1,397 companies sell roughly $5.6 billion in insurance to companies and private citizens statewide. Additionally, Maryland's 100 domestic insurers alone have an excess of $50 billion in assets.

Maryland's budget as a percentage of premium tax falls, well short of the 10% figure commonly accepted among industry experts as the adequate resource level for a State Insurance Department. In fact, only 11 States operate on 10% or more of the premium tax. Consider this against the background of the 1988 joint recommendation of the Consumer Insurance Interest Group and the National Association of Professional Insurance Agents that recognized the "overall goal of allocating a minimum of 10 percent of premium taxes collected" (CIIG/PIA).

Indeed, varied industry experts unanimously agree on the issue of inadequate funding. From the highly criticized Public Citizen report, Insurance: The Next Industry in Crisis, to the U.S. General Accounting Office report, Insurance Regulation: Problems in the State Monitoring of Property/Casualty Insurer Solvency, the consensus is that State regulators incur "serious problems in fulfilling their responsibilities in insurer solvency regulation because of lack of funds" (GAO).

It is important that the State regulators have the automation necessary to properly perform their functions. It is important that Insurance Departments have adequate funding to properly review and approve rates, and to properly examine companies' books. Additionally, funding should be available to permit States to target examine companies on an annual basis.

A budget that represents 10% of the premium tax would provide sufficient funds for State Insurance Departments to tackle these goals and perform at least adequate jobs monitoring the insurance industry in their respective States.

Insurance is an increasingly complicated industry with solvency ramification that pervade all levels of our society. If insurance solvency regulation remains inadequately funded, the victim of such negligence will invariably be the citizen.

STATE VERSUS FEDERAL REGULATION

It is impossible to separate the regulatory function of rate making and the approval of rates from the regulatory function of overseeing solvency without causing detrimental effect. The regulator must balance political and public pressure for lower rates with the need for a rate to be adequate. Adequacy pertains not only to continued solvency, but, also to maintaining enough return to keep the necessary capital in the industry. Currently in Maryland we have 29 people devoted to reviewing some 40,000 rates and forms annually for the some 1400 companies doing business in my State today. Maryland is slightly above average in numbers in this area. Consider the difficulty of a federal bureaucracy dealing with these issues.

In addition, although the rate making methodology is identical across all the States, the factors involved in establishing a rate in the Baltimore/Washington corridor are entirely different from those involved in the State of Utah. An awareness of each individual State's demographics is an important factor in judging rates.

Another significant reason for keeping insurance regulation at the State level is that States currently police one another. A Pennsylvania domestic with a large portion of business in Maryland is reviewed carefully not only by the Pennsylvania Department but by the Maryland Department. Similarly, a large Maryland domestic is reviewed by other States in which the company has a considerable book of business. A rather public insolvency that occurred in 1990 was discovered by the actions of a State neighboring the domiciliary State. With unitary regulation, such an opportunity would not present itself.

Also, The NAIC presently provides a strong repository of information that is shared by all the States. The NAIC standard convention blanks, which all States have adopted, plus access to the data on the NAIC computers does induce certain standards across all States. It is clearly less expensive to maintain these than to duplicate them in a federal bureaucracy. There is no indication that the federal bureaucracy could do its job better than the many States.

INSURANCE INDUSTRY

The insurance industry is far from monolithic. The significant initial division is between life companies on one hand, and property and casualty companies on the other. Then within each division you have large companies versus small companies; State versus regional and nationals; direct insurers versus reinsurers; licensed insurers versus surplus line insurers. Most of the insurance companies, however not the insurance volume, are still small State or regional companies.

The distinction between life and property and casualty, should be strongly noted. The kinds of insurance they write are different. Many of the life products are more like certain investment and banking products than insurance products. Indeed the solvency issues that threaten the life industry are similar to those that threaten the thrift and banking industry (e.g. junk bonds and weak real estate investments). These issues have nothing in common with the property and casualty industry. The solvency issues facing the property and casualty industry are those of inadequate loss reserves and failure of reinsurance companies.

SUMMATION

I strongly urge continued State regulation of insurance with federal oversight of certain minimum standards to which the States and their insurance companies must adhere. I also urge that any discussion of allowing financial institutions (e.g banks, etc...) to participate in the selling of insurance demonstrate considerable appreciation for the difference between life insurance and property and casualty insurance. The two branches of insurance deserve to be viewed as separate industries and the entrance of new participants in each branch presents unique repercussions for industry issues.

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APPENDICES

APPENDIX 1: MARYLAND BUDGET TO PREMIUM TAX RATIO, 1989-1992

APPENDIX 2: 1989 NAIC STATE RESOURCE SURVEY DATA RANKED BY RATIO OF BUDGET TO PREMIUM TAX

APPENDIX 3: 1989 NAIC STATE RESOURCE SURVEY DATA RANKED BY BUDGET

APPENDIX 4: 1989 NAIC STATE RESOURCE SURVEY DATA RANKED BY PREMIUM TAX

MARYLAND BUDGET TO PREMIUM TAX RATIO

		BUDGET	PREMIUM TAX	RATIO
1989	ACTUAL	$8.4 MIL	$123.6 MIL	6.76%
1990	ACTUAL	$7.5 MIL	$133.8 MIL	5.61%
1991	APPROPRIATION	$7.9 MIL	$143.3 MIL	5.52%
1992	ALLOWANCE	$8.0 MIL	$152.7 MIL	5.24%

*1991 AND 1992 premium tax are estimates

1989 NAIC DATA RANKED BY RATIO

STATE	BUDGET	PREMIUM TAX	RATIO	RANK
CONNECTICUT	3,949,746	2,783,846	141.88%	1
FLORIDA	40,674,224	240,163,366	16.94%	2
NEVADA	6,561,831	45,486,526	14.43%	3
DELAWARE	2,768,400	22,489,520	12.31%	4
NEW YORK	59,032,140	496,000,000	11.90%	5
ALASKA	2,654,800	22,683,530	11.70%	6
TEXAS	51,246,939	449,809,981	11.39%	7
NEBRASKA	4,027,800	35,458,762	11.36%	8
IDAHO	3,552,300	31,833,400	11.16%	9
NORTH CAROLINA	18,874,394	173,324,992	10.89%	10
WYOMING	1,257,354	11,817,903	10.64%	11
MAINE	3,380,079	34,178,515	9.89%	12
ILLINOIS	14,726,000	157,239,027	9.37%	13
KENTUCKY	5,748,700	65,353,000	8.80%	14
KANSAS	4,641,593	61,865,559	7.50%	15
VERMONT	1,450,000	20,000,000	7.25%	16
WASHINGTON	6,449,410	91,935,268	7.02%	17
MARYLAND*	8,354,578	123,639,038	6.76%	18
WISCONSIN	4,803,500	71,310,450	6.74%	19
PENNSYLVANIA	11,414,000	190,100,000	6.00%	20
CALIFORNIA	66,576,000	1,137,472,195	5.85%	21
SOUTH CAROLINA	5,440,207	92,971,383	5.85%	22
NEW HAMPSHIRE	2,052,631	35,484,376	5.78%	23
VIRGINIA	10,380,150	190,281,656	5.46%	24
IOWA	4,472,396	84,439,972	5.30%	25
NEW MEXICO	2,437,200	46,424,516	5.25%	26
ARKANSAS	2,990,609	59,055,728	5.06%	27
OHIO	12,437,210	250,752,608	4.96%	28
LOUISIANA	6,013,994	126,044,151	4.77%	29
UTAH	2,007,400	42,375,303	4.74%	30
RHODE ISLAND	1,932,035	40,994,470	4.71%	31
OKLAHOMA	4,286,391	94,608,967	4.53%	32
GEORGIA	6,815,245	152,694,716	4.46%	33
NORTH DAKOTA	853,750	19,871,135	4.30%	34
COLORADO	3,313,000	79,255,124	4.18%	35
MINNESOTA	4,367,000	115,338,075	3.79%	36
ARIZONA	3,182,500	88,997,253	3.58%	37
WEST VIRGINIA	1,697,540	49,722,218	3.41%	38
TENNESSEE	4,672,400	137,716,400	3.39%	39
MISSISSIPPI	3,001,818	88,966,595	3.37%	40
MONTANA	902,243	26,764,755	3.37%	41
INDIANA	3,309,158	102,113,083	3.24%	42
SOUTH DAKOTA	752,322	24,044,006	3.13%	43
ALABAMA	3,447,042	139,420,922	2.47%	44
HAWAII	N.A.	53,757,099	N.A.	45
MASSACHUSETTS	6,154,395	N.A.	N.A.	46
MICHIGAN	N.A.	N.A.	N.A.	47
MISSOURI	N.A.	122,768,371	N.A.	48
NEW JERSEY	12,245,000	N.A.	N.A.	49
OREGON	N.A.	51,467,477	N.A.	50
AVERAGE	8,626,148	116,025,505	7.43%	

*MARYLAND DATA IS CORRECTED FOR CHANGES IN 1989

1989 NAIC DATA RANKED BY BUDGET

STATE	BUDGET	PREMIUM TAX	RATIO	RANK
CALIFORNIA	66,576,000	1,137,472,195	5.85%	1
NEW YORK	59,032,140	496,000,000	11.90%	2
TEXAS	51,246,939	449,809,981	11.39%	3
FLORIDA	40,674,224	240,163,366	16.94%	4
NORTH CAROLINA	18,874,394	173,324,992	10.89%	5
ILLINOIS	14,726,000	157,239,027	9.37%	6
OHIO	12,437,210	250,752,608	4.96%	7
NEW JERSEY	12,245,000	N.A.	N.A.	8
PENNSYLVANIA	11,414,000	190,100,000	6.00%	9
VIRGINIA	10,380,150	190,281,656	5.46%	10
MARYLAND*	8,354,578	123,639,038	6.76%	11
GEORGIA	6,815,245	152,694,716	4.46%	12
NEVADA	6,561,831	45,486,526	14.43%	13
WASHINGTON	6,449,410	91,935,268	7.02%	14
MASSACHUSETTS	6,154,395	N.A.	N.A.	15
LOUISIANA	6,013,994	126,044,151	4.77%	16
KENTUCKY	5,748,700	65,353,000	8.80%	17
SOUTH CAROLINA	5,440,207	92,971,383	5.85%	18
WISCONSIN	4,803,500	71,310,450	6.74%	19
TENNESSEE	4,672,400	137,716,400	3.39%	20
KANSAS	4,641,593	61,865,559	7.50%	21
IOWA	4,472,396	84,439,972	5.30%	22
MINNESOTA	4,367,000	115,338,075	3.79%	23
OKLAHOMA	4,286,391	94,608,967	4.53%	24
NEBRASKA	4,027,800	35,458,762	11.36%	25
CONNECTICUT	3,949,746	2,783,846	141.88%	26
IDAHO	3,552,300	31,833,400	11.16%	27
ALABAMA	3,447,042	139,420,922	2.47%	28
MAINE	3,380,079	34,178,515	9.89%	29
COLORADO	3,313,000	79,255,124	4.18%	30
INDIANA	3,309,158	102,113,083	3.24%	31
ARIZONA	3,182,500	88,997,253	3.58%	32
MISSISSIPPI	3,001,818	88,966,595	3.37%	33
ARKANSAS	2,990,609	59,055,728	5.06%	34
DELAWARE	2,768,400	22,489,520	12.31%	35
ALASKA	2,654,800	22,683,530	11.70%	36
NEW MEXICO	2,437,200	46,424,516	5.25%	37
NEW HAMPSHIRE	2,052,631	35,484,376	5.78%	38
UTAH	2,007,400	42,375,303	4.74%	39
RHODE ISLAND	1,932,035	40,994,470	4.71%	40
WEST VIRGINIA	1,697,540	49,722,218	3.41%	41
VERMONT	1,450,000	20,000,000	7.25%	42
WYOMING	1,257,354	11,817,903	10.64%	43
MONTANA	902,243	26,764,755	3.37%	44
NORTH DAKOTA	853,750	19,871,135	4.30%	45
SOUTH DAKOTA	752,322	24,044,006	3.13%	46
HAWAII	N.A.	53,757,099	N.A.	47
MICHIGAN	N.A.	N.A.	N.A.	48
MISSOURI	N.A.	122,768,371	N.A.	49
OREGON	N.A.	51,467,477	N.A.	50
AVERAGE	8,626,148	116,025,505	7.43%	

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APPENDIX 4

1989 NAIC DATA RANKED BY PREMIUM TAX

STATE	BUDGET	PREMIUM TAX	RATIO	RANK
CALIFORNIA	66,576,000	1,137,472,195	5.85%	1
NEW YORK	59,032,140	496,000,000	11.90%	2
TEXAS	51,246,939	449,809,981	11.39%	3
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AVERAGE	8,626,148	116,025,505	7.43%	

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Senator METZENBAUM. Thank you very much, Mr. Donaho.

The Chair is embarrassed to say that there is another committee hearing which I must attend for a very brief period of time. I will be back in probably 5 to 10 minutes, but the subcommittee will stand in recess for that period of time.

[Recess.]

Senator METZENBAUM. The chair apologizes for having to interrupt the hearing, but I had no choice.

Senator Wesely, we are very happy to have you with us, sir.

Senator WESELY. Wesely.

Senator METZENBAUM. Wesely?

Senator WESELY. Wesely, yes, thank you.

Senator METZENBAUM. We are happy to have you with us, sir.

STATEMENT OF DON WESELY

Senator WESELY. Senator Metzenbaum, it is a pleasure to be here. It is an honor to have a chance to testify before you and the subcommittee. My name is Don Wesely, State senator from Nebraska. I have come a long way to join you today. I cochair the National Conference of State Legislatures' Task Force on Insurance Company Insolvency. We have formed the task force last fall, and I was named a cochair and Dick Finan from Ohio is my colleague as cochair of the task force.

The task force was formed by Speaker John Martin of Maine, and we have been working diligently since the formation of the task force last fall. I guess I come before you, Senator Metzenbaum, to give you good news. The issues you have raised earlier in your opening comments, I think, were very relevant. It is unfortunate, I think, that we have waited so long to have model legislation proposed and enacted by the States, but I think things have changed as of last year.

In 1990 we saw a great deal of attention paid to this issue that had not been there previously. As you know, lawmakers tend to follow the interests of the public, and the public has now had their interest focused on this particular issue. I think with the First Executive stories that have come out and the further concerns that are expressed there and elsewhere, I think that interest will only grow.

As a result of the attention being paid to the issue, this task force has been formed and NCSL has made this a high-priority issue for our State legislatures. NCSL does represent all the State legislatures across the country.

We, in December, adopted a resolution which is included in your packet of material from me, which aggressively supported the model legislation proposed by NAIC. It called for the States to adopt that model legislation and to see it implemented. That is an important thing to note. NCSL does not typically recommend to our member States adoption of State legislation. That gets us in trouble with some of our members and we don't like to do that.

But in this case, we thought it was so important that we not only took the action; we made it an emergency action and adopted it immediately and made it immediately the policy of the NCSL. We then took that policy and we wrote letters to every legislative leader across the country asking them to consider the resolution and consider adoption of the model legislation. We included it in our national magazine in January to alert people to the issue, and we have had some results.

Thirty-eight States have introduced legislation regarding model acts proposed by NAIC. Eleven States have already enacted some of that model legislation. In fact, again, I bring you good news; Nebraska is among those.

For instance, you mentioned in one of your charts the model regulation to define standards for companies in hazardous financial condition. Nebraska just a few weeks ago adopted that. We are also joined, I understand, by South Carolina, West Virginia, and Iowa. So the number of States has already doubled from the chart that you had just in the last few weeks, and I hope that we will be joined by many other States as we move forward on this agenda.

We hope that by the end of 1992 most of the States of this country will have adopted the full complement of NAIC model legislation. We think that we have to give not only this legislative session, but the 1992 legislative session, because of the time it does take to introduce the bills, draft them and have them passed. It does take some time to do that, but we think by the end of 1992 we hope you will have us back and we will be able to report to you that most of the States have moved on this, and have moved aggressively in adopting these model acts. We are pushing hard on that.

We are also seeing other needs beyond the model acts. That is the first step. We think that is important, but we also want to look at guaranty funds. In a couple of days in Lincoln, as a matter of fact, my home town, we will be having our task force meeting to look at how we can further work on issues like guaranty funds, investment codes.

In fact, in Nebraska, again, we just adopted last week a very restrictive investment code dealing with the junk bond investments. There is no model act on this, and the Nebraska Legislature has adopted our own junk bond restriction, as well as other restrictions on real estate investment and other types of activity.

I just want to conclude by saying, Senator, that the NCSL plans to work with you and this subcommittee and the Senate and the House. We welcome the congressional interest in this issue; it has spurred the States on to action. I think the States are responding in a very constructive fashion. I think we have been cooperative in trying to work with all parties involved and interested in this issue.

We believe that the States overall do a good job of regulating insurance companies, but we acknowledge we can and must do better, and we are dedicated to achieving that goal. I think that, again, I bring you good news about action on the part of the State legislatures and the NCSL and my own State of Nebraska, and I am pleased for the opportunity to join you here today.

I did present some material that goes through in much more detail the concerns and information that you might be interested in.

[The prepared statement of Senator Wesely follows:]

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WILLIAM POUND
EXECUTIVE DIRECTOR

Statement of

Senator Don Wesely

Nebraska Legislature

On Behalf of the

National Conference of State Legislatures

Concerning

State Legislation to Address Insurance

Company Insolvencies

Senate Committee on the Judiciary

Subcommittee on Antitrust, Monopolies and Business Rights

April 9, 1991

1560 BROADWAY SUITE 700 DENVER COLORADO 80202 303-830-2200 FAX 303 863-8003

Mr. Chairman and Members of the Committee:

My name is Don Wesely. I am a member of the Nebraska unicameral Legislature, where I chair the Committee on Health and Human Services. I also serve as co-chair of the Task Force on Insurance Company Insolvencies of the National Conference of State Legislatures (NCSL).

I appear today on behalf of NCSL to comment on state legislation to reform state insurance regulation as a means of controlling the disturbing trend of insurance company insolvencies. I appear today also on behalf of my constituents in the State of Nebraska, where we have adopted recently a comprehensive set of solvency regulation measures.

As you know, NCSL represents all the legislatures in the American states, commonwealths, and territories. My testimony is based on NCSL policy resolutions, which represent the consensus judgment of our members. In general, NCSL's policy resolutions reflect our dedication to a strong federal system of government. Our advocacy activity is restricted in ordinary circumstances to issues of state-federal relations being considered by Congress, federal administrative agencies, and the U.S. Supreme Court.

Last December, however, NCSL made an exception to its general practice of not adopting policy urging particular state legislation. In light of our serious concerns about the effectiveness of state insurance regulation in dealing with insurance company insolvencies and upon the recommendation of the task force that I chair, NCSL endorsed the solvency policing agenda of the National Association of Insurance Commissioners (NAIC) and urged the speedy adoption of NAIC model laws related to solvency.

The NAIC standards and model laws, we conclude, are minimum requirements for the effective regulation by a state of the financial solvency of insurance companies. NCSL's policy statement further urges each state to consider whether the enactment of additional safeguards beyond these minimum NAIC requirements would be appropriate.

For example, in Nebraska, we adopted in the current legislative session not only NAIC model laws but also legislation implementing stringent new regulation of insurance company investments.

The NCSL Task Force on Insurance Company Insolvencies continues to study this problem and may issue further recommendations for state or federal action. We will meet in Lincoln, Nebraska on Thursday of this week to hear testimony on capital standards, early intervention by regulators, and guaranty funds. In May, we will meet in Washington, DC where according to our tentative agenda we will hear testimony related to the regulation of reinsurance and surplus line carriers, procedures for coordinating the rehabilitation or liquidation of insurance companies that operate in several states, and criminal sanctions for looting an insurance company.

We welcome these hearings by the Antitrust Subcommittee, Mr. Chairman, frankly, because the publicity will tend to provide a further impetus for the adoption of the NAIC model acts. These hearings also should spur NCSL and state legislative committees across the country to look for measures beyond the NAIC model laws that will protect the public interest.

Criticism by Congress of state action, or inaction, in this area to date has generally been constructive. Although auto insurance, product liability, medical malpractice, and rate regulation have been hot issues in state legislatures for several years, it is a fair criticism that state legislation related to the nuts and bolts of insurance solvency regulation has been too often neglected.

But thanks in part to hearings, investigations and reports by congressional committees, as well as by consumer groups, state legislative committees and the industry itself, the attention of the nation's state legislatures is now focused on insurance solvency legislation and the administration of state insurance departments.

I conducted a session at the NCSL Annual Meeting in Nashville, last August, where we looked closely at the issue of insurance company insolvencies and drew a standing room crowd of state legislators. Among other presentations we heard Jack

Burbidge, of IDS Financial Services, report on that company's projection that 20 percent of major life insurers face a serious risk of insolvency in the event of a severe economic downturn. The IDS projection, of course, is controversial and there is serious debate about whether the 20 percent figure is unduly alarmist. Nonetheless, it gets your attention as a state legislator when you hear a respected firm argue that one fifth of the one hundred largest life companies might be at risk. At the conclusion of that session, we met with incoming NCSL President, Speaker John Martin of Maine. He agreed that NCSL should take extraordinary steps to address the problem of insurance company insolvencies.

Upon assuming the Presidency of NCSL, Speaker Martin appointed a special Task Force on Insurance Company Insolvencies and charged it with finding means of reforming state solvency regulation.

In December, the task force met and adopted a comprehensive statement on insurance company insolvencies. This statement was subsequently considered by NCSL's officers pursuant to our emergency policy process and was unanimously approved as official NCSL policy.

The NCSL policy states that immediate state action is required to strengthen state insurance departments and to establish standards of financial regulation that will protect the safety and soundness of insurance companies. To achieve these goals, the NCSL policy specifically urges every state to adopt the model laws and regulations developed by the National Association of Insurance Commissioners, as minimum standards.

As the nation pays for a savings and loan debacle estimated to cost $150 billion to $500 billion, we cannot ignore warnings that insurance company insolvencies also could spin out of control. The warnings may or may not be overstating the case, but there is no question that we have a problem and must act swiftly to correct it.

I do not want to suggest that we face the immediate prospect of another thrift crisis. None of the responsible reports that I have studied suggest that. The vast majority of insurance companies are profitable and administered honestly by capable officers and directors. Most insurance companies, I am told, are better capitalized than the typical troubled thrift. And, whatever the problems faced by life insurers with investments, these are far more manageable than the problems resulting from thrift investments in real estate development, for example.

At the same time, the Mission and Transit failures, as documented in the Failed Promises report of the House Energy and Commerce Committee, illustrate that, just as in the case of saving and loans, losses can quickly mount to billions of dollars when insurance companies are mismanaged. Some of the management practices of the property and casualty companies investigated by the House committee bear a resemblance to the practices of failed thrifts.

The difficulty with investments appears more on the life insurance side. Junk bond and real estate investments appear to be a problem. The parallel to thrift investments in real estate and low grade securities is obvious. Even more worrisome is the danger of an asset to liability mismatch of the kind that mortally wounded much of the thrift industry in the late 1970s and early 1980s.

With respect to junk bonds, I am told that First Executive Life at one time had something like 49 percent of its assets in low-grade bonds. The IDS report says that "life insurers hold roughly 30 percent of $200 billion of low-grade or junk bonds outstanding." As the junk bond market goes sour, the potential solvency risks increase. I believe we need to seriously consider strict restrictions on such investments. That has been our approach in Nebraska.

In addition, life insurers are heavily invested in commercial mortgages at a time when that market is depressed. Vacancy rates for office building, we have been told, exceed 25 percent in Dallas and 14 percent in New York City. IDS reports that several large insurers have more than 50 percent of total assets in mortgages. At one time, commercial mortgages were regarded as a relatively safe investments, but with the massive overbuilding of commercial office space, resulting from the 1981 tax act and the Garn-St Germain Act, this is no longer a quiet and predictable area for investment by life insurers.

Another risk faced by life insurers is a potential mismatch between liabilities and assets, that could result if in the future interest rates that must be paid to attract new buyers of life insurance annuity products and guaranteed investment contracts (GICs) approach or exceed what life insurance companies earn on long-term investments. The reliance of life insurers on GICs and similar investment products puts them at risk in this area potentially in the same way that depository institutions are exposed to risk when inflation picks up dramatically. We recall what happened to thrifts that were stuck in the late 1970s with a large portfolio of home mortgages paying low interest at a time of inflation when high interest had to be paid to retain deposits. This was the fundamental cause of the thrift debacle in the opinion of many analysts.

Again, to keep a balanced view, we have received no evidence that life insurers are undercapitalized in the same way that thrifts were in the early 1980s. And, in contrast to the fast operators who took control of too many thrifts, it is my impression that most life insurance companies are conservatively and honestly managed, though undoubtedly there are exceptions. Also the industry reassures us that the commercial mortgage investments of life insurers, who after all have years of experience in this field, are more prudent than the short-term construction and development loans that got many thrifts into trouble. A few companies, like First Executive Life, may have plunged into junk bond investments, but it is my impression that most companies have not invested a disproportionate share of their assets in low-grade bonds.

Different points of view are reasonably held by different parties regarding the potential risk of insurance company insolvencies. I leave that for the financial experts to debate, because clearly there is a consensus that a problem exists and that insurance solvency regulation must be reformed. Such reforms are in everybody's interest. Consumer groups, state regulators, and state legislators have called for reform. Most of the industry is itself seeking more effective solvency regulation. Conservatively-managed firms, after all, first lose market share to the high-fliers and then must pay through guaranty fund assessments when they crash. Moreover, the industry is naturally eager to reassure policyholders about the safety of their investments and contracts. This industry will be profitable only if consumers are sure of its soundness.

The public interest in ensuring the continued solvency of the industry, of course, is overwhelming. The public relies on the insurance industry to pay medical bills and to provide retirement income, income protection in case of death or disability, protection from catastrophic loss, and safe investment opportunities.

Life insurance company solvency is especially important for pension plans. Few workers or retirees consider that their pensions depend on the solvency of life insurance companies. So far, not a single worker has lost a penny of pension benefits because of an insurance company failure. But, it could happen.

While defined benefit plans are regulated by ERISA and insured by the Federal Pension Benefit Guaranty Corporation (PBGC), workers rely increasingly on defined contribution plans. Guaranteed investment contracts (GICs) written by life insurance companies have the largest share of the $150 billion market for defined contribution plans. We must ensure the safety of these retirement plans.

Insurance companies also are involved in pension benefits in circumstances where a company has terminated its defined benefit plan and substituted in its place annuities purchased from insurance companies. While still complying with ERISA, companies terminating their defined benefit plan in this way can pocket money left over after the purchase of annuities. Since 1980, about $20 billion has been taken out of pension plans in this way. These retirement annuities, again, must be protected.

Workers who depend for their retirement on GICs and annuities therefore depend also on the solvency of life insurance companies. State guaranty funds add a layer of protection, but three states, Colorado, Louisiana, and New Jersey, have not yet adopted guaranty funds for life and health companies. Moreover, eleven states exclude unallocated annuities from guaranty fund coverage, so that a GIC purchased in the company's name on behalf of pension plan participants is not covered. State caps on guaranty fund payments on unallocated annuities, also, can limit protection.

This all adds up to an overwhelming case for reform of solvency regulation.

The NCSL policy provides that: "Improving state regulation of insurance for solvency will require attention (1) to laws and regulations, (2) to regulatory practices and procedures, and (3) to the need for additional resources, expertise and state legislative oversight to ensure their effective implementation."

A series of laws and regulations developed by the NAIC, as a minimum, must be in place, including:

(1) adequate authority for insurance departments to examine insurance company finances and to order corrective actions;

(2) adequate capital and surplus requirements and limits on risk retained by property/casualty companies based on their capital and surplus;

(3) minimum standards for liabilities and reserves;

(4) requirements that insurance companies adopt adequate accounting procedures and that they value and admit assets according to recognized standards;

(5) regulations to ensure the safety of investments;

(6) strict regulation of credit for reinsurance;

(7) requirements for annual CPA audits and actuarial opinions;

(8) mechanisms for placing a insurance company into receivership;

(9) establishment of adequate guaranty funds for both property/casualty and life/health companies;

(10) regulation of managing general agents and reinsurance intermediaries;

(11) participation in the NAIC's IRIS system for early detection in insolvencies; and

(12) adequate regulation of risk retention groups and producer controlled insurers.

These laws and regulations must not only be adopted: they must be enforced vigorously. NCSL recognizes in its policy statement that regulatory practices and procedures must be improved. Specifically, NCSL recommends in accord with the NAIC solvency policing agenda:

(1) that each state retain capable staffs of financial analysts and examiners;

(2) that each state regularly examine all domestic companies and accord priority to examinations of companies in adverse circumstances, and

(3) that state insurance departments communicate effectively and coordinate their actions in dealing with multistate insolvencies and problem companies.

Implementation of these model acts, regulations, and administrative reforms will cost money. It will require the more efficient use of existing resources. It will require new money. Unfortunately, most states are facing difficult budget challenges at this time. NCSL's policy asks states to consider the imposition of special assessments on insurance companies to defray the increased cost.

I am gratified at the initial reaction of state legislatures to the NCSL policy statement and to the calls by insurance commissioners, industry executives and consumer advocates to adopt the NAIC model laws and similar reforms. It is too early to give a final tally of spring 1991 legislative action, but the NAIC reports that there has been legislative action so far in 38 states. Eleven states have already adopted this session new legislation or regulations implementing the NAIC standards. A detailed breakdown of the status of state legislative action, provided by the NAIC, is attached to my statement.

In Nebraska, we have enacted a comprehensive set of solvency bills, including model acts related to holding companies, credit for reinsurance, rehabilitation and liquidation, risk retention, and IRIS financial data reporting. Nebraska also has promulgated model regulations related to standards for companies in hazardous financial condition and life reinsurance agreements.

Arkansas similarly has enacted already in the current legislative session model laws related to examinations, holding companies, credit for reinsurance, and IRIS. Georgia has enacted this spring model acts on holding companies, credit for reinsurance, rehabilitation and liquidation, IRIS, producer controlled insurers, managing general agents, and reinsurance intermediaries.

South Carolina has enacted recently six model laws and regulations. And, West Virginia has adopted seven models.

We expect state legislatures to continue to adopt model legislation for the remainder of the 1991 session. It is my hope and expectation that over the next two or at most three years the NAIC model laws and regulations will largely be put in place. I am optimistic that we will succeed if we retain enthusiasm for this project and if we retain a broad coalition of supporters.

I believe we must adopt model legislation at the state level on a voluntary basis. This will ensure a state commitment to follow through in implementing the laws. Federal mandates could be counterproductive. They could shift the debate in state capitols away from the solvency problem itself. Mandates generate resentment as the federal government takes credit for addressing a problem while the states pay the bill. Mandatory federal standards could result in grudging acceptance without real commitment. They could result also in an undesirable blurring of responsibility between federal and state governments.

I hope and expect that state legislatures will voluntarily adopt the model laws and that states will enforce the laws aggressively.

To get the models enacted across the country, we must practice the politics of inclusion. A variety of legislators, industry trade groups, and consumer advocates, who might disagree about other insurance issues, have been brought together to protect the solvency of the system. I am encouraged by this development. It explains the intense level of ongoing state legislative activity.

Indeed, our NCSL Task Force is just such a broad coalition. We have brought together a group of legislators and legislative staff, some of whom may disagree absolutely about tort reform or insurance antitrust issues, but all of whom agree on the immediate need to adopt the NAIC model solvency laws and to improve state insurance regulation.

In summary, Mr. Chairman, NCSL and the nation's state legislatures have taken rapid action to address the problem of insurance company insolvencies. (1) In August, NCSL held a meeting, in connection with our national convention, to examine the solvency issue. Immediately thereafter, Speaker Martin of Maine, NCSL's incoming President, constituted a special task force on insurance company insolvencies. (2) In December, the task force met and adopted an aggressive statement urging state action to protect insurance company solvency. Immediately thereafter, using our emergency policy process, the NCSL officers approved the statement as official NCSL policy. (3) In January, the NCSL task force distributed its policy to legislative leaders across the country. In that same month, we featured the issue of insurance company insolvencies as the cover story in State Legislatures magazine, which is distributed to every one of the 7,642 state legislators and to nearly 4,000 senior legislative staff across the United States. (4) Since January, 11 states including my own have adopted NAIC model acts and regulations. Legislative action on NAIC models is ongoing in 38 states.

NCSL and its Task Force on Insurance Company Insolvencies will continue to work on this issue. The task force has a heavy schedule of meetings and projects between now and the NCSL Annual Meeting in August. We still have important problems to address, but we are on the move.

Again, Mr. Chairman and members of the committee, I appreciate this opportunity to testify and look forward to working with you over a period of time to bring public attention to these issues.

Biographical Sketch

Senator Don Wesely
26th District
Lincoln, Nebraska

Don Wesely was born on March 30, 1954 in David City, Nebraska. Senator Wesely was the third youngest person ever to serve in the Nebraska Unicameral Legislature when he was elected in 1978 (59%). Senator Wesely was re-elected in 1982 (68%), in 1986 (83%) and in 1990 (98%). He represents the 26th Legislative District in Lincoln, Nebraska. He has served as a Delegate to the 1984 and 1988 Democratic National Conventions.

Since 1985, Senator Wesely has served as Chairman of the Health and Human Services Committee of the Nebraska Legislature. He also serves on the Banking, Commerce, and Insurance Committee, the Intergovernmental Cooperation Committee, and the Select Committee on Children.

As a member of the Nebraska Legislature, Senator Wesely has taken a leadership position to enact more than 130 measures, including legislation establishing the Older Nebraskans Act, a prohibition of the use of campaign funds for personal expenses, the Disabled Persons and Family Support Act, the Community Aging Services Act, a solar energy tax credit, the Nebraska Nursing Homes Act, the Comprehensive Health Insurance Pool, Business Development Centers of Nebraska, a measure providing prenatal and health care for high-risk pregnant woman, restrictions on the jailing of the mentally ill, the Adult Protective Services Act, the State Employees Collective Bargaining Act, the Shareholders Protection Act, measures to increase investigations of child abuse, and a measure that allows the spouse of a nursing home patient to retain essential assets.

Senator Wesely currently serves as co-chair of the Task Force on Insurance Company Insolvencies on the National Conference of State Legislatures (NCSL). He has served as vice-chair of NCSL's Committee on Commerce, Labor and Regulation and as vice-chair of NCSL's Task Force on Developmental Disabilities.

Senator Wesely serves on the National Advisory Panel of the Child Care Action Campaign, is a Lincoln Board Member of the United Nations Association, U.S.A., and is a board member of the Consumer Credit Counseling Service of Nebraska. He has served in the past as co-chairman of the Coalition to Stop the Raid on America, as co-chairman of the Nebraska Hunger Drive Coalition and Nebraska Shares - Famine Relief Campaign, and as a board member of the Lincoln Youth Service System.

Senator Wesely has been honored as Citizen of the Year by the Nebraska Association of Substance Abuse Directors, Public Citizen of the Year by the Nebraska Association of Social Workers, Best Legislator by KFOR, Lincoln, Outstanding Young Man of Nebraska by the Nebraska Jaycees, Mental Health Citizen of the Year by the Nebraska Mental Health Association, and recipient of the Robert F. Kennedy Award by Nebraska Young Democrats.

Senator Wesely attended Lincoln public schools. He received his B.A. degree from the University of Nebraska at Lincoln. He also attended graduate school at UNL. He is employed as a Senior Research Associate by the Lincoln Telephone Company. He was employed previously by the SRI Research Center, the Cotner Center for the Living Development Project, Southeast Nebraska Small Farms Action Group, and Geis Investments and Insurance. Senator Wesely, his wife Geri, and their three children live in Lincoln, Nebraska.

Appendices

Appendix A: Letter from Senator Don Wesely and Senator Dick Finan, co-chairs of NCSL Task Force on Insurance Company Insolvencies, to legislative leaders.

Appendix B: NCSL Policy Statement on Insurance Company Insolvencies.

Appendix C: NAIC tally of 1991 state action on model laws and regulations.

Appendix D: Articles from the January 1991 issue of State Legislatures magazine, "The Gathering Storm: Insurance Company Insolvencies" and "Are Pension Plans in Jeopardy?"

Appendix A

NATIONAL CONFERENCE OF STATE LEGISLATURES

WASHINGTON OFFICE 444 NORTH CAPITOL STREET, N.W. SUITE 500 WASHINGTON, D.C. 20001
202-624-5400 FAX 202-737-1069

JOHN MARTIN
SPEAKER OF THE HOUSE
MAINE
PRESIDENT, NCSL

WILLIAM RUSSELL
CHIEF LEGISLATIVE COUNSEL
VERMONT
STAFF CHAIR, NCSL

WILLIAM POUND
EXECUTIVE DIRECTOR

January 4, 1991

Dear Legislative Leader:

We are writing, in our capacity as co-chairs of NCSL's Task Force on Insurance Company Insolvencies, to communicate our concern about the insolvency issue and to transmit the policy statement recently adopted by the National Conference of State Legislatures recommending aggressive state action to address the problem of insurance company insolvencies.

A consensus has developed among state regulators, insurance executives and consumer advocates that state regulation for solvency must be improved. In this connection, the National Association of Insurance Commissioners (NAIC) has proposed a solvency policing agenda, including a series of model acts to address insurance company solvency problems.

As the enclosed policy statement indicates, NCSL recommends swift action by legislatures in early 1991 to adopt the NAIC model laws and policing agenda. The NAIC standards, in our view, are minimum requirements for effective state regulation of solvency. Each state should consider whether additional safeguards beyond these minimum standards are required.

State legislatures must act quickly to reform state insurance regulation, for three reasons. First, a recession, that increases the risk of major insolvencies, is looming. The financial security of policyholders must be protected. Second, state finances are threatened. State taxpayers could be asked to pay for insurance company insolvencies. Third, the threat of federal preemption is imminent. If states fail to act, it could result not only in a loss of authority, but also a loss of revenue from the insurance premium tax.

The worst case scenarios of some analysts predict an insurance insolvency crisis, similar in its dynamics to the $150 billion savings and loan crisis. A report by IDS Financial Services, for example, projects that 20 percent of major life insurers would face the risk of failure in a severe recession. These projections may be exaggerated, but there is little disagreement that state regulation of insurance for solvency must be improved.

Given that states are the only regulators and solvency guarantors of insurance companies, we believe state solvency legislation must be put on a fast track.

1560 BROADWAY SUITE 700 DENVER, COLORADO 80202 303-830-2200 FAX 303-863-8003

Again, we urge your careful consideration of the attached NCSL policy statement recommending adoption of the NAIC model laws and policing agenda.

Sincerely,

Senator Don Wesely,
Nebraska

Senator Dick Finan,
Ohio

Appendix B

National Conference of State Legislatures

OFFICIAL POLICY

Statement on Insurance Company Insolvencies

The safety and soundness of insurance companies operating in the United States is a prime objective of state insurance regulation. To ensure that this objective is met, an effective financial surveillance and regulation system is needed. This will require immediate state action to strengthen state insurance departments and to create standards for financial regulation that will strengthen the safety and soundness of insurance companies.

First of all, state insurance regulation must be strengthened in order to protect policyholders. The public depends on solvent insurance companies to provide retirement income, income protection in case of death or disability, protection from catastrophic loss, and safe investment opportunities.

Secondly, solvency regulation must be improved in order to protect state treasuries. When an insurance company fails, healthy companies are assessed to pay off policyholders. Many states allow such assessments, under state guaranty fund systems, to be offset against state premium taxes. In addition, some state pension funds and a few bond issuers have purchased guaranteed investment contracts that depend on the solvency of life insurance companies. Finally, if state guaranty fund systems were to collapse under the weight of too many insolvencies, some moral obligation on the state to protect policyholders might be alleged.

A third important reason for state action, as soon as possible, is to provide an alternative to federal intervention. Some consumer advocates and insurance executives already are calling for federal legislation that would preempt state authority. Additionally, there is a concern that such federal action could lead to federal preemption of the states' insurance premium tax base. We believe there are many advantages to state regulatory authority, including staff expertise that has developed over many years. The National Conference of State Legislatures (NCSL) believes that a heavy burden of proof must be met before federal intervention and preemption are justified. The NCSL recognizes that swift and effective action by state legislatures to reform state solvency regulation will serve to deter any unjustified federal preemption.

Improving state regulation of insurance for solvency will require attention (1) to laws and regulations, (2) to regulatory practices and procedures, and (3) to the possible need for additional resources, expertise and state legislative oversight to ensure their effective implementation. In order to achieve these goals, NCSL recommends adoption of the model laws and regulations developed by the National Association of Insurance Commissioners (NAIC), as summarized below in A and B.

444 North Capitol Street, N.W. • Suite 500 • Washington, D.C. 20001 • (202) 624-5400

A. LAWS AND REGULATIONS

1. Examination Authority: Each insurance department should have adequate authority to examine the finances of insurance companies whenever it is deemed necessary.

2. Capital and Surplus Requirements: State law should require that insurers have and maintain a minimum level of capital and surplus to transact business. State law should require additional capital and surplus based upon the type, volume and nature of insurance business transacted.

3. Accounting Practices and Procedures: Each insurance department should require that all companies adopt appropriate accounting practices and procedures.

4. Corrective Action: State law should provide sufficient authority for the state insurance department to order a company to take necessary corrective action when it is deemed to be in hazardous financial condition or to cease and desist in certain practices which, if not corrected, could place the company in a hazardous financial condition.

5. Valuation of Investments: Each department should require that securities and other invested assets owned by insurance companies be valued in accordance with recognized standards.

6. Holding Company Systems: State statute should provide for the proper regulation of insurance holding companies.

7. Risk Limitation: State statute and regulation should prescribe the maximum net amount of risk to be retained by a property and liability company for an individual risk, based upon the company's capital and surplus.

8. Investment Regulations: State statute should require a diversified investment portfolio for all domestic insurers both as to type and issue and include a requirement for liquidity. Foreign companies should be required to substantially comply with these provisions.

9. Admitted Assets: State statute should describe those assets which may be admitted, authorized or allowed as assets in the statutory financial statement of insurers.

10. Liabilities and Reserves: State statute should prescribe minimum standards for the establishment of liabilities and reserves resulting from insurance contracts issued by an insurer.

11. Reinsurance Ceded: State statute should provide for regulation of credit for reinsurance and reinsurance agreements.

12. CPA Audits: State statute or regulation should contain a requirement for annual audits of domestic insurance companies by independent certified public accountants.

13. Actuarial Opinion: State statute or regulation should contain a requirement for an opinion on life and health policy claim reserves and loss, and loss adjustment expense reserves of property and casualty companies by a qualified actuary or specialist on an annual basis for all domestic insurance companies.

14. Receivership: State statute should set forth a receivership mechanism for the administration, by the insurance commissioner, of insurance companies found to be insolvent.

15. Guaranty Funds: State statute should ensure the payment of policyholder obligations subject to appropriate restrictions and limitations when a company is deemed insolvent.

16. Regulation of Managing General Agents: State statute should provide for regulation of managing general agents.

17. Regulation of Reinsurance Intermediaries: State statute should provide for regulation of reinsurance intermediaries.

18. Regulation Information: State statute should require domestic insurance companies to participate in the NAIC Insurance Regulatory Information System (IRIS).

19. Risk Retention Groups: State statute should provide appropriately for the regulation of risk retention groups and purchasing groups.

20. Producer Controlled Insurers: State statute should provide for regulation of business transacted with a producer controlled property/casualty insurer.

B. REGULATORY PRACTICES AND PROCEDURES

1. Financial Analysis: Each state insurance department should have a sufficient staff of financial analysts with the capacity to effectively review the financial statements as well as other information and data to discern potential and actual financial problems of domestic insurance companies.

2. Examinations: Each state insurance department should have the resources to regularly examine all domestic companies.

3. Professionalism: Each department's examination staff should consist of a variety of specialists with the training and/or experience that will allow for the effective examination of any insurer.

4. Priority Examinations: In scheduling financial examinations, each department should accord priority to companies that are experiencing adverse financial circumstances.

5. Interstate Communication: When a domestic company is identified as troubled, this should be communicated to other insurance departments in jurisdictions in which the carrier transacts business. When a foreign company is identified as troubled, this should be communicated to the domiciliary insurance department of the carrier.

The standards set forth in sections A and B are submitted as minimum requirements for the effective regulation by a state of the financial solvency of those insurance companies doing business within that state. Each state should consider whether the enactment of additional safeguards beyond these minimum requirements would be appropriate for that jurisdiction.

For most states, the enactment and implementation of the standards set forth herein will entail additional expense. To determine the precise needs in furthering the goals stated herein, state legislatures and regulators could embark on a thorough review of existing resources, management operations, and policy implementation procedures. State legislatures could exercise appropriate oversight of their insurance departments through their standing committees and budget process, and through performance, management and compliance audits. In order to obtain necessary funding without further burden to taxpayers, states could consider the imposition of a special assessment on insurance companies doing business within the state in order to defray the increased cost of regulation.

Appendix C

NAIC
BILLS INTRODUCED ON
MODEL LAWS CONTAINED IN ACCREDITATION STANDARDS

Code: A = amendments pending, generally include current model provisions. N = New provisions, generally based on model.
* after indicates bill or regulation adopted.

	AL	AK	AZ	AR	CA	CO	CT	DE	DC
Model Law on Examinations (w/i 2 years)				N*					
Model Reg. to Define Standards for Co. in Hazardous Financial Condition									
Holding Company Act			A	A*					
Holding Company Regulation									
Credit for Reinsurance Act			N	N*					
Reg. on Life Reinsurance Agreements									
CPA Audit Law									
Actuarial Opinion on Loss Reserves L/H							N		
Rehabilitation and Liquidation Model Act			N						
L/H Guaranty Fund			A		A	N		A	
P/C Guaranty Fund									
IRIS Model Act			A	N*		N			
Risk Retention Act						N			
Business Trans. w/Producer Controlled P/C Insurer Act			N						
MGA Act (w/i 2 years)			N				N		
Reinsurance Intermediaries Act (w/i 2 years)			N		N				

4/3/91

NAIC
BILLS INTRODUCED ON
MODEL LAWS CONTAINED IN ACCREDITATION STANDARDS

Code: A = amendments pending, generally include current model provisions. N = New provisions, generally based on model.
* after indicates bill or regulation adopted.

	FL	GA	HI	ID	IL	IN	IA	KS	KY
Model Law on Examinations (w/i 2 years)						N		N	
Model Reg. to Define Standards for Co. in Hazardous Financial Condition							N*		
Holding Company Act		A*				A	A	A	
Holding Company Regulation									
Credit for Reinsurance Act		N*		N			N		
Reg. on Life Reinsurance Agreements									
CPA Audit Law	A		N						
Actuarial Opinion on Loss Reserves L/H	N								
Rehabilitation and Liquidation Model Act	A	N*						N	
L/H Guaranty Fund				A					
P/C Guaranty Fund				A			A		
IRIS Model Act		N*		N					
Risk Retention Act									
Business Trans. w/Producer Controlled P/C Insurer Act		N*					N		
MGA Act (w/i 2 years)		N*		N		N	N		
Reinsurance Intermediaries Act (w/i 2 years)		N*				N	N		

4/3/91

NAIC
BILLS INTRODUCED ON
MODEL LAWS CONTAINED IN ACCREDITATION STANDARDS

Code: A = amendments pending, generally include current model provisions. N = New provisions, generally based on model.
* after indicates bill or regulation adopted.

	LA	ME	MD	MA	MI	MN	MS	MO	MT
Model Law on Examinations (w/i 2 years)									
Model Reg. to Define Standards for Co. in Hazardous Financial Condition						N		N	
Holding Company Act						A		A	
Holding Company Regulation									
Credit for Reinsurance Act		N				N	N	A	
Reg. on Life Reinsurance Agreements									
CPA Audit Law							N	N	
Actuarial Opinion on Loss Reserves L/H									
Rehabilitation and Liquidation Model Act			N	N			N	N	
L/H Guaranty Fund			A			A			
P/C Guaranty Fund							A		
IRIS Model Act									
Risk Retention Act				N				A	
Business Trans. w/Producer Controlled P/C Insurer Act			N					N	
MGA Act (w/i 2 years)			N			N	N		
Reinsurance Intermediaries Act (w/i 2 years)								N	

4/3/91

NAIC
BILLS INTRODUCED ON
MODEL LAWS CONTAINED IN ACCREDITATION STANDARDS

Code: A = amendments pending, generally include current model provisions. N = New provisions, generally based on model.
* after indicates bill or regulation adopted.

	NE	NV	NH	NJ	NM	NY	NC	ND	OH
Model Law on Examinations (w/i 2 years)							N		N
Model Reg. to Define Standards for Co. in Hazardous Financial Condition	N*						N		N
Holding Company Act	A*		A			A	A	A	A
Holding Company Regulation									
Credit for Reinsurance Act	A*		A				A	N	N
Reg. on Life Reinsurance Agreements	N*						N		
CPA Audit Law							N		
Actuarial Opinion on Loss Reserves L/H									
Rehabilitation and Liquidation Model Act	A*		A				A	N	
L/H Guaranty Fund				N			A		
P/C Guaranty Fund									
IRIS Model Act	N						A		
Risk Retention Act	A*								
Business Trans. w/Producer Controlled P/C Insurer Act							N	N	N
MGA Act (w/i 2 years)			N				N	N	N
Reinsurance Intermediaries Act (w/i 2 years)			N				N	N	

4/3/91

NAIC
BILLS INTRODUCED ON
MODEL LAWS CONTAINED IN ACCREDITATION STANDARDS

Code: A = amendments pending, generally include current model provisions. N = New provisions, generally based on model.
* after indicates bill or regulation adopted.

	OK	OR	PA	RI	SC	SD	TN	TX	UT
Model Law on Examinations (w/i 2 years)	N								
Model Reg. to Define Standards for Co. in Hazardous Financial Condition					N*				
Holding Company Act				A	A*		A	A	
Holding Company Regulation									
Credit for Reinsurance Act				N	N*		A*	A	
Reg. on Life Reinsurance Agreements					N*				
CPA Audit Law				N				N	
Actuarial Opinion on Loss Reserves L/H		N		N			N		
Rehabilitation and Liquidation Model Act					A*	A*	N		
L/H Guaranty Fund		A						A	A*
P/C Guaranty Fund							A	A	
IRIS Model Act				N			N		
Risk Retention Act				N	A*		N		
Business Trans. w/Producer Controlled P/C Insurer Act							N		
MGA Act (w/i 2 years)	N	N		N			N		
Reinsurance Intermediaries Act (w/i 2 years)	N			N				N	

4/3/91

NAIC
BILLS INTRODUCED ON
MODEL LAWS CONTAINED IN ACCREDITATION STANDARDS

Code: A = amendments pending, generally include current model provisions. N = New provisions, generally based on model.
* after indicates bill or regulation adopted.

	VT	VA	WA	WV	WI	WY	PR	VI
Model Law on Examinations (w/i 2 years)				N				
Model Reg. to Define Standards for Co. in Hazardous Financial Condition				N*				
Holding Company Act			A	A*		N*		
Holding Company Regulation								
Credit for Reinsurance Act		N*				N*		
Reg. on Life Reinsurance Agreements								
CPA Audit Law		N		A*				
Actuarial Opinion on Loss Reserves L/H								
Rehabilitation and Liquidation Model Act	N			N*				
L/H Guaranty Fund		A*		A*				
P/C Guaranty Fund								
IRIS Model Act		N*		N*				
Risk Retention Act				A*		A*		
Business Trans. w/Producer Controlled P/C Insurer Act								
MGA Act (w/i 2 years)								
Reinsurance Intermediaries Act (w/i 2 years)								

Every effort has been made to make this information complete and correct. For further information you should check the bills and regulations pending. NAIC 4/3/91
charts/accred/bills

NAIC
BILLS INTRODUCED ON
MODEL LAWS CONTAINED IN ACCREDITATION STANDARDS

MODEL LAWS ON EXAMINATIONS

AR	HB 1792	Adopted
IN	SB 125	Passed Senate, Amended in House
KS	SB 53	Passed Senate, Amended in House
OH		Will Introduce by Middle of April
OK	SB 170	Passed Senate
NC	SB 342 HB 351	Introduced
WV	HB 2902	Reported Favorably

MODEL REG. TO DEFINE STANDARDS FOR COMPANIES IN HAZARDOUS FINANCIAL CONDITION

IA	Reg. 191-5.23 to 191-5.24	Adopted
MN	HB 12 SB 37	In Committee
MO		Regulation Pending
NE		Regulation 55 Adopted
NC	SB 342 HB 351	Introduced
OH		Will Introduce by Middle of April
SC	HB 3508	Adopted
WV	HB 2462	Adopted

HOLDING COMPANY ACT

AZ	HB 2369	Passed House
AR	HB 1792	Adopted
CA	SB 347	Adopted
IN	SB 125	Passed Senate, Amended in House
IA	SB 518	Awaiting Governor's Signature
KS	SB 67	Passed Senate
MN	SB 482	Reported Out of Committee

HOLDING COMPANY ACT (CONT.)

MO	HB 389	House Insurance Committee
NE	LB 236	Adopted
NH	HB 589	Reported Out of Committee
NY	AB 2174	Referred to Insurance Committee
NC	SB 342 HB 351	Introduced
ND	HB 1242	Passed Both Houses
OH		Will Introduce by Middle of April
RI	HB 6882	Referred to House Corporation Committee
SC	HB 3508	Adopted
TN	HB 797 SB 973	In Committee
TX	HB 2	In Committee
VT	SB 163	Passed Both Houses
WA	SB 5443	In Committee
WV	HB 2462	Adopted
WY	SB 135	Adopted

CREDIT FOR REINSURANCE ACT

AZ	HB 2369	Passed House
AR	HB 1792	Adopted
GA	SB 347	Awaiting Governor's Signature
ID	HB 181	Passed Both Houses
IA	SB 518	Awaiting Governor's Signature
ME	HB 255	Joint Hearing
MN	HB 12 SB 37	Referred to Financial Institutions Referred to Commerce
MS	SB 2635	Awaiting Governor's Signature
MO	SB 223	Referred to Insurance Committee
NE	LB 236	Adopted

CREDIT FOR REINSURANCE ACT (CONT.)

NH	HB 638	Reported With Amendment
NC	SB 342 HB 351	Introduced
ND	HB 1242	Passed Both Houses
OH		Will Introduce by Middle of April
RI	HB 6202	Referred to Corporation Committee
SC	HB 3508	Adopted
TN	SB 972	Adopted
TX	SB 1141	In Committee
VA	SB 670	Adopted
WY	SB 14	Adopted

REGULATION FOR LIFE REINSURANCE AGREEMENTS

NE	Ch. 57	Regulation Adopted
NC	SB 342 HB 351	Introduced
SC	Reg. 69-35	Ratified by Legislature (HB 3509)

CPA AUDIT LAW

FL	HB 2024	Introduced
HI	HB 1993	Passed House
MS	HB 1255	Passed House
MO	SB 308	Passed Senate
NC		Regulation Pending
RI	SB 890	Referred to Corporations Committee
TX	HB 2	In Committee
VA		Regulation Pending
WV	HB 2462	Adopted

ACTUARIAL OPINION ON LOSS RESERVES L/H

CT	Reg. 38A-1	Pending Approval
FL	HB 2024	In Committee
OR	HB 2210	Referred to Business Committee

ACTUARIAL OPINION ON LOSS RESERVES L/H (CONT.)

RI	SB 890	Referred to Corporations Committee
TN	SB 467 HB 689	Amended

REHABILITATION AND LIQUIDATION MODEL ACT

AZ	HB 2369	Passed House
FL	SB 2024	In Committee
GA	SB 347	Adopted
KS	SB 111	Passed Senate
MD	SB 229	Reported out of Committee
MA	HB 3439 HB 4957	Referred to Insurance Committee
MS	SB 2637	Passed both Houses
MO	SB 238	Amended
NE	LB 236	Adopted
NH	HB 575	Reported Favorably
NC	SB 342 HB 351	 Introduced
ND	HB 1242	Passed Both Houses
SC	SB 589	Passed Senate
SD	HB 1040	Adopted
TN	SB 467	Amended
TX	HB 2409	In Committee
VT	SB 96	Passed Senate
WV	HB 2462	Adopted

L/H GUARANTY FUND

AZ	HB 2366 SB 1105	Reported Favorably Referred to Rules
CA	SB 369	Hearing
CO	HB 1325	
DE	HB 141	Reported Out of Committee

L/H GUARANTY FUND (CONT.)

ID	HB 276	Passed Both Houses
MD	HB 70	Passed House
MN	HB 12	Referred to Committee
NJ	AB 3641	Referred to Insurance Committee
NC	SB 342 HB 351	Introduced
OR	HB 2212	Recommended to Business
TX	SB 613 HB 2409	Referred to Floor In Committee
UT	HB 375	Adopted
VA	SB 554	Adopted
WV	HB 2462	Adopted

P/C GUARANTY FUND

ID	SB 1045	Reported Favorably
IA	SB 518	Awaiting Governor's Signature
MS	SB 2791	Passed Senate
TN	HB 528	Referred to Commerce Committee
TX	HB 2409	In Committee

IRIS MODEL ACT

AZ	HB 2369	Passed House
AR	HB 1792	Adopted
CO	HB 1243	Passed Both Houses
GA	SB 347	Adopted
ID	HB 182	Awaiting Governor's Signature
NE	LB 237	Awaiting Governor's Signature
NC	SB 342 HB 351	Introduced
RI	HB 6202	Referred to Corporations Committee
TN	SB 467 HB 689	Amended

IRIS MODEL ACT (CONT.)

VT	SB 163	Passed Both Houses
VA	SB 581	Adopted
WV	HB 2462	Adopted

RISK RETENTION ACT

CO	HB 1243	Reported with Amendment
MA	HB 85	Referred to Insurance Committee
	HB 1560	Referred to Insurance Committee
MO	HB 451	Referred to Insurance Committee
NE	LB 236	Adopted
RI	HB 6973	In Committee
SC	SB 591	Passed Senate
TN	SB 467	Amended
	HB 689	
WY	HB 130	Adopted

BUSINESS TRANSACTED WITH PRODUCER CONTROLLED P/C INSURER ACT

AZ	HB 2369	Passed House
GA	SB 347	Awaiting Governor's Signature
IA	HB 518	Awaiting Governor's Signature
MD	HB 201	In Conference Committee
MO	HB 386	In Committee
NC	SB 342	
	HB 351	Introduced
ND	HB 1242	Passed Both Houses
OH		Will Introduce by Middle of April
TN	SB 467	Amended
	HB 689	

MGA ACT

AZ	HB 2369	Passed House
CT	HB 6859	Reported Favorably
GA	SB 347	Awaiting Governor's Signature
ID	HB 187	Passed Both Houses

MGA ACT (CONT.)

IA	SB 518	Awaiting Governor's Signature
IN	SB 125	Passed Senate, Amended in House
MD	HB 207 SB 225	Hearings
MN	HB 12 SB 37	In Committee
NH	HB 574	Reported With Amendment
NC	SB 342 HB 351	Introduced
ND	HB 1242	Passed Both Houses
OH		Will Introduce by Middle of April
OK	SB 171	Passed Senate, Reported With Amendment in House
OR	HB 2215	In Committee
RI	HB 6790	
TN	SB 467 HB 689	Amended

REINSURANCE INTERMEDIARIES

AZ	HB 2369	Passed House
CA	SB 901	Introduced
GA	SB 347	Awaiting Governor's Signature
IN	SB 125	Passed Senate, Amended in House
IA	SB 518	Awaiting Governor's Signature
MO	HB 386	In Committee
NH	HB 692	Passed House
NC	SB 342 HB 351	Introduced
ND	HB 1242	Passed Both Houses
OK	HB 1342	Dead
RI	HB 6786	In Committee
TX	HB 2	In Committee

Every effort has been made to make this information complete and correct. For further information you should check the bills and regulations pending. NAIC 4/3/91
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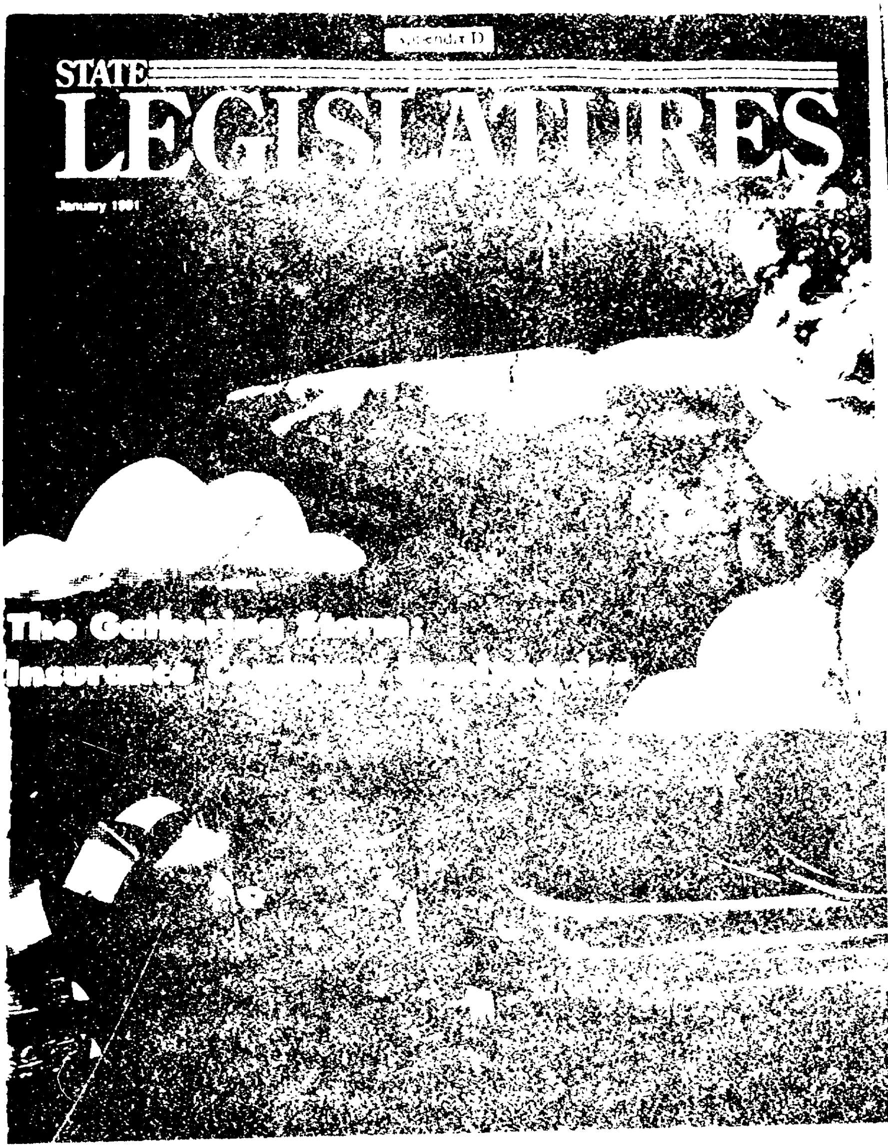
STATE
LEGISLATURES
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The Gathering Storm: Insurance Company Insolvencies

In the wake of the savings and loan collapse, are insurance companies next?

William T Waren

As the nation [illegible] savings and loan debacle estimated to cost $150 billion to $500 billion, warnings are sounding that insurance company failures also could spin out of control. Recent reports by a congressional committee, US Financial Services and Public Citizen, a consumer group founded by Ralph Nader, suggest that the pattern of thrift failures could be repeated in the insurance arena, which is entirely regulated by states and insured by state guarantee funds.

Widespread insurer insolvencies not only would constitute an indictment of state regulation but also could impact state finances. When an insurance company fails, healthy companies are assessed to pay off policyholders. Many states allow such assessments under state guarantee fund systems to be offset against state premium taxes. In addition, some state pension funds and a few bond issuers have purchased guaranteed investment contracts that depend on the solvency of life insurance companies.

Many insurance industry representatives and members of the National Association of Insurance Commissioners (NAIC) regard the reports as alarmist. Franklin Nutter, president of the Alliance of American Insurers, says the vast majority of insurers are financially sound. Nonetheless, state regulators and insurance executives agree that state regulation must be improved to prevent [illegible]

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surance company insolvencies.

Allegations of misconduct run through *Failed Promises* the report of the U.S. House Energy and Commerce Committee's subcommittee on investigations. Congressman John Dingell of Michigan is the subcommittee chairman The report says The business of insurance is uniquely suited to abuse by mismanagement and fraud

The report is a series of case studies. with particular attention given to the failures of Mission Insurance Company and Transit Casualty Company.

In the early 1980s. Mission sought rapid growth by delegating authority to managing general agents (MGAs). in particular to two wholly-owned subsidiaries. Sayre & Toso and Pacific Reinsurance *Failed Promises* suggests that Mission focused on fee income and sales volume generated by these subsidiaries. while disregarding standard underwriting practices and assuming significant risks.

The report says that Mission wrongly assumed that it retained little exposure to these risks because most of this business was itself reinsured Reinsurance is insurers insurance. so to speak For a price. the reinsurer agrees to indemnity the insurer for all or part of the cost of claims under the original policy

According to the report Both Mission and its reinsurers had ample reason to enjoy the party while it lasted The reinsurers took hundreds of millions of dollars in premiums. while Mission puffed up its own financial image and earnings

Ultimately Mission was sunk by high losses from the risky business it wrote and by the failure of reinsurers. many of whom are now insolvent or alleging fraud to cover losses Letters of credit. posted by reinsurers as guarantees that they would pay so far have limited value In February 1987. the California Insurance Commissioner placed Mission into liquidation The receiver currently estimates the cost of resolving the Mission failure at $1 6 billion

Executives of Mission and its subsidiaries deny fraud or mismanagement. Ronald Bengston. the former president of Pacific Reinsurance. testified before the Dingell committee that he is a competent insurance professional who performed his duties to the best of his ability All I can say Bengston told the committee. is that we were just doing the best job we could.'

Failed Promises tells a similar story about the collapse of Transit Casualty. Chartered in 1945 in Missouri. Transit Casualty operated conservatively and profitably for many years as a property casualty insurer for long-haul trucks and buses. In 1979. after a change of management and a move to California. Transit shifted away from its traditional business and pursued a riskier high-growth policy

As with Mission Insurance. Transit's plan was to expand rapidly into new markets by using managing general agents (MGAs) and to reinsure most of the risk.

An insurance company may delegate to MGAs the power 'to underwrite business. obligate the company. handle claims and even arrange for reinsuring the business ' The subcommittee concludes that it is dangerous for a company to hand over responsibility for its business to the MGA.' who is not subject to state regulation and who has an 'inherent conflict between writing quality business and earning commissions on the volume of business written."

The report is especially critical of Transit's relationship with Carlos Miro. a young man who it says 'wanted to be a millionaire ' Although only 26 years old when he began acting as Transit's sub-agent in 1981 Miro. according to *Failed Promises* 'immediately seized his big opportunity for great wealth."

Miro according to the report. wrote large amounts of high risk. general commercial liability and workers compensation insurance For example. he wrote a workers compensation policy for Wal-Mart stores in 18 states for a premium of $3 5 million per year an amount the subcommittee report claims to be half of what state law required According to the report. 'Losses from the Wal-Mart policies have cost Transit $22 million and it is just the largest of many such deals.'

Miro also established his own reinsurance company in the Cayman Islands "where regulation is so lax that it is a crime to ask who owns an insurance company.' The report alleges that by using a captive reinsurer for the insurance he wrote Miro was able to keep another 65 percent of premiums

The report concludes that Miro's insurance empire was essentially a poorly run slush fund in Dallas that used premiums from new policies to pay incoming claims. creating the familiar Ponzi-scheme pattern of growth and collapse."

Another MGA for Transit was the National Underwriting Agency in Chicago The subcommittee report cites an actuarial evaluation that Transit could lose as much as $2.4 billion as a result of the business written by National Underwriting for pharmaceutical firms asbestos companies and similar high risk clients -

The officers and directors who launched Transit on its ambitious business plan for the 1980s according to the report. abandoned ship prior to the firm's insolvency. 'after helping themselves to generous cash payments and other benefits." These allegations are disputed by Joseph Mitchell president of

Transit's parent company and a Transit board member. He told the Dingell committee that he and members of his family "directly suffered a loss of $13 million." The Transit receiver is suing former directors and officers for $400 million.

Altogether, the failure of Transit Casualty Company could cost $2 billion to $4 billion, according to *Failed Promises*. George P. Bowie, the former CEO of Transit, however, alleges that these huge figures reflect only the inability of the receiver to collect the reinsurance that is owed. Bowie is now under indictment.

Property and casualty insurers are also the target of a recent study by Public Citizen, a consumer group founded by Ralph Nader. In a study, *Insurance: The Next Industry Crisis?*, Public Citizen looked at six statistical indicators of solvency related to a company's surplus (savings set aside to meet unexpected losses), risk exposure, liquidity, and the degree to which it has rapidly expanded and contracted its policy-writing in response to interest rates and the so-called "insurance cycle." Of the 20 largest property and casualty insurers, three companies, AIG, Liberty Mutual and USF&G, according to Public Citizen were found to be potentially "at risk in a significant economic downturn." The credibility of the Public Citizen study, however, was diminished by errors in the analysis of data in the original report which first indicated that five companies were at risk.

The insurance industry and the National Association of Insurance Commissioners (NAIC) have blasted the Public Citizen report, while the report of the Dingell committee has played to mixed reviews among industry executives and state regulators.

"Amateur hour" is how Robert H. Gruhl, senior vice-president of Liberty Mutual Insurance, characterized the Public Citizen report that names his company as one of the three "at risk" majors. "This report, which is irresponsible and false, represents uninformed opinion about the strength of the major insurance companies it reports on." Aetna called the report "a concoction of arbitrary financial tests, incorrect information and sloppy analysis." NAIC called the report naive.

As for *Failed Promises*, Earl Pomeroy, North Dakota's insurance commissioner and president of the NAIC, in a reply to the committee calls the report "unduly apocalyptic." While the report appropriately called attention to the seriousness of solvency issues, Pomeroy regards the comparisons drawn to the thrift crisis as overstated.

Neither *Failed Promises* nor a recent GAO report on the industry, it should be emphasized, presents conclusive evidence that fraud and mismanagement are typical among property/casualty insurers. Indeed, industry representatives contend that such behavior is far from typical. Says Debra Wozniak, assistant counsel at State Farm Insurance, "There are still many good players, honest companies that work hard to provide a good product to their consumers."

Morag Fullilove, senior vice-president of the Alliance of American Insurers, also notes that the analogy to the thrift crisis can be misleading. Compared to the thrift industry, she says, the property casualty industry has assets that are far more liquid, has far more capital and has investments that are far more conservative.

Peter Lefkin, assistant vice-president of Fireman's Fund, is less sanguine. He says, "The insurers are only deluding themselves if they believe they will collect on all the reinsurance contracts that they hold and they are deluding themselves about the value of some of the assets they hold. Generally, the insurance industry has been culpable of very bad accounting practices."

Potential problems are not limited to property/casualty firms, according to IDS Financial Services, a major life insurance company. In its report, *Will the U.S. Life Insurance Industry Keep Its Promises?* IDS concludes that "there is significant risk that one-fifth, or 20 percent, of today's major life insurers will become insolvent should there be a severe economic downturn or decline in major investment markets. And, we feel that unfavorable economic and market conditions are highly likely sometime during the 1990s." These insurers, IDS analysts say, may not have adequate surplus funds to weather such an economic downturn.

Ed Zimmerman of the American Council of Life Insurance (ACLI) cautions, however, that we should keep in mind that these projections are based on assumptions made by IDS analysts about the likelihood of a "near depression" as well as assumptions about the risk of certain investment strategies and the amount of surplus required to ride out a crisis.

IDS is especially concerned about junk bond investments. Market confidence in the safety of such bonds has dropped sharply. This presents a problem, for instance, at First Executive Life Insurance which has 49 percent of its assets in low-grade bonds. IDS reports that "life insurers hold roughly 30 percent of $200 billion of low-grade or junk bonds outstanding. This equals 14 percent of all corporate issues held by life insurance companies or 6.4 percent of their invested assets."

Guaranteed investment contracts with life insurance companies holding large junk bond portfolios, unfortunately, were purchased by state and local bond issuers in Louisiana, Nebraska and several municipalities in other states. For example, the Nebraska Investment Finance Authority issued $200 million in bonds to pay for farm loans. In a so-called arbitrage play, the proceeds were then invested in GICs with First Executive that pay higher interest than the state pays to bondholders. First Executive could offer high interest GICs because of the even higher interest earned on junk bond investments with Drexel Burnham. As the junk bond market goes sour, however, the purchasers of the Nebraska bonds fear for the health of First Executive and the safety of their investments. Similar problems face pension funds that bought GICs backed by junk bonds.

In addition, life insurers, as is their traditional practice, are invested heavily in commercial mortgages at a time when "see-through" skyscrapers and high commercial vacancy rates are common in some cities and at a time when the real estate market is depressed. IDS reports that several large insurers have more than 50 percent of total assets in mortgages.

Another risk faced by life insurers according to IDS, is a mismatch between liabilities and assets. Given the current uncertainty about interest rates and inflation, mismatches could result in the future if interest rates that must be paid to attract new buyers of insurance and annuity contracts approach or exceed what life insurers earn on long-term investments. Old insurance contracts do not necessarily provide a cushion in this situation. Policyholders can simply cash out or "put" their insurance contracts and then reinvest in new contracts offering a higher return.

A different view of the financial strength of the life insurance industry was given by Richard Minck, executive vice-president of the American Council of Life Insurance, in testimony before the U.S. Senate Finance Committee. "Life insurers," he said, "have a long history of making conservative, long-term investments."

Minck sees little parallel between the real estate investments of failed thrifts and the real estate investments of insurance companies. "Most insurers with significant commercial mortgage holdings are national lenders and are able to diversify both geographically and by property type." Life insurance companies also tend to avoid, he says, the short-term construction and development loans that got thrifts into trouble.

As for the junk bond issue, Minck says a large portion of such bonds held by insurance companies are private placement bonds for which special covenants and collateral are available to provide additional financial protection.

Finally he notes "Life insurance companies took major steps and have been very aggressive in moving to improve matching of assets and liabilities. This can be seen in the shortened maturities of their bond and mortgage portfolios in the early 1980s."

With state regulation blamed for the insurance industry's solvency problems, the federal government may intervene. Public Citizen supports federal legislation establishing minimum standards for state regulation for solvency and direct federal solvency regulation where states fail to meet standards. And Congressman Dingell has made it clear that he will not wait patiently for the states to act if delay increases the risk of another savings and loan crisis.

Even a few insurance executives are exploring the idea of federal regulation of the insurance industry. Most insurance companies remain opposed to federal legislation, according to Bob Zeman, assistant general counsel at the National Association of Independent Insurers, but the American Insurance Association, representing many of the larger companies, will not rule out the possibility of limited federal involvement. Fireman's Fund is actively exploring options for federal legislation. Industries do not often ask for tighter regulation, especially by the federal government. But consider that conservatively managed firms first lose market share when less risk-averse firms underprice their product and then are forced to pay through guarantee fund assessments for their competitors' insolvencies.

Insurance commissioners think that state solvency regulation can be strengthened, as an alternative to federal intervention. NAIC's solvency policing agenda includes efforts to establish financial regulatory standards including a formal certification mechanism for state insurance departments. NAIC also will seek a system for uniform reinsurance evaluation and improvements in the financial examination process. The commissioners propose, in addition, a series of model acts intended to prevent solvency problems by better regulating managing general agents, the reinsurance process and the relationship between brokers and captive insurers. Capital and surplus requirements are also important items for discussion.

Because states are the only regulators of the insurance industry and the only authority responsible for guarantee funds Nebraska Senator Don Wesely is concerned that if a solvency crisis develops the potential liability, both economic and political, for state governments will be substantial.

Wesely sees parallels between the problem of insurance company insolvencies and bank and thrift insolvencies, especially in those states that formerly provided state guarantee funds for banks as an alternative to federal deposit insurance. "In Nebraska," Wesely said, "we had a bank a month fail in the early 1980s . . . but we were fortunate enough to have the FDIC there. It was still very traumatic but deposit insurance was there to care for most people. We also found in Nebraska," Wesely continued, "an institution that failed that was not a federally insured institution but came under a state guarantee corporation that was inadequately funded. I know a number of states that have had that experience. Unfortunately in our own state we never did fully reimburse those individuals. We have had turmoil in our state since 1983 as a result of that."

The American Council of Life Insurance believes that state guarantee funds do provide effective protection and that criticism of the system is based on faulty assumptions especially about the adequacy of reserves and capital.

On the other hand, Caroline Smith DeWaal, an attorney with Public Citizen, says "If we have a major insolvency, it is clear that state guarantee funds could not handle it. There definitely would be a need to bail out the state guarantee funds. Where the money would come from is anybody's guess. The states might have a moral obligation to pay, though the federal government also might have to get involved."

Insurance company insolvencies will be an important issue for state legislators in 1991 regardless of whose analysis of the depth of the problem is more credible. The industry wants to assuage the growing concerns of policyholders. Regulators want to resolve doubts about their effectiveness. And state legislators want assurance that guarantee funds will protect policyholders without draining the state treasury. ■

Are Pension Plans in Jeopardy?

State insurance commissioners are keeping an eye on pension plans that depend on the solvency of life insurance companies.

Lanny Proffer

Most American workers take the security of their pension plans for granted. It would not occur to them that their anticipated pension checks might depend on the solvency of life insurance companies. So far no one has lost a pension because of the failure of an insurance company, but it could happen. State insurance commissioners are taking the possibility seriously.

Pension and retirement plans come in two types. The first is the defined benefit plan in which the amount of the pension is determined by a formula that takes into account salary or wage levels and years of service. Responsibility for payment of pension benefits under these plans lies exclusively with the employer. Most of these plans are regulated by the Employee Retirement Income Security Act (ERISA). In the event of the employer's failure to pay, the federal Pension Benefit Guaranty Corporation (PBGC) insures the workers' benefits.

The defined contribution plan is the second type: in these plans the amount of the retirement benefit depends on the earnings of the contributions made by or on behalf of the employee. The Internal Revenue Service regulates these plans.

Life insurance companies get involved in two ways. Many defined contribution plans allow employees to select an option that offers a guaranteed rate of return on their investment fund for a specific period of time – usually 3 to 5 years. These Guaranteed Investment Contracts (GICs) are written by life insurance companies and banks, with life insurance companies having the lion's share of the $150 billion market.

The GICs appeal to employees who are concerned about the risk and volatility of the stock market. Where it is offered, two out of three employees select the GIC. While the GICs offer a great deal of predictability and security they are only as good as the companies that write them.

Insurance companies also get involved in pension plans through the sale of annuities. The great bull market in equities of the 1980s so increased the value of many corporate pension plan portfolios that they had substantial surpluses over and above their obligation to the workers. These surpluses were an enticing target during takeover attempts and for other corporate investment purposes. While still complying with the letter of ERISA, a company may terminate its plan and purchase annuities for all the plan participants. These annuities are purchased from insurance companies. Any money left over after the purchase of the annuities belongs to the corporation and may be used for any purpose it chooses. Since 1980 approximately $20 billion has been taken out of corporate retirement plans by this means. As with the GICs, the workers depend on the continued solvency of the insurance companies for their pension benefits.

Should a life insurance company become insolvent, most states have an insurance guaranty fund to protect their citizens. These funds are established by state statute and most follow the National Association of Insurance Commissioners (NAIC) model. In certain circumstances, however, the protective umbrella may not provide enough coverage. Four states – California, Colorado, Louisiana and New Jersey – and the District of Columbia do not have guaranty funds. Eleven states exclude unallocated annuities from coverage by the fund. Unallocated as opposed to allocated annuities are not identified with a specific individual. Thus the GIC type of purchase where the company pays the annuity premium in its own name on behalf of all or a number of pension plan participants would not be covered.

Lanny Proffer is chief counsel for Portland State University, Portland, Ore.

Exclude unallocated annuities: Hawaii, Kansas, Kentucky, Massachusetts, Missouri, Oklahoma, Oregon, South Dakota, Utah, Virginia and Wyoming.

Include unallocated annuities: Alabama, Arkansas, Connecticut, Georgia, Illinois, Iowa, Michigan, Mississippi, Ohio, North Dakota, Tennessee, Texas and Washington.

Even in cases when a company terminates its pension plan and purchases annuities in the names of each of its covered employees, or even if the guaranty funds specifically include unallocated annuities (as 13 states do), the protection provided may be inadequate. Before 1986 the NAIC model statute suggested only a $100,000 cap on unallocated annuities. This means that a company investing thousands of dollars each year in an insurance company to fund annuities for its employees may be limited to a recovery of only $100,000 from the guaranty fund. Since 1986 the NAIC model act has recommended a $5 million cap on such accounts.

Whether in the sale of annuities or GICs, insurance companies have been a safe haven. By tradition and by state regulation, life insurance company investment portfolios have been conservatively acquired and responsibly maintained. However, we no longer live in ordinary times. The financial world has changed radically in recent years. Competitive pressure to produce higher rates of return has affected the practices of all financial institutions.

In an attempt to bolster their rates of return the insurance industry has increased its holding in high-interest, high-risk junk bonds. At the end of 1988, 30 percent of these bonds were owned by insurance companies.

Fortunately for most insurance companies their holdings in non-investment grade bonds are a small part of their investment portfolios. However, the disclosure that half of Executive Life of California's cash and invested assets were in junk bonds and that the company was taking an $859 million charge against earnings to reflect the declining value of these bonds prompted many plan sponsors to look more carefully at the companies writing their GICs and to diversify their contracts. It also prompted state regulators to scrutinize the companies under their jurisdiction.

In June the National Association of Insurance Commissioners approved new reporting standards that should give state regulators more information on the bond holdings of the companies they supervise and at the same time discourage heavy accumulation of non-investment grade bonds. Arizona and New York prohibit life insurance companies from holding more than 20 percent of their investment portfolios in non-investment grade bonds.

It should be emphasized that only a very few insurance companies would be affected by such regulations as those promulgated by New York or Arizona. Most life insurance companies have less than 5 percent of their portfolios in the riskier bonds. Still, there have been exceptions, and states are well-advised to be cautious.

Senator METZENBAUM. Thank you very much, Senator Wesely. That indeed is encouraging information that you bring us, and it is pleasing to this Senator to know that you and others in the National Association of State Legislatures are actively moving in this direction, I think it is very, very helpful.

Before I ask any questions, I think we ought to hear from Ross Sargent. We are very happy to have you with us, sir, and we are very sad that State Senator Pat Johnston couldn't be with us. We understand that he was willing to come at another time and couldn't come, and it was our schedule probably more than his schedule that created the problem. But we are happy to have you make any statement on his behalf. Please proceed, sir.

STATEMENT OF ROSS SARGENT

Mr. SARGENT. Thank you very much, Mr. Chairman. My name is Ross Sargent. I am the chief of staff to California State Senator Patrick Johnston, and I thank you for inviting me to appear here this morning and to put the senator's written remarks into the record and to respond to any questions that you have.

As you have stated, the senator is sorry that he couldn't be here. He has a couple of bills that are up this morning in Sacramento.

I come here as the senator's chief of staff. I previously served as the senior consultant to the California Assembly's Committee on Finance and Insurance, which was chaired by then Assemblyman Johnston prior to his recent election to the State senate.

During 1989 and 1990, Senator Johnston's Finance and Insurance Committee conducted a series of oversight and investigation hearings into insurance fraud; insurance insolvencies; California savings and loan failures; risky investment practices by life insurers, including Executive Life and its junk bond portfolio; and the regulatory adequacy of the California Department of Insurance, as well as its relationship to the National Association of Insurance Commissioners.

Although our committee's focus on the practices of the NAIC was limited, our experience with that association was such to raise certain concerns in Senator Johnston's mind about that association's role in insurance solvency strengthening.

Senator Johnston's written testimony chronicles in detail his and the committee's frustration in dealing with the NAIC and enlisting its cooperation in our hearings on the junk bond investment practices of Executive Life and the role played by the NAIC's Security Valuations Office. If the experience of our committee reflects the NAIC's normal policy of nonresponsiveness toward other State legislative committees, then Senator Johnston has serious reservations about the degree of reliance that policymakers should place on the work product and recommendations coming out of that body.

If the NAIC cannot change this policy voluntarily as to its accountability, then it is the considered opinion of Senator Johnston that Federal legislation may be in order to make the NAIC more accountable through State or Federal oversight. It is this lack of present oversight accountability that is the potential Achilles heel of this association's reputation and credibility.

A second concern, in addition to the NAIC's noncooperation, in our experience, was the apparent deficiency in the underwriting standards and practices of the NAIC Security Valuations Office, the so-called SVO. The SVO department performs a function for various State commissioners akin to that performed in the commercial marketplace by the likes of Standard & Poor's, Moody's, and Duff & Phelps. They analyze and rate new issues of bonds and securities, as well as engage in other credit-watching functions.

From such ratings, from that of investment grade to junk bonds, a State insurance commissioner then determines from the insurer's investment portfolio how much to require the insurer to set aside as a protective safety net in the form of a statutory mandatory securities valuation reserve. Such a rating and set-aside process is crucial to the regulator's ability to keep an insurer from falling into insolvency by virtue of that company's having invested heavily in below-investment-grade bonds without adequate reserves.

Our committee learned that the NAIC, unlike its commercial cousins, Standard & Poor's or Moody's, rated securities submitted to it by brokerage houses such as Drexel, Burnham, Lambert and others by simply applying a mechanical and mathematical formula test to the new issues. The rating of the bonds did not take into account whether the issuing company had, in fact, a plant that was standing or burned down, whether it manufactured 50,000 widgets a day or if the officers and managers were onsite or in jail.

The SVO bond rater simply applied a mechanical test and did not go to the site and engage in any hands-on underwriting. Thus, even though the NAIC has recently changed and upgraded their bond-rating criterion, for which they are to be commended, a year after we commenced our investigation of Executive Life we are still not aware that they have changed and strengthened their underwriting standards and practices with respect to onsite inspection.

Third, the senator expresses his concerns based on our committee's hearings wherein the NAIC enunciates a policy that its rating of securities and bonds is merely advisory to the State insurance commissioner in the State where the insurer is domiciled, and that it is up to the State insurance commissioner in the State of domicile to make his or her own independent judgment as to the safeness and soundness of the securities and bonds carried in the insurer's portfolio.

Yet, we are told in sworn testimony by former Insurance Commissioner Roxani Gillespie that she and most, if not all, insurance commissioners rely exclusively on the NAIC Security Valuation Office for all bond ratings because State commissioners do not possess their own in-house bond-rating capability.

Thus, the NAIC disclaimer that "we rate them, but don't you folks rely on them" is not very reassuring, especially in light of the fact that there are literally billions of pages of insurance company annual statements. This sort of catch-22 Senator Johnston feels is troubling. A final concern is that the NAIC, in the Senator's perspective, is often reactive rather than proactive.

I would be happy to answer any questions that you may have, Mr. Chairman.

[The prepared statement of Patrick Johnston, presented by Mr. Sargent, follows:]

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SENATE
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SENATOR
PATRICK JOHNSTON
FIFTH SENATORIAL DISTRICT
SERVING ALPINE, AMADOR, CALAVERAS, MONO, SACRAMENTO, SAN JOAQUIN, TUOLUMNE AND YOLO COUNTIES

COMMITTEES:
BANKING & COMMERCE
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NATURAL RESOURCES & WILDLIFE
PUBLIC EMPLOYMENT & RETIREMENT

Mr. Chairman and fellow members, it is a pleasure to appear before your Committee this morning both to deliver the written testimony of Senator Patrick Johnston, who is unable to be with you this morning due to legislative hearing's in Sacramento, and to respond to any of the Committee's questions.

Although I am presently the Chief of Staff to Senator Johnston, my familiarity with the subject matter of today's testimony is based on the periods of 1989 and 1990 while I was the Senior Consultant to then Assemblyman Johnston while he was chairman of the California Assembly's Finance and Insurance Committee. It was during that period of time that Chairman Johnston's Committee held numerous oversight and investigation hearings into insurance company failures in California and in more recent months conducted numerous hearings regarding insurance company insolvencies.

What follows is the written testimony of Senator Johnston:

Written Testimony of Senator Patrick Johnston

As a Member of the California State Senate and the former Chairman of the California State Assembly's Committee on Finance and Insurance I am pleased to present this written testimony, in lieu of my personal appearance, on matters relative to the regulation of the insurance industry, the investment practices of insurers, and the need for remedial legislation.

It is my understanding that my Chief of Staff, Ross Sargent, will present my testimony to your Committee and make himself available to respond to any of your questions.

Having admired the work of Congressional Subcommittees, like yours, that were engaging in meaningful oversight and investigation, my Finance and Insurance Committee embarked in 1989 on a mission of oversight and investigation into areas that were relevant to our Committee's jurisdiction, as well as timely to our State's needs and concerns. Little did we know then that there would be an unlimited source of things to investigate: within this past year, my Committee has conducted investigations and held hearings on (1) the insolvency of Coastal Insurance Company, (2) the failure of Lincoln Savings and Loan, (3) fraud within the precious commodities market, and (4) the investment practices of life insurers who have over-invested in junk bonds.

As to these various areas, I realize that this Subcommittee's interest this morning is limited to insurance, so I will primarily concentrate on informing your Subcommittee as to the results of our legislative and oversight activities relating to insurance company insolvency issues, including hearings, reports and inquiries undertaken.

In April 1989, we commenced oversight and investigation hearings into the causes which led to the insolvency and liquidation of the Coastal Insurance Company. The Committee's investigation, including five separate hearings, took over nine months, and culminated in a report, which made certain findings and proposed remedial legislation.

Coastal Insurance Company, a California domiciled company was an insurer that marketed sub-standard auto insurance throughout the State, through two wholly-owned subsidiary production agencies, FGS Insurance Agency and Public Insurance.

Coastal was declared insolvent and taken over by the Insurance Commissioner after two years earlier having acquired FGS, a near-defunct auto insurance agency, for a purchase price of $17.5 million, from an insurance broker name Sid Field, who held a restricted insurance license due to his violations of California Insurance Code violations.

Coastal's insolvency was brought about as a result of totally inadequate underwriting, massive fraudulent sales activity by FGS sales agents, non-existent claims practices, under-reserving, filing false and misleading financial statements with the Department of Insurance, and lax regulatory action by the Department of Insurance, which had this Company on its internal "Watch List" for over five years.

Coastal's insolvency cost California auto policyholders some $80 million due to assessments that the California Insurance Guarantee Association had to impose in order to pay this defunct Company's claims.

In addition to the causes just mentioned relating to Coastal's demise, the Committee also found that the very same subsidiary which led to Coastal's insolvency, namely FGS, had been operated by Sid Field, as its President, for over a year and a half after the Department of Insurance had revoked his insurance license for failing to comply with the terms of his probation. To add insult to injury, this same Mr. Field, who had been paid $17.5 million for the soul of FGS to Coastal, was allowed to buy FGS back pursuant to a purchase agreement he made with Coastal's President, Harry Miller, at a weekend meeting just preceding the Department of Insurance's coming in and shutting Coastal down. This buy-back purchase price was a paltry $150,000, no amount of which had ever been paid by Sid Field. This transaction took place in February 1989.

Since that time, although the California Department of Insurance has filed a formal administrative disciplinary proceeding against the license of FGS Insurance Agency due to it permitting Sid Field to control th agency while he had a revoked license - I regret to inform you, that as of today, FGS Insurance is still in business, signing up policyholders by the droves.

In December 1989, we commenced an examination into the effect of junk bonds on the solvency of life insurers in California. This inquiry was prompted by the revelation that one of California's largest life insurance companies, Executive Life, had attempted to improve its financial picture by transferring over $700 million in junk bonds to six wholly-owned subsidiaries and convert such junk into what are called "collateralized bond obligations". This move was discovered by Professor Joseph Belth of Indiana University and reported in trade publications and business journals. The California Department of Insurance, alerted by such accounts, proceeded to examine the transaction and there after in January 1990, ordered Executive Life to reverse that transaction.

Our Committee's concern was further heightened upon learning that First Executive, through its subsidiaries, had written over $52 billion in policies and had 50 percent of its assets in junk bonds and that many of these junk bonds were non-performing or in default. This issue was deemed crucial, in our Committee's opinion, since California was only one of six States that did not have a life insurance guarantee fund. We now have such a fund (AB 4076 - Johnston).

Compounding our concern about the financial soundness of the life insurance industry was the stark reality that as of December 31, 1989, the California Department of Insurance had 74 insolvent insurers either under conservatorship or in liquidation. Of the 1900 California insurance firms, more than 200 are presently under the Department's "special surveillance".

Against this backdrop, we concluded it was appropriate and timely to examine the investment practices of life insurers; especially, those who were heavily laden with junk bonds since junk bonds present three major concerns to regulators: credit risk, liquidity risk, and reinvestment risk. The overall concern is that such junk bonds will dilute the quality of the overall insurer's portfolio and will not be available for the policyholders in the event of a recession.

As a percentage of total assets, junk bonds held by life insurers have more than doubled since 1982. Since 1985, junk bond acquisitions by savings and loans exploded. As of December 1985, there was approximately $59 billion of junk bonds issued in the United States (with over 70 percent of that amount having been issued through Drexel, Burnham, Lambert and Michael Milken); by December 1987 over $150 billion had been issued with a rate of default of only three percent. But as of January 1990, over $200 billion of junk bonds had been issued and the annual rate of default had climbed to an alarming 10 percent.

Of concern to our Committee, in particular, was First Executive Corporation because of its ties to California and the large market share that it holds of policies written in our State. First Executive Corporation, a life insurance holding company, has two life insurance companies in New York and California, and controls approximately $18 billion in assets. It has a long-standing reputation in the life insurance industry as having one of the largest portfolios of junk bonds.

The National Association of Insurance Commissioners (NAIC) reports that there are 2,020 reporting life insurance companies. At the end of 1988, there was $85 billion in junk owned by such companies. That figure, according to Professor Joseph Belth of Indiana University, equals 108 percent of all insurance companies combined statutory net worth of $79 billion, and seven percent of the companies combined statutory assets of $1.2 trillion.

Of California domiciled life insurers, only Executive Life Insurance Company, the California subsidiary of First Executive, had exceedingly high junk bond assets and ratio of junk bonds to net worth. As of December 31, 1988, for example, Executive Life had 50 percent of its assets in junk bonds and had a ratio of junk bonds to net worth of 2,845.

Over a six month period, the Finance and Insurance Committee investigated and held hearings on Executive Life's heavy reliance on junk bonds as a prudent investment strategy as well as their statutory reporting conduct and management practices relating to: (a) attempts to convert junk bonds in investment grade securities (so-called "collateralized bond obligations") in order to improve the quality of their statutory financial statement; (b) allegations that the Company had purchased large junk bond positions in companies taken over by corporate raiders, assisted by Michael Milken; (d) issuance of guaranteed investment contracts (GICs) without statutory authority.

Expert testimony at our hearing, included Professor James Van Horne, A.P. Giannini Professor of Finance, Stanford University Graduate School of Business, John Byrne, Chief Executive Officer of Fund American Companies, Ben Stein, economist, lawyer, and author, as well as others from the insurance industry, who enlightened the Committee about the origin and dangers of junk bonds.

Professor Van Horne testified that junk bonds have not yet been tested under true adverse economic conditions, such as a recession. He also echoed the statements of Professors Altman and Asquith, who have opined that the default rates projected by Michael Milken were in error. For example, default rates on junk bonds that have a 10 year life time are over 30 percent (based on a default rate of three percent per year). However, for the past year the annual default rate on junk bonds has been running at about 10 percent.

The one area that our Committee was not able to fully develop, based on the unavailability of Messrs. Carr and Milken, was the nature and extent of Executive Life's relationship to Michael Milken's inner circle of insurer's and purchasers of junk bonds, commonly referred to as Milken's "Daisy Chain".

As I mentioned earlier, the Assembly Finance and Insurance Committee was unable to secure the attendance of Mr. Carr or his Vice President for Investments, Mr. Marcian, to testify before our Committee on the strengths and advantages of junk bonds as a prudent insurance investment asset. However, as soon as the Committee commenced hearings on proposed legislation that would establish a Life Insurance

Guarantee Fund and impose a limitation on the amount of junk bonds that an insurer could hold in its portfolio - modeled after New York and Arizona's 20 percent limitation, the Committee was soon overrun by lobbyists representing First Executive, First Capital, Zenith Insurance, and thee Alliance for Capital Access - all charter members of the Milken "Daisy Chain" or close associates of Milken.

While at the same time other insurance companies, and life insurance trade associations were stating that any life insurance guarantee fund should be established only if it had a provision limiting junk bond investment activity, the disciples of Milken were painting a picture of doom and gloom for America's economic future if access to capital was cut off by imposing any limit on the amount of junk a life insurer could acquire. When asked why such junk bonds could not be marketed to other insurance companies that had substantial capacity to increase their junk bond holdings, there would be no answer. When asked why just a few select life insurance companies held over 20 percent of junk bonds if they were such a marvelous investment product, there would be no answer.

Although this bill (AB 4076 - Johnston) would not have required a life insurer holding in excess of 20 percent in junk to divest itself of such excess junk, and although the Commissioner of Insurance, Roxani Gillespie, endorsed such a limitation in testimony before our Committee, and even though there exist almost unlimited capacity among other life insurers to buy junk bonds if there continues to be an alternative need for capital access, such a provision limiting junk was unable to get out of Committee due to the intensive lobbying efforts of those few, but powerful opponents, to any restriction on junk bond investments by life insurers.

With respect to the California Department of Insurance's role in monitoring Executive Life, the testimony of Commissioner Gillespie was most revealing.

Ms. Gillespie acknowledged, first of all, that she was aware of New York's Department of Insurance having in 1987 ousted three senior Executive Life-NY officers, yet these defrocked officers continued to remain, without any scrutiny by the California Department, as officers of the sister-company in California, Executive Life. Ms. Gillespie felt no compulsion to examine the fitness and suitability of these officers to remain with Executive Life since, in her words, she "...never had to deal with any of them."

When she was asked why the Department of Insurance didn't monitor more closely Executive Life's amassing of huge amounts of junk bonds, the Commissioner stated that in a situation like that "...we would defer to the federal regulator which is the SEC and we sort of watched the SEC's actions with regards to this vehicle (junk bonds) to this product. It was a product that was very much hated by the rest of the market so we had to be very careful to separate sort of the competitive gossip that we heard versus reality and we did defer to the SEC to a great extent."

Of course, what goes unspoken by the Commissioner, is that it is not the responsibility of the SEC to regulate the quantity and quality of assets held by life insurers - that is a function of a state's Department of Insurance. In keeping with your Committee's inquiry regarding the NAIC and insurance, we received testimony from the Commissioner that the California Department of Insurance relied entirely on the NAIC for the valuation of securities held by life insurers.

Significantly, however in the 10-K filed with the SEC by Executive Life on April 2, 1990, it was revealed that Standard and Poors rated Executive Life's bonds as comprising approximately 57 percent junk bonds whereas the NAIC's Securities Valuation Office rated such bond holdings as amounting to only 38 percent junk, a much more liberal rating standard.

This latter revelation, regarding the valuation of junk bonds, raises serious questions about the efficacy and safety of the NAIC's role in the rating of junk bonds.

After my Committee learned of the role that the NAIC played in the rating of junk bonds, and particularly about the NAIC's role in having approved the transformation, Executive Life, of $750 million of junk bonds into collateralized bond obligations (an action that the Department of Insurance ultimately reversed after it became public), we felt it imperative that the Committee hear from the NAIC's Securities Valuation Office and how they go about rating junk bonds. Our experience in enlisting the cooperation of the NAIC was less than satisfactory. Enclosed are copies of correspondence which reveals the difficulty we encountered in enlisting the cooperation of the NAIC.

When the NAIC finally provided spokespersons, their attorney and a person not familar with the Executive Life bond rating, they consistently deferred to the State Commissioners as the one having the final say-so on how junk bonds held by insurers are evaluated. In essence, the NAIC states their role is merely advisory; yet, according to most available research, almost all state insurance departments defer to the NAIC for the purpose of rating bonds and other securities held by insurers. This Catch-22 is a trap for regulators and a hazard to insurer insolvency.

During our investigation and hearings relating to junk s and investment practices by life insurers, I kept ng repeatedly (by those heavily into junk bond investments) the word - "game"; such as, "this is the way the game works", "this is how the game is played", "in this game, you have to make your spreads". At no time, did such persons ever utter the words, "fiduciary" or "policyholders". Somehow, I get the feeling that we have allowed game players and deal makers to privatize the profits while at the same time socializing the risks. In my opinion, the only way to reverse this trend is to insist on vigorous regulation and swift prosecution with stiff penalties for those who violate financial laws.

What the Finance and Insurance Committee found in its numerous hearings was that there was more than just anecdotal evidence of insurance company incompetence and fraudulent management that was driving certain companies over the cliff. In the case of Coastal Insurance Company, an auto insurance company, and its affiliate FGS Insurance Agency (an insurer that cost the State Guaranty Fund some $80 million) of sales people without any underwriting safe guards and the failure of Pacific Standard Life Insurance, which was owned and operated by Gene Phillips of the Southmark Corporations, who compelled according to testimony for our Committee, officers and directors of a soley-owned subsidiary in invest the companies assets in junk bonds, raw land, and under appraised properties as well as the travail of Executive Life Insurance which was heavily invested in junk bonds that had been foisted on the company by the convicted junk bond king, Michael Milken. All of these failures or concerns led the Committee to focus on the reasons for such failures.

What the Committee found, essentially was a combination of forces that led to such failures. The first was incompetent and in certain cases fraudulent management. The other factor was regulatory laxity and/or lack of regulatory oversight. With respect to the latter, what troubled the Committee on Finance and Insurance was the apparent regulatory difficulties in state examining and overseeing insurance operations that are multi-state in scope. Insurance regulators rely on an examination of annual statements and to a less extent, on quarterly statements that are submitted by companies through the Insurance Commissioners on an annual basis. Such statements we found, at least in California were not required to be audited, and was an open invitation for companies, especially in the case of Coastal Insurance to cook the books and in fact submit false annual statements. That deficiency has been corrected at least from a legislative stand point, by the enactment of a bill that will require such statements to be audited by independent CPA's. The other fact we found was that such annual statements, even if accurately completed, are often times "stale" by the time they are viewed by a regulator. For a company that has significant financial strength, of course this presents no problem, however for a company that is in trouble the fact that such annual statements are not reviewed by a regulator until some six to ten months after the data is provided, this delay can result in irreparable financial harm to policyholders when there is not sufficient time to intervene by the regulator.

With regard to the NAIC's role in performing functions relied on by the California Insurance Commissioner and recommending enactment of legislation, our Committee uncovered what is, in my opinion, an over reliance on information provided by the NAIC.

The NAIC was organized by State Insurance Commissioners to provide the states information that could be collected on a national basis and to engage in a collaborative effort to avoid duplication and pool their informational resources so as to more effectively regulate an interstate industry. Such an objective, it appeared to the Committee, was both sensible and commendable. But what we found in theory did not match what occurs in practice.

In the case of Executive Life, we found that the NAIC was responsible for California's rating of all securities held by Executive Life and all other life insurance companies through the NAIC's Security Valuation Office (SVO). That office's function is to analyze and rate securities and bonds being issued by companies that will be acquired by insurance companies as part of their investment portfolio. It is a function similar to that performed for years by Standard and Poors and Moodys and other commercial rating institutions.

In the case of Executive Life the Committee found that junk bonds issued through Drexel, Burnham, Lambert and acquired in large volumes by Executive Life were rated by the NAIC's SVO division at levels far more favorable in rating than such ratings accorded the same junk bonds by Standard and Poors and Moodys. This rating inconsistency peaked the Committee's curiosity as to whether such rating variance was simply an anomaly or was indicative of other rating problems within the NAIC's office.

Accordingly the Committee sought the testimony of the SVO, in its hearings on Executive Life, especially those bonds that were rated by the NAIC which resulted in Executive Life's attempt to transform $800 million of junk bonds into what the company called Collateralized Bond Obligations, which if accepted by the California Insurance Commissioner, would have transformed such junk bonds into investment grade securities. I was concerned that this rating practice could jeopardize insurer solvency and accordingly attempted to receive testimony from the NAIC as to how their bond rating functions were performed. To the Committee's frustration and disappointment our encounters with the NAIC were less than satisfactory.

Specifically, Mr. Sargent contacted the NAIC's New York SVO office and talked to Mr. Bill Smythe of that office who was familiar with the rating of the Executive Life junk bond issues being converted to investment grade securities. Ross Sargent asked Mr. Smythe if he would be willing to come to California and testify before my Committee on how the SVO performed its bond rating task and how the particular junk bonds in question involving Executive Life had been rated as investment grade securities. Mr. Smythe initially said he would be more than willing to come to testify as long as either the Executive Director or the President of the NAIC approved his appearance. He requested an invitation be sent to the NAIC Director requesting his appearance. Accordingly, I wrote to the NAIC requesting Mr. Smythe's appearance before our Committee in order to testify on the SVO's rating of junk bonds. Shortly thereafter Mr. Smythe called Mr. Sargent and informed him that he would be busy for the indefinite future and therefore would be unable to appear before the Committee. Sensing that the SVO was being somewhat reticent in allowing Mr. Smythe to testify I wrote to the then President of the NAIC, Mr. Earl Pomeroy, requesting his assistance as President of that body in having Mr. Smythe appear and testify as to the SVO's role in rating junk bonds. Mr. Pomeroy indicated that he did not have any control over the matter and it would be up to the Executive Director of the NAIC to give such approval. Sensing that the Committee was being given the run around we then requested then Commissioner Roxani Gillespie of California to request the NAIC's cooperation.

Eventually the NAIC sent their legal counsel to testify before the Committee but not the SVO analyst who had first hand knowledge abcut the rating of Executive Life's junk bonds. (Attached are copies of correspondence on this matter marked Exhibits "A", "B", "C" and "D".)

My concern, from this experience, was that the NAIC's rating standards were far more liberal than those of commercial rating agencies and that an organization like the NAIC (which is relied on by State Insurance Commissioners who do not have their own in-house rating capability) could jeopardize the integrity of the regulatory process by allowing investment instruments to permeate an industry that are unsafe and unsound.

To the NAIC's credit, since our hearings of last year, they have promulgated new rating standards that are far more stringent than those in existence at the time of our hearing on Executive Life. However, this experience with the NAIC still leaves unanswered the question of the NAIC's accountability to policy makers who have the responsibility for enacting legislation, often times legislation which is based on NAIC Model Acts.

As was noted at the Committee hearings on Executive Life the NAIC is touted as an independent analysis and research organization for State Insurance Commissioners. If they are utilized as a quasi-regulatory body, then they should be accountable in some measure to explain how their process works and to what extent they are financed and staffed as well as what is their relationship to the industry that they are making recommendations on. Among other things that caused the Committee concern as to the independence and reliability of the NAIC was how this organization is financed. Information provided to the Committee indicated that for the most part the NAIC is funded through a series of annual and quarterly conventions held throughout the country that are attended by industry representatives who pay fees which in turn provide the funding base for the operation of the NAIC's research staff.

It is my opinion the the NAIC can be a valuable adjunct to the insurance industry regulatory matrix but that in order for it to enjoy the confidence of the public and legislative bodies it must be accountable to either state or federal policy makers. To that end, I feel it is appropriate that this committee consider legislation which would strengthen this Association's role, but only if it has accountability either to the Congress or state legislatures.

Not to do so could result in the deals of the 80's becomi the consequences of the 90's.

California Legislature

Assembly Committee on Finance and Insurance

March 15, 1990

Mr. Earl Pomeroy, President
National Association of Insurance Commissioners
600 East Boulevard Avenue
Bismark, North Dakota 58505

Dear Mr. Pomeroy:

Ross Sargent, of my Committee staff, has advised me that he talked to you about two weeks ago concerning the NAIC permitting Mr. Bill Smythe of the Securities Valuation Office to testify before the Finance and Insurance Committee relative to how the NAIC rates securities held by insurers. He indicated that at the time he talked with you that you were most supportive of the idea and did not foresee any problem with making Mr. Smythe available for our forthcoming hearing on April 3, 1990. Mr. Sargent also indicated that he had been in touch with Mr. Smythe and that Mr. Smythe had expressed his willingness to come to Sacramento, subject of course to the NAIC Board's approval.

I was extremely disappointed to learn that Mr. Smythe will now "..be busy for the indefinite future," and therefore unable to appear for the April 3rd hearing, especially in view of Mr. Smythe's and your previous indications that there should be no problem.

In order for this Committee to make informed policy decisions with respect to how, or if, insurer's investment practices should be limited or regulated, it is imperative that we have a comprehensive and intelligent understanding of the NAIC's Securities Valuations Office role in rating securities; especially, since the California Department of Insurance relies exclusively on the NAIC's rating process.

I hereby ask for your cooperation and assistance in making Mr. Smythe available to the Committee on April 3, 1990 at 9:00 a.m. in Room 4202 of the State Capitol.

EXHIBIT "A"

Mr. Earl Pomeroy
March 15, 1990
Page 2

Brad Wenger of ACLIC has indicated that you have expressed a willingness to come before the Committee and testify about a life insurance guarantee fund. I think that your testimony, like that of Mr. Smythe's, would be most helpful and well received.

I look forward to our mutual cooperation.

Sincerely yours,

PATRICK JOHNSTON

PJ:rse

MAR 21 1990

State of North Dakota
DEPARTMENT OF INSURANCE

Fifth Floor State Capitol
Bismarck, North Dakota 58505
Telephone (701) 224-2440
Consumer "HOTLINE" 1-800-247-0560

EARL R. POMEROY
COMMISSIONER OF INSURANCE

March 22, 1990

Honorable Patrick Johnston
Chairman, Assembly Committee on
Finance and Insurance
State Capitol
P.O. Box 942849
Sacramento, CA 94249

Dear Chairman Johnston:

Thank you for your letter of March 15, 1990, regarding your request to solicit the testimony of Bill Smythe of the National Association of Insurance Commissioners' staff.

I had spoken with Ross Sargent of your staff sometime prior to the receipt of your letter. After an enjoyable visit, I recall informing Ross that I was not in a position as North Dakota Insurance Commissioner to direct NAIC staff relative to the inquiries of your committee. I expressed my admiration for your good work on a variety of important insurance issues though I did not intend to convey an impression that I had authority to direct Mr. Smythe's attendance.

I trust the California Insurance Department will make every effort to assist you in any way possible.

With best regards,

Earl R. Pomeroy

Earl R. Pomeroy
Commissioner of Insurance
N.D. Insurance Department

ERP/njb

EXHIBIT "B"

California Legislature

Assembly Committee on Finance and Insurance

April 6, 1990

Ms. Roxani Gillespie
Insurance Commissioner
100 Van Ness Avenue
San Francisco, CA 94102

Dear Commissioner Gillespie:

I am pleased to hear that you will be available to testify before the Finance and Insurance Committee on May 1, 1990 relative to the need for a life insurance guaranty fund and issues related to that subject.

As you are aware from our previous conversations and correspondence we have scheduled a hearing for April 17, 1990 on the investment practices of insurers, in order to ascertain if such practices pose a threat of insolvency which may require the establishment of a guarantee fund. An integral part of our investigation involves the investment practices of Executive Life Insurance Company, the wholly owned subsidiary of First Executive. This company's massive reliance on junk bonds, acquired in the main through Michael Milken and Drexel, Burnham, Lambert, has prompted many financial analysts to opine that such reliance puts this company, and those engaged in similar investment practices, at risk as to their solvency.

In December of 1989, your Department challenged the actions of First Executive in transferring over $750 million of junk bonds to six wholly owned subsidiaries in an attempt to convert such junk into "collateralized bond obligations." In order for this committee to fully understand the regulatory statutory accounting implications of such financial legerdemain it is crucial that the committee receive testimony from those individuals possessing first-hand knowledge as to how such junk bonds and collateralized bond obligations are analyzed and rated.

EXHIBIT "C"

Ms. Roxani Gillespie
Page Two
April 6, 1990

It is my understanding, from conversations my staff has had with Mr. Norris Clark of your department, that California, like its sister states, defers to the National Association of Insurance Commissioners (NAIC) and its Securities Valuation Office (SVO) for all analysis and rating of securities acquired by insurers. Accordingly, the personal appearance of a knowledgeable and informed representative of the NAIC's valuation office is essential to this legislative committee's ability to carry out it's investigation and oversight responsibilities in a timely and competent fashion. Thus far, our efforts to obtain a spokesperson from the NAIC have been thwarted and I am deeply troubled by this less than cooperative attitude by an association that is relied on by legislative policy makers and regulators, yet has no accountability to any branch of government of this state, or to its citizens.

On February 13, 1990, I wrote a letter to Mr. Bill Smythe of the NAIC's Securities Valuation Office, formally inviting him to testify before our Committee after Mr. Smythe had advised Ross Sargent, our senior consultant, that he would be pleased to attend and give testimony on how securities were analyzed and rated, so long as the NAIC Board gave him permission to do so. About March 1, 1990, Mr. Sargent was telephoned by Mr. Smythe who apologetically informed Mr. Sargent that he, Mr. Smythe, would be "too busy for the foreseeable future to come to California and testify on this subject matter." Thereafter, on March 15, 1990, I wrote Mr. Earl Pomeroy, the newly-elected President of the NAIC to express by disappointment over the NAIC Board's action in not permitting Mr. Smythe to testify on junk bonds and how they are rated. On March 21, 1990, Mr. Sargent personally called on Mr. Pomeroy at the Commissioner's office in Bismarck, North Dakota and was advised by the Commissioner as NAIC President he was not in a position to direct the NAIC staff to cooperate with the inquiries of our Committee's investigation. Mr. Pomeroy also informed Mr. Sargent that the NAIC would be very uncomfortable coming before any legislative committee and explaining the role it plays in analyzing and rating securities that are acquired by insurers. Subsequently, I received a letter from Mr. Pomeroy confirming the conversation he had with Mr. Sargent.

Quite frankly, I am amazed and distressed that an organization established to serve and support the insurance departments of our states, an organization, that in many instances, assumes functions and responsibilities that would otherwise be undertaken by the various state departments of

Ms. Roxani Gillespie
Page Three
April 6, 1990

insurance, arrogates unto itself the decision as to whether it should explain to state legislatures how it performs its functions and responsibilities. Perhaps, the time has come to re-examine whether California should conduct its own insurance examinations, securities analysis and ratings, and other functions that are presently being performed by the NAIC. With responsibility comes accountability and I would hope this Committee can enlist your support in conveying that message to the NAIC.

Accordingly, in keeping with my conversation with you on April 2, 1990, I would ask you to urge the NAIC Board to reconsider its action and grant permission to Mr. Smythe to attend the Committee's hearing on April 17, 1990.

Please advise me by April 13, 1990 if you have been successful in securing the Association's cooperation in this regard.

Sincerely,

PATRICK JOHNSTON

PJ/pyr
Enclosure
cc: NAIC Board of Directors
Mr. Earl Pomeroy
National ~~Association~~ of State Legislators
Char Mathias Council

California Legislature

Assembly Committee on Finance and Insurance

STATE CAPITOL
P O BOX 942849
SACRAMENTO CA 94249-0001
(916) 445-9 60

April 18, 1990

Ms. Roxani Gillespie
Insurance Commissioner
100 Van Ness Avenue
San Francisco, CA 94102

Dear Commissioner Gillespie:

This is to acknowledge receipt of Assistant Commissioner Mathias' letter of April 16, 1990 responding to my letter of April 6, 1990 wherein I requested your assistance in securing the attendance of Mr. Smythe of the NAIC before our Committee on April 17.

I am disappointed to learn that the NAIC continues to refuse to send Mr. Smythe to our hearing. The NAIC's , proposal for cooperating with the Committee, through a letter writing dialogue or by our traveling to their offices in New York, is totally unacceptable.

As I mentioned in my April 6 letter, the NAIC serves the states - it is not the other way around. For the NAIC to set the parameters as to how, when, and where they will respond to legislative inquiries is beyond the pale rational comprehension.

I hereby ask that you urge the NAIC to reconsider its declination of the Committee's request and make Mr. Smythe available. As you are aware, the Committee has scheduled a follow-up hearing for May 1, 1990 at which time you will be testifying. It would be timely and appropriate for Mr. Smythe to attend at that time. By copy of this letter to Mr. Pomeroy and the NAIC Board of Directors, I enlist their cooperation in reconsidering their previous action.

EXHIBIT "D"

Ms. Roxanie Gillespie
Page Two
April 18, 1990

Also, please provide me with copies of the communications you received from Mr. Pomeroy and the NAIC's director, which formed the basis for Ms. Mathias' response of April 16.

Please advise me by no later than April 26 of the NAIC's response.

Sincerely,

PATRICK JOHNSTON

PJ/pyr
cc: Mr. Earl Pomeroy
NAIC Board of Directors
National Council of State Legislatures
Char Mathias

Senator METZENBAUM. Thank you very, very much. That was a very strong and powerful statement, and it certainly raises cause for concern which provides reason for us to continue our inquiry in this area.

Commissioner Donaho, from the statistics we have compiled it is clear that the States have been slow in implementing many model laws. In your view, why do States have difficulty in implementing these model insurance laws?

Mr. DONAHO. Well, I think there are several. One—and I speak as a commissioner who has, A, not been there too long, but also who does not come from the insurance industry. But based upon my experience, I can readily see why previous insurance commissioners did not push very much because they probably would rather have been comfortable, because the more you push for new activities and new regulation and new ideas, the more work you have to do. You stir up a great many things. You stir up not only people who are in favor of your position, but people who are against it.

Maryland also is not a State given to the adoption of model laws, which I think is somewhat of a characteristic of the original 13 States that they don't necessarily adopt everything that is recommended nationally.

However, we certainly were very pleased in our recent effort with the fact that the NAIC model laws were available because they fit into our program of improving our capability for regulating solvency and other matters. But I can understand, also, the opposition from both the industry and the attitude of consumer groups when legislation is proposed. It is not easy to get model legislation adopted, and certainly it has to be adapted to the needs of the State and to its general attitude on statutory drafting.

Senator METZENBAUM. In your experience, was the opposition of the industry to the passage of model laws greater, or was the opposition of the consumer groups greater to the model laws?

Mr. DONAHO. I think in our recent experience it was about equal. For example, the industry was very much opposed to the notification of impairment, personal liability on the part of the CEO's. On the other hand, the consumer affairs representatives were equally vigorous in opposing immunity for the insurers on disclosure of fraud. So they balanced one another out.

Senator METZENBAUM. Thank you very much, Commissioner.

Senator Wesely, you testified that the Nebraska Legislature recently passed, and the Governor signed, the NAIC models necessary for accreditation by the NAIC. Do you, as a State legislator, rely on the NAIC to come up with good model legislation, or do you think other States rely on the NAIC when considering insurance legislation?

Senator WESELY. Senator, I think the NAIC model acts are very vital. We look to them first rather than reinvent the wheel. They have put the time and effort in, and so we do rely on those acts.

Senator METZENBAUM. Does it disturb you as a State legislator to learn that out of 383 members of 30 advisory committees of the NAIC, there are only 13 consumer representatives and they only serve on 4 of the 30 committees? Does that bother you?

Senator WESELY. Well, it concerns me. We look at the end product, though, and we feel like the model acts are excellent pieces of legislation. So the process troubles me, but the end product of that process seems to be a good base on which to build.

Senator METZENBAUM. I believe the function of the NAIC is important to the States, and I have no problem with that. I can understand the matter of not trying to reinvent the wheel every time you deal with the insurance industry, I also think that State legislators like yourself have a right to expect that the models from the NAIC are the product of a balanced process.

As I pointed out previously, with respect to the imbalance, do you think that as the cochair of the legislators' advisory committee—I am not sure exactly what the title is—that you have for the National Association of State Legislatures you might be in a position to make your voices heard, as well as ours, in pressing the NAIC to see to it that there is more consumer representation?

Senator WESELY. Well, we would be willing to try and express that. We have had a good relationship with NAIC. We have had an excellent working relationship since we formed in the fall, and I believe that we have a chance to make an impact with them on that question.

Senator METZENBAUM. Are you willing to make that effort to try?

Senator WESELY. Yes. Our task force will meet later this week and I will bring that issue up with the members and see what their feelings are.

Senator METZENBAUM. Do you think it appropriate, Senator, that the NCSL also discuss with the NAIC this matter of funding for the travel expenses of consumer representatives, since the reality of life is that the insurance company representatives have no problem in having their expenses covered and the insurance commissioners have no problem in having their expenses covered, but that consumer organizations quite often have such limited budgets that they aren't in a position to provide the funding? And we are talking about peanuts when you are talking about the actual costs of doing business in this industry.

It seems to me that although Mr. Pomeroy had said there are some problems with deciding which one or who should come, that that matter could very well be handled by having consumer groups themselves work out such choices and such details, and that it is highly appropriate for the NAIC to provide that very modest funding that would be needed. Do you think the NCSL could be helpful in this respect?

Senator WESELY. Senator, I would be again willing to bring that issue up and perhaps discuss it with NAIC. To give you an example, I understand NCSL in some cases will provide funding for consumer members of our work groups. So we have a policy that would be more in line with your views on that, and so we could certainly discuss with NAIC.

Senator METZENBAUM. We would appreciate it, and we would appreciate it if you would let us hear the results of both conversations when and if those occur.

Frankly, you are to be congratulated for your success in getting the models passed into law in Nebraska. Unfortunately, not all

States have been moving that fast, as you well know. It has taken 20 years for 47 States to adopt the model on the life and health insurance guaranty fund, and your State adopted it just after 4 years of its having been opened up or brought to the attention of legislators.

Some models have not been adopted by State legislatures at all. Do you have any thoughts as to why so many State legislatures have so much difficulty in moving forward and passing the model laws?

Senator WESELY. I do, Senator. As a fellow legislator, I understand our plates are full with many different issues, and it seems to me the first thing with any sort of action on an issue is that you have to have the attention of the legislatures. And I think that, frankly, this issue has not been to the forefront until last year. It was simply not a priority issue, but it has changed.

I think last year saw that attention has now been drawn to the issue. So the second step, I think, is that we are learning about it. We are studying it, we are examining it. And then I think the third step is action, and that is happening, actually, quite rapidly for this issue.

So I think the first line of defense I would have in response is I just don't think we paid as much attention to this issue as we should have, but that is not going to happen in the future, I don't think. I think you are seeing NCSL, the Congress, and I think the public saying something has to happen.

You asked a question about industry opposition. In Nebraska, we have had excellent cooperation with the industry. In fact, they have helped us pass the model legislation. In fact, they helped us pass the legislation that went beyond it with the investment restrictions. But I do understand that in some States there is some industry opposition that has been a problem, and so that may be part of the answer to your question as well.

Senator METZENBAUM. Thank you very much, Senator Wesely, and thank you for being with us.

Mr. Sargent, from your experience as senior consultant to the Assembly Finance and Insurance Committee in California, do State legislators rely on NAIC model laws?

Mr. SARGENT. Yes; I think our experience is that that is the case, Senator. I think there is a considerable degree of reliance on the NAIC model laws.

Senator METZENBAUM. What problems have you faced in California in trying to pass strong insurance legislation?

Mr. SARGENT. Well, as you will see on that chart, it is only California that has joined very belatedly its sister States in enacting a guaranty fund just last year. That was A.B. 4076 that was authored by Senator Johnston, and we had quite a history in trying to get that guaranty fund legislation through the California Legislature.

The guaranty fund bill was modeled to some extent after the NAIC model act, but, in addition, it contained a limitation on junk bonds. We felt it was prudent—the Senator certainly did—to put into that law a limitation on junk bonds, similar to New York and Arizona that put a cap on junk bonds of 20 percent.

Quite frankly, that provision of the bill was heavily lobbied in our committee. The Alliance for Capital Access came out from

Washington, as well as lobbyists from Executive Life and Zenith and others who were heavily into junk bonds, and said that junk was the greatest thing since sliced bread and that capital access would dry up in this country unless insurance companies could engage in a feeding frenzy on junk bonds.

As a last resort, the senator offered to grandfather in those companies that exceeded 20 percent, and even with that concession the provision to limit junk bonds was defeated. So we saw the bill was going to go down unless we took that provision out, so reluctantly the senator had to take that limitation on junk bonds out of the bill so the guaranty fund bill could pass.

Having said that, there were still reservations about the guaranty fund bill passing because the industry for years in California wanted to have a premium tax offset which the industry in other States enjoy. When they are assessed for contributions to the guaranty fund, insurance companies are allowed to deduct from their taxes any assessments they pay to the guaranty fund, which is probably appropriate and proper.

In California, we could not do that because in California the way insurance companies are taxed is cranked into our constitution. So if you want to amend the way insurance companies are taxed or given any deductions, you have to go to the people and put it on the ballot. And I think it was the feeling of the legislature, and even the industry, that the people of California were not about to pass an initiative that gave the industry a tax offset for a guaranty fund.

But I think there was the momentum that we needed a guaranty fund in California, especially with the problems that Executive Life of California was having, which is domiciled in our State. So, reluctantly, the industry, and to the credit of ACLI, supported the guaranty fund bill without a tax offset provision.

However, we did make certain exceptions to the model act. For example, we have a deductible which other States don't have. So if there is a $100,000 limit on annuities and a life insurance policy, you can only get 80 percent if the company fails; there is a 20-percent deductible. The rationale is so that consumers, to some extent, share in the risk-taking and will examine a company a little more closely before they invest with a company that may have investments in risky assets.

Senator METZENBAUM. Do you also have some limit of $300,000?

Mr. SARGENT. Yes. There is a $250,000 limit on life insurance death benefits, Senator, but for annuities it is $100,000. We exclude unallocated annuities, but there is a $250,000 cap on life insurance.

Senator METZENBAUM. In one statement, you said that the amount of money that the insurance companies pay into the guaranty fund—they want to have a tax credit for that, which is probably proper. And as I am sitting here, I am saying to myself, well, how does that differ from the savings and loans coming to the Federal Government for a bailout? One way or the other, the taxpayer becomes the fall guy.

If you can deduct it from the amount that they pay in taxes to California, then the people are winding up paying for the guaranty fund, and I am a little curious as to why you feel it is proper to have a tax deduction.

Mr. SARGENT. Well, first of all—and I suppose I am playing the devil's advocate in asserting the industry's argument. Their first argument is that all other States give them that.

Senator METZENBAUM. That is not a very good argument.

Mr. SARGENT. I understand, right.

Senator METZENBAUM. That just shows how powerful they are as a lobby.

Mr. SARGENT. Right, right. The other rationale, Senator, is that the fund is funded by the industry, so the taxpayers are not really paying for it. It is an industry-based assessment that is paid for by policyholders, but policyholders would pay for it by the costs they would——

Senator METZENBAUM. You are saying that they can deduct the amount that they pay from their taxes.

Mr. SARGENT. That is true. So to that extent, there would be an indirect subsidy by the taxpayers.

Senator METZENBAUM. I would think so. It would seem to me that senator Johnston, who has obviously been very fair and open-minded and concerned about the consumer, would probably be the kind of senator who would be concerned about the taxpayers. And where you get this tax credit for the amounts paid into the guaranty fund—that is just another nice way of saying the American people are going to be the suckers, just as they are in the savings and loan deals. I just am a little bit surprised, so give him my thoughts and concerns about that, if you will.

Mr. SARGENT. I will do that.

Senator METZENBAUM. Gentlemen, thank you very much for being with us this morning.

Our last panel includes Mr. Phil Schwartz of the American Insurance Association, and Mr. Dan Mica, a former member of the Congress and old friend, executive vice president of the American Council of Life Insurance. We are happy to have both of you here.

Mr. Schwartz and Mr. Mica, I would hope that when you get ready to testify that you would address yourselves to this point that I have just raised as to why there is legitimacy for the tax deductibility of the amount paid into the guaranty fund. I gather that tax deductibility is with respect to State taxes, not Federal taxes, but if you would be good enough to comment on it, I would appreciate it, all within your 5-minute time.

Mr. Phil Schwartz, please proceed.

STATEMENTS OF A PANEL CONSISTING OF PHILLIP SCHWARTZ, VICE PRESIDENT, FINANCIAL REPORTING, AND ASSOCIATE GENERAL COUNSEL, AMERICAN INSURANCE ASSOCIATION, ACCOMPANIED BY DAVID PRATT, VICE PRESIDENT, FEDERAL GOVERNMENT AFFAIRS; AND DANIEL A. MICA, EXECUTIVE VICE PRESIDENT, AMERICAN COUNCIL ON LIFE INSURANCE, ACCOMPANIED BY RICHARD MINCK, EXECUTIVE VICE PRESIDENT; DICK BARNSBACK, CHIEF COUNSEL FOR STATE RELATIONS; AND JACK BLAINE, SPECIAL CONSULTANT

Mr. SCHWARTZ. Thank you, Mr. Chairman. Mr. Chairman, I have submitted formal comments and I hope that you will include those in the record. I would like to summarize my testimony.

Senator METZENBAUM. They will be included in their entirety in the record.

Mr. SCHWARTZ. Thank you.

Senator METZENBAUM. You might just say briefly who the American Insurance Association is.

Mr. SCHWARTZ. I am Phillip Schwartz. I am vice president, financial reporting, and associate general counsel with the American Insurance Association. With me today is David Pratt, vice president for Federal Government affairs with AIA.

The American Insurance Association is a trade association comprised of 239 companies that write all lines of property and casualty insurance throughout the United States. I am extremely pleased to be here this afternoon to discuss with you our interest in improving regulation for insurance company solvency and AIA's activity in the various States to get the NAIC financial regulations standards adopted.

The American Insurance Association and its members are very supportive of regulations for solvency, and I would like to take this opportunity to list just a few of those reasons for this concern.

First, we believe that insurance buyers have a right to expect that their insurance company will be able to fulfill its contractual obligations. Second, our members are doubly penalized by the acts of financially unsound insurers. Not only do financially sound insurers lose business to the artificially low prices of unsound companies, but when the results lead to liquidation, the healthy companies also must pay those claims through the guaranty associations which protect policyholders and claimants when an insolvent insurance company is unable to meet its obligations.

Third, AIA companies are concerned that adverse legislative, regulatory, and judicial developments may be increasing the risk of future insolvencies, particularly for insurers writing certain commercial coverages.

Fourth, consistent with their interest in preventing insolvencies, AIA companies also have an interest in minimizing the time and expense of having to comply with regulatory requirements that may differ from State to State. Finally, our members wish to avoid any decline in the public's confidence in the insurance industry caused by a perceived solvency crisis.

In light of these and other considerations, AIA has always been in the forefront of improving State regulation for solvency. While the experts generally agree that the industry is financially sound, AIA believes that it is important to strengthen the existing insurance regulatory system in order to avoid possible solvency problems in the future.

Improvement to State regulation for solvency is an AIA property for the 1991 legislative sessions. AIA is working hard in the States to get NAIC model laws enacted. As of April 5, last Friday, we have seen favorable activity in more than 40 States. When added to the two States that have already been accredited by the NAIC, we think there has been responsible reaction to a relatively new program.

In conclusion, AIA is committed to improving State solvency regulation. Such regulation has a long history of adapting to changes in the types of financial problems confronting insurers. At the same time, we remain concerned that solutions to all of the shortcomings of the current insurance regulatory system may not be available on a State-by-State basis or from the NAIC.

The limitations of 50 separate entities attempting to regulate a business that often operates in a national or international arena may necessitate some Federal involvement to bolster the will needed to take action against troubled companies and to bring uniformity and order into the process. As part of AIA's deliberations, we are exploring various Federal alternatives that might be feasible to enhance State regulation for solvency.

Thank you for this opportunity to share AIA's views on this significant subject. I would be glad to answer any questions.

[The prepared statement of Mr. Schwartz follows:]

STATEMENT OF THE AMERICAN INSURANCE ASSOCIATION

TESTIMONY
OF
PHILLIP SCHWARTZ
VICE PRESIDENT - FINANCIAL REPORTING AND
ASSOCIATE GENERAL COUNSEL
AMERICAN INSURANCE ASSOCIATION
ON STATE ADOPTION OF NAIC MODEL INSURANCE LAWS
BEFORE THE
SUBCOMMITTEE ON ANTITRUST, MONOPOLIES AND BUSINESS RIGHTS
OF THE COMMITTEE ON THE JUDICIARY
U.S. SENATE
APRIL 9, 1991

American
Insurance
Association

The American Insurance Association is a national trade organization of casualty insurers.

TESTIMONY OF PHILLIP SCHWARTZ

U.S. SENATE

COMMITTEE ON THE JUDICIARY

APRIL 9, 1991

MR. CHAIRMAN, MEMBERS OF THE COMMITTEE, LADIES AND GENTLEMEN, GOOD MORNING. MY NAME IS PHILLIP SCHWARTZ, AND I AM VICE PRESIDENT - FINANCIAL REPORTING AND ASSOCIATE GENERAL COUNSEL OF THE AMERICAN INSURANCE ASSOCIATION ("AIA"). I AM EXTREMELY PLEASED TO BE HERE THIS MORNING TO DISCUSS WITH YOU OUR INTEREST IN IMPROVING REGULATION FOR INSURANCE COMPANY SOLVENCY AND AIA'S ACTIVITY IN THE VARIOUS STATES TO GET THE NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS' ("NAIC") FINANCIAL REGULATION STANDARDS ADOPTED.

I. BACKGROUND

THE AMERICAN INSURANCE ASSOCIATION IS A TRADE ASSOCIATION COMPRISED OF 239 COMPANIES THAT WRITE ALL LINES OF PROPERTY AND CASUALTY INSURANCE THROUGHOUT THE UNITED STATES. DURING 1990, OUR MEMBERS WROTE POLICIES WITH PREMIUMS OF ABOUT SIXTY BILLION DOLLARS. LET ME ASSURE YOU THAT REGULATION FOR SOLVENCY IS OF PRIMARY CONCERN TO AIA MEMBERS. I WOULD LIKE TO TAKE THIS OPPORTUNITY TO LIST JUST A FEW OF THE REASONS FOR THIS CONCERN.

FIRST, WE BELIEVE THAT INSURANCE BUYERS HAVE A RIGHT TO EXPECT THAT THEIR INSURANCE COMPANY WILL BE ABLE TO FULFILL ITS

CONTRACTUAL OBLIGATIONS. FINANCIAL PROTECTION IS THE ESSENCE OF INSURANCE, AND IT IS OUR BASIC PURPOSE FOR EXISTENCE AS AN INDUSTRY.

SECOND, OUR MEMBERS ARE DOUBLY PENALIZED BY THE ACTS OF FINANCIALLY UNSOUND INSURERS. NOT ONLY DO FINANCIALLY SOUND INSURERS LOSE BUSINESS TO THE ARTIFICIALLY LOW PRICES OF UNSOUND COMPANIES; BUT, WHEN THE RESULTS LEAD TO LIQUIDATION, THE HEALTHY COMPANIES ALSO MUST PAY THOSE CLAIMS THROUGH THE GUARANTY ASSOCIATIONS WHICH PROTECT POLICYHOLDERS AND CLAIMANTS WHEN AN INSOLVENT INSURANCE COMPANY IS UNABLE TO MEET ITS OBLIGATIONS. EACH YEAR, AIA MEMBER COMPANIES ARE ASSESSED MILLIONS OF DOLLARS TO FUND STATE GUARANTY ASSOCIATIONS. IN 1989, FOR EXAMPLE, NET GUARANTY FUND ASSESSMENTS FOR THE P/C INSURANCE INDUSTRY TOTALLED MORE THAN $800 MILLION. UNDER THE GUARANTY FUND SYSTEM, WELL-MANAGED INSURANCE COMPANIES--LIKE THOSE WHICH COMPRISE THE MEMBERSHIP OF THE AMERICAN INSURANCE ASSOCIATION--IN EFFECT PAY THE COSTS WHEN THE REGULATORY SYSTEM IS UNABLE TO PREVENT INSOLVENCIES.

THIRD, AIA COMPANIES ARE CONCERNED THAT ADVERSE LEGISLATIVE, REGULATORY, AND JUDICIAL DEVELOPMENTS MAY BE INCREASING THE RISK OF FUTURE INSOLVENCIES, PARTICULARLY FOR INSURERS WRITING CERTAIN COMMERCIAL COVERAGES. THIS IS ESPECIALLY TROUBLESOME FOR AIA MEMBER COMPANIES, WHICH REPRESENT ABOUT FORTY PERCENT OF THE MARKET FOR THE COMMERCIAL LINES OF INSURANCE.

FOURTH, CONSISTENT WITH THEIR INTEREST IN PREVENTING INSOLVENCIES, AIA COMPANIES ALSO HAVE AN INTEREST IN MINIMIZING

THE TIME AND EXPENSE OF HAVING TO COMPLY WITH REGULATORY REQUIREMENTS THAT MAY DIFFER FROM STATE TO STATE. WE BELIEVE THAT THE INDUSTRY AND THE PUBLIC WOULD BENEFIT FROM A MORE EFFICIENT AS WELL AS A MORE EFFECTIVE REGULATORY SYSTEM.

FINALLY, OUR MEMBERS WISH TO AVOID ANY DECLINE IN THE PUBLIC'S CONFIDENCE IN THE INSURANCE INDUSTRY, CAUSED BY A PERCEIVED SOLVENCY CRISIS. THE RECENT SAVINGS AND LOAN CRISIS PROVIDES A SALIENT EXAMPLE OF THE WAYS IN WHICH THE EROSION IN PUBLIC CONFIDENCE CAN EXACERBATE SUCH PROBLEMS.

IN LIGHT OF THESE AND OTHER CONSIDERATIONS, AIA HAS ALWAYS BEEN IN THE FOREFRONT OF ATTEMPTING TO IMPROVE STATE REGULATION FOR SOLVENCY. THIS HAS TAKEN MANY FORMS OVER THE YEARS; INCLUDING LEADERSHIP IN DEVELOPMENT AND IMPROVEMENT OF THE NAIC EARLY WARNING SYSTEM FOR IDENTIFYING THOSE INSURERS MOST IN NEED OF IMMEDIATE REGULATORY ATTENTION, DEVELOPMENT OF AN ACCOUNTING PRACTICES MANUAL TO FACILITATE UNIFORM PROCEDURES AMONG STATES AND SUPPORT FOR NAIC MODEL LAWS AND REGULATIONS WHICH STRENGTHEN SOLVENCY REGULATION. WE VIEW OUR PARTICIPATION IN THIS COMMITTEE'S INQUIRY AS A WELCOME CONTINUATION OF OUR HISTORICAL INVOLVEMENT IN WORKING TOWARD MORE EFFECTIVE AND MORE EFFICIENT REGULATION FOR SOLVENCY.

II. OVERVIEW OF FINANCIAL ISSUES

IN DISCUSSING THE FINANCIAL PERFORMANCE OF THE P/C INSURANCE INDUSTRY, I WOULD LIKE TO COMMENT ON THREE ISSUES: FIRST, THE CURRENT FINANCIAL CONDITION OF THE INDUSTRY; SECOND, HISTORICAL

DEVELOPMENTS REGARDING THE INCIDENCE OF INSOLVENCY; AND THIRD, THE REASONS WHY PARALLELS BETWEEN INSURERS AND SAVINGS AND LOANS ARE WITHOUT MERIT.

A. CURRENT FINANCIAL CONDITION

FOR THE PAST FIVE YEARS, THE FINANCIAL CONDITION OF THE P/C INSURANCE INDUSTRY HAS BEEN THE SUBJECT OF CONSIDERABLE PUBLIC DEBATE. THIS DEBATE HAS HAD TWO CENTRAL--YET CONTRADICTORY--THEMES. WHILE SOME INDUSTRY CRITICS HAVE MAINTAINED THAT INSURERS ARE EARNING EXCESSIVE LEVELS OF PROFIT, MORE RECENTLY, THERE HAVE BEEN CONCERNS THAT THE INDUSTRY IS ON THE BRINK OF INSOLVENCY. IRONICALLY, THERE ARE SOME SPECIAL INTEREST GROUPS WHICH PERSIST IN THE VIEW THAT BOTH OF THESE DEVELOPMENTS ARE OCCURRING SIMULTANEOUSLY!

THE TRUTH OF THE MATTER IS THAT INSURERS ARE NOT EARNING EXCESSIVE PROFITS, NOR ARE THEY THREATENED WITH IMMINENT INSOLVENCY. P/C INSURANCE IS A CYCLICAL INDUSTRY WHICH, OVER TIME, HAS MAINTAINED A MODEST LEVEL OF PROFITABILITY. BASED ON A SAMPLE OF 35 INDUSTRIES OVER A TEN YEAR PERIOD, P/C INSURERS' PROFITABILITY HAS BEEN SOMEWHAT LOWER THAN MOST OTHER INDUSTRIES; MOREOVER, BECAUSE OF THE CYCLICAL NATURE OF THE INDUSTRY, INSURERS' FINANCIAL RESULTS ARE ALSO MORE VARIABLE THAN MOST OTHER INDUSTRY GROUPS.

WHILE THESE RESULTS RAISE LEGITIMATE CONCERNS ABOUT THE INDUSTRY'S ABILITY TO ATTRACT AND RETAIN INVESTORS, THEY DO NOT SIGNAL A SOLVENCY CRISIS. IN 1989, A YEAR WHICH SAW RECORD CATASTROPHES, INCLUDING HURRICANE HUGO AND THE SAN FRANCISCO

EARTHQUAKE, THE INDUSTRY'S RETURN ON NET WORTH WAS 9.6%. PRELIMINARY ESTIMATES INDICATE THAT THE RETURN ON NET WORTH FOR 1990 WILL BE APPROXIMATELY THE SAME. EVEN THE WEAKEST ONE-FIFTH OF THE INDUSTRY HAS SHOWN POSITIVE NET INCOME IN THE MOST RECENT THREE YEARS FOR WHICH DATA ARE AVAILABLE. AND, THE INDUSTRY'S ASSET PORTFOLIO IS CONSERVATIVE AND REASONABLY LIQUID.

THESE AND OTHER MEASURES OF P/C INSURER FINANCIAL CONDITION ARE CAREFULLY MONITORED BY STATE INSURANCE REGULATORS, THE SECURITIES AND EXCHANGE COMMISSION (FOR PUBLICLY TRADED COMPANIES), INDEPENDENT FINANCIAL ANALYSTS, AGENTS AND BROKERS, AND OTHERS WHO ARE CONCERNED ABOUT INSURER SOLVENCY. WHILE THE EXPERTS GENERALLY AGREE THAT THE INDUSTRY IS FINANCIALLY SOUND, MANY BELIEVE THAT IT IS IMPORTANT TO STRENGTHEN THE EXISTING INSURANCE REGULATORY SYSTEM IN ORDER TO AVOID POSSIBLE SOLVENCY PROBLEMS IN THE FUTURE. THIS IS A VIEW WHICH AIA STRONGLY SUPPORTS.

B. HISTORICAL DEVELOPMENTS

MOST ECONOMISTS BELIEVE THAT IT IS UNREALISTIC TO CONTEMPLATE ANY INDUSTRY WITHOUT SOME INSOLVENCIES. INDEED, INSOLVENCIES OFTEN INDICATE THAT A HIGH DEGREE OF COMPETITION EXISTS IN AN INDUSTRY--A CONDITION WHICH ACCURATELY DESCRIBES THE P/C INSURANCE INDUSTRY. THE INDUSTRY IS COMPRISED OF SOME 3800 COMPANIES, AND THE LARGEST INSURER HAS LESS THAN 10% OF THE MARKET.

IN 1990, 14 P/C INSURANCE INDUSTRY COMPANIES WERE DECLARED INSOLVENT. THIS TOTAL IS DOWN FROM THE PREVIOUS YEAR (AND MOST

OF THE YEARS BETWEEN 1984-1989), BUT REPRESENTS AN INCREASE OVER THE INCIDENCE OF INSOLVENCY DURING THE EARLY 1980'S. DESPITE SOME CYCLICAL VARIATIONS, THE NUMBER OF INSOLVENT COMPANIES AS A PERCENTAGE OF ALL INSURANCE COMPANIES--AND THEIR ASSETS AS A PERCENTAGE OF THE INDUSTRY'S ASSET STRENGTH--HAVE REMAINED VERY SMALL. IN 1989, A YEAR WHICH SAW A PEAK IN THE NUMBER OF INSOLVENCIES, ONLY ABOUT ONE IN EVERY 150 P/C INSURERS FAILED, AND THESE COMPANIES ACCOUNTED FOR ONLY ABOUT ONE-FIFTH OF ONE PERCENT OF TOTAL INDUSTRY ASSETS.

IN AN EFFORT TO UNDERSTAND WHY INSURANCE COMPANIES FAIL, A.M. BEST COMPANY, THE LARGEST OF THE INDEPENDENT FINANCIAL RATING FIRMS, RECENTLY CONDUCTED A STUDY OF 365 INSURER INSOLVENCIES WHICH OCCURRED OVER THE PAST 20 YEARS. THE STUDY HAS NOT YET BEEN PUBLISHED BUT A.M. BEST PRESIDENT ARTHUR SNYDER RECENTLY SHARED SOME PRELIMINARY RESULTS WITH MEMBERS OF OUR ASSOCIATION. THESE RESULTS INDICATE THAT 41% OF THE INSOLVENT COMPANIES WERE YOUNG (LESS THAN 10 YEARS OLD); 62% WERE SMALL (LESS THAN $5 MILLION IN SURPLUS); AND 81% DEMONSTRATED UNUSUAL PREMIUM GROWTH. IN ADDITION, A.M. BEST FOUND THAT HALF OF THE INSOLVENCIES WERE CAUSED BY A COMBINATION OF RAPID GROWTH, UNDERPRICING, AND DEFICIENT RESERVES; 20% WERE CAUSED BY ERRONEOUS FINANCIAL REPORTING OR FRAUDULENT BUSINESS PRACTICES; 15% WERE CAUSED BY INADEQUATE OR UNCOLLECTIBLE REINSURANCE; AND 15% WERE RELATED TO SIGNIFICANT CHANGES IN THE OWNERSHIP OR OUTLOOK OF THE COMPANY. THIS ANALYSIS HIGHLIGHTS SOME OF THE ISSUES WHICH SHOULD BE ADDRESSED IN ORDER TO IMPROVE REGULATION

FOR SOLVENCY.

C. NO PARALLELS TO S & L CRISIS

FINANCIAL EXPERTS GENERALLY REJECT THE NOTION THAT THE SOLVENCY RISKS FACING THE P/C INSURANCE INDUSTRY ARE COMPARABLE IN NATURE OR SEVERITY TO THOSE FACED BY THE SAVINGS AND LOAN INDUSTRY PRIOR TO THE ONSET OF THE S & L CRISIS. INDEED, THE COMPARISON ONLY SERVES TO CONFUSE AND ALARM CONSUMERS UNNECESSARILY AND COULD LEAD TO REGULATORY PROPOSALS WHICH ARE POORLY SUITED TO THE SOLVENCY NEEDS OF P/C INSURERS.

IN A RECENT REPORT ENTITLED RATING THE RISKS, FINANCIAL INDUSTRY CONSULTANT ORIN KRAMER ASSESSED THE SOLVENCY THREAT OF KEY SECTORS OF THE FINANCIAL SERVICES SECTOR--SAVINGS AND LOANS, COMMERCIAL BANKS, P/C INSURERS, AND LIFE INSURANCE COMPANIES. THE STUDY EXAMINES PAST AND PRESENT FINANCIAL PERFORMANCE OF EACH SECTOR USING A VARIETY OF MEASURES, SUCH AS FINANCIAL LEVERAGE, PROFITABILITY, CHANGES IN NET WORTH, AND RISKINESS OF ASSETS. IT CONCLUDES THAT THERE IS NO EVIDENCE THAT THE INSURANCE INDUSTRY IS FACING A SYSTEMIC SOLVENCY CRISIS OR THAT CIRCUMSTANCES WHICH WOULD PRODUCE SUCH A CRISIS ARE LIKELY TO OCCUR. ACCORDING TO KRAMER, "WHATEVER ITS UTILITY AS A CONVENIENT CAPTION, THE THRIFT/INSURER COMPARISON IS ANALYTICALLY BANKRUPT."

IN ADDITION TO THESE FINANCIAL INDICATORS, I WOULD LIKE TO STRESS ANOTHER KEY DIFFEPENCE--NAMELY, THE REGULATORY RESPONSE TO THE INCIPIENT PROBLEMS FACING THE TWO INDUSTRIES WHEREAS REGULATION OF THE SAVINGS AND LOAN INDUSTRY WAS LIBERALIZED TO PERMIT OPERATIONS TO BECOME MORE RISKY, REGULATORS OF THE

INSURANCE INDUSTRY HAVE ENACTED STRICTER SOLVENCY STANDARDS OVER THE PAST DECADE. HAVING SAID THAT, IT IS IMPORTANT TO NOTE THAT INSURANCE REGULATION FOR SOLVENCY CAN BE IMPROVED, SHOULD BE IMPROVED AND IS BEING IMPROVED.

III. PROBLEMS CONFRONTING REGULATORY SYSTEM

AS PART OF OUR EFFORT TO IDENTIFY WAYS TO IMPROVE REGULATION FOR INSURER SOLVENCY, AIA HAS IDENTIFIED A NUMBER OF PROBLEMS WHICH CURRENTLY CONFRONT THE REGULATORY SYSTEM. THE MOST SERIOUS OF THESE IS THE LACK OF "WILL" ON THE PART OF STATE REGULATORS TO TAKE ACTION AGAINST TROUBLED COMPANIES, WHETHER DUE TO POLITICAL PRESSURE OR CONCERN THAT THEY WILL BE BLAMED FOR AN INSOLVENCY WHICH OCCURS WHILE THEY ARE IN OFFICE. REGULATORS MAY DELAY AN INEVITABLE INSOLVENCY BY ATTEMPTING A FRUITLESS RESCUE, OR SIMPLY FAILING TO TAKE NECESSARY ACTIONS. DUE TO THE REGULATOR'S ACTIONS (OR INACTIONS), THE INSOLVENCY, WHEN IT OCCURS, IS LIKELY TO BE WORSE THAN IT WOULD HAVE BEEN IF ACTED UPON EARLIER.

IN ADDITION, THE FOLLOWING CONCERNS EXIST:

1. DELAYS IN THE PROCESS OF IDENTIFYING TROUBLED COMPANIES AND TAKING THE NECESSARY REGULATORY ACTION;

2. INADEQUATE RESOURCES DEDICATED TO SOLVENCY REGULATION;

3. FAILURE TO FOCUS REGULATORY RESOURCES ON COMPANIES MOST NEEDING ATTENTION;

4. INCONSISTENT STATE FINANCIAL STANDARDS, VALUATION RULES, AND REPORTING REQUIREMENTS;

5. INCONSISTENCY BETWEEN CONCERN ABOUT SOLVENCY AND RATE

REGULATORY REGIMES THAT FAIL TO APPROVE NEEDED RATE INCREASES;

6. INCREASING BURDEN OF GUARANTY FUND ASSESSMENTS, PARTICULARLY IN THE COMMERCIAL LINES; AND

7. INCONSISTENCY AMONG GUARANTY FUND COVERAGE RULES.

IV. ELEMENTS OF AN EFFECTIVE SOLUTION

HAVING IDENTIFIED THESE PROBLEMS, AIA IS WORKING TO DEVELOP AND ANALYZE RESPONSIVE SOLUTIONS. IN DOING SO, WE NEED TO ASSURE THAT PROPOSED SOLUTIONS DO NOT INADVERTENTLY CREATE NEW PROBLEMS THAT WILL JEOPARDIZE FUTURE SOLVENCY NEEDS. THE SAVINGS AND LOAN EXPERIENCE HAS HIGHLIGHTED THE NEED TO PROCEED CAUTIOUSLY IN THIS REGARD. AIA ALSO WISHES TO AVOID THE CREATION OF A REGULATORY SYSTEM THAT IS LESS EFFECTIVE OR LESS EFFICIENT THAN WHAT IS CURRENTLY IN PLACE.

IN ADDITION TO IDENTIFYING SPECIFIC PROBLEMS THAT SHOULD BE SOLVED, DURING THE COURSE OF OUR DELIBERATIONS, WE HAVE IDENTIFIED FOUR DESIRABLE FEATURES THAT SHOULD BE INCLUDED IN ANY ENHANCED SYSTEM OF INSURANCE REGULATION. THESE INCLUDE THE FOLLOWING:

1 REMOVING IMPEDIMENTS TO THE FREE FLOW OF CAPITAL - RECENT PUNITIVE INSURANCE LEGISLATION HAS COMBINED UNWARRANTED RATE ROLLBACKS AND OTHER PUNITIVE MEASURES WITH "LOCK-IN" PROVISIONS. THIS COMBINATION NOT ONLY PREVENTS AN INSURER FROM EARNING A REASONABLE RATE OF RETURN, BUT ALSO PREVENTS THE COMPANY FROM VOLUNTARILY LEAVING AN UNPROFITABLE MARKET. SUCH RESTRICTIONS COULD HAVE LASTING, ADVERSE EFFECTS ON INSURER

SOLVENCY. WE BELIEVE THAT ASSURING THE FREE FLOW OF CAPITAL IS ESSENTIAL TO MAINTAINING A HEALTHY INSURANCE INDUSTRY AND SHOULD BE INCLUDED IN ANY PROPOSAL TO STRENGTHEN SOLVENCY REGULATION.

2 REMOVING COMMERCIAL AND EXCESS COVERAGES FROM GUARANTY ASSOCIATIONS - THE GUARANTY FUND SYSTEM IS INTENDED TO PROVIDE A SAFETY VALVE FOR PROTECTION OF POLICYHOLDERS AND CLAIMANTS IN THE EVENT OF AN INSOLVENCY. IT IS NOT INTENDED TO SERVE AS A SUBSTITUTE FOR THE PREVENTION OF INSOLVENCIES. THERE IS GROWING CONCERN, HOWEVER, THAT THE GUARANTY FUNDS MAY IN FACT BE SERVING AS A DISINCENTIVE FOR CLOSE SCRUTINY OF INSURANCE COMPANY SOLVENCY, PARTICULARLY BY SOPHISTICATED COMMERCIAL CUSTOMERS WHO HAVE THE ABILITY TO EVALUATE THE FINANCIAL STRENGTH OF THEIR INSURERS.

WE BELIEVE THAT REMOVING LARGE COMMERCIAL COVERAGES AND EXCESS LEVELS OF COVERAGES FROM GUARANTY ASSOCIATIONS WOULD REINFORCE THE PREEMINENCE OF SOLVENCY REGULATION. SUCH REFORMS WOULD INTRODUCE MORE EVALUATION OF FINANCIAL CONDITION OF INSURERS INTO THE MARKET PLACE. SOPHISTICATED PURCHASERS OF COMMERCIAL AND EXCESS LEVELS OF INSURANCE WOULD BECOME MORE CONCERNED ABOUT THE SOLVENCY OF THEIR INSURERS AND WOULD NOT NECESSARILY PURCHASE COVERAGE FROM THE INSURER WHICH OFFERED THE LOWEST PRICE. THIS WOULD MITIGATE THE EFFECTS OF UNSCRUPULOUS RATE CUTTING AND, IN EFFECT, DISCOURAGE PURCHASERS FROM EXACERBATING THE CONDITION OF FINANCIALLY TROUBLED INSURERS, BY KNOWINGLY BUYING UNDERPRICED COVERAGE.

IN ADDITION, THESE REFORMS WOULD HELP PREVENT STRAIN ON THE

GUARANTY FUNDS, WHICH WERE ORIGINALLY DESIGNED TO RESPOND TO THE INSOLVENCIES OF AUTO INSURERS (WHERE INDIVIDUAL POLICYHOLDERS, NOT SOPHISTICATED CORPORATE CUSTOMERS, ARE INVOLVED). THIS, IN TURN, WOULD HELP PROTECT THE HEALTH OF WELL-MANAGED COMPANIES, WHICH FUND THE GUARANTY ASSOCIATIONS.

ANOTHER ESSENTIAL ELEMENT OF ANY GUARANTY ASSOCIATION MECHANISM IS AN EFFECTIVE RECOUPMENT PROVISION TO AVOID DIMINUTION OF INSURERS' SURPLUS AND THE RESULTING REDUCTION OF CAPACITY.

3 FOCUSING RESOURCES AND ATTENTION ON REGULATION FOR SOLVENCY - AIA STRONGLY BELIEVES THAT SOLVENCY MUST BE THE FIRST PRIORITY OF REGULATION. IN RECENT YEARS, THERE HAS BEEN A TENDENCY FOR SOME REGULATORS, UNDER INTENSE POLITICAL PRESSURE FROM THOSE WHO ADVOCATE RATE REDUCTIONS IRRESPECTIVE OF THE UNDERLYING ECONOMICS--TO STRAY FROM THAT PRIORITY. IN ADDITION, OTHER REGULATORS WHO APPRECIATE THE PREEMINENCE OF SOLVENCY REGULATION MAY LACK ADEQUATE RESOURCES TO DO THEIR JOBS EFFECTIVELY. SUCH CONSTRAINTS RAISE THE POSSIBILITY OF INSUFFICIENT QUALIFIED PERSONNEL, AS WELL AS THE LACK OF APPROPRIATE TECHNOLOGY.

WE BELIEVE THAT IT IS CRITICAL TO FOCUS APPROPRIATE RESOURCES ON PREVENTING AND DETECTING INSOLVENCIES. IN ADDITION, THE AVAILABILITY OF ADDITIONAL RESOURCES MIGHT SPEED UP THE REGULATORY REACTION ONCE A TROUBLED INSURER IS IDENTIFIED. FURTHER, THE RESOURCES CURRENTLY EXPENDED ON THE EXAMINATION PROCESS COULD BE MORE CONSTRUCTIVELY UTILIZED IF THE EMPHASIS OF

STATE EXAMINERS WERE CONCENTRATED ON TROUBLED INSURERS RATHER THAN ON THOSE MOST CAPABLE OF PAYING THE COSTS OF THE EXAMINATIONS.

4 AVOIDING DUPLICATE AND CONFLICTING REGULATION - THERE ARE NUMEROUS EXAMPLES OF DUPLICATE AND CONFLICTING STATE REGULATION FOR SOLVENCY. FOR EXAMPLE, ALTHOUGH APPROXIMATELY SEVENTEEN STATES HAVE ADOPTED SOME FORM OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANT REQUIREMENT, NO TWO STATES HAVE ADOPTED EXACTLY THE SAME REQUIREMENTS. ANOTHER EXAMPLE RELATES TO CREDIT FOR REINSURANCE. ALTHOUGH MANY STATES HAVE LISTS OF AUTHORIZED REINSURERS, SEVERAL STATES REQUIRE THAT ALL LICENSED INSURERS AMEND THEIR ANNUAL STATEMENTS TO REFLECT CREDIT FOR REINSURANCE PLACED WITH REINSURERS AUTHORIZED IN THOSE PARTICULAR STATES. THUS, INSURERS MUST FILE DIFFERENT ANNUAL STATEMENTS IN EACH OF THESE STATES. CONFLICTING REGULATIONS SUCH AS THESE SERVE NO USEFUL PURPOSE IN THE OVERALL REGULATION FOR SOLVENCY AND RESULT IN EXPENSIVE AND UNNECESSARY EFFORTS ON THE PARTS OF INSURANCE COMPANIES.

V. IMPROVING THE SYSTEM

AIA IS COMMITTED TO FURTHER STRENGTHENING THE STATE INSURANCE REGULATORY SYSTEM. IMPROVEMENT TO STATE REGULATION FOR SOLVENCY IS AN AIA PRIORITY FOR THE 1991 LEGISLATIVE SESSIONS. WE ARE CONVINCED THAT, ON THE WHOLE, THE STATE SYSTEM WORKS WELL AND THAT IT CAN BE IMPROVED.

THE NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS IS

PROMOTING IMPROVEMENTS TO THE EFFECTIVENESS OF STATE REGULATION FOR SOLVENCY, AS OUTLINED IN A REPORT ENTITLED "STATE ACTIONS TO IMPROVE INSURANCE REGULATION." IN OUR VIEW, THE MOST IMPORTANT OF THE NAIC'S APPROACHES IS THE DEVELOPMENT OF FINANCIAL REGULATION STANDARDS, DISCUSSED BELOW. OTHER EFFORTS INCLUDE IMPROVED REINSURANCE EVALUATION, MORE EFFECTIVE EXAMINATIONS, AN ENHANCED SOLVENCY SURVEILLANCE SYSTEM, AND THE DEVELOPMENT OF RISK-BASED CAPITAL REQUIREMENTS. AIA FULLY SUPPORTS THE NAIC'S ON-GOING EFFORTS.

IN JUNE, 1989, THE NAIC ADOPTED A POLICY STATEMENT ON FINANCIAL REGULATION STANDARDS. THE STANDARDS ARE BEING USED TO DETERMINE WHETHER INDIVIDUAL STATES WILL BE "ACCREDITED" BY THE NAIC. FLORIDA AND NEW YORK ARE THE FIRST TWO STATES TO BECOME ACCREDITED.

THE STANDARDS ARE DIVIDED INTO THREE MAJOR AREAS: 1) LAWS AND REGULATIONS; 2) REGULATORY PRACTICES AND PROCEDURES; AND 3) ORGANIZATIONAL AND PERSONNEL PRACTICES. THE LAWS AND REGULATIONS, WHICH ARE THE FOCUS OF THIS HEARING, ORIGINALLY INCLUDED SIXTEEN ENUMERATED CATEGORIES, AMONG WHICH ARE: EXAMINATION AUTHORITY, CAPITAL AND SURPLUS REQUIREMENTS, ACCOUNTING PRACTICES, REINSURANCE, CPA AUDITS, LIQUIDATION PROCEEDINGS AND GUARANTY FUNDS. THE SIXTEEN CATEGORIES WERE EXPANDED TO NINETEEN IN DECEMBER, 1990, WITH THE ADDITION OF REINSURANCE INTERMEDIARIES, MANAGING GENERAL AGENTS AND EXAMINATIONS.

AIA IS WORKING HARD IN THE STATES TO GET THESE NAIC MODEL

LAWS ENACTED. AS OF APRIL 5, 1991, WE HAVE SEEN FAVORABLE ACTIVITY IN MORE THAN 40 STATES. WHEN ADDED TO THE TWO STATES THAT HAVE ALREADY BEEN ACCREDITED BY THE NAIC, WE THINK THERE HAS BEEN RESPONSIBLE REACTION TO A RELATIVELY NEW PROGRAM.

AIA ALSO HAS SUGGESTIONS (IN ADDITION TO THE NAIC FINANCIAL REGULATION STANDARDS) FOR IMPROVING THE STATE REGULATORY SYSTEM. THEY INCLUDE RECOMMENDATIONS TO IMPROVE REGULATION FOR SOLVENCY, MAKE THE LIQUIDATION PROCESS MORE EFFICIENT, AND EXPAND THE CAPACITY OF THE GUARANTY ASSOCIATIONS TO ASSIST THOSE CLAIMANTS WHO NEED SUCH PROTECTION. DEVELOPING AND REVISING THESE SUGGESTIONS IS AN ONGOING PROCESS BECAUSE THE NEEDS OF THE SYSTEM ARE CONSTANTLY CHANGING.

VI. CONCLUSION

AIA IS COMMITTED TO IMPROVING STATE SOLVENCY REGULATION. SUCH REGULATION HAS A LONG HISTORY OF ADAPTING TO CHANGES IN THE TYPES OF FINANCIAL PROBLEMS CONFRONTING INSURERS.

AT THE SAME TIME, WE REMAIN CONCERNED THAT SOLUTIONS TO ALL OF THE SHORTCOMINGS OF THE CURRENT INSURANCE REGULATORY SYSTEM MAY NOT BE AVAILABLE ON A STATE-BY-STATE BASIS, OR FROM THE NAIC. THE LIMITATIONS OF FIFTY SEPARATE ENTITIES ATTEMPTING TO REGULATE A BUSINESS THAT OFTEN OPERATES IN A NATIONAL OR INTERNATIONAL ARENA MAY NECESSITATE SOME FEDERAL INVOLVEMENT TO BOLSTER THE "WILL" NEEDED TO TAKE ACTION AGAINST TROUBLED COMPANIES, AND TO BRING UNIFORMITY AND ORDER INTO THE PROCESS. AS PART OF AIA'S DELIBERATIONS, WE ARE EXPLORING VARIOUS FEDERAL ALTERNATIVES THAT

MIGHT BE FEASIBLE TO ENHANCE STATE REGULATION FOR SOLVENCY.

THANK YOU FOR THIS OPPORTUNITY TO SHARE AIA'S VIEWS ON THIS SIGNIFICANT SUBJECT. I WOULD BE GLAD TO ANSWER YOUR QUESTIONS.

Senator METZENBAUM. Thank you very much, Mr. Schwartz. We appreciate your testimony. I will have some questions, but I think we will hear from Mr. Mica first. It is obvious to me that the American Insurance Association works its people very hard. It looks as if David Pratt has lost some weight since he has gone to work with you. [Laughter.]

Mr. Mica, I won't comment on whether you have picked up a few pounds since you left the Congress or not. I will stay away from that subject. Please proceed.

STATEMENT OF DANIEL A. MICA

Mr MICA. Thank you. That is kind of you, Mr. Chairman, and I am pleased to be here. I am Dan Mica, the executive vice president of the American Council of Life Insurance. We represent, in answer to your question, 616 life insurance companies and approximately 90 percent of the life policies in force.

Senator METZENBAUM. Would you like to introduce your colleagues who are seated at the table with you?

Mr. MICA. I will do that. I did want to say, Mr. Chairman, that I will change the title of my remarks to "We Can Always Try Harder and Do Better" after listening to what some of your questions are. That is the point of what we intend to discuss here.

I have with me three associates. Richard Minck is executive vice president of the council; Jack Blaine, the former general counsel and now special consultant at ACLI; and Dick Barnsback, who is our chief counsel for State relations. Together, these gentlemen, incidentally, have over 80 years of experience in working with insurance commissioners and legislators and regulators of the life insurance industry.

First, Senator, of course, we would like to commend you and the subcommittee for your interest in the financial stability of what we consider one of the most important industries in this nation. Our industry is very large, very diverse, with over 2,000 companies. We provide essential products protecting the assets of millions of Americans and play an important role in providing long-term capital needs for our Nation's growth.

We are exceedingly proud of our leadership in our industry and the industry's performance and record of service. However—and I think is why we are here—because of the difficulties of a very few companies, the financial stability of the insurance industry as a whole has been questioned, and there have been suggestions that the financial condition of the industry is so fragile that insurers may be on the verge of repeating the experience of the thrift industry.

Industrywide—and I repeat, industrywide—nothing could be further from the truth. The life insurance industry is not facing a crisis. Of course, we acknowledge there are concerns and problems, but far from going the way of the savings and loan industry, the life insurance industry remains what it always has been—safe, secure, and, above all, dedicated to honoring the commitments made to millions of policyholders. That is indeed the business.

This is not an isolated opinion by industry trade associations. It is the view of many well-respected, well-known authorities who have taken the time to study in detail the industry and its financial situation. Let me quote just a few briefly, and I will roll a few of these together to save time.

A.M. Best says, "We would not support the dire conclusions indicating that the industry's financial condition is analogous to that of the thrift industry." Standard & Poor's says something similar: "Standard & Poor's does not believe that the insurance industry is headed for a savings and loan-type crisis," and they go on to say some nice things about the industry.

Kramer & Associates, a well-known industry analyst, the Department of Commerce, Freddie Mac, Ernst & Young—and even the GAO, the General Accounting Office of the United States, says the insurance industry has not experienced the magnitude of difficulties that the savings and loan industry has, and industry analysts do not believe large numbers of companies are in imminent danger of failing.

Those are just a few, and we think they are representative of people who spent the time and took the energy to look below the surface of some of the headlines. They are governmental agencies, financial analysts, and industry professionals. Why do so many who are truly knowledgeable about the details of the industry feel this way?

I think first we would be sure to comment that the industry itself, life insurers—and I have learned this—are conservative investors. The high-flyer is the exception, not the rule. They invest in high-grade bonds. Their mortgages are usually on fully occupied properties.

Life insurers are permanent lenders. They are nominally impacted by the kinds of swings we are seeing right now in the market. A very important point: Their investment portfolios—mortgages, bonds, stocks—are very broadly diversified to spread the risk, and that has been very important with this trouble particularly in the Northeast region.

Mortgages, for example, comprise about 20 percent of the total assets. They are diversified geographically across property types so as to cushion against regional real estate market problems, and indeed it has been successful. In a recession—and we have had some problems—mortgage delinquencies are likely to rise, but the delinquent mortgages held by life insurers currently represent about one-half of 1 percent of all assets.

Bond portfolios, which make up 55 percent of the industry's assets, are diversified among Treasuries, government obligations, and corporate bonds. Corporate bonds are further diversified among various industries, companies, and maturities.

I see the time is running out. I will try to highlight a few points here, Mr. Chairman.

Some companies, of course, have invested in items that are of higher risk than would be prudent. As a result, they may be impaired. However, it is relatively few companies that are in this situation, and new rules—rules that were recommended by the NAIC, by State legislators, by the ACLI and others—are now being put into effect to remedy some of these problems brought to the industry's attention.

Senator METZENBAUM. Will you please wind up?

Mr. MICA. Yes, I will, Mr. Chairman. Simply stated, the industry does have a network of laws that truly does cover a broad basis for protection for its policyholders. We all agree that policyholders need to be protected. We know we need to do a better job in some areas. We are committed to do that, and to that end, your committee was provided with a copy of this report that our board of directors spent over a year doing on solvency concerns, recommending at least 16 specific actions that we believe, if implemented, would go a long way to addressing some of the problems you addressed today.

Thank you, Mr. Chairman.

[The prepared statement of Mr. Mica follows:]

STATEMENT

OF

DANIEL A. MICA
EXECUTIVE VICE PRESIDENT
AMERICAN COUNCIL OF LIFE INSURANCE

TO THE
SUBCOMMITTEE ON ANTITRUST, MONOPOLIES
AND BUSINESS RIGHTS
COMMITTEE ON THE JUDICIARY

UNITED STATES SENATE

APRIL 9, 1991

Good Morning. I'm Dan Mica, Executive Vice President of the American Council of Life Insurance. I'm pleased to accept your invitation to testify this morning. I've brought three associates. They are: Richard Minck, Executive Vice President for the Council; Jack Blaine, our former general counsel and now special consultant; and Dick Barnsback, who is the Council's Chief Counsel for State Relations. Together these gentlemen have over 80 years of experience working with state insurance commissioners and legislators on the regulation of life insurance.

Senator, this Subcommittee is to be commended for its interest in the financial stability of one of America's most important industries. Our industry is large and quite diverse with over 2000 companies. We provide essential products protecting the assets of millions of Americans. We are exceedingly proud of the leadership of our industry and the industry's performance and record of service.

Because of the difficulties of a very few companies, the financial stability of the insurance industry has been questioned and there have been suggestions that the financial condition of the industry is so fragile that insurers may be on the verge of repeating the experience of the thrift industry.

Industry wide, nothing could be further from the truth. There is nothing to support these scare headlines. The life insurance industry is not facing a crisis. Far from going the way of the savings and loan industry, the life insurance industry remains what it always has been: safe, secure and above all, committed to honoring the commitments made to its millions of policyholders.

This is not an isolated opinion by a trade association paid to extol the industry's virtues and stability. It is the view of many respected authorities who've taken the time to study our industry. Allow me to quote just a few:

"...We would not support the dire conclusions...indicating that the industry's financial condition is analogous to that of the thrift industry..." -- A. M. Best

"S&P does not believe that the insurance industry is headed for a savings and loan type crisis, or that it will inevitably face the difficulties of the magnitude that the banking industry is now facing." -- Standard & Poor's

"...there is no evidence today that the insurance industry faces a systemic solvency crisis, and there is no reasonable probability that the circumstances that might produce such a crisis will, in fact occur." -- Orin Kramer, Kramer Associates

"The insurance industry has not experienced the magnitude of difficulties that the savings and loan industry has, and industry analysts do not believe large numbers of companies are in imminent danger of failing." -- U.S. General Accounting Office

"Overall, life insurers were financially sound and healthy in 1990...the incidence and threat of insolvency in the life insurance industry remains low compared...with the savings and loan industry" -- U.S. Department of Commerce

"Insurance companies are not the next crisis" -- Freddie Mac

I hear the S&L comparison a lot, and it's way overdone" -- Ernst & Young

These are representative of the assessments being made by financial analysts and industry professionals.

Why are so many knowledgeable people share this feeling about life insurance? Perhaps a few observations might explain this.

First, life insurers are conservative investors. The high fliers are the exception not the rule.

We invest principally in high grade bonds.

Our real estate investments are mainly in mortgages on fully occupied commercial properties.

Life insurers are permanent lenders. They are nominally impacted by swings in the market value of their investments.

Second, a very important point is that our entire investment portfolio -- mortgages, bonds, stocks -- is very broadly diversified to spread the investment risks.

Mortgages, for example, which comprise on average about 20 percent of total assets, are diversified geographically and across property types so as to cushion against depressed regional real estate markets.

In a recession, mortgage delinquencies are likely to rise. But, delinquent mortgages held by life insurers currently represent only about one-half of one percent of all assets.

Bond portfolios, which make up about 55 percent of industry assets, are diversified among Treasuries, government obligations and corporate bonds. Corporate bonds are further diversified among industries, companies and maturities. Almost all bonds held are in good standing. Bonds in default represent only one-fifth of one percent of assets.

Medium and lower grade bonds represent less than 6 percent of industry assets. Most of these were in private placements loans. Medium and lower grade public bonds (the LBO loans of the 80s) account for only 2 percent of assets. A significant share of these holdings were held by a handful of companies.

What's important to recognize is that with such a small percentage of industry assets devoted to these medium and lower grade bonds, even a major decline in market values would have only a negligible effect in aggregate on our business and customers.

Some companies may have invested more in these risks than was wise and could become impaired as a result. However, relatively few companies are in this situation, and new rules are being implemented to assure that other companies will not follow suit.

Third, life insurers face very predictable liabilities and realize generally stable flow of income. This allows them to match assets to liabilities and use c rrent income to meet liquidity needs rather than being forced to sell assets in a depressed market.

We do recognize that industry trends and aggregations can and do obscure the performance of individual companies. And, within any highly competitive environment, such as the insurance marketplace, some companies will excel while other companies could encounter problems. When problems occur, the public confidence in all insurance companies is at risk. Hence, it is in the interest of the life insurance industry that laws, regulations and regulators minimize the chance for life company insolvencies. If companies do become insolvent, policyholders must be protected.

Our industry's leaders are committed to strong solvency regulation by the states; our companies respond to individual insolvencies through work-out arrangements whereby they assume the obligations of the company together with appropriate assets. Beyond that, guaranty associations are in place in all but a few states to protect policyholders. Finally, healthy insurers are assessed the amount required to keep policyholders whole. The obligation to pay for other companies mistakes is a powerful motivation to support strong state regulation solvency.

Insurance is a highly regulated business, operating under laws that are the product of more than a century of experience. The aim of these laws is very simple -- to protect consumers from unfair practices and to guard the financial stability of insurance companies so that claims will be paid when the need arises.

The regulatory process is one that needs ongoing review and refinement. We constantly are working to improve the quality and capacity of state regulators to ensure that life insurers remain solvent. This past fall, we published the results of a year long study of solvency concerns by a task force that had been appointed by our Board. This report, copies of which have been furnished to the Subcommittee, offered recommendations that, if implemented, would strengthen the regulatory systems to detect and prevent possible insolvencies already in place.

The ACLI's Board of Directors has committed the Council to an aggressive campaign to seek the enactment of these recommendations, and we have launched legislative plans in all 50 states and the District of Columbia. We are exceedingly pleased by our member companies support and, more so, with the extent of legislative activity so early in our campaign.

In summary, the life insurance business is financially strong and stable. This fact reflect both management competence and the effectiveness of state laws and regulations. The public's confidence is essential to us. Keeping that trust is our most important job, one we work hard at every day. Without it, we couldn't remain in business.

This completes my oral presentation. I would be happy to respond to your questions.

STATEMENT

OF

AMERICAN COUNCIL OF LIFE INSURANCE

TO THE
SUBCOMMITTEE ON ANTITRUST, MONOPOLIES
AND BUSINESS RIGHTS
COMMITTEE ON THE JUDICIARY

UNITED STATES SENATE

APRIL 9, 1991

STATEMENT OF THE AMERICAN COUNCIL OF LIFE INSURANCE
TO THE
SENATE ANTITRUST, MONOPOLIES & BUSINESS SUBCOMMITTEE
ON
DEVELOPMENT AND IMPLEMENTATION OF STATE INSURANCE MODEL LAWS

April 9, 1991

This statement is presented in response to the invitation of the Subcommittee to provide comments on model laws prepared and adopted by the National Association of Insurance Commissioners (NAIC). The American Council of Life Insurance (ACLI) is the major national trade association of life insurance companies. It has a membership of 616 life insurance companies which, in the aggregate, have approximately 94 percent of the life insurance in force in the United States.

We appreciate the opportunity to comment on the success of the states in regulating the life insurance business for solvency. One measure of this success is the relatively few insolvencies that have occurred in the life insurance business in the last decade and the relatively small amounts involved. During this period 134 life insurance companies became impaired or insolvent and state guaranty funds contributed $474 millions to provide benefits to policyholders. These amounts are of a very much lower order of magnitude than the losses from insolvencies of other financial institutions during the period.

The National Association of Insurance Commissioners (NAIC) and the models and laws and regulations developed by its committees provide invaluable assistance to the legislatures and insurance departments of all states in helping to strengthen state

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regulation. The NAIC committees meet publicly and with input from all interested parties, including insurance companies, consumerists, academicians, federal representatives and the press develop solutions to problems that are of concern to many states.

The ACLI has a long history of support for strong, effective state regulation of the life insurance industry. This support encompasses both principle facets of regulation: the assurance of fair and equitable treatment of applicants, insureds and beneficiaries; and the assurance that the obligations of life insurance companies will be met through effective solvency regulation.

The purpose of today's hearing is to examine how model laws are adopted by the National Association of Insurance Commissioners and the record of enactment of NAIC model laws in the various states. In responding to the Subcommittee's request for testimony on this subject this statement will focus on those model laws that relate to that aspect of regulation relating to solvency of insurers, since we believe that is the primary focus of general concern to the Subcommittee.

Model Laws in General

One category of model laws that should be mentioned in brief are those that address corporate practices, or market conduct, and when a few states have enacted them they effectively become implemented nationally. An illustration is the Model Insurance Information and Privacy Protection Act. Insurers doing business in one or two of the states enacting that law will implement the requirements for all of their business activities. Once insurers are required to establish the specified procedures and systems, they are more easily and economically implemented on a nationwide basis.

The Model Act requiring independent annual audits of financial statements, mentioned later, also illustrates the kind of law that, once required of a company by one state, is effective for all of that company's business in the country. It is frequently stated, and it is true, that not all model laws need be enacted in every state to effect a nationwide result for a substantial percentage of the business. Despite this, states should act on model legislation of importance to policyholders in that state even if many other states already have adopted such legislation.

Late last year the ACLI Board of Directors adopted a report of the ACLI Task Force on Solvency Concerns. Copies of that report have been furnished to members of the Subcommittee. The recommendations in that report reflect a continuation of ACLI's support for strong solvency regulation, including support for enactment of specific model laws and other actions by the NAIC and individual states. Most of the model laws discussed in this statement are set forth either in the ACLI Task Force report or in the NAIC Financial Regulation Standards, or both.

A. Model Laws An Essential Ingredient to State Regulation

During development of state insurance regulatory agencies that accompanied the nation's rapid industrial growth in the second half of the nineteenth century, the National Association of Insurance Commissioners was formed to share information and to work on solutions to common problems. One of its earliest actions was development of the uniform form of financial statement to be used in all states. However, the development of model laws probably dates from the beginning of this century with the Armstrong Investigation in New York in 1905. Both the NAIC and the National Association of Attorneys General responded to the findings in those hearings with proposals for model laws, some of which remain today in modified form in the statutes of various states.

1. Growth of Model Laws and Regulations. The development of model laws and model regulations is essential to the function of an industry as large and complex as the American insurance industry, regulated as it is by the various states. For similar reasons the National Conference of Commissioners on Uniform State Laws prepares uniform laws for enactment by the states, dealing with a wide variety of commercial activities (e.g., the Uniform Commercial Code). The NAIC serves that same function and acts as the body through which model laws and model regulations for insurance industry acts and practices are prepared. There are structural and substantive differences between the two organizations, but their respective procedures for

development of model and uniform laws are similar. A distinction between model acts and uniform laws may be made on the premise that the former, unlike uniform laws, are not necessarily meant to be adopted uniformly or in all states.

Despite the lengthy history of the NAIC, the vast majority of model laws and regulations have been adopted in the last two or three decades, and a major share of the solvency regulatory measures in the last few years. This is attributable in part to the McCarran Act, which became law in 1945, but more significantly it is a reflection of the tremendous growth and change in the insurance industry.

Immediately after the McCarran Act, the NAIC took on a more significant role. Not only had attention been focused on insurance as a national industry, that Act conditioned the anti-trust exemption to conduct by insurers that is regulated by the states. Setting a pattern that has been followed since, the NAIC prepared and adopted a Model Act to Regulate Unfair Trade Practices, a regulatory law needed by each state in order to comply with the McCarran Act's mandate. A problem had been identified and a solution was crafted to solve it. All states subsequently adopted that Model Act or statutory authority substantially similar.

In the decades since then, the NAIC has prepared and adopted over a hundred model laws, each of which has addressed an identified problem. Some of these model laws have achieved rapid acceptance by the respective state legislatures; others have not been widely adopted for a variety of reasons.

2. How Model Laws and Regulations are Prepared. The process of drafting and promulgating model laws and model regulations by the NAIC is basically similar to the legislative process followed by the Congress or the state legislatures, with the obvious distinction that after adoption by the NAIC they must be enacted by the state legislatures in order to take effect. In general that process is as follows:

* A problem is identified by one or more persons - insurance regulators, an industry group, a consumer group, or an unrelated industry - and brought before a committee of the NAIC.
* Hearings are typically held or public airing of the issue is conducted in one or more forums as part of the process of identifying the scope of the problem and optional remedies for solution.
* If the problem to be solved cannot be addressed through an accounting rule, a change in the annual statement blank or a model regulation (pursuant to an identified source of statutory authority) it may be concluded that a model law is needed, at which time it is assigned to an appropriate task force or committee.
* NAIC committee, composed of regulators, frequently appoints an advisory committee which typically

includes a number of representatives of insurance industry interests, but frequently with representation from consumer interests, academia, private law firms or interested non-industry parties.

* Initial drafts of model laws may be prepared by NAIC staff, an insurance department staff, the advisory committee or others. Regardless of the source of the original draft, subsequent drafts up to and including the final version adopted by the NAIC membership, are the subject of public hearings.

3. Role of Advisory Committees. Advisory committees serve an important role in this process as they bring together expertise and knowledge not otherwise available to the regulators. Those interests may or may not be in agreement on various issues that arise during the process. This could be true of competing insurer interests or between insurers and consumer or other representative groups. In its participation in this process, ACLI refers the proposals to committees made up of its member company representatives to attempt to arrive at a consensus position. That position is then presented to the advisory committee and to the NAIC.

While model laws are prepared and adopted by the NAIC to address identified problems, it should also be noted that the standards these models set serve other functions. Regardless of the McCarran Act, insurers are in the same position as most other industries in being constrained from agreeing on industry standards in the absence of legislative authority or regulatory requirements. Thus, when our industry recognizes problems that need correction, unlike industry groups in other countries, U.S. insurers need legislative or regulatory solutions to address them.

B. Financial Regulatory Apparatus

To review solvency regulation one must begin with those regulatory controls that are in place uniformly on a nationwide basis through the NAIC. These controls exist by virtue of actions taken by the NAIC, and their enforcement is pursuant to general statutory requirements obligating insurers to file annual statements on a NAIC form.

1. Annual Financial Statement. Each insurer doing business within a state must submit to the insurance commissioner an annual statement of its financial position in a form prescribed by the NAIC. These statements, which are also filed with the NAIC, contain a comprehensive disclosure of the company's financial activities during the preceding year. The basis for this annual statement is statutory accounting, which is very conservative. Statutory accounting rules, which control all information reported in the annual statement are set by the NAIC.

Nearly all the statements are submitted in computer usable form (diskette) so that the information can be quickly entered into the NAIC computerized data base. These data then become part of the Insurance Regulatory Information System (IRIS), which evaluates the company's operating results to determine if the company has experienced any substantial deviations from industry norms. If a company shows a number of abnormal results, an analysis is conducted by a special team of NAIC-appointed state insurance examiners to ascertain whether there is cause for regulatory concern. The data and the analytical conclusions are shared with state insurance departments for appropriate action.

While substantially all insurers file copies of their annual statements with the NAIC, a Model Act has been adopted to require participation by all insurers to pick up those companies not now filing, even though they represent less than 1/2 of one percent life insurance in force.

Insurers in 21 states are also required to submit annual audited financial reports to the state insurance department. The reports, prepared by independent certified public accountants, must address the financial condition of the company for the preceding calendar year as well as the results of operations, cash flow, and changes in capital and surplus. The reports must also include a summary of the ownership and the relationships of the insurer and all affiliated companies. In addition, the independent auditor must furnish the insurance commissioner with a written report describing any significant deficiencies in the insurer's internal control structure. The insurer must then provide a description of remedial action taken or proposed to correct the matter. In December 1990, the NAIC adopted changes to the 1991 annual statement which included an instruction requiring all insurers to have annual audits by independent CPA's and to file their audited reports as supplements to the annual statements on or before June 1. The NAIC had previously adopted a Model Rule Requiring Annual Audited Financial Reports which is now superseded by the recent action.

2. Financial Examinations. A state insurance department may examine the affairs of any insurer doing business in the state as it deems necessary. Moreover, every domestic insurer is subject to comprehensive financial examinations whenever considered necessary, and many states require additional mandatory examinations on a periodic basis, typically every three to five years. The examination is conducted by a team of trained professionals, often representing more than one state insurance department. While the authority for examinations exists in state insurance laws, the coordination of examinations of insurers on a multi-state basis is done through the NAIC to avoid redundancy. It is done in accordance with clearly established guidelines which have been developed by the NAIC and designed to explore every facet of the company's financial affairs. Upon completion of the examination, a full public report on the condition of the company is filed with the domestic insurance department and provided to the company. In its ongoing efforts to strengthen the examination system, the NAIC in December 1990 adopted a Model Law on Examinations. This Model Law is part of the NAIC Financial Regulatory Standards and focuses on the scope and frequency of examinations of insurers.

3. Reserves for Contract Obligations. All states have enacted laws, based on an NAIC model, that specify conservative standards for determining the minimum values that a company may place on its obligations under its in-force policies. The values of these obligations, referred to as reserves, must be recognized in the company's financial statement as liabilities. The model law was strengthened in December 1990 to require an annual opinion from a qualified actuary that the reserves, when considered with the assets held to support those reserves, are adequate to meet the company's obligations under its policies.

Because the Standard Valuation Law specifies the interest rates and mortality tables to be used, in the almost 50 years since it was first adopted by the NAIC, new mortality tables were developed, economic conditions changed and new products were developed -- all of which have necessitated periodic revisions of these laws. The NAIC in 1981 amended this model law to make several major substantive changes, including variable interest rates tied to a Moody's corporate bond rate. All states enacted those changes within three years of their adoption by NAIC. ACLI has cooperated and worked closely with the NAIC in the development of those changes, as well as the more recent amendments approved in 1990. This Model Act in particular typifies the evolutionary nature of model laws, and the ability of the states to enact changes in a relatively short time in areas where prompt action is necessary.

4. Categorization and Valuation of Assets. The NAIC Securities Valuation Office provides state regulators and insurance companies with a source for uniform prices and quality ratings for insurers' securities holdings. These price and quality ratings form what are known as "Association Values," to be used by insurers in preparing their annual statements to be filed with state regulators.

Under the NAIC's Mandatory Securities Valuation Reserve requirements, insurance companies are required to establish a financial statement liability to absorb fluctuations and losses on bonds and stocks held by the company. These requirements were strengthened last year, and the NAIC is currently conducting a further review of the nature and adequacy of the requirements.

5. Investment Laws. A major area of insurance regulation that has heretofore not been the subject of model legislation is that of insurance company investment authority. Since the investment authority of insurance companies is determined by the insurer's state of domicile, there has not, prior to a recent announcement by the NAIC, been an effort made to prepare a model investment law. A sizeable number of state investment codes do bear substantial similarity since many states followed the pattern set by New York and a few other states in their early insurance codes.

In the past twenty years a number of states have revised their life insurance company investment codes to reflect changing economic conditions as well as the new investment products available. Furthermore, some of the older investment laws, such as that of New York prior to its revision a few years ago, were very restrictive in terms of detailed qualitative, as well as quantitative, standards. As a consequence they constantly needed amendments as new investment vehicles were developed or economic changes occurred. In December, 1990, the NAIC exposed for comment a draft Model Regulation on Investments in Medium and Lower Quality Obligations. The proposed regulation provides an aggregate cap for medium and lower grade bonds, as well as graded caps based on the qualify of the investment. It is anticipated that this model regulation will be adopted by the NAIC in June 1991.

6. <u>Capital and Surplus</u>. Another matter of state insurance law not heretofore subjected to model legislation is in the required capital and surplus needed to obtain, or maintain, a license to do business. The amounts vary and typically reflect a state's policy in encouraging the formation of domestic insurance companies. Studies and papers on the subject of appropriate capital requirements agree in their conclusions only to the extent that there can't be too much, and that the right amount is dependent on a variety of factors. The NAIC is currently at work on developing standards for risk based capital requirements that will provide guidance in this area. This work is expected to be the subject of another model law.

7. <u>Holding Company Act</u>. The Insurance Holding Company Regulatory Model Act was first developed in the 1960's in

response to two business forces; acquisition of insurers by non-insurance corporations and the formation by insurers of general business corporations as a means of diversifying activities into other financial services. Regulators were concerned about the relationship between non-insurance interests and their regulated insurance company affiliates. That model law was subjected to major change in 1985, in part in response to the insolvency of insurance subsidiaries of the Baldwin-United corporation, when evidence showed that certain inter-affiliate transactions were not subjected to regulatory scrutiny pursuant to the Act's provisions. Again, ACLI worked closely with the NAIC in development of the original model law and the later revision, and continues to support enactment of the current version in the various states. All but one state has enacted either the Model Act or laws providing substantially similar regulatory oversight. However, not all states have enacted the later amendments to the Model Act and in particular Section 5 of the 1985 revision, dealing with inter-affiliate transactions.

This Model Law is on the NAIC Financial Regulation Standards

8. Reinsurance. In 1984 the NAIC adopted a Model Law on Credit for Reinsurance to address the problem of collectibility of reinsurance claims by restricting or denying credit against reserves for reinsurance ceded to reinsurers that do not meet certain standards, or fail to post acceptable security. Revisions were made to the Model Law in 1989 and it is included in the NAIC's Financial Regulation Standards. Eight states have enacted

the Model Law or substantially similar legislation, or regulation, and thirty-six states have laws or regulations in place that relate to credit for reinsurance but could be strengthened by appropriate amendments.

The NAIC also has a Model Regulation for Life Reinsurance Agreements that provides a mechanism for ensuring that a meaningful transfer of risk exists in financial reinsurance treaties. This Model Regulation is also included in the NAIC's Financial Regulation Standards, and it has been adopted in seven states.

In December, 1990, the NAIC adopted a Model Regulation on Credit for Reinsurance that implements the Model Law on that subject. While not yet included in the NAIC Financial Regulation Standards, ACLI supports promulgation of the Model Regulation.

C. How Insolvencies Are Handled

Despite effective state regulation, life insurance companies do become insolvent. The states have enacted laws to protect their citizens in such cases.

1. Life & Health Insurance Guaranty Association Model Act. The NAIC first adopted this Model Law in 1970, following its adoption of a Model Guaranty Law for Property-Casualty Insurance. The latter was prompted by a series of insolvencies of high risk automobile insurers in the 1960's, and that Model Law was enacted in a relatively short period of time by all but one or two states. The Life and Health Guaranty Association Model Law moved at a somewhat slower legislative pace, reflecting the

relative lack of urgency by state legislatures. Forty-seven states have now enacted life and health insolvency guaranty legislation patterned on the current model law or earlier versions.

2. Rehabilitation and Liquidation. Model Insurers Rehabilitation and Liquidation Act covers the process of insurance company receivership and liquidation, including the rights, responsibilities and priorities of all affected parties. In December 1989 the Model Law was amended by the NAIC to separate the provisions relating to supervision and place them in a new model law. This model act is in the NAIC Financial Regulations Standards and seventeen states have enacted it or legislation substantially similar.

3. Administrative Supervision. The NAIC Administrative Supervision Model Act was adopted to establish authority in the state insurance commissioner to take administrative action against an insurer, without having to petition a court for a formal order of rehabilitation or conservation. By acting early following evidence that a company is on a perilous financial course, it is possible to prevent an insurer from going insolvent and facing formal rehabilitation or liquidation proceedings. This model law is part of the NAIC Financial Regulation Standards. While only four states have enacted this Model Law, states which enacted the earlier version of the Model Insurers Supervision, Rehabilitation and Liquidation Act have similar administrative authority.

The NAIC Financial Regulation Standards and Accreditation Program is, for practical purposes, in its first legislative year. While the standards were adopted in June 1989, the certification program was not adopted until June 1990. Since all but one state legislature is in session this year, 1991 is the first test of the state legislatures' willingness to enact the necessary model laws. ACLI legislative records indicate that, as of April 5, 1991, 146 bills were pending in 35 state legislatures to enact one or more of the relevant model laws of the NAIC Financial Regulations Standards. It is, of course, still early in the session for many state legislatures, and additional activity can be expected between now and the end of the year.

D. The Success of State Regulation for Solvency

In recent years, the number of life insurance companies becoming insolvent has grown. Assessments made by state guaranty funds to protect policyholders have increased. However, the amounts of money involved have been small in the context of the size of the business. The total assessments needed to cover all impairments or insolvencies since the state guaranty funds were first established amount to less than $500,000,000. That is less than 1/20 of one percent of current assets held by life insurance companies. Compare that to FDIC assessments estimated to be needed for the current year or the funds needed for the savings and loans.

1. <u>Financial Strength of the Life Insurance Business</u>. The financial strength of the life insurance business reflects both the quality of its assets and the integrity of its investment practices. Investment managers generally agree that the fixed-income bonds and mortgages invested in by life insurance companies are very conservative investments. Usually, life insurance commercial mortgages are not made until properties are producing a steady stream of income. Both mortgage borrowers and bond issuers are contractually obligated to make periodic payments to life insurance companies.

The investment portfolio of the life insurance business is and has been primarily in fixed-income securities and mortgages which generate a steady cash flow. For example, total corporate and government bonds as a percent of total general account assets has not been less than 41 percent throughout the postwar period and stood at 58 percent at the end of 1989. Total investment in bonds plus mortgages was 87 percent of general account assets in 1950 and 80 percent on January 1, 1990. Real estate holdings over the years have been less than 5 percent of general account assets. Investment in common and preferred stocks as a share of assets has never been higher than 7 percent in the last 45 years and was 5 percent at the end of 1989. The common stock share stood at only 4.3 percent at the end of 1989. Commercial mortgages, which are backed by income-producing properties, comprise 92 percent of total mortgage holdings at year-end 1990.

As suggested above, the industry's investments are well diversified with very small exposure to the volatility of the stock market. Commercial mortgages are diversified across U.S. regions and types of properties. The bond portfolios are diversified among government obligations, foreign government bonds and corporate bonds. Corporate bonds are also diversified, not only among companies and industries, but also by maturities.

2. Quality of Bond Investments of Life Insurance Companies. The National Association of Insurance Commissioners (NAIC) Securities Valuation Office (SVO) categorizes, by credit quality, all public and privately placed bonds held by life insurance companies. The NAIC rating system is based on assessments made by the staff of the SVO. Their ratings take only into account corresponding ratings by the public bond rating agencies when they are available. Bonds of the federal government and those carrying a U.S. government guarantee have been in an exempt category because there is no credit risk (7-8 percent of general account assets). The SVO in 1990 took steps to substantially tighten its oversight of bond quality and of security valuation reserves against defaults.

In 1990, the NAIC further improved its continuing oversight of the quality of life insurance bond investments by increasing the maximum Mandatory Securities Valuation Reserves (MSVR) for medium-grade bonds in life company portfolios and the rate of accretion required of companies to reach the maximums for medium and lower-grade bonds within a reasonable period of time.

Through December 31, 1989, bonds had been classified by the NAIC Securities Valuation Office into four categories for the purpose of determining the appropriate MSVR maximum reserve. The new standards established in 1990 refined this to six categories. The increase was accomplished by dividing the old 2% "Yes" category into a new Category 1 with a 1 percent reserve, Category 2 to continue with a 2 percent reserve, and Category 3 to have a 5 percent reserve. The periods allowed for reserves to build up to the maximums were shortened. In this way the reserve standards for bondholdings were substantially tightened.

In a subsequent step, the NAIC instructed the SVO to recategorize all public and private bond issues into the six new categories before year-end 1990. In this process, some bonds migrated downward in rating category; some migrated upward from where they had been at the end of 1989. The following table estimates how bondholdings were distributed among the six categories in a preliminary ACLI special survey of 100 large companies as of December 31, 1990. The results were taken from bond portfolios in companies representing 75 percent of the general account assets of the industry. Actual holdings as reported in 1990 annual statements are not yet available at this time (April 9, 1991).

ACLI Preliminary Bond Quality Distribution Survey,
General Account Portfolio, December 31, 1990

1990 Quality Rating per NAIC	Publicly Traded Bonds	Private Placements	All Bonds
1	77.5%	41.6%	64.8%
2	16.7	38.8	24.3
3	2.2	10.2	5.0
4	2.8	5.7	4.0
5	0.6	2.5	1.3
6	0.2	1.2	0.6
	100.0%	100.0%	100.0%

The six categories approximate a continuum of credit quality from highest to lowest. Among the six NAIC categories, Categories 1 and 2 are viewed by the SVO as higher grade; Category 3 is viewed as medium grade; and Categories 4, 5 and 6 are seen as lower grade in terms of credit quality. As can be seen in the table, most of the lower grade bonds held by life insurance companies at the end of 1990 were private placements. Only 3.6 percent of the public bonds held by life companies were lower grade. This is because life companies have generally invested conservatively and most companies have not been in the market for the public bonds used to finance leverage of buyouts, almost all of which were issued in the 1980s.

For a century, life companies have been profitably making private placement loans to companies not large enough to get the highest public bond ratings from the credit rating agencies. The yield on these private placements has been greater than higher quality public corporate bonds so as to compensate lenders for the additional risk or lower liquidity. Yet, private placement bonds have more protection against credit risk than their higher yield would indicate. Private placement bonds normally are better collateralized than public bonds of similar grade; they have stronger covenants protecting lender interests, and there has been greater recovery of assets for lenders after default than for public bonds. Private placement lending has long been a profitable business for life insurance companies and a major source of long-term financing for second tier corporations, those not large enough to use the higher grade public corporate bond market.

Reported statistics on the quality of bonds in life company portfolios often overlook the fact that almost all bonds held by life insurance companies are in good standing. That is, they are paying interest as agreed. When they fall behind 60 days or more in payments, they are "in default." In the years from 1978 through 1989, the bond default rate as a percent of general account assets went above one-fourth of one percent of the general account only twice (.26% in 1983; .28% in 1987). A reasonable level of holdings of medium and lower grade direct placements and public bonds should not be of concern since the credit quality of the total bond portfolio, not a small segment of that portfolio, is most relevant to financial strength measurement. Also, in any solvency threat, all the assets of the general account and company surplus stand behind insurance company guarantees to policyholders and annuitants.

3. Real Estate Investments of Life Insurance Companies. Because the liabilities of life insurance companies are intermediate to long term in duration, investments too can appropriately be intermediate to long term. Thus, mortgage loans have long been a major investment category of companies in this industry. Over 90 percent of the mortgage loans made by life insurance companies are for commercial properties--apartments, shopping centers, office buildings, and industrial buildings.

There are several kinds of real estate loans, some much riskier than others. Life companies are not involved in all phases of real estate lending. Short-term loans are made to acquire undeveloped land, to develop land, and to construct buildings on developed land. Life insurance companies are typically not involved in these types of lending.

As the buildings are completed, short-term construction loans are paid off when long-term mortgage loans are made. This is the phase in which life insurance company lending comes in. Mortgage loans by life companies usually are not made until a building is nearly leased up with tenants or when the borrower has received third-party income enhancements or credit support. Loans are usually not made for more than 75 percent of a building's value. Lenders most often require that net monthly income on the property will be 20 percent or more larger than the cost of servicing the mortgage debt.

Life insurance mortgage loans are also protected by broad diversification over types of properties and across national regions. This diversification often means that declines or increases in one sector or region are at least partially offset by an opposite trend in other sectors. Classifying mortgages by types of buildings, the largest holdings share is in office building mortgages (40.4%) and the smallest share is in hotel/motel mort- gages (4.9%). Classifying by regional share, largest is the Pacific with 21.8% of mortgages held; next is the South Atlantic region with 20.5%. Smaller regional holdings are in the New England states (6.6%), West North Central (4.8%) and Mountain (4.2%).

Even though delinquency rates on agricultural mortgages have been falling since mid-1986, and commercial mortgage delinquency rates have been improving in the hard hit Mountain and West South Central states, the national trend of mortgage delinquency rates rose in 1990. This has been mainly the result of sharp increases in delinquency rates in the New England and Atlantic regions.

Under present real estate conditions, the annual rate of completed foreclosures was 1.42 percent of all mortgages for 1990. Prior to foreclosing on a property, companies make every effort to restructure a mortgage loan to make it work out. However, that cannot always be done and sometimes life insurers are left with no other alternative but to foreclose. Because of their deep pockets, robust cash flow, and long-term liabilities, life companies do not have to make distressed sales of properties on which they have to foreclose. If the company can see that business or real estate value cycles are likely to improve or a property is otherwise currently undervalued, they are able to hold it and improve it if necessary for later sale.

The life insurance industry holds about 25 percent of all outstanding commercial mortgages, less than the share held by commercial banks. The top 30 life companies hold most of this. Mortgages as a percent of life insurance industry general account assets fell from 29 percent in 1980 to 22 percent in 1989. Over the same period, commercial banks increased their asset share of mortgage lending.

Foreclosed property owned is not excessive in this industry. For perspective, in assessing the size of the problem in life insurance, the thrift industry's Resolution Trust Corporation had $16.4 billion in foreclosed properties to dispose of at year-end 1989. All insured savings associations reportedly had $40.6 billion in repossessed assets and real estate held at the end of 1989. The commercial banks held $12.5 billion in "other real estate owned" at the end of 1989. In contrast, at year-end 1989 the life insurance industry held only $6.3 billion in "real estate acquired in satisfaction of debt," one-half of one percent of general account assets.

4. Recent Trends in Solidity of Life Insurance Companies. Neither the 1990 downturn in the non-investment-grade bond market or the slump in real estate markets has noticeably impaired the financial strength of the insurance industry. The industry has repeatedly shown its resilience in managing economic dislocation. Before the relatively minor stresses of 1990, the most

recent macroeconomic problem imposed on the business was the high inflation followed by deep economic recession in the late 1970s and early 1980s.

Double-digit inflation and a deep recession in the years from the late 1970s through 1982 provided serious new challenges to the industry and its investments. Those challenges did not seriously impair the financial strength of the life insurance industry as a whole. In those years there was a decline in margins on products being sold. At the same time, there arose a threat of disintermediation, manifested in an increase in policy loans at contractually guaranteed low interest rates. These loans peaked at 10.1 percent of assets in 1981. Another challenge introduced at that time was the growing range of interest-sensitive products which put further pressure on companies to seek higher current rates of return on investments.

The following measures of financial strength indicate that, in the aggregate, companies remained sound during that trying period from the late 1970s into the 1980s. Bonds in default comprised .07 percent of general account assets at year-end 1979, peaked at .26 percent at year-end 1983, at .28 percent at year-end 1987, and stood at .19 percent in 1989. Policy loans as a percent of general account assets fell to 7.4 percent in 1985 and were down to 5.0 percent of assets in 1989. Liquidity in terms of cash plus short-term assets was 1.9 percent of assets in 1979; companies increased this to 4.2 percent in 1983, and it was 3.7 percent at year-end 1989.

The industry's capital ratio, capital plus surplus plus the Mandatory Securities Valuation Reserve (MSVR) to total assets was 7.9 percent at the end of 1989 as compared with 8.2 percent at the end of 1979. This ratio is in a healthy range, but by itself provides insufficient information to gauge the financial strength of the industry or of particular firms. In the last decade, the mix of liabilities protected by capital and surplus has been changing. As a result, mortality risk is lower, but interest rate risk is higher. A careful assessment of the risks under management by each firm would be necessary to learn more about the adequacy of capital overall.

Of critical importance in assessing the adequacy of capital is having good knowledge of the adequacy of reserves. As reserves are more conservatively estimated, the industry would be financially stronger, yet the capital ratio would be lower. Regulators are moving toward establishing a "valuation actuary" responsibility within the firm to assure the best management of reserve liabilities and assets.

5. Managing Maturities of Assets and Liabilities. Life insurance companies took major steps and have been very aggressive in moving to improve duration matching of assets and liabilities. This can be seen in the shortened maturities in their bond and mortgage portfolios in the early 1980s. Bond acquisitions in over 10-year maturities fell from 85 percent of acquisitions in 1980 to

53 percent in 1983 and 48 percent in 1989. Similarly, the over 10-year share of mortgage acquisitions fell from 95 percent in 1980 to 48 percent in 1983 and 19 percent in 1989. This enabled companies to better match the maturities of their assets with maturities of their liabilities. The purpose of this has been to better manage the higher risks inherent in volatile market interest rate movements.

6. Profitability. After some years of declining profitability, in 1988 and 1989 life insurance companies began what appears to be a turnaround. On May 29, 1990 A.M. Best Insurance Management Reports reported that, "For the second consecutive year the life/health industry's statutory operating performance improved significantly in 1989 due in part to lower premium growth, greater cost containment measures and better persistency. The U.S. life/health industry's net operating gain increased 30 percent from the prior year-end results--the same percentage growth as in 1988. Moreover, the industry posted a 13.6 percent return on equity in 1989, compared with 11.7 percent in 1988.

More than one rating service has concluded that, having come through the past decade in an environment of heightened competition and increased risk in their product lines, many insurers are changing their emphasis from growth to profitability. This is perhaps the most important argument in support of the great financial strength of this business, the adaptability to changing conditions. Financial strength can trend downward for a period of time, but there are self-correcting forces which lead companies to reduce costs, discard unprofitable business lines, retard capital-using asset growth, improve product pricing, and take other optional steps to strengthen their financial position.

Summary

In conclusion, the regulation of life insurance companies for solvency by the states has been successful over many years through all kinds of economic conditions.

The NAIC, through its diverse committee structure, the development of model laws and regulations, and the increasingly important services to the states, i.e., the NAIC data base, has been an essential part of this effort.

The process is an open one that lends itself to continuing review and corrections as experience develops. We intend to continue to participate in the process fully in the future.

Senator METZENBAUM. We appreciate your comments, Mr. Mica. There is no question that the American people are very much concerned. We know that Travelers wrote off $650 million in real estate loans. We know that Equitable wrote off $850 million in real estate loans. We know that Executive Life lost something like $460 million; I forget whether it was the last quarter or the last half of last year. We read in the paper this morning that policyholders may be called upon to suffer substantially if Executive Life goes under. We hear about guaranty funds, and then we hear that there are limits with respect to those guaranty funds.

My question to you is what is the life insurance industry prepared to do to see to it that there will be no losses suffered by the policyholders of life insurance companies, whether it is Executive Life, Travelers, Equitable. We know Equitable went out to raise some money. I don't know what happened in that connection as far as turning it from a mutual into a stock company.

Many companies that you represent are mutuals. The availability of information and the opportunity to know more about the companies' actual workings is quite limited in the mutual companies.

My question to you is what assurances can you give today, representing the American Council of Life Insurance, that the policyholders are not going to suffer if any one of the companies that are presently being talked about or any one of the companies that we don't know anything about and don't know that they are in jeopardy—that the policyholders will be protected and that the life insurance industry will see to it that they be protected.

Mr. MICA. Well, first, I think the track record is clear that in the past, particularly in the *Baldwin-United* case, which was the last major problem that existed, the insurance industry did indeed come together and make sure that policyholders were protected.

Second, I think there is a whole list of other questions that need to be answered as to the way the courts handled this particular situation, this pending situation, but I was reminded by our professional staff that policyholders come first in the line of assets. All other vendors, lessors—everyone else is at the end of the line. So the amount of money in question may be far less than anyone would expect by looking at the total picture.

Lastly, the guaranty funds would then be used in that area, and it is likely—and this is sheer speculation—that if you went beyond that, there would be additional assessments against the industry. In my testimony which I skipped over, I described a system whereby assessments are indeed made against the industry to cover just these types of problems.

So I would just add this note of caution, if I may, Senator. I think the industry is prepared to do everything and anything within its power to prevent loss to policyholders because our business is based on consumer confidence. But I just received this morning the National Journal. The headline on it—one of the more prominent publications used here on Capitol Hill—says "America Risk-Free," and it talks about the cost of going from nominal risk to zero risk.

The Federal Government—and the figure I was astounded at—now has liabilities that are $5,981 billion in liabilities to back up zero risks and all of the guaranties they have offered. Somewhere along the line we have to think in terms of managing risk, prudent risk, and whether or not we would put into place a Federal or State system for zero risk, and right now I am not sure anybody is looking for zero risk.

Senator METZENBAUM. I guess my real question is—and you may have answered it—if, for example, Executive Life goes under, will the insurance industry see to it that no policyholder suffers any loss at all?

Mr. MICA. That would be our intent. Obviously, we, like you, would want to see exactly how it is structured, how the courts handle it, and there are a number of legal variables. But let me call on Dick Minck, who has dealt personally with the *Baldwin-United* case.

Mr. MINCK. Good afternoon, Senator.

Senator METZENBAUM. We are happy to have you with us, Mr. Minck.

Mr. MINCK. Thank you, sir. I think we are a little bit ahead of where we can give you an answer that is 100 percent reliable one way or another. The first thing is that the company is still in existence; the State has not taken it over. The next thing is if the State does take it over, you will have to go to the courts for an order and you will have to have a receiver look at it to determine what the situation is with regard to the assets that the company has and the liabilities that the company has.

Once that is done, then the State and the people administering the company will have a number of options, one of which may be to find a buyer. That may take some period of time. In the case of Baldwin, it was probably about a 4-year period of time. At no time were we able to make an unconditional commitment that nobody would ever lose a penny under the Baldwin thing. In fact, nobody did, but I think it is much too early to know all of the things that are going to happen. We just don't know what the State is going to do, nor how the people administering the estate, if, in fact, the company is taken over.

Senator METZENBAUM. In previous situations when a company went into bankruptcy court, what happened to the policyholders after that point? Were they paid at the time of decease or were they just told to stand in line?

Mr. MINCK. I think if you are prudent—and I think I will refer to some of my other associates on it who have had experience in the legal profession. But if you are administering an estate and you are behaving prudently in that position, you might have a deferral period for allowing claims—that is, preventing a run on the bank—so that you can marshal the assets intelligently and so that all of the policyholders will receive the best possible outcome.

Senator METZENBAUM. You can't have too much of a run on the bank if payment is conditioned upon death, unless you have a catastrophe.

Mr. MINCK. No; but all of the contracts have cash values, sir.

Senator METZENBAUM. Pardon?

Mr. MINCK. I say all of the life insurance contracts provide cash surrender values. All of the annuities typically will provide cash surrender values. So you can, in fact, have demands.

Senator METZENBAUM. I would guess that in the case of First Executive, much of that has already transpired.

Mr. MINCK. There has been a lot of hammering, certainly, Senator.

Mr. BLAINE. If I may, I am Jack Blaine, Senator. Fortunately, historically, in handling life impairments and insolvencies, assets have generally been sufficient to pay life insurance beneficiaries; that is, death claims can be paid and disability claims can be paid. So the situation that Mr. Minck described of preventing the run on the bank is important in keeping the healthy policyholders from taking their cash values, whether it be life insurance or annuities, and leaving the scene and leaving, in the case of life insurance, perhaps, less healthy, and at the same time stripping assets out of the estate before the administrator can get it tidied up and into order.

That process still pretty much follows today, even with guaranty funds that do come in at the point where benefits cannot be paid or there are insufficient assets to meet the other obligations to policyholders of the company.

Mr. MINCK. The other thing, Senator—and this is perhaps a key difference between the treatment of life insurance insolvencies and property and casualty insolvencies—that is a concern that the insurance protection continue for the policyholders. With a property and casualty sort of contract where you just have year-to-year coverage, there is no great harm done if the insured then goes to another insurer and renews the coverage that terminates.

In the case of a life insurance contract, the individual may not be able to obtain insurance. So the protection that Mr. Blaine referred to of taking care of those continuing policyholders is a very important one, and a lot of the activities of the States are conditioned on that.

Senator METZENBAUM. Representing the American Council of Life Insurance, I would urge upon all of you that you determine as a policy matter in your hierarchy whether or not the policyholders are going to be protected or not, because the stories that are out on the street at the moment certainly provide a cause for concern for all of the American people, not only for those who hold policies with Executive Life.

I hear it, I get it in the mail. What about the solvency of the insurance industry, and will we be losing what we put in? I think that the earlier the life insurers address themselves to this concern, the better and more stable the industry will be. Frankly, one industry will probably be more prosperous as well, because I can see people turning off and just putting their money into other kinds of bonds and stocks rather than insurance companies, and saying if somebody is going to lose it, I may as well lose it myself.

Let me go on with a few questions.

Mr. MICA. Senator, if I may comment on that, in my testimony I did reference that, and indeed it is a consensus of the American Council of Life Insurance that policyholders should be protected. I guess we get into some questions of exactly how, and when we see some of these problems unfold we are going to try to do it.

One other point, if I may. I notice this chart has been up, and if I may just comment, I had reason to be involved in a very similar process in my previous career and, in fact, asking that consumers be added to a board very similar to that, and, in fact, got the companies involved to agree to pay the expenses, as you had indicated, which resulted in all the consumer groups saying that the groups who took the expenses were then paid pawns of the industry. They then passed a resolution saying that none of their people could take any expenses.

We went around and around on this, so it is a difficult one, but it is fraught with danger. I know what you are trying to accomplish, but when they took the money, they were immediately disqualified.

Senator METZENBAUM. Well, I don't know the circumstances. I think that paying actual out-of-pocket expenses would not affect their bias; at least I would hope not.

As I mentioned to the earlier witnesses, I am concerned about the process in which NAIC models are drafted and adopted. Consumer representation is sorely lacking in the advisory committees. I have said that before. You state in your written testimony that the NAIC advisory committees, "frequently," have representatives from consumer interests. As you heard me say earlier, 26 have no consumer representatives. I think you would agree that is not a balanced environment in which to draft model legislation.

Do you feel that the American Council of Life Insurance could use the prestige and weight of their position to bring about some changes by the NAIC? There is no question you are a major factor in the industry, and there is no question that if you were to make it clear that——

Mr. MICA. If I may speak, and I cannot speak on behalf of the board without getting certain policy approvals, but I would say very clearly that it would be in our interest to look into your concerns here to see what is the actual situation, what can be done to make it more clear that consumers do indeed have a right to participate if they are not being asked to participate.

I do have thoughts, as you put it up, Senator, just in my learning curve in this industry. I have sat in on some of these meetings. Some of them are highly technical. Some, I would not think that many consumer groups would have an interest in. So I think what we might want to do is—and I would be happy to do this—have our staff take a look at the process, see who wants to serve, who hasn't been allowed to serve; see if indeed the types of committees they are not serving on are the ones that they would somehow be needed on or could offer some expertise; and take a look at that and bring it to our policymaking board to see if they could accommodate some of your concerns. I don't have a problem with that at all. In fact, I think that is a legitimate question.

Senator METZENBAUM. Mr. Schwartz, would you care to address yourself to the same question; and that is whether the American Insurance Association would be willing to make some representations and try to use the prestige of their position and their relationship with the NAIC to bring about more consumer representation on their committees?

Mr. SCHWARTZ. Let me give you a personal example, Senator, if I may. Last month, the NAIC appointed me chairman of an advisory committee that was asked to assist in amending the insurance expense exhibit which is included in the annual statement. I was told that the members of the advisory committee would be appointed by the NAIC. The NAIC would be informed of any meetings that the advisory committee wanted to hold, and the NAIC representatives would attend the meetings of the advisory committee.

I hope that this project will improve the reporting of insurance operations, and therefore improve regulation for solvency. But I must say that up to this point I know of no consumer interest in this subject. It is a highly esoteric one; it goes to detailed reporting of financial information. I would think that if consumers were interested, they would be welcome.

But my experience is that on subjects like this—and I think Mr. Mica made the same point that many of these advisory committees are really highly technical and what they are trying to do is hammer out a desire of the regulators and trying to get industry input as to how that can best be done on a uniform and consistent basis.

Because of the technical nature of these subjects—and, basically, those are the ones that the commissioners look for help on.

Senator METZENBAUM. What is the name of that committee?

Mr. SCHWARTZ. The advisory committee that I have been asked to chair is one that is looking at the insurance expense exhibit in the annual statement, which shows the results of operations for the various lines of business within the insurance companies.

Senator METZENBAUM. Insurance expense exhibit?

Mr. SCHWARTZ. Yes, sir.

Senator METZENBAUM. Would that show what the salaries of officers are paid?

Mr. SCHWARTZ. It includes information relating to the expenses of the company.

Senator METZENBAUM. But without specifics? It wouldn't say whether the officer gets $1.6 million or whether he gets $3.8 million or whether he gets $400,000?

Mr. SCHWARTZ. No, sir.

Senator METZENBAUM. Do you think that that might be helpful, and it is something that policyholders have a right to know, particularly if it is a mutual insurance company?

Mr. SCHWARTZ. That is information that might be helpful to certain people, but in the project that we are working on we are trying to determine the results of the operation. The annual statement that the insurance companies file—a lot of people don't understand that those annual statements run on for hundreds of pages and detail tremendous amounts of information.

The particular project that this is attempting to address has to do with summarizing the operations of the company by line of business—for example, private passenger auto, liability, physical damage, workers compensation—and to summarize the results of the operations in a summarized form.

Senator METZENBAUM. If you knew some consumer groups that were interested in serving on the committee, assuming that they were credible people, would you be willing to put them on, since it is my understanding that you have the authority to appoint?

Mr. SCHWARTZ. That is not correct. I do not have the ability to appoint. The NAIC makes all appointments. The NAIC appoints the chairman and appoints all the people on the committee. At least that is what I was told when I was asked to be chairman.

Senator METZENBAUM. Staff confirms your representation, sir.

Mr. PRATT. Mr. Chairman, could I amplify on that point? We have a very active dialog with Consumer Federation of America, Consumers Union, and other groups here in Washington and at various points around the country in all 50 States. Because of the dialogue that we have, I think it would be something that we would be interested in talking to them about in light of the questions that you have asked today to find out what their interests are and to see—realizing that we don't have the authority to put these people on, we could at least talk to them and see where their interests are in some of these matters.

Senator METZENBAUM. Thank you very much, David.

Mr. Mica, you talk about how safe and secure the life insurance industry is. Mr. Sargent testified earlier that California had 74 insolvent insurers under conservatorship or in liquidation—I think that was in his statement—and that 200 of the State's 1,900 insurance companies are under special surveillance by the California Insurance Department.

Now, that is a pretty high percentage, 200 out of 1,900, and 74 in conservatorship or in liquidation. Does that sound to you as if the industry is so safe and secure?

Mr. MICA. Well, I think we would have to take a look at who they are, Mr. Chairman, first. Two hundred could represent less than a half a percent of the industry, or a very small fraction of 1 percent.

Senator METZENBAUM. This is 200 out of the State's 1,900.

Mr. MICA. But I am talking about the size of the business, and so on. There may be an industry that has opened up and called itself an insurance business—opened its doors, and immediately is not having success and they are in trouble. So I think you have to look at those 200 and see what the situation is.

Let me also call on Mr. Minck.

Mr. MINCK. Yes. I think, Mr. Chairman, it might be a mixture of companies in all sorts of insurance operations. I don't believe there are 1,900 life insurance companies doing business in California.

Senator METZENBAUM. I think, small or large, when the loss hits the policyholder doesn't know, and it is the policyholder who suffers. So it is not enough to say, well, it is just the small companies because there are human beings involved. The figures we are using came from the statement of Senator Johnston—"compounding our concern about the financial soundness of the life insurance industry," and then he goes on with those numbers that I just gave you. So it is the life insurance industry about which——

Mr. MICA. We would like an opportunity to reconfirm that in writing because that doesn't match with what my perception is of the entire national situation, let alone California.

Senator METZENBAUM. I would guess there is an additional copy, and if not we will provide you with a copy.

Let me conclude this hearing by saying, A, that I am very pleased to have participating with us the American Insurance Association and the American Council of Life Insurance Companies. We welcome your participation and want you to understand that we believe that such activities as we may be involved in as we inquire into this industry, the public would be better served if we worked together rather than if we worked at odds with each other.

I have had the feeling—and I have said publicly on a number of occasions that our doors are open to you; that we welcome cooperation rather than confrontation. Unfortunately, in the past we have had more confrontation than cooperation. I don't say this in a pejorative way, but rather say it in reporting the actual facts.

And so I would say to you that, A, we are grateful to you for joining us today. The information you have submitted is very helpful. We will be giving more and more attention to this industry as we proceed forward. We want the industry to be successful and to be healthy, and the policyholders to be protected and the stockholders to make a profit, but we also want to be certain that the policyholders are protected and that there be no need to call upon the Federal Government for any bailout. I don't think that is our only concern. I think it is our concern that the policyholders be protected.

So let me conclude this hearing by saying that we are pleased that you are here, and please know that our doors are open to you and we would be happy to discuss any aspect of our inquiry after this hearing.

I will ask of myself unanimous consent to put supplemental charts in the record and to hold the record open for answers to send written questions that we will have of some of the witnesses. Since I am the only one present, I guess I can say that the unanimous consent has been granted and, without objection, we will put the supplemental charts, as well as the present charts, in the record.

We will also hold the record open for answers to some questions that we will still have.

Having said that, gentlemen, thank you very much for being with us this morning. This hearing stands concluded.

[Whereupon, at 12:54 p.m., the subcommittee was adjourned.]

APPENDIX

SENATE JUDICIARY SUBCOMMITTEE ON ANTITRUST, MONOPOLIES AND BUSINESS RIGHTS

HEARING
HOW INSURANCE LAWS ARE MADE:
THE NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS
AND STATE ADOPTION OF NAIC MODEL LAWS
APRIL 9, 1991

SUPPLEMENTARY CHARTS

TABLE OF CONTENTS

NAIC MODEL LAWS WHERE THE STATES WERE SLOW IN ADOPTING

1. LIFE AND HEALTH GUARANTY FUND
Creates an association of insurers to pay benefits and continue coverage of life and health insurance policyholders, subject to appropriate restrictions and limitations, when an insurance company is deemed insolvent. Members of the association are subject to assessment to provide funds to carry out the purpose of the Act.

2. LIFE AND HEALTH POLICY LANGUAGE SIMPLIFICATION
Establishes minimum standards for language used in life and health insurance policies in order to facilitate the insured's understanding of the coverages provided.

3. PARTICIPATION IN IRIS
Requires each insurance company authorized to transact business in the State, to file annually with the NAIC a copy of its annual statement convention blank, for use by the NAIC Insurance Regulatory Information System (IRIS), which compiles data to provide early warning to State Insurance Departments of possible solvency problems in insurers.

4. ADVERTISING OF LIFE INSURANCE
Establishes minimum standards and guidelines to assure full and truthful disclosure to the public of all material and relevant information in the advertising of life insurance policies and annuity contracts. Authorizes Commissioner to review advertisements and to enforce this Act.

5. REQUIRING ANNUAL AUDITED FINANCIAL REPORTS
Requires an annual examination by independent CPAs of insurance companies financial statements.

6. INSURERS REHABILITATION AND LIQUIDATION
Provides a comprehensive scheme for the rehabilitation and liquidation of insurance companies covered by this Act.

7. LIFE INSURANCE DISCLOSURE
Requires insurers to deliver to purchasers of life insurance, information (including a Buyer's Guide) which will improve the buyer's ability to select the most appropriate plan of life insurance for the buyer's needs. Applies to any solicitation, negotiation or procurement of life insurance.

8. INSURANCE HOLDING COMPANY SYSTEM REGULATORY ACT
Authorizes the Commissioner to deny the acquisition of direct or indirect control of a domestic insurance company if it is found that the acquisition could be harmful to the policyholders.

9. PROPERTY AND LIABILITY INSURANCE GUARANTY FUND
Creates an association of insurers to ensure payment of covered claims under certain insurance policies, subject to appropriate restrictions and limitations, when an insurance company is deemed insolvent. Members of the association are subject to assessment to provide funds to carry out the purpose of the Act.

10. ASSET VALUATION LAW
Establishes guidelines for the valuation of bonds and other securities held by insurance companies.

11. CREDIT FOR REINSURANCE
A credit for reinsurance allows a ceding insurer to treat reinsurance ceded as an asset or a reduction of liability on its financial statement. This Act would not allow a credit unless the assuming insurer meets licensing and net worth requirements, and allows the State to examine its books.

12. RISK RETENTION ACT
Regulates the formation and operation of purchasing groups, who purchase insurance on a group basis, and risk retention groups, who assume and spread all or any portion of the liability exposure of its group members.

13. MANAGING GENERAL AGENTS
Defines managing general agent (MGA) as a person who manages all or part of the business of an insurer, acts as agent for the insurer producing business equal to 5% of insurer's surplus, and either adjusts or pays claims or negotiates reinsurance. The Act subjects MGAs to license and reporting requirements, and gives Commissioner examination authority over them.

Model Act

Adopted 1971

1971	MARYLAND, NEW HAMPSHIRE, WASHINGTON
1972	CONNECTICUT, KANSAS, VERMONT
1973	NEVADA, NORTH CAROLINA
1974	MONTANA
1975	NEBRASKA, OREGON
1976	
1977	ARIZONA, IDAHO, MINNESOTA, WEST VIRGINIA
1978	INDIANA, KENTUCKY
1979	PENNSYLVANIA, Wisconsin
1980	
1981	GEORGIA, ILLINOIS, OKLAHOMA
1982	ALABAMA, DELAWARE, FLORIDA, MICHIGAN
1983	
1984	MAINE
1985	MASSACHUSETTS, MISSISSIPPI, NEW MEXICO, NEW YORK, RHODE ISLAND, TEXAS
1986	UTAH, VIRGINIA
1987	HAWAII, IOWA
1988	MISSOURI, SOUTH CAROLINA
1989	ARKANSAS, NORTH DAKOTA, OHIO, SOUTH DAKOTA, TENNESSEE
1990	ALASKA, CALIFORNIA, WYOMING

<u>States Adopting</u>
46 MODEL LEGISLATION
1 Related Legislation

Source: NAIC, January 1991

Life and Health Insurance Policy Language Simplification Model Act
Adopted 1978

1977	Maryland, Minnesota, Texas
1978	[Model Adopted]
1979	ARKANSAS, CONNECTICUT, MAINE, MASSACHUSETTS, NEBRASKA, NEW JERSEY, NORTH CAROLINA, OHIO, OREGON, Rhode Island
1980	WISCONSIN
1981	SOUTH CAROLINA, SOUTH DAKOTA, TENNESSEE, VIRGINIA
1982	ARIZONA, INDIANA
1983	GEORGIA, FLORIDA, MONTANA, NEVADA, WEST VIRGINIA,
1984	NEW YORK
1985	NEW MEXICO
1986	NORTH DAKOTA, Utah
1987	OKLAHOMA
1988	HAWAII, Kentucky
1989	
1990	

<u>States Adopting</u>
26 MODEL LEGISLATION
6 Related Legislation

Source: NAIC, January 1991

Participation in the NAIC Insurance Regulatory Information System (IRIS) Model Act

Adopted 1985

1969	Indiana
1976	Alaska
1980	
1981	Minnesota
1982	
1983	NORTH DAKOTA
1984	New Mexico
1985	ARIZONA, ILLINOIS, NORTH CAROLINA, Florida
1986	KENTUCKY, MISSOURI, OHIO, OKLAHOMA, Utah, Kansas [Model Adopted]
1987	TEXAS, VIRGINIA, WASHINGTON, WYOMING Arkansas
1988	HAWAII, SOUTH CAROLINA, NEW HAMPSHIRE, Iowa
1989	NEBRASKA
1990	Maine

STATES ADOPTING
16 MODEL LEGISLATION
10 Related Legislation

Source: NAIC, January 1991

Rules Governing the Advertising of Life Insurance

Adopted 1975

1969	Arizona
1970	Maryland
1971	Minnesota
1972	Ohio
1973	FLORIDA, South Dakota
1974	
1975	CALIFORNIA, WASHINGTON, Kentucky [Model Adopted]
1976	CONNECTICUT, ILLINOIS, IOWA, MISSOURI, TENNESSEE
1977	KANSAS
1978	NORTH CAROLINA
1979	
1980	GEORGIA, NEW YORK
1981	ALABAMA, Texas
1982	VIRGINIA
1983	
1984	MICHIGAN, Wisconsin
1985	NEW JERSEY
1986	
1987	
1988	
1989	Utah
1990	NEBRASKA, OKLAHOMA

States Adopting
18 MODEL LEGISLATION
9 Related Legislation

Source: NAIC, January 1991

Model (Rule) Regulation Requiring Annual Audited Financial Reports

Adopted 1980

1975	ILLINOIS
1976	MASSACHUSETTS
1977	
1978	
1979	PENNSYLVANIA, WISCONSIN
1980	[Model Adopted]
1981	
1982	
1983	
1984	New York
1985	Florida, Maine
1986	
1987	Delaware, Maryland
1988	
1989	INDIANA, KANSAS, NEW JERSEY, TEXAS, WEST VIRGINIA
1990	COLORADO, LOUISIANA, NEBRASKA, NORTH CAROLINA, OHIO, Connecticut

<u>States Adopting</u>
14 MODEL LEGISLATION
6 Related Legislation

Source: NAIC, January 1991

Adopted 1936

1913	Nebraska
1933	Maryland
1936	[Model Adopted]
1937	Illinois
1939	Massachusetts, Missouri
1940	Rhode Island
1942	Mississippi
1947	Washington
1951	Texas
1953	Delaware
1954	Arizona
1957	Oklahoma, West Virginia
1958	Louisiana
1959	Arkansas
1960	Georgia
1963	Colorado
1966	ALASKA
1967	WISCONSIN, Oregon, Wyoming
1968	Vermont
1969	MINNESOTA, NEW HAMPSHIRE, Tennessee
1970	KENTUCKY, MAINE
1971	Nevada
1975	New Jersey
1977	Kansas
1979	CONNECTICUT, INDIANA, MONTANA, PENN
1981	IDAHO
1982	OHIO, Florida
1983	North Dakota
1984	IOWA, New York
1985	New Mexico
1986	UTAH, Virginia
1988	HAWAII, SOUTH CAROLINA, California
1989	NEBRASKA, NORTH CAROLINA, SOUTH DAKOTA
1990	MICHIGAN

States Adopting
20 MODEL LEGISLATION
30 Related Legislation

Source: NAIC, January 1991

Life Insurance Disclosure Model Regulation
Adopted 1970

1962	Louisiana
1963	IOWA
1967	Kansas, Minnesota
1974	Arkansas
1975	Kentucky
1976	NEW JERSEY, Texas [Model Adopted]
1977	VERMONT
1978	CONNECTICUT, MONTANA, NEBRASKA, NEVADA, OHIO, UTAH, California
1979	ARIZONA, DELAWARE, INDIANA, MISSOURI, NORTH CAROLINA, OREGON RHODE ISLAND, SOUTH CAROLINA, TENNESSEE, WEST VIRGINIA, Pennsylvania
1980	GEORGIA, ILLINOIS, MAINE, MARYLAND, MASSACHUSETTS, NORTH DAKOTA, SOUTH DAKOTA, WASHINGTON
1981	ALABAMA, NEW MEXICO
1982	FLORIDA
1983	NEW HAMPSHIRE
1984	WISCONSIN
1985	
1986	
1987	
1988	
1989	
1990	

<u>States Adopting</u>
42 MODEL LEGISLATION
8 Related Legislation

Source: NAIC, January 1991

Regulatory Act
Adopted 1969

1969	CALIFORNIA, CONNECTICUT, MAINE, MARYLAND, NEBRASKA, Wisconsin, [Model Adopted]
1970	GEORGIA, IOWA, LOUISIANA, MASSACHUSETTS, MICHIGAN, NEW JERSEY, OKLAHOMA
1971	ARKANSAS, INDIANA, MINNESOTA, MONTANA, NEW HAMPSHIRE, NORTH CAROLINA, OHIO, OREGON, RHODE ISLAND, TEXAS, VERMONT, WASHINGTON
1972	IDAHO, KENTUCKY, SOUTH DAKOTA
1973	ALABAMA, DELAWARE, NEVADA
1974	MISSISSIPPI, WEST VIRGINIA
1975	KANSAS
1976	ALASKA
1977	ILLINOIS
1978	ARIZONA, PENNSYLVANIA
1979	
1982	
1983	MISSOURI, NORTH DAKOTA
1984	New York
1985	FLORIDA, NEW MEXICO
1986	TENNESSEE, UTAH, VIRGINIA
1987	
1988	HAWAII, SOUTH CAROLINA
1989	
1990	

<u>States Adopting</u>
46 MODEL LEGISLATION
2 Related Legislation

Source: NAIC, January 1991

Guaranty Association Model Act
Adopted 1970

1963	COLORADO
1969	MAINE, VERMONT, California, Michigan
1970	ALASKA, IDAHO, IOWA, KANSAS, LOUISIANA, MASSACHUSETTS, MISSISSIPPI, NEW HAMPSHIRE, OHIO, PENNSYLVANIA, WEST VIRGINIA, Georgia, South Dakota
1971	CONNECTICUT, MARYLAND, MINNESOTA, MISSOURI, MONTANA, NEBRASKA, NEVADA, NORTH CAROLINA, OREGON, TENNESSEE, WASHINGTON, WYOMING, Texas
1972	KENTUCKY
1973	INDIANA
1974	NEW JERSEY
1977	ARIZONA, ILLINOIS, Arkansas
1979	Wisconsin
1980	OKLAHOMA
1981	ALABAMA
1982	DELAWARE, FLORIDA
1983	
1984	New York
1985	NEW MEXICO, NORTH DAKOTA
1986	UTAH, VIRGINIA
1987	
1988	HAWAII, RHODE ISLAND, SOUTH CAROLINA

<u>States Adopting</u>
42 MODEL LEGISLATION
8 Related Legislation

Source: NAIC, January 1991

Adopted 1975

1921	NORTH CAROLINA, New Hampshire
1927	Kansas
1929	NEBRASKA
1931	RHODE ISLAND
1932	NEW JERSEY, TENNESSEE
1935	CALIFORNIA, INDIANA, PENNSYLVANIA
1939	MISSOURI
1949	CONNECTICUT
1956	Michigan
1957	OKLAHOMA, WEST VIRGINIA
1959	ARKANSAS, MONTANA
1960	GEORGIA
1961	IDAHO
1963	Illinois
1966	ALASKA, SOUTH DAKOTA
1967	OREGON
1968	VERMONT
1969	MAINE
1970	OHIO, Kentucky, Massachusetts
1971	ALABAMA, NEVADA
1973	WASHINGTON
1975	[Model Adopted]
1978	MICHIGAN
1979	Wisconsin
1981	COLORADO, MARYLAND
1982	FLORIDA, Iowa
1983	ARIZONA, NORTH DAKOTA
1984	NEW YORK
1985	NEW MEXICO, Utah
1986	VIRGINIA
1988	HAWAII, SOUTH CAROLINA

<u>States Adopting</u>
35 MODEL LEGISLATION
9 Related Legislation

Source: NAIC, January 1991

Model Law on Credit for Reinsurance

Adopted 1984

1930	Mississippi
1947	Washington
1948	Massachusetts
1951	TEXAS
1953	DELAWARE
1957	Oklahoma, West Virginia
1958	Louisiana
1959	MONTANA, Arkansas, Florida, Ohio
1960	Georgia
1961	Arizona, California, Idaho
1963	Maryland
1965	Illinois, Kansas
1966	Alaska, South Dakota
1967	Minnesota, Oregon
1970	KENTUCKY
1971	ALABAMA, Nevada
1975	Pennsylvania
1979	Colorado
1983	Indiana, North Dakota, Wyoming
1984	New York [Model Adopted]
1985	MAINE, NEBRASKA, NORTH CAROLINA, TENNESSEE, UTAH, New Mexico, Rhode Island
1986	VERMONT, NEW HAMPSHIRE, Virginia
1988	Hawaii
1990	CONNECTICUT, MISSOURI

States Adopting
14 MODEL LEGISLATION
31 Related Legislation

Source: NAIC, January 1991

Model Risk Retention Act
Adopted 1983

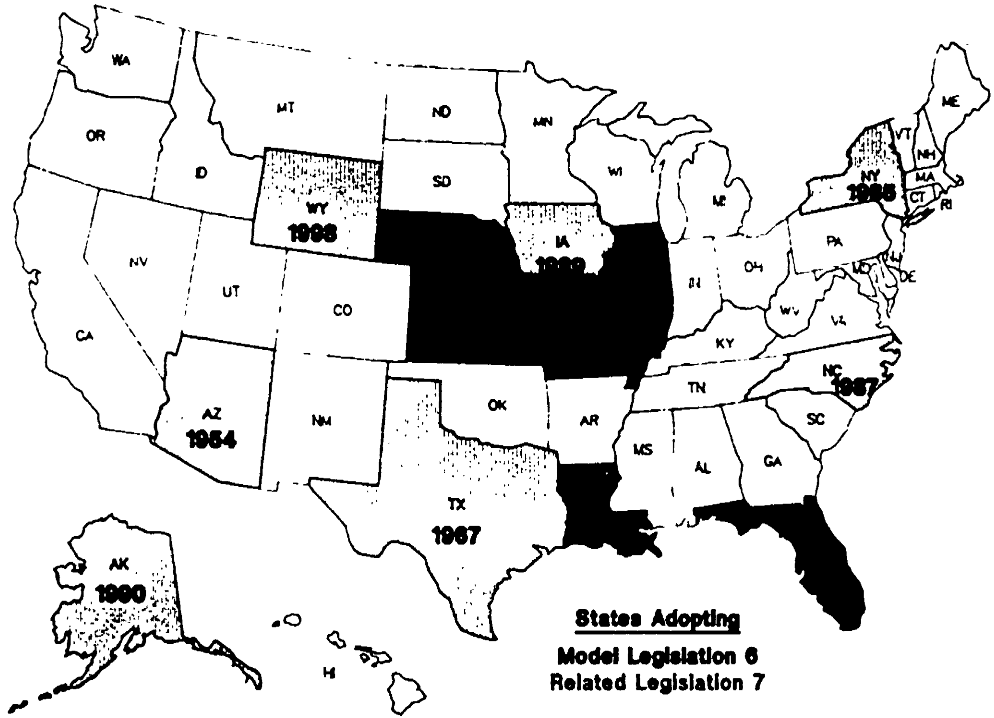
1963	Colorado
1981	Vermont
1983	TEXAS [Model Adopted]
1984	
1985	Delaware
1986	KANSAS, KENTUCKY, MAINE, NORTH CAROLINA
1987	LOUISIANA, FLORIDA, ARKANSAS, ARIZONA, CONNECTICUT, GEORGIA, HAWAII, ILLINOIS, IDAHO, MARYLAND, MINNESOTA, MONTANA, NEBRASKA, WEST VIRGINIA, VIRGINIA, OREGON, OKLAHOMA, NORTH DAKOTA, SOUTH DAKOTA, WASHINGTON, WYOMING, Tennessee
1988	INDIANA, IOWA, MISSISSIPPI, SOUTH CAROLINA, NEW YORK, NEW HAMPSHIRE, NEW MEXICO, Rhode Island, Wisconsin
1989	MISSOURI, MICHIGAN, OHIO, NEW JERSEY, Alaska

States Adopting
37 MODEL LEGISLATION
7 Related Legislation

Source: NAIC, January 1991

Managing General Agents Act

Adopted 1990



305

1. DEFINE STANDARDS AND COMMISSIONERS AUTHORITY FOR COMPANIES DEEMED TO BE IN HAZARDOUS FINANCIAL CONDITION
Authorizes Commissioner to take necessary corrective action, or cease and desist certain practices, which could place the insurance company in a hazardous financial condition.

2. CRIMINAL SANCTIONS FOR FAILURE TO REPORT IMPAIRMENT
Provides criminal penalty for failure of the CEO of an insurer to immediately notify the Commissioner of an impairment with the insurer.

3. LIFE REINSURANCE AGREEMENTS
Provides that no credit for reinsurance shall be taken, if the principal purpose for entering such reinsurance agreement is producing significant surplus aid for the ceding insurer.

4. P/C POLICY SIMPLIFICATION
Establishes minimum language and format standards to make property and casualty policies easier to read.

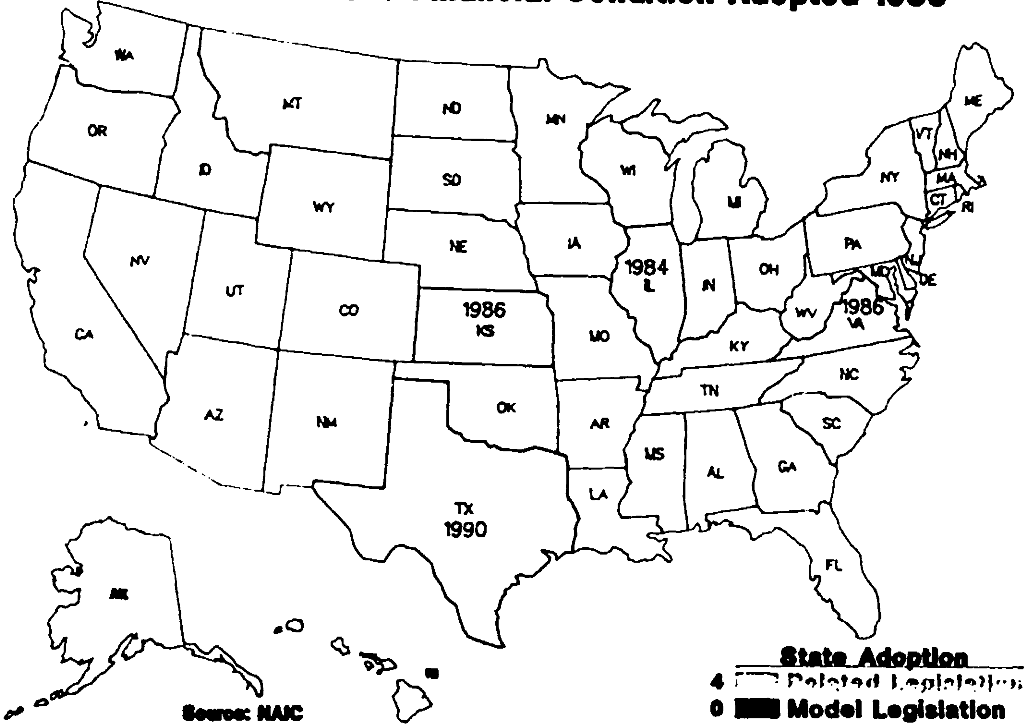
5. STATE INSURANCE DEPARTMENT FUNDING
Creates in the State Treasury an Insurance Regulatory Trust Fund which shall receive all payments from Filing, License and Miscellaneous Fees, Insurer Examination Charges, Trust Fund Investments, and Retaliatory Fees imposed by the Commissioner. The monies in the Trust Fund shall be appropriated only for use by the Insurance Department.

6. BUSINESS TRANSACTED WITH PRODUCER CONTROLLED P/C INSURER
Requires disclosure of the relationship between the producer or broker and the insurer, including disclosure to the Commissioner of the amount of commission paid to the producer or broker annually. In the event of an insolvency, where the Commissioner finds a violation of this Act contributed to the insolvency, the controlling producer must reimburse the guaranty fund for losses attributable to business written by that producer.

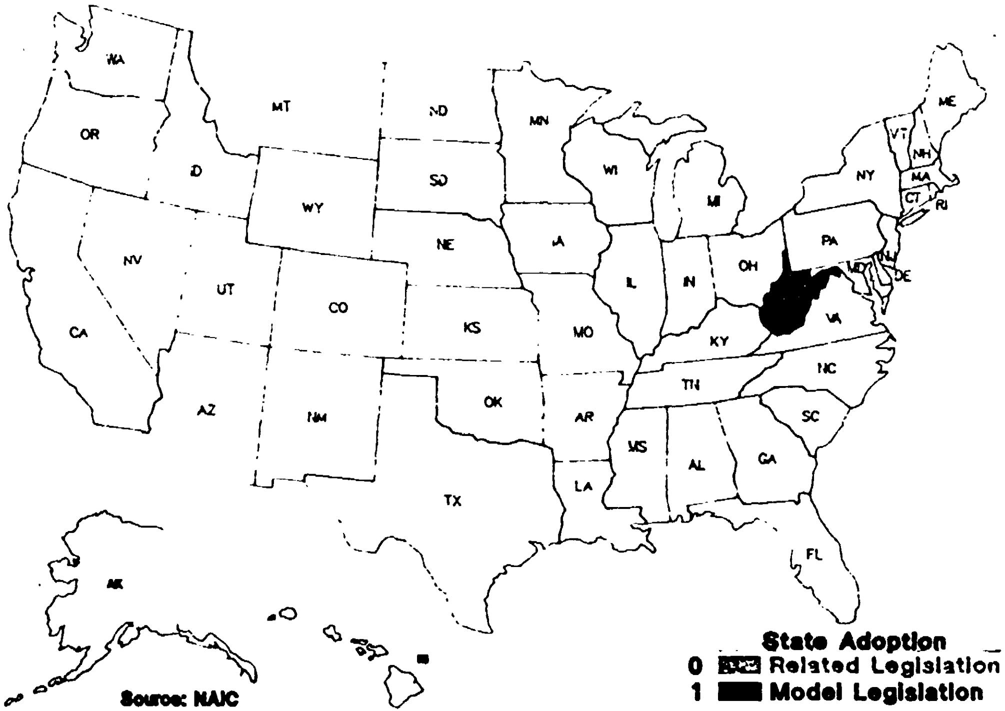
7. INSURANCE INFORMATION AND PRIVACY PROTECTION
Establishes standards for the collection, use and disclosure of information gathered in connection with insurance transactions by insurance institutions, agents or insurance-supported organizations. Attempts to balance the need for information by those conducting the business of insurance, and the public's need for fairness in insurance information practices.

8. ADMINISTRATIVE SUPERVISION
Insurers may be subject to administrative supervision by the Commissioner, for fraudulent conduct, failure to comply with the insurance code, exceeding its powers granted under certificate of authority, or if its continuance in business would be hazardous to the public.

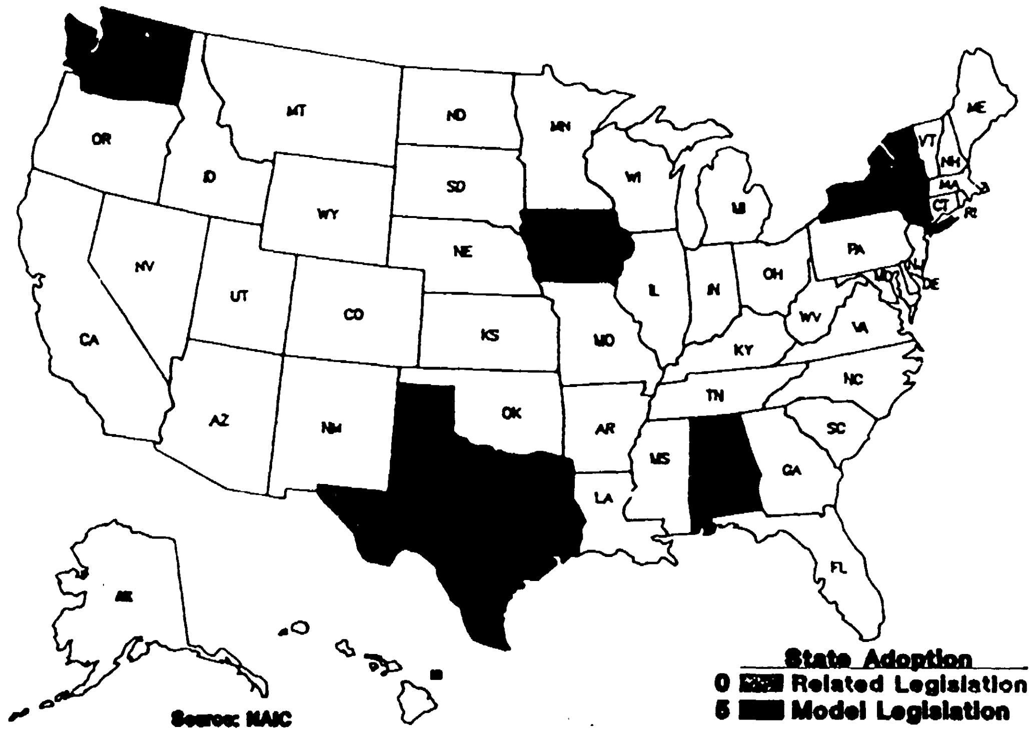
Model Regulation to Define Standards and Commissioners Authority for Companies Deemed to be in Hazardous Financial Condition Adopted 1985



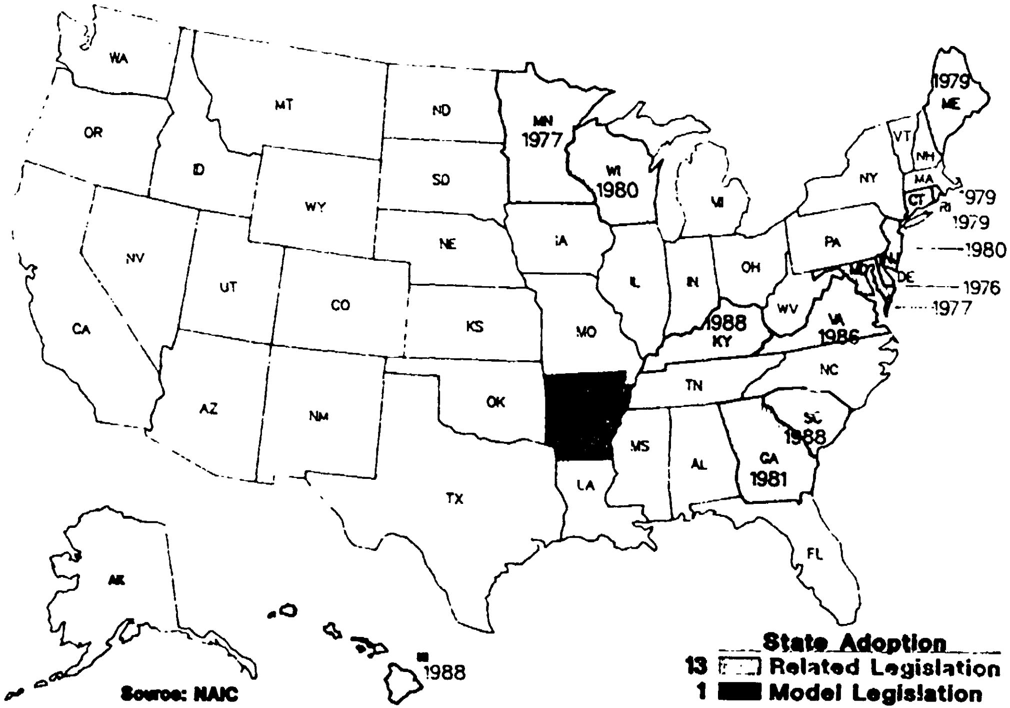
Criminal Sanctions for Failure to Report Impairment
Model Bill Adopted 1973



Model Regulation Life Reinsurance Agreements Adopted 1986

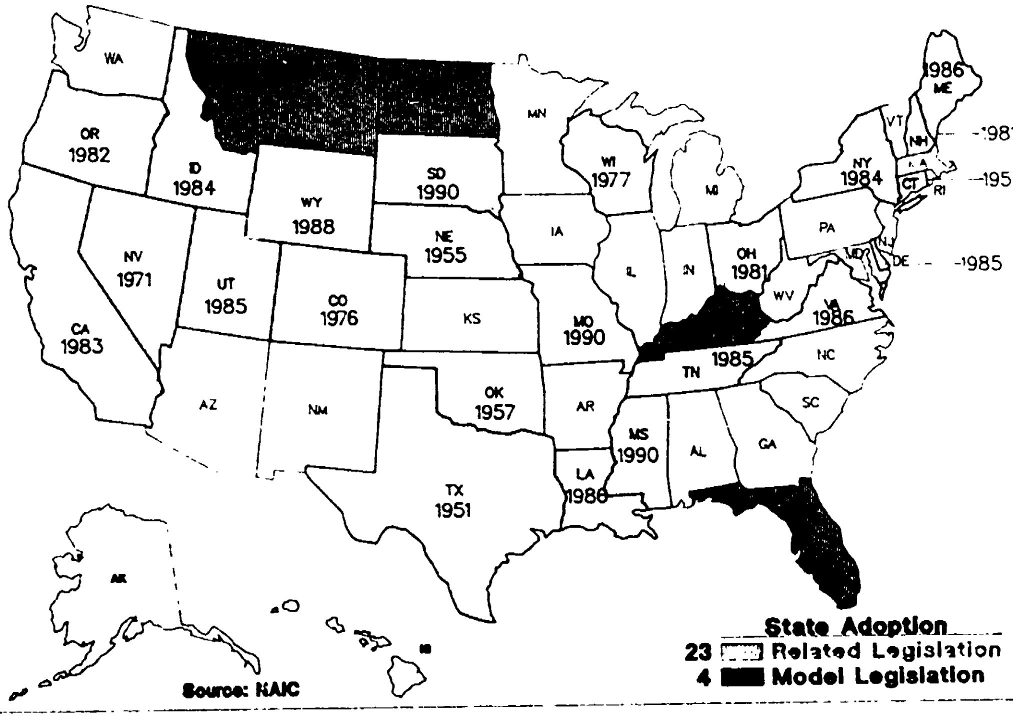


Property and Casualty Insurance Policy Simplification Model Act Adopted 1980

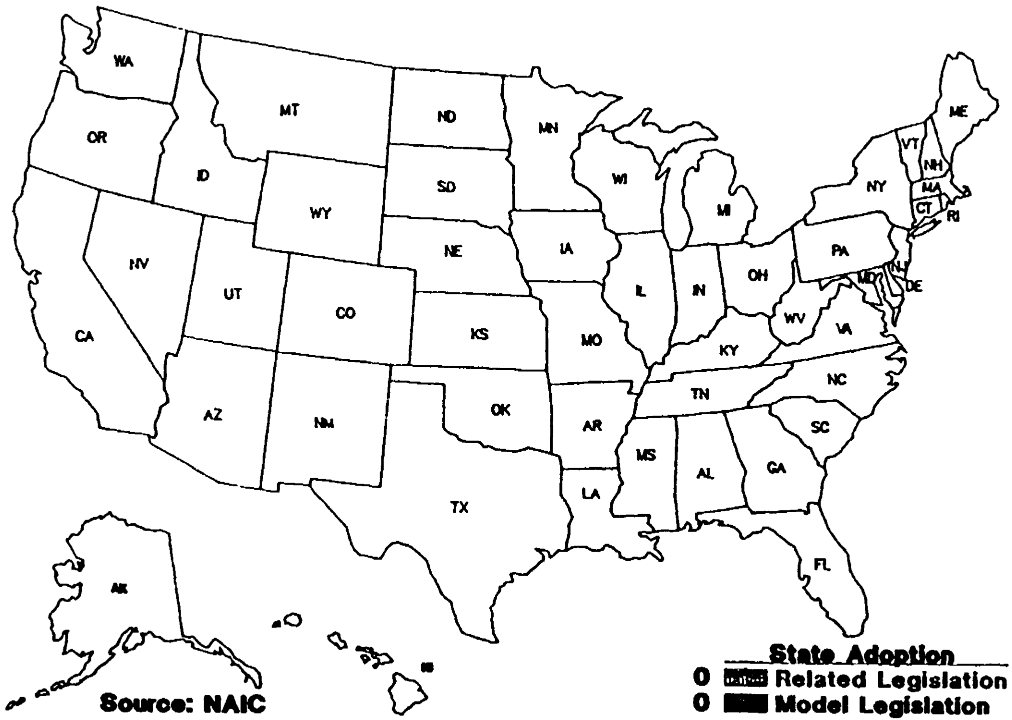


310

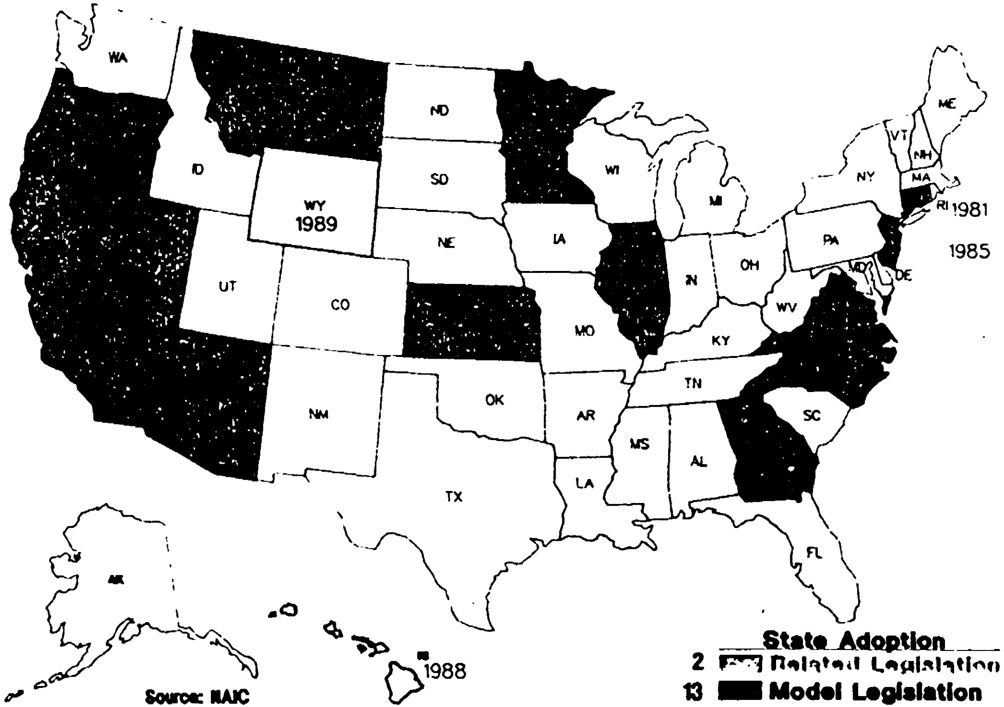
Model State Insurace Department Funding Bill Adopted 1983



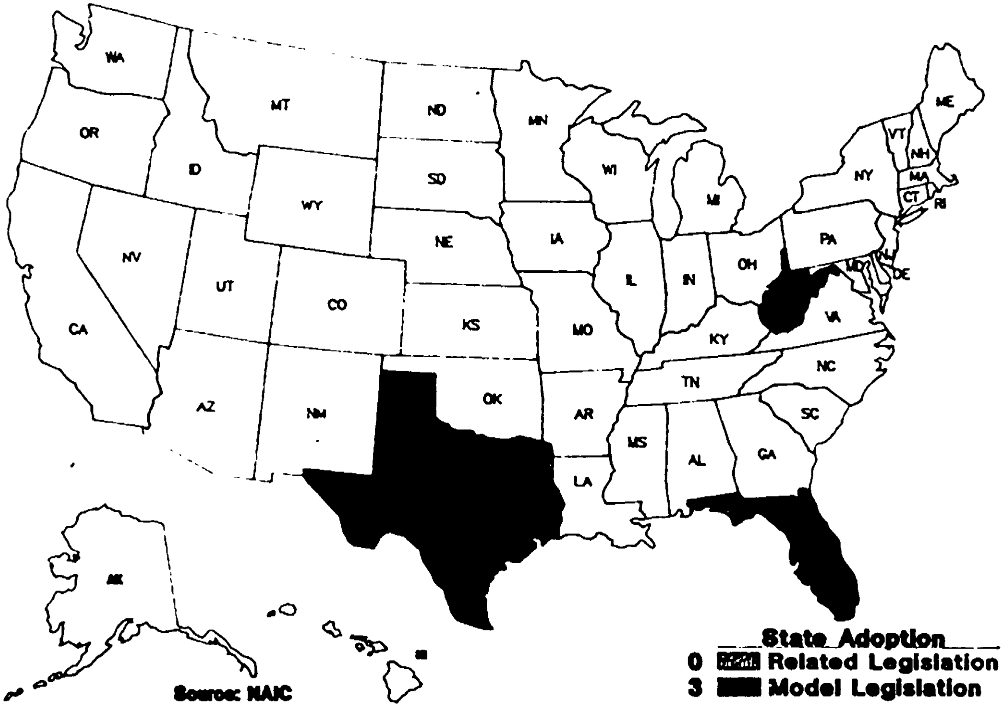
Business Transacted with Producer Controlled Property Casualty Insurer Act Adopted 1989



NAIC Insurance Information and Privacy Protection Act
Adopted 1980



Administrative Supervision Model Act Adopted 1990



OTHER NAIC MODEL LAWS

MODEL	YEAR ADOPTED	# OF STATES ADOPTING	# OF STATES ADOPTING RELATED LEGISLATION
AGENTS/BROKERS/PRODUCERS			
Agents and Brokers Licensing Act	1973	4	42
Agents Continuing Education Model Regulation	1978	7	29
Single License Procedure Model Act	1988	0	5
ANNUITIES/VARIABLE CONTRACTS			
Interest-Indexed Annuity Contracts Model Regulation	1988	0	0
Model Annuity and Deposit Fund Disclosure Regulation	1978	4	5
Model Variable Annuity Regulation	1975	23	12
Model Guaranteed Annuity Regulation	1985	1	2
Model Variable Contract Law	1970	33	16
Variable Life Insurance Model Regulation	1974	31	10
COMPANY ORGANIZATION, MANAGEMENT, SECURITIES			
Uniform Deposit Law	1953	2	47
Organization and Ownership of New Insurance Companies	1959	0	49

MODEL	YEAR ADOPTED	# OF STATES ADOPTING	# OF STATES ADOPTING RELATED LEGISLATION
Redomestication Model Bill	1980	22	6
Model Indemnity Contracts Act	1912	11	34
CREDIT INSURANCE			
Credit Life Insurance and Credit Accident and Health Insurance Model Act	1958	38	8
Credit Life and Credit Accident and Health Insurance Model Regulation	1960	13	34
INSIDER TRADING AND PROXIES			
An Act Concerning Insider Trading of Domestic Stock Insurance Company Equity Securities	1965	48	2
Regulations Adopted Pursuant to an Act Concerning the Insider Trading of Domestic Stock Insurance Company Equity Securities	1966	31	3
Regulation Regarding Proxies, Consents, and Authorizations of Domestic Stock Insurers	1965	44	2
INSOLVENCY			
State Post-Assessment Property and Liability Insurance Guaranty Association Model Plan of Operation	1970	3	2

MODEL	YEAR ADOPTED	# OF STATES ADOPTING	# OF STATES ADOPTING RELATED LEGISLATION
LIFE INSURANCE			
Group Life Insurance Definition and Group Life Insurance Standard Provisions Model Act	1917	38	19
Universal Life Insurance Model Regulation	1984	11	1
Modified Guaranteed Life Insurance Regulation	1986	1	1
Model Policy Loan Interest Rate Bill	1981	45	4
Industrial Life Insurance Model Bill	1983	13	11
Replacement of Life Insurance and Annuities Model Regulation	1970	38	4
Accelerated Benefits Guideline	1990	1	9
LONG-TERM CARE INSURANCE			
Long-Term Care Insurance Model Act	1987	37	10
Long-Term Care Insurance Model Regulation	1988	22	7
MISCELLANEOUS			
Model Insurance Fraud Statute	1980	6	16
Model Legislation Creating a Fraud Unit in a State Department of Insurance	1980	1	4

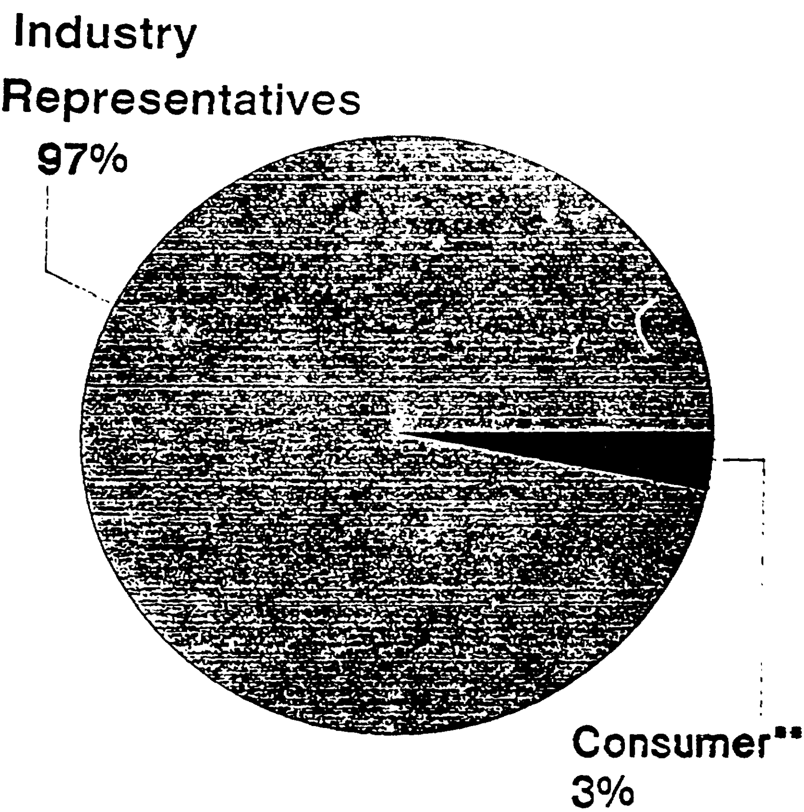
Model Immunity Act	1983	15	10
PROPERTY AND CASUALTY INSURANCE			
Property Insurance Declination, Termination and Disclosure Model Act	1979	5	22

MODEL	YEAR ADOPTED	# OF STATES ADOPTING	# OF STATES ADOPTING RELATED LEGISLATION
NAIC Automobile Insurance Declination, Termination and Disclosure Model Act	1980	1	45
Personal Lines Property and Casualty Insurance Policy Simplification Model Regulation	1980	7	8
Non-personal Lines Property and Casualty Insurance Policy Simplification Model Regulation	1981	1	2
Group Personal Lines Property and Casualty Insurance Model Act	1987	0	7
PROPERTY AND CASUALTY INSURANCE RATING LAWS			
Property and Liability Model Alternative Competitive Pricing and Appropriate Support Systems Act	1981	36	13
REINSURANCE			
Model Non-Admitted Insurance Act	1983	0	28

MODEL	YEAR ADOPTED	# OF STATES ADOPTING	# OF STATES ADOPTING RELATED LEGISLATION
Reinsurance: A Model Act for the Regulation of Reserves Ceded to Non-Admitted Reinsurers	1977	1	33
Model Surplus Lines Law	1983	7	36
Minimum Surplus as Regards Policyholders to Assume Property or Casualty Reinsurance	1989	0	0
STANDARD NON-FORFEITURE AND VALUATION			
Standard Non-Forfeiture Law for Individual Deferred Annuities	1977	44	0
Standard Non-Forfeiture Law for	1942	49	0
UNAUTHORIZED INSURANCE			
Unauthorized Insurers False Advertising Process Act	1960	17	7
Unauthorized Insurers Model Statute	1969	26	9
Unauthorized Insurers Process Act	1949	41	8
UNFAIR TRADE PRACTICES			
Unfair Trade Practices Act	1947	45	4
Model Regulation for Complaint Records to be Maintained Pursuant to the NAIC Unfair Trade Practices Act	1973	10	2

MODEL	YEAR ADOPTED	# OF STATES ADOPTING	# OF STATES ADOPTING RELATED LEGISLATION
Model Regulation on Unfair Discrimination in Life and Health Insurance on the Basis of Physical or Mental Impairment	1979	10	14
Model Regulation on Unfair Discrimination on the Basis of Blindness or Partial Blindness	1978	35	7
After Market Parts Model Regulation	1987	15	4
Unfair Claims Settlement Practices Act	1990	43	2
Unfair Property/Casualty Claims Settlement Practices Model Regulation	1976	19	8
WORKERS' COMPENSATION			
Alternative Model Workers' Compensation Competitive Rating Act	1983	3	12
Private Employers Workers' Compensation Group Self-Insurance Model Act	1984	2	11
Public Employer Workers' Compensation Group Self-Insurance Model Act	1984	0	6

Composition of Advisory Committees*



*Based on data provided by NAIC
**Includes Industry Analyst Joseph Belth

ATTACHMENT SIX

RESOLUTION

WHEREAS, it is the responsibility of State Insurance Regulators to represent the interests of the insurance-consuming public and the regulators have solicited and welcomed consumer participation at all times to assist in fulfilling this responsibility; and

WHEREAS, it is the objective of the National Association of Insurance Commissioners to assist the state regulators in fulfilling their responsibilities to the insurance-consuming public; and

WHEREAS, the NAIC has continuously encouraged participation by interested representatives of consumer groups in activities of the NAIC for a number of years including the appointment of consumers to advisory committees; solicitation of consumer presentations at Executive Committee and key task force meetings; waiver of registration fees for annual and zone meetings; and

WHEREAS, the NAIC has met with representatives of various organizations, including the American Diabetes Association and the National Federation of the Blind, in an effort to assure fair insurance coverage for all groups; and

WHEREAS, the NAIC has assisted consumer representatives in exploring various avenues of obtaining funding for consumer participants; and

NOW THEREFORE BE IT RESOLVED, that the policy of the National Association of Insurance Commissioners will continue to be to encourage participation by consumer representatives in the activities of the NAIC; and it will continue to be the policy not to fund travel expenses for representatives of consumer groups to attend NAIC meetings.

ADVISORY COMMITTEES IN 1991[1]

Total # of Advisory Committees	-	30
Total # of Industry Representatives	-	383
Total # of Consumer Representatives	-	14 (Serving on only 4 committees)
Total # of Advisory Committees with no membership listed	-	2

Sale of Future Revenue/Securitization of Nonadmitted or Unrecorded Assets Advisory Committee

No Description Available

Industry Representatives	Consumer Representatives
20	0

Emerging Issues Advisory Committee

To assist Emerging Issues Working Group in identifying and addressing emerging statutory insurance accounting issues.

Industry Representatives	Consumer Representatives
8	0

[1] As of 4/1/91. Compiled from data provided by the NAIC.

Premium Deficiency Reserve Advisory Committee

No Description Available

Industry Representatives	Consumer Representatives
12	0

Property & Casualty Reinsurance Advisory Committee

To provide reference and technical expertise on matters before the Study Group.

Industry Representatives	Consumer Representatives
15	0

Reinsurance Advisory Committee

To assist regulators in drafting proposed changes to the Annual Statement Blank regarding reinsurance disclosure.

Industry Representatives	Consumer Representatives
17	0

Schedule D Advisory Committee

No Description Available

Industry Representatives	Consumer Representatives
7	0

Insurance Expense Exhibit Advisory Committee

To provide input to the Working Group as respects its analysis and development of revisions to the Insurance Expenses Exhibit.

Industry Representatives	Consumer Representatives
17	0

Bar Code Advisory Committee

No Description Available

Industry Representatives	Consumer Representatives
7	0

Biographical Data Form Advisory Committee

No Description Available

Industry Representatives	Consumer Representatives
5	0

Life & Health Financial Ratios Advisory Committee

To assist the regulatory groups in monitoring the effectiveness of the IRIS Ratios.

Industry Representatives	Consumer Representatives
15	0

Property & Casualty Financial Ratios Advisory Committee

No Description Available

Industry Representatives	Consumer Representatives
11	0

Risk Based Capital Advisory Committee

No Description Available

Industry Representatives	Consumer Representatives
8	0

Life Risk Based Capital Advisory Committee

No Description Available

Industry Representatives	Consumer Representatives
16	0

Property & Casualty Risk Based Capital Advisory Committee

To furnish input on the development of a draft formula and model legislation.

Industry Representatives	Consumer Representatives
16	0

Financial Examiners Handbook Advisory Committee

To assist regulatory group in identifying suggested changes to the NAIC Financial Examiners Handbook.

Industry Representatives	Consumer Representatives
11	0

Product Development Advisory Committee Corporate-Owned Life Insurance

No Description Available

Industry Representatives	Consumer Representatives
4	0

Long Term Care Advisory Committee

No Description Available

Industry Representatives	Consumer Representatives
25	6

Long Term Care Technical Actuarial Advisory Committee

No Description Available

Industry Representatives	Consumer Representatives
15	1

Medicare Supplement Standardization Advisory Committee

To furnish comment to the Medicare Supplement and Other Limited Benefit Plans (B) Task Force on the development of standardized Medicare supplement policies pursuant to the Omnibus Budget Reconciliation Act of 1990.

Industry Representatives	Consumer Representatives
6	6

Uniform Filing Procedures Advisory Committee

No Description Available

Industry Representatives	Consumer Representatives
14	0

General Advisory Committee

No Description Available

Industry Representatives	Consumer Representatives
5	0

MGA/Reciprocals Advisory Committee

To offer comment generally to the working group on draft legislation.

Industry Representatives	Consumer Representatives

No Membership Listed

Assumption Reinsurance Advisory Committee

To provide assistance and technical expertise regarding the assumption of reinsurance as the Working Group drafts model law/regulation.

Industry Representatives	Consumer Representatives
13	1

Reinsurance Advisory Committee

To provide input on matters involving reinsurance before the Task Force.

Industry Representatives	Consumer Representatives
33	0

Casualty Actuarial (Technical) Advisory Committee

Determine necessity of revisions to Schedule P reserve lists and loss reserve discounting actuarial opinion.

Industry Representatives	Consumer Representatives
12	0

Nonforfeiture Law Advisory Committee

No Description Available

Industry Representatives	Consumer Representatives
13	0

Standing Technical Advisory Committee

No Description Available

Industry Representatives	Consumer Representatives
17	0

Reinsurance Advisory Committee

No Description Available

Industry Representatives	Consumer Representatives
20	0

MSVR Advisory Committee

To furnish input to the Mandatory Securities Valuation Reserve (MSVR) Study Group.

Industry Representatives	Consumer Representatives
1	0

Health Care Insurance Access Advisory Committee

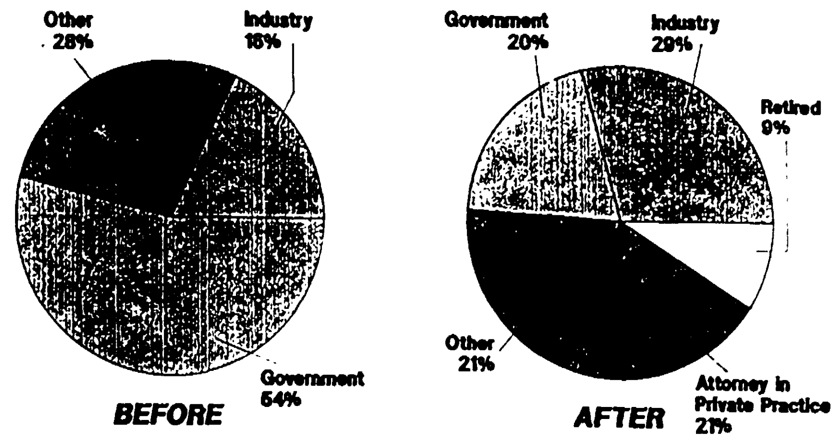
To assist the Health Care Access Working Group in developing a mechanism addressing availability of health insurance.

Industry Representatives	Consumer Representatives

No Membership Listed

SENATE JUDICIARY SUBCOMMITTEE ON
ANTITRUST, MONOPOLIES AND BUSINESS RIGHTS

Occupational Background and Subsequent Employment of Past State Insurance Commissioner



Other Includes Attorney, Banker, College Professor, Computer Consultant, Securities Broker, Business Consultant, Partner: Peat Marwick

Other Includes Fund Raiser, Banker, College Professor, Unknown, Unemployed, Partner: Peat Marwick

Compiled from data provided by the NAIC.

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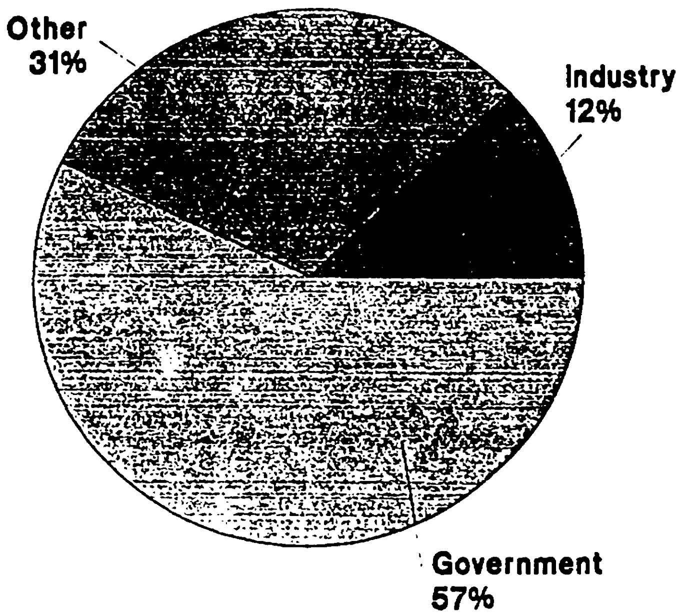
Occupation of Current Commissioner's Immediately Prior to Appointment

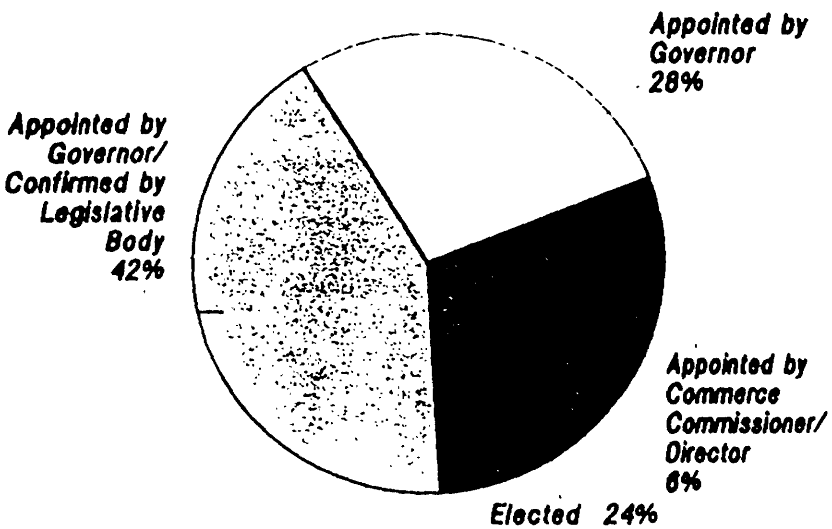


Other Includes: Attorney, College Professor, Real Estate Developer, Unknown, Business Consultant, High School Teacher

Compiled from data provided by the NAIC.

SENATE JUDICIARY SUBCOMMITTEE ON
ANTITRUST, MONOPOLIES AND BUSINESS RIGHTS

Selection Process for State Insurance Commissioner



APPOINTED BY GOVERNOR:
AL, AR, IN, KY, MA, NV, NM, PA, RI, SC, SD, TN, TX, VA

APPOINTED BY GOVERNOR/CONFIRMED BY LEGISLATIVE BODY:
AZ, CO, CT, ID, IL, IA, ME, MD, MI, MN, MO, NE, NH, NJ, NY, OH, UT, VT, WVA, WI, WY

ELECTED:
CA, DE, FL, GA, KS, LA, MS, MT, NC, ND, OK, WA

APPOINTED BY COMMERCE COMMISSIONER/DIRECTOR:
AK, HI, OR

Compiled from data provided by the NAIC.

Consumers Union

Publisher of Consumer Reports

November 20, 1990

Commissioner Earl Pomeroy
Department of Insurance
Capitol Building, Fifth Floor
Bismarck, North Dakota 58505

Dear Commissioner Pomeroy:

We are writing to express our concerns about the need for improved National Association of Insurance Commissioners procedures to ensure adequate consumer input into ongoing proceedings on Medicare supplement insurance and long-term care insurance. While we heartily applaud your own efforts to increase consumer input, there continues to be imbalance in industry and consumer involvement. The problem is severe, and needs your attention. Below are some of our concerns and recommendations.

Imbalance. Both the Medicare supplement and long-term care advisory committees are unbalanced, both "on paper," and even more dramatically "in effect," reflecting the inability of many consumer representatives to attend meetings that are out-of-town. Some (though not all) consumer representatives would be able to attend more meetings if the NAIC could pay travel expenses. We urge you to reconsider earlier proposals to do this. We also urge you to tap into the extensive expertise that is available through state counseling programs. Ideally, you could find six to ten states' equivalent of Bonnie Burns to advise you on these important issues.

One regrettable effect of the imbalance on the Long-Term Care Advisory Committee is the distribution of a "revised" document, intended to replace the NAIC's exposure draft, that was prepared by the HIAA and industry members of the Committee, with minimal (if any) consumer input. Not surprisingly, many key consumer protection measures were deleted. (Gail has written a separate letter to Susan Gallinger about substantive concerns in long-term care.)

With regard to Medicare supplement insurance, increased consumer input is not merely an option for the NAIC -- it's the law. As you know, P.L. 101-508 includes strong language requiring the NAIC to consult with issuers of Medicare supplement policies, consumer groups, Medicare beneficiaries, and other qualified individuals. The law specifies that **balanced representation** among the interested groups is to be achieved. The present system does not meet this requirement for balance.

Washington Office
Suite 520 2001 S Street Northwest Washington D C 20009 (202) 462-6262

Domination of Advisory Committees by Industry Interests. Too often, we find that despite our efforts to participate actively in the work of the advisory committees, the industry representatives control the work product. This problem has surfaced in the drafting of the consumer guide for long-term care insurance for Continuing Care Retirement Communities. Trudy's offer to help in the drafting of the consumer guide was rejected; instead industry representatives are drafting it. With less than two weeks before the proposed guide will be circulated to the NAIC, Trudy has not even been able to review the final draft.

Poor Communication. We are finding that the communication has not been very good. For example, we received only eight days notice of the November 9 long-term care advisory committee meeting. Even if these meetings are held nearby, it is often impossible to change prior commitments if notice is short. Representing individual company interests on advisory committees is an understandably high priority for most company representatives who serve on advisory committees. In contrast, our participation on these committees has to be juggled against many other professional commitments, hence advance notice is very important to us. In general, we find that too little paper comes our way about committee developments, and this limits our participation as well. Papers that are distributed at meetings we can't attend rarely get distributed to us.

Need for Impartiality. Gail has a number of concerns about the proposed consumer survey for Medicare supplement insurance simplification. Due to limited NAIC funds, companies may fund the survey. We are troubled by this, and by the likelihood that companies -- with huge financial interests in the outcome of the survey -- will have an inordinate amount of influence over the selection of the survey research firm, the design of the questionnaire, and the wording of the final report. The need for impartiality is great, and at this point we have no reason to be confident that the procedure or the results will be unbiased. Because of the need for unbiased pricing information (estimating the price implications of various standardized packages, for example), consumer representatives have been urging the NAIC to seek impartial expertise. We urge you to act on this recommendation.

The problems that we have encountered raise troubling questions about the inordinate influence that the insurance industry continues to wield in the regulatory process. We believe that this is an appropriate time for the NAIC to review its procedures involving consumer input into Advisory Committees, especially in light of the recent provision in the Budget Act calling for balanced input. Specific recommendations are:

-- Appoint a neutral chairman for the Medigap Advisory Committee, or appoint an additional consumer co-chair (possibly Jim Firman) to help increase consumer input to the Medicare supplement insurance advisory committee;

-- Revisit the issue of NAIC funding for travel expenses for consumer representatives;

-- Appoint a separate consumer subcommittee of the Medicare supplement insurance advisory committee;

-- Contact each state with a counseling program to explore whether the coordinator could recommend someone (possibly himself/herself) to serve on the long-term care and/or Medicare supplement insurance advisory committee(s);

-- Put all advisory committees on notice that the NAIC is considering how to increase the participation of consumer representatives. Each committee chair should be informed that it is not acceptable for meetings to be held in the absence of at least some consumer representation. Each committee chair should be held accountable and be questioned about what efforts were made to solicit consumer input into committee recommendations. Each committee chair should be requested to improve communication (including prompt notification of meetings) with consumer representatives on committees;.

-- Advisory committee chairs should be instructed not to make representations about "committee" positions unless consumer representatives are in agreement; and

-- Reconstitute advisory committees with an equal number of consumer and industry representatives, even if this means that the size of committees will decrease.

Thank you for considering these recommendations. We look forward to working with you on these important issues.

Sincerely,

Gail Shearer
Manager, Policy Analysis

Trudy Lieberman
Senior Editor

cc: Carole Olson Gates
Bonnie Burns
Lucia DiVenere
Jim Firman
Larry Kirsch
Steve Broebeck

Background material

ALABAMA	**Appointed by Governor**
Incumbent: (from 1988)	**Mike Weaver** Before: 1988 - Division Chief, AL Dept. of Economic and Community Affairs
1987-88:	**John S. Greeno** Before: Vice President, Reliance Insurance Co.; After: Retired
1986-87:	**Michael Debellis** Before: State Dept. of Commerce After: Consumer Services Division Supervisor, State Insurance Dept.
ALASKA:	**Appointed by Commissioner of the Dept. of Commerce and Economic Development, indefinite term**
Incumbent: (from 1990)	**David Walsh** Before: Private practice of law; Anchorage Assembly.
1988-89:	**Paul Roller** Before: Deputy Director, State Division of Insurance After: Running fund raising campaign for gubernatorial candidate Sturgurlewski
1985-88:	**John L. George** Before: Deputy Director, State Dept. of Insurance; Risk Manager for State After: Administrator for Alaska Municipal League Joint Insurance Association
ARIZONA	**Appointed by Governor, confirmed by Senate**
Incumbent: (from 1988)	**Susan Gallinger** Before: Deputy Director, Dept. of Insurance
1988:	**Vern R. Pierson** Before: Branch Manager, Northbrook Property and Casualty After: Brokerage firm of Corroon and Black of AZ
1984-88:	**S. David Childers** Before: Risk Manager and Lead Attorney, Salt River Project After: Attorney - Storey & Ross, Phoenix, AZ

ARKANSAS	**Appointed by Governor**
Incumbent: (from 1991)	**Lee Douglass** Before: Deputy Insurance Commissioner
1988-90:	**Ron Taylor** Before: Deputy commissioner, State Dept. of Insurance; 1983-85, Asst. Commissioner of Finance; with Dept. of Insurance since 1979. After: Unemployed.
1985-88:	**Robert M. Eubanks, III** Before: Security Broker, Dabbs Sullivan (division of George Baum & Co. After: Attorney - Mitchell, Williams, Selig, Jackson & Tucker
CALIFORNIA	**Elected (as of Nov. 1989), term co-extensive with Governor**
Incumbent: (from 1990)	**John Garamendi** Before: Senate Majority Leader, 1984 to present; State Senate since 1976.
1986-90:	**Roxani Gillespie** Before: 1983-86, Deputy Insurance Commissioner, State Insurance Department. After: Unknown.

1984-86:	**Bruce Bunner** Before: Partner, Peat, Marwick, Mitchell & Co., Los Angeles, CA After: Partner, Peat, Marwick, Mitchell & Co., Los Angeles, CA
COLORADO	**Appointed by Governor, confirmed by Senate**
Incumbent: (from 1989)	**Joann Hill** Before: Audit Manager, Colorado State Audit Office
1985-89:	**John Kezer** Before: With State of Colorado at least seven years prior to becoming commissioner; private law practice before that. After: Private law practice
CONNECTICUT	**Appointed by Governor, confirmed by either house, four-year term**
Incumbent: (From 1991)	**Robert Googins** Before: Director of Insurance Law Center, University of Connecticut School of Law
1988-91:	**Peter F. Kelly** Before: Served as both Chief, Examinations Division and Director, Financial and Regulated Affairs, State Insur. Dept.; with Insurance Dept. since 1954.
1983-88:	**Peter W. Gillies** Before: Deputy State Attorney General; served in Attorney General's office eight years. After: Attorney, LeBeouf, Lieby, Lamb & MacRae, Hartford, CT
DELAWARE	**Elected, four-year term**
Incumbent: (from 1985)	**David Levinson** (serving second term) Before: Real estate developer, builder, lawyer
DISTRICT OF COLUMBIA Acting:	**Appointed by Mayor, indefinite term** **Patrick Kelly** Before: D.C. Department of Insurance
1983-91	**Margurite Stokes** Before: 1981-83, Recorder of Deeds, District of Columbia After: Retired.

FLORIDA	**Elected, four-year term**
Incumbent: (from 1989)	**Tom Gallagher** Before: Florida Dept. of Professional Regulation; 1974-86, Florida House of Representatives; owner, mortgage software business.
1980-88:	**William D. Gunter** Before: Teacher, investment banker, insurance agent; 1972, elected Congressman, U.S. House of Representatives; 1966, elected State Senator. After: Senior Vice President, Rogers-Atkins Insurance Inc., and CEO, Bill Gunter & Assoc. -- consulting and government relations.
GEORGIA	**Elected, four-year term**
Incumbent: (from 1990)	**Tim Ryles** Before: Communications Workers of America; Georgia Insurance Dept.
1986-90:	**Warren D. Evans** Before: 1975-86, Representative, Georgia General Assembly: attorney. After: Retired.
1970-86:	**Johnnie L. Caldwell** Before: attorney, 20 years. After: Attorney.
HAWAII	**Appointed by Director of Commerce and Consumer Affairs, confirmed by Governor, serves at the pleasure of the Director**
Incumbent: (from 1987)	**Robin Campaniano** Before: State Dept. of Commerce; Counsel, Honolulu law firm (White & Tom);District Counsel, Honolulu office of Small Business Administration, 1980-86.
1985-86:	**Mario R. Ramil** Before: State employee After: Director, State Dept. of Labor
IDAHO	**Appointed by Governor, confirmed by Senate, serves at the pleasure of the Governor**
Incumbent:	**George Newmeyer** Before: Deputy Director, Idaho Department of Transportation

1988-1991	**Anthony J. Fagiano** Before: 1986-87, Administrator of Regulation and Actuary, state Insurance Department. After: Contract Actuary, Idaho Insurance Department.
1984-87:	**Wayne L. Soward** Before: Administrator of Regulations, State Dept. of Insurance; also, Supervisor, Public Services Consumer Protection Division. After: Deputy Liquidator, Pacific Marine Insurance Co. of Washington and Alaska
ILLINOIS	**Appointed by Governor, confirmed by Senate**
Acting:	**James Schacht** Before: Deputy Director, Department of Insurance
1989-91	**Zachary Stamp** Before: Director of Legislative Affairs in Governor's Office since 1986; General Counsel for Senate Republican staff 1983-85. After: Private practice of law.
1983-89:	**John E. Washburn** Before: Director of Legislative Affairs for governor; Senate staff budget analyst; Dept. of Business and Economic Dev. Ofc. of Minority Business. NAIC President in 1988. After: Deputy Governor, State of Illinois
INDIANA	**Appointed by Governor, four-year term.**
Incumbent: (from 1989)	**John J. Dillon, III** Before: Member of J.W. Flynn, Indianapolis independent insurance agency; exec. vp and CEO of Rockwood Insurance Co. of Indiana
1985-88:	**Harry E. Eakin** Before: Auditor, Marion County, IN After: Dept. of Public Safety, Indianapolis
IOWA	**Appointed by Governor and confirmed by Senate, four-year term**
Incumbent: (from 1990)	**David Lyons** Before: First Deputy Commissioner; Legal counsel, Iowa legislature.

1987-90:	**William D. Hager** Before: 1983-86, Attorney specializing in insurance law and employee benefits; general counsel and chief lobbyist for American Academy of Actuaries, Washington, DC. After: President, NCCI.
KANSAS	**Elected, four-year term**
Incumbent: (from 1990)	**Ron Todd** Before: Assistant Commissioner, KS Dept. of Insurance, 1971-90; with KS Dept. of Insurance since 1956.
1970-1990:	**Fletcher Bell** Before: Assistant Insurance Commissioner. NAIC president prior to 1979. After: Retired
KENTUCKY	**Appointed by Governor**
Incumbent: (from 1990)	**Elizabeth Wright** Before: Deputy Commissioner of KY Dept. of Insurance.
1989	**Leroy L. Morgan** Before: 1982-89, Director, State Risk & Insurance Division.
1984-89:	**Gil McCarty** Before: Director, Life and Health Divison, State Insurance Dept. (joined Dept. in 1967). After: Vice President, Physicians Insurance Exchange Mutual
LOUISIANA	**Elected, four year term**
Acting:	**Hunter P. Wagner, Jr.** Before: Unknown
1988-1991	**Douglas D. Green** Before: Computer Consultant -- owned private software company. After: Unemployed.
1972-88:	**Sherman A. Bernard** Before: 1963-65, Exec. Director of Jefferson Parish Housing Authority.
MAINE	**Appointed by Governor, confirmed by appropriate legislative committee and Senate, five year term**

Incumbent: (from 1987)	**Joseph E. Edwards, CPCU, CLU** Before: President, Avalon Computers, Lexington, MA; Exec. vp, Laub Group, Inc., Milwaukee, WI. Is also an Employee Benefits Specialist and Chartered Financial Consultant.
1979-87:	**Theodore T. Briggs, CPCU** Before: Deputy Superintendent for State Insurance Bureau; with Bureau since 1966. After: Medical Mutual Insurance Co.
<u>**MARYLAND**</u>	<u>**Appointed by Governor and Secretary of Licensing and Regulation, confirmed by Senate, serves at the pleasure of the Governor and the Secretary.**</u>
Incumbent: (from 1989)	**John A. Donaho** Before: National and international government and business consultant.
1988-89:	**E. Susan Kellogg** Before: 1986-88, Marketing Director, Metropolitan Life Insurance Co. After: Faculty at Hood College; industry consultant.
1984-87:	**Edward J. Muhl** Before: Deputy Insurance Commissioner for MD; ten years as Director of Claims, Auto Insurance Fund. President of NAIC, 1987. After: Royal Insurance Companies, Raleigh, NC
<u>**MASSACHUSETTS**</u>	<u>**Appointed by Governor, term co-terminous with Governor**</u>
Incumbent:	(vacant)
1989-90:	**Timothy H. Gailey** Before: Asst. Secretary of Consumer Affairs and Business Regulation; 1974-85, Attorney, Hale & Dorr.
1987-89:	**Roger Singer** Before: First Deputy Commissioner; Asst. Secretary of Consumer Affairs; Asst. Attorney General in Consumer Protection. After: General Counsel, Commercial Union Insurance Co.
1985-87:	**Peter Hiam** Before: Chairman, MA Rate Setting Commission; Staff Director, Boston Finance Commission; also General Counsel to Health Dept.

After:

MICHIGAN	**Appointed by Governor, confirmed by Senate, four-year term**
Incumbent: (from 1989)	**Dominic D'Annunzio** (acting) Before: Deputy Commissioner's Office of Financial Analysis and Examinations
1985-88:	**Herman W. Coleman** Before: Asst to the Secretary of U.S. Dept. of Education. After: American Automobile Association, Dearborn, MI.
MINNESOTA	**Appointed by Governor, confirmed by Senate, indefinite term (Note: Is "Commissioner of Commerce", not Commissioner of Insurance. In June 1983, Departments of Banking, Insurance and Securities & Real Estate were consolidated into one department. Hatch chaired the commission responsible for this consolidation.)**
Incumbent: (from 1991)	**Bert J. McKasy** Before: Chief of Staff, Sen. Dave Durenberger (R - MN).
1989-90:	**Tom Borman** Before: Attorney, Minneapolis law firm specializing in real estate development and finance. After: Private practice of law.
1983-89:	**Michael A. Hatch** Before: State Chair of Democrat Farmer-Labor Party; 1973-80, private attorney.
MISSISSIPPI	**Elected, four year term**
Incumbent: (from 1976)	**George Dale** Before: Teacher, coach, high school principal
MISSOURI	**Appointed by Governor, confirmed by Senate.**
Incumbent: (from 1989)	**Lewis E. Melahn** Before: CEO, Melahn Insurance Agency, Mexico, MO
1986-88:	**Lewis R. Crist** Before: Branch Manager, CNA Insurance Co. After: St. Louis Bar Plan Insurance Co.
1981-85:	**C. Donald Ainsworth**

	Before: Managing vp, Alexander & Alexander After: Executive vp, Safety Mutual Casualty Corp.
MONTANA	**Elected, four-year term (as State Auditor & Commissioner)**
Incumbent: (from 1984)	**Andrea "Andy" Bennett** Before: Three terms in MT House of Representatives
1962-85:	**E. V. Omholt** (No information available.)
NEBRASKA	**Appointed by Governor, confirmed by Senate, serves at pleasure of the Governor**
Incumbent: (from 1987)	**William H. McCartney** Before: 1986-87, Account Executive, Alexander & Alexander, Omaha, NE; 1981-86, Enron Corp.; 1976-81, Attorney, Guarantee Mutual Life Co., Omaha, NE.
1985-87:	**Michael J. Dugan** Before: Attorney, private practice. After: Attorney with Kennedy, Holland, DeLacy & Svoboda.
NEVADA	**Appointed by Director of Commerce, term indefinite**
Acting:	**Teresa Rankin** Before: Chief Insurance Asst., Nevada Department
1990-91:	**Al Iuppa** Before: Deputy Insurance Commissioner After: Unemployed.
1984-90:	**David A. Gates** Before: Joined NV Insur. Dept. in 1983 as Chief Assistant Commissioner; prior to 1983, Assistant Counsel, National Association of Independent Insurers. President of NAIC, 1989. After: Independent insurance consultant.
NEW HAMPSHIRE	**Appointed by Governor, confirmed by Council, five-year term**
Incumbent: (from 1983)	**Louis E. Bergeron** Before: CEO, Bergeron Agency, Inc., Concord, NH; served in NH Senate 1974-82.

NEW JERSEY	**Appointed by Governor, confirmed by Senate.**
Incumbent: (from 1990)	**Samuel F. Fortunato** Before: Vice president, Metropolitan Insurance Co.
1986-90:	**Kenneth D. Merin** Before: Previously served as Commissioner of Insurance; also, Director, State Office of Policy and Planning. After: Kroll and Tract.
1985-86:	**Hazel F. Gluck** Before: Director, State Lottery; member, NJ State Assembly; Director of Consumer Affairs, Ocean City, NJ. After: Commissioner, Dept. of Transportation.
NEW MEXICO	**Appointed by State Corporation Commission, term indefinite.**
Incumbent: (from 1988)	**Fabian Chavez, Jr.** Before: Economic development consultant providing advice and assistance in the development and implementation of programs in various private sectors and governmental areas. Two years in NM House of Representatives, eight in Senate.
1981-88:	**Vicente B. Jasso** Before: With State Insurance Dept. since 1955, Deputy Insurance Superintendent 1964-81. After: Insurance consultant, Santa Fe, NM.
NEW YORK	**Appointed by Governor, confirmed by Senate, four-year term.**
Incumbent: (from 1990)	**Salvatore R. Curiale** Before: First Deputy Superintendent, 1984-90.
1983-90:	**James P. Corcoran** Before: Vice President for Government Relations, Prudential Insurance Co. of America; Assistant General Counsel, Mutual Insurance Co. of NY (MONY). After: Attorney.
NORTH CAROLINA	**Elected, four-year term.**

Incumbent: (from 1985)	**James E. Long** Before: 1980-85, both Chairman of NC Property Tax Commission and Counsel to the Speaker of the State House of Representatives. Served three terms as state legislator. President, NAIC, 1991.
NORTH DAKOTA	Elected, four-year term
Incumbent: (from 1985)	**Earl R. Pomeroy** Before: Two terms in State House of Representatives, while an attorney in private practice. President, NAIC, 1990.
OHIO	Appointed by Governor, confirmed by Senate, serves at the pleasure of the Governor.
Incumbent: (will begin 3/91)	**Harold Duryee** Before: Federal insurance administrator.
1983-91:	**George Fabe** Before: Criminal lawyer; also served as arbitrator with American Arbitration Association.
OKLAHOMA	Elected, four-year term
Incumbent: (from 1975)	**Gerald Grimes** Before: 1973-78, Deputy Commissioner, State Insurance Dept.; with State Insurance Dept. since 1970.
OREGON	Appointed by Director of Commerce, confirmed by Governor
Incumbent:	**Gary K. Weeks** Before: Deputy Director, Department of Human Resources
1987-90:	**Theodore R. Kulongoski** Before: Partner, Kulongoski, Durham, Drummonds & Columbo, Portland, OR; 1977-83, member of state senate After: Retired.
1981-86:	**Josephine Driscoll** Before: Oregon Asst. Commissioner of Insurance - three months; 1966-81, with MT Insurance Dept.; 1955-66 with general agency in Seattle. President, NAIC, 1986. After: Standard Insurance Company
PENNSYLVANIA	Serves at the pleasure of the governor

Incumbent: (from 1987)	**Constance B. Foster** Before: Attorney in private practice
1984-87:	**William R. Muir, Jr.** Before: State Inspector General; also, Commissioner on the Appeals Board for Workers' Compensation After: Deceased
RHODE ISLAND	**Appointed by Governor, term indefinite Serves statutorily as State Bank Commissioner and Commisioner of Insurance**
Incumbent: (from 1991)	**Maurice Paradis** Before: Instructor of Business, Providence College.
1988-90:	**Robert J. Janes** Before: 1983-88, Executive Vice President, Morton Smith Inc.; 1970-83, Vice President of Sales, Insurance Underwriters Inc. After: Returned to Morton Smith Inc.
1986-88:	**Marc A. Pfeiffer** Before: Senior Vice President-Corporate Services Group, General Counsel, and Corporate Secretary for Bank of New England-Old Colony, Providence. After: Superior Court Judge
1985-86:	**Clifton Moore** Before: CEO, Business Development Corp. and Business Opportunity, Inc. After: Unknown
SOUTH CAROLINA	**Appointed by SC Insurance Commission**
Incumbent: (from 1985)	**John G. Richards** Before: 1981-85, Deputy Chief Insurance Commissioner; with State Insurance Dept. since 1973.
SOUTH DAKOTA	**Appointed by Governor**
Incumbent: (from 1987)	**Mary Jane Cleary** Before: Chief Appeals Referee, SD Dept. of Labor's Unemployment Insurance Division

1984-87:	**Susan L. Walker** Before: Deputy Director, SD Division of Securities; joined Securities Division in 1980. After: Executive of SD Lottery
TENNESSEE	Appointed by Governor, four-year term.
Incumbent: (from 1987)	**Elaine A. McReynolds** Before: Assistant Vice President, American General Life and Accident Insurance Co., Nashville; assistant secretary and manager, National Life and Accident Insurance Co.
1984-87:	**John C. Neff** Before: Investment Counsellor and Consultant, Capital Investment Services and John C. Neff and Associates; Investment Vice President and Financial Vice President, State Farm Mutual Insurance Companies After: Pinnacle Care Inc., Brentwood, TN
TEXAS	A Commissioner is designated by the Texas Insurance Board, term indefinite.
Incumbent:	**Claire Korioth** Before: Attorney in private practic
1988-90:	**A. W. "Woody" Pogue** Before: 1983-1988, Deputy Commissioner, State Board of Insurance's Life Group; with Board of Insurance since 1969. After: Unknown.
1985-87:	**Doyce R. Lee** Before: With Board of Insurance since 1975; 1980-85, legal counsel to Commissioner and supervisor of legal section; prior to 1975, private practice attorney. After: Private practice attorney; does some regulatory work, part of which is insurance related.
UTAH	Appointed by Governor, confirmed by Senate, four-year term.
Incumbent: (from 1985)	**Harold C. Yancey, CPCU** Before: Resident manager, American Agencies, Inc., for Utah, Idaho, Arizona.

1977-85:	**Roger C. Day** Before: Administrative Assistant for Planning, Beneficial Life Insurance Co.; Executive Director, Utah Health Plan. President, NAIC, 1983. After: Private insurance consultant, lobbyist.
<u>VERMONT</u>	<u>**Commissioner of Banking and Insurance is appointed by Governor, confirmed by Senate, and serves a two-year term.**</u>
Incumbent: (from 1990)	**Jeffrey Johnson** Before: General Counsel, Deputy Director, VT Dept. of Insurance.
1988-90:	**Gretchen Babcock** Before: Deputy commissioner, State Banking Division; 1981, General Counsel, Dept. of Banking and Insurance; also Assistant Attorney General, State Consumer Protection Division. After: Federal Reserve Board.
1986-87:	**Thomas P. Menson** Before: Executive Vice President and CEO, BankVermont Corp. After: Secretary of Administration for VT
1985-86:	**David T. Bard** Before: Senior Vice President-New Business and Product Development, Chittenden Trust Co. After: New England IBM Employees Federal Credit Union, Essex Junction, VT
<u>VIRGINIA</u>	<u>**Appointed by State Corporation Commission, serves at the pleasure of Commission**</u>
Incumbent: (from 1987)	**Steven T. Foster** Before: County Administrator, Spottsylvania and King George Counties
1981-86:	**James M. Thomson** Before: 1968-81, Director, Dominion Bankshares Corp.; founder and Director, Fidelity S&L and Dominion National Bank; member, VA General Assembly, 1956-78. After: retired
<u>WASHINGTON</u>	<u>**Elected, four-year term**</u>
Incumbent: (from 1977)	**Richard G. Marquardt** Before: Director, Washington State Selective Service System; former fuel oil industry executive; state senator, 1966-70.

WEST VIRGINIA	**Appointed by Governor, confirmed by Senate, serves at the pleasure of the Governor**
Incumbent: (from 1989)	**Hanley C. Clark** Before: Deputy Insurance Commissioner; entered state government in 1980
1985-88:	**Fred E. Wright** Before: Professor of finance, WV University, Morgantown After: Director, Public Employees Insurance Agency
WISCONSIN	**Appointed by the Governor, confirmed by Senate, four-year term**
Incumbent: (from 1987)	**Robert D. Haase** Before: Faculty member, Univ. of WI; 1965-69, Commissioner of Insurance.
1982-87:	**Thomas Fox** Before: Assistant General Counsel, American Family Mutual Insurance Co. After: Attorney, Madison, WI.
WYOMING	**Appointed by Governor, serves at Governor's pleasure.**
Incumbent: (from 1990)	**Kenneth Erickson** Before: Director of WY Dept. of Administration and Fiscal Control.
1989-90:	**Ralph Thomas** Before:
1987-89:	**Gordon Taylor** Before: Vice President and Marketing Director, Security Bank, Glenrock, WY. After: Unknown.
1984-86:	**Robert W. Schrader** Before: Attorney and judge, Buffalo, WY. After: Attorney, Cheyenne, WY.

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Editor's note: In 1978 the National Association of Insurance Commissioners appointed an advisory committee on manipulation. I requested appointment to the committee, and eventually was appointed after being turned down twice. Recently I decided to describe my experience, because I believe some lessons may be learned from it.

A CASE STUDY IN THE OPERATION OF NAIC ADVISORY COMMITTEES

An advisory committee on manipulation was appointed in 1978 and reconstituted in 1979 by the National Association of Insurance Commissioners (NAIC). One purpose of this article is to explain why the committee was appointed, why it was reconstituted, and how it operated. Another purpose of the article is to offer some suggestions about the use of advisory committees by the NAIC.

Background

Actuarial manipulation—sometimes called actuarial hanky-panky or actuarial legerdemain—is the act of rigging policies to look better than they are. Manipulation has been around for a long time. Examples are the steepening of dividend scales, the creative use of terminal dividends (especially those that emerge suddenly at the end of the tenth or twentieth year), the kinking of cash-value schedules (especially around the tenth or twentieth year), and the use of dividend formulas that favor new buyers at the expense of longtime policyowners.

Arthur Pedoe, an actuary, made this reference to manipulation in an article published in 1932:

> **For years the Contribution Plan of Dividend Distribution has been manipulated so as to increase the dividends to newer entrants at the expense of the policies of longer durations and especially of the paid-up policies.**

James Reiskytl, an actuary at Northwestern Mutual, made these comments early in 1979 in a letter to the advisory committee on manipulation:

> **The public record shows that there are mutual companies that have not changed their dividend scales for blocks of old business for long periods of time, some as long as twenty years. At the same time, these companies have introduced improved illustrated dividends for new issues every few years. Thus, old policyholders have received no share of improving mortality and higher investment earnings, even though such improvements are passed along to successive new groups. At best it may be some sort of half-baked, undefined investment year method. At least it appears to clearly qualify as malignant manipulation.**
>
> **We know that often the actuaries of these companies have been concerned, but they have received no support from their companies, nor from the regulators, nor even from the actuarial profession. Nobody cares. We think it is time somebody cared!**

The Advisory Committee

The traditional net cost method is susceptible to various forms of manipulation, and that fact has long been known to actuaries and others. When the attention of the life insurance industry turned to the interest adjusted method in the early 1970s, it was recognized that the new method was also susceptible to manipulation, but to a lesser extent than the traditional net cost method. (For an example of the susceptibility of the interest adjusted method, see "Actuarial Hanky-Panky at the Travelers" in our December 1974 issue.)

When a model life insurance disclosure regulation based on the interest adjusted method was adopted in 1976 by the NAIC, the drafters of the model recognized its susceptibility to manipulation. It was not until late in 1978, however, that an advisory committee on manipulation was appointed.

The advisory committee consisted initially of seven actuaries: Kenneth Clark (Lincoln National), Thomas Eason (Security Mutual of Nebraska), Walter Miller (New York Life), Richard Murphy (Aetna Life), Paul Overberg (Allstate Life), Norman Peacor (Massachusetts Mutual), and Julius Vogel (Prudential) The committee was chaired initially by Mr. Vogel. The committee reported to the NAIC's life insurance cost disclosure task force, which was chaired by Erma Edwards (Nevada insurance department). The task force in turn reported to the NAIC's life insurance subcommittee, which was chaired by Richard Barnes (Colorado insurance commissioner)

The advisory committee on manipulation was appointed at least in part because of two articles that appeared in *The Insurance Forum*. (See "Actuarial Hanky-Panky at Gulf Life" in the January 1978 issue, and "More on Gulf Life's President's Preferred Policy" in the June 1978 issue.) In January 1979, I was told an "industry advisory committee on manipulation" had been appointed I tried to find out what the committee was doing, so that I could determine what to send the committee I was unable to obtain significant information about the committee's work from either Mr Vogel or Ms Edwards

In frustration, I contacted the NAIC central office I was told that the NAIC no longer had "industry advisory committees," but only "advisory committees," and that it was possible for individuals not in the industry to serve on such committees

On March 1, 1979, I wrote to Commissioner Barnes suggesting it would be desirable to have independent members on the committee, mentioning my interest in the subject of manipulation, and asking to be appointed to the committee. Commissioner Barnes said my request had been turned down, but indicated that because of my letter a decision had been made to expand the committee I later learned the new appointees were Thomas Kelly (an actuary in the New York insurance department), E J Moorhead (a retired actuary), and Harold Skipper (an insurance professor at Georgia State University)

I wrote again to Commissioner Barnes and again requested appointment to the committee I indicated that, if my request was denied again, I might attend future meetings of the committee as an observer unless barred from doing so

Commissioner Barnes responded that he was not in a position to tell the chairman of the task force what individuals should be appointed to the advisory committee His letter included these statements

> **I recognize in part your concern and recognize that you have some very personal reasons and axes to grind in wanting to be on the Advisory Committee. I can assure you there will be no star chamber or secret sessions and that you will certainly be welcome to sit in on any sessions which you can attend.**

Webster's third edition defines an "ax to grind" as "a selfish end to gain" or "an ulterior purpose to further" While attacks on one's motives are always painful, Commissioner Barnes' comment was especially hard to take because it implied that the committee's original seven members—all actuaries representing an industry that engages in manipulation and a profession that allows manipulation—did *not* have any "axes to grind"

I wrote a letter to Ms Edwards repeating my request for appointment to the committee, and enclosed a list of my writings on the subject of manipulation Ms Edwards turned down my request

Meanwhile, copies of the correspondence were circulating among NAIC officials On April 17, 1979, the NAIC's executive committee decided that I should be appointed to the advisory committee The committee was reconstituted, and I was appointed to it The new chairman was Mr Kelly (It is my understanding that Mr Vogel resigned as chairman when the committee was reconstituted) Also appointed to the committee were Brenda Roberts (a consumer affairs specialist at Fireman's Fund) and, later, William Scheel (an insurance professor at the University of Connecticut)

Committee Secrecy

When I first learned of the existence of the advisory committee and was unable to obtain significant information about its activities, I wondered whether the committee intended to conduct its deliberations in secret I was concerned because of a previous experience with an industry advisory committee on replacement In that case, I tried to obtain copies of preliminary drafts of a model replacement regulation only to be told that the drafts were confidential When the committee released its model, the NAIC adopted it without change In other words, an industry group developed, in secret meetings and without public input, the replacement regulation under which the industry later operated

My concern about secrecy was heightened by an interesting incident In Commissioner Barnes' second letter to me, he said I was welcome to attend committee meetings as an observer The committee had already held two meetings, and a third was scheduled for April 13, 1979 Shortly after word of Commissioner Barnes' comment about "no star chamber or secret sessions" reached the committee, the planned third meeting was abruptly cancelled

At the beginning of the first meeting of the reconstituted advisory committee, it was agreed that the deliberations of the committee would be confidential until the filing of a report with the task force Those independent members who opposed the cloak of secrecy were outvoted by the industry representatives Subsequently there was even a question of whether the report would remain confidential only until it was sent to the life insurance cost disclosure task force of the NAIC by the advisory committee, or whether the report would remain confidential

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until it was formally accepted by the task force.

At that same first meeting of the reconstituted advisory committee, I requested the minutes of the two meetings of the original committee, together with all memoranda, correspondence, and other documents generated by the original committee. My request was denied. At no time were the new members of the reconstituted committee allowed access to the work of the original committee.

The desire of the industry representatives for secrecy raises some questions. For example, can the industry circumvent the antitrust laws by meeting as advisory committees ostensibly under the aegis of the NAIC? A discussion of such questions is beyond the scope of this article.

The Industry Majority

When the advisory committee had to make important decisions, industry domination of the committee was evident. Industry representatives outnumbered the independent members, and controlled the outcome whenever they chose to do so.

In advance of one meeting, I drafted and circulated four motions that I said would be made at the meeting. The purpose of the motions was to stimulate discussion of the disclosure approach (described later in this article). We did not get to the motions until late in the meeting when several members were ready to leave. When the motions were finally made, three of them were voted down by the industry majority without discussion. The chairman ruled that the fourth motion was out of order. I appealed the chairman's ruling, but it was upheld by the industry majority.

At another meeting, as the time drew near for the submission of an interim report to the life insurance cost disclosure task force, I said I anticipated filing a statement of dissent to accompany the interim report. Mr Peacor felt so strongly about the matter that he wrote a letter to Ms Edwards. The letter contained these statements:

> **It seems that if the Committee writes a report with which Professor Belth agrees, then he is willing to give it his stamp of approval. On the other hand, should the Committee prepare a report with which Professor Belth disagrees, then he will write his own. It seems to me that that leads to an interesting conclusion:**
>
> **1. The Committee does not need Professor Belth, or**
>
> **2. Professor Belth does not need the Committee, or**
>
> **3. Both of the above**
>
> **I will leave to your judgment whether this suggests a course of action with respect to his membership.**

To my knowledge, Ms Edwards did not answer Mr. Peacor's letter, and I was not dismissed from the committee. However, the letter was a surprise because I had never before encountered a situation in which a minority report was unwelcome.

Scope of Manipulation

When I first learned that an advisory committee on manipulation had been appointed, my immediate concern was whether the committee would deal with manipulation broadly or narrowly. I wondered, for example, whether the committee would deal only with such items as kinky cash-value schedules, and avoid such items as dividend formulas that favor new buyers at the expense of longtime policyowners.

The reconstituted committee found it impossible to agree upon a definition of manipulation. There were intense arguments over the scope of the committee's charge. At one stage, Mr Kelly sought clarification of the charge. The result was the following statement that appeared in a report of the life insurance cost disclosure task force:

> **In closed session, the task force voted to instruct the Manipulation Advisory Committee to limit its initial activities to the detection and prevention of manipulation in new sales as opposed to ongoing disclosure for in-force policies.**

I was never able to find out who orchestrated the above decision by the task force, or why the action was taken in closed session. The result, however, was that the advisory committee was barred initially from dealing with the kinds of manipulation referred to by Messrs Pedoe and Reiskytl.

I urged the committee to adopt a broad definition of manipulation. That definition, to which the committee never agreed, was as follows:

> **Manipulation is present when, because of the absence of requirements for rigorous disclosure of the structure of all its new and existing policies, at least some of a company's offerings tend to make the company look better to a policyowner or to a prospective buyer than the company deserves to look. The emphasis in this definition is on the policyowner or prospective buyer. When manipulation is said to be present, there is no intent to suggest that the manipulation is necessarily deliberate on the part of the company.**

Dealing with Manipulation

There are two approaches to dealing with manipulation in life insurance—prohibition and disclosure. The prohibition approach involves the development of rules for identifying manipulation and the development of procedures for the enforcement of those rules. For several reasons, including the limited resources of the state insurance departments, I am opposed to the prohibition approach.

The disclosure approach, on the other hand, is based on the idea that companies should be free to develop and price their products, but should be required to disclose the price structures of those products. Under this approach, it is assumed that, because of possible criticism from agents and policyowners, companies would not try to market products that have been manipulated. I urged the committee to emphasize the disclosure approach.

The recommendations that came out of the committee were based on the prohibition approach. The committee developed a system for detecting some forms of manipulation in some types of policies. I believe that no state has yet implemented the system.

Yearly Prices

As soon as I joined the advisory committee, I brought in numerous examples of manipulated policies. In many cases the manipulation became evident when one merely glanced at a column of yearly prices per $1,000 of protection. When the committee decided to recommend a system for detecting manipulation, it was clear to all the members of the committee that such a system would have to be based on discontinuities in yearly prices.

The discussion and the voting in the committee on precisely what yearly prices would serve as the basis of the detection system demonstrated the anti-disclosure views of the committee's industry majority. I recommended that the system be based on yearly prices per $1,000 of protection. (I have been suggesting for more than twenty years that yearly prices per $1,000 of protection are an indispensable component of any system of rigorous disclosure for life insurance consumers.) The numerator is the yearly price of the protection, the denominator is the amount of protection expressed in thousands of dollars, and the quotient is the yearly price per $1,000 of protection.

The industry majority voted instead for what everyone agrees is a meaningless measure of yearly price. The numerator is the yearly price of the protection, the denominator is the face amount expressed in thousands of dollars, and the quotient is without meaning. (If a carton contains apples and oranges, and if the price of the apples is divided by the combined number of apples and oranges, the quotient is without meaning.) I believe the industry majority voted as it did to avoid endorsing the yearly price per $1,000 of protection.

Expenses

During the first year of the advisory committee's operation, the independent members absorbed their own travel expenses incurred in attending committee meetings. (I incurred expenses of about $1,000.) During the second (and last) year of the committee's operations, the NAIC reimbursed the independent members for their out-of-pocket expenses.

Conclusion

The advisory committee on manipulation was dominated by insurance industry representatives. Furthermore, I believe the committee was too large, met too often, and failed to do enough work between meetings.

Ideally, the NAIC should not have advisory committees. It should have within its ranks the expertise necessary to draft model bills and model regulations. To the extent the ideal is not met, however, advisory committees may be needed.

When an advisory committee is appointed, I believe these principles should apply: (1) the appointment of the committee should be accompanied by a carefully planned and precisely worded charge to the committee; (2) the committee should consist of not more than five members; (3) the committee should be financed by the NAIC; and (4) the chairman and the other members of the committee should be independent of the insurance industry, although the committee should be free to solicit input from insurance industry representatives and others. In short, an advisory committee should be an arm of the NAIC, and in that capacity should be independent of the industry just as the NAIC itself should be independent of the industry.

A New Committee

In June 1984, the NAIC appointed a yield index advisory committee. I was appointed to the committee, although I had not sought appointment.

The advisory committee was appointed because some individuals in the NAIC are concerned about the use of gross interest rates in the advertising and sales efforts associated with so-called interest sensitive products, including universal life. The first priority of the new committee, according to its charge, is "to develop a yield index for interest sensitive life insurance products and any other life insurance products that are marketed with emphasis on the interest element."

The new committee is chaired by Walter Miller (a New York Life actuary who was a member of the advisory committee on manipulation). There are six other industry representatives on the committee, and one other independent member—James Hunt (an actuary associated with the National Insurance Consumer Organization).

The first meeting of the committee was held on October 4 at Chicago's O'Hare airport. Mr. Hunt and I did not attend because the NAIC has not yet made arrangements for reimbursement of the out-of-pocket expenses incurred by the independent members. The second meeting was held on November 15 in Indianapolis (a 75-minute drive from my home). I attended, but Mr. Hunt (who would have had to travel from Boston) did not. The third meeting is scheduled for December 18 in Boston, so that Mr. Hunt can attend.

The yield index advisory committee is operating in a more open, constructive manner than the advisory committee on manipulation. On the basis of my experience thus far with the yield index advisory committee, I believe significant progress for the benefit of consumers is possible.

FROM THE MAILBAG

"I do not agree with everything you write, but I savor the mental arguments I have had with you. There is no man or woman alive who can substantiate an opinion that could be reasonably respected unless he or she listens to both sides of the story. Concerning the cost of your publication, during the course of my business year I will spend in excess of $30 for lunches listening to people who have absolutely nothing to say." —Mark D. McKillop, Phoenix Mutual Life, Williamsville, New York