

NOLHGA JOURNAL

A PUBLICATION OF THE NATIONAL ORGANIZATION OF LIFE AND HEALTH INSURANCE GUARANTY ASSOCIATIONS

NOLHGA and the Guaranty Association System: The Year in Review

by Peter Marigliano,
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When the guaranty association system looks back at 1999, one insolvency will likely come to the top of the list of system issues – that of the Thunor Trust companies. The insolvency of the seven companies, while relatively modest in total dollars, was certainly big in the amount of publicity it received. However, much more kept NOLHGA and the guaranty association system busy in 1999. Other new insolvencies challenged the system, including Statesman National in Texas and National Affiliated Investors Life in Louisiana.

Of course, ongoing insolvencies like Centennial Life and Executive Life continue to be a major focus of the system and NOLHGA. Finally, the system began grappling with issues like financial services reform and non-indemnity health care provider coverage.

Managing Insolvencies

Clearly, the Thunor Trust insolvency was the most highly publicized insolvency since Executive Life. With stories of astrology readings, midnight diamond purchases and an international manhunt prevalent in national media, a failure on the part of the guaranty associations to manage the insolvency of the Thunor Trust could have shaken consumer confidence in the industry. However, the high-profile case also presented an opportunity for the system to show just how good it is at resolving insolvencies. Only months after the insolvency, assumption reinsurance transactions for four of the seven insolvent companies were nearing completion, with the others not far behind.

The lack of any media attention focusing on the victims of the insolvency clearly points to the fact that NOLHGA and the system handled the insolvencies in the manner in which regulators

and the industry have come to expect. Statesman National, a small Texas insolvency was another example of system effectiveness, with an assumption reinsurance agreement completed in only three months. (A complete report on the resolution of the insolvency can be found in the Fall 1999 edition of the *NOLHGA Journal*.)

Progress has also been made in handling the complicated Centennial Life insolvency. Starting with a claims backlog numbering in the thousands at the beginning of 1999, the Centennial Life task force and the receiver have nearly eliminated the bulk of that backlog of claims. In addition, litigation with Centennial reinsurer, AXA Re resulted in an award of \$36 million to the estate. While the nature of health insolvencies makes resolving them more difficult than life insolvencies, the Centennial Task Force is making headway in winding down the company.

The Confederation Life insolvency, another triumph for the system, also neared a close in 1999, from the perspective of guaranty association obligations. By mid-1999 all blocks of business had been transferred. The insolvency was resolved in such an efficient fashion that all poli-

cyholder claims will be paid in full and all guaranty association costs will be reimbursed.

Significant distributions, totaling more than \$41 million, were received in the Kentucky Central insolvency. In addition, the bulk of Kentucky Central's real estate inventory was sold.

Final distributions were made in two insolvencies: New Jersey Life on January 8 and Consolidated National Life on August 8.

In the National Heritage Life case, the trust set up to manage NHL assets performed well during 1999 with guaranty associations receiving \$40.5 million from the trust this year.

Another large insolvency, that of Mutual Benefit Life, was also largely wound down in 1999; at the end of the insolvency, it appears that guaranty associations will have paid very little to resolve this multi-billion dollar problem.

Significant progress was also made in the American Standard Life case, one of the more contentious insolvencies that the system has been involved with. The stockholder of ASL has vigorously opposed the insolvency of the company and the sale of

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What Do We Talk About When We Talk About "NOLHGA"?

That question occurred to me recently after I read the story by the late, underappreciated, American writer Raymond Carver, "What We Talk About When We Talk About Love." The story involves, among other things, the difficulties people have understanding and communicating with each other when they use the same word ("love," for example) to describe quite different concepts.

I am often struck by the different concepts people apparently have in mind when they refer to "NOLHGA." To some, "NOLHGA" seems to mean the NOLHGA staff. To others, it is the insurance industry. Others still see it as NOLHGA's Board of Directors (made up of State Association Board members and administrators). Some think only of their own state's Association. Some perceive NOLHGA

as the outside consultants who work on insolvency projects. Other people conflate the roles of NOLHGA and insurance receivers. Some confuse NOLHGA with assuming carriers who sometimes contract to protect consumers threatened by an insolvency. And still others think of NOLHGA as some sort of government body, like the FDIC.

None of those conceptions is accurate, and none of them gives a meaningful picture of what NOLHGA is, or what it does for the American insurance marketplace. In seeking an accurate description of NOLHGA, I am drawn to the language used in some of the legal documents to which NOLHGA is a party: "NOLHGA is a voluntary association of its members organized as a corporation. Its members consist of life and health insur-



ance guaranty associations established by the laws of the states and other various jurisdictions of the United States of America."

Of course, that only begins to tell the story. In one sense, NOLHGA is nothing more or less than its fifty-two separate member associations. It is, after all, only the member associations that have statutory obligations to protect consumers in an insolvency. But it is equally true that the member companies of each association are essential to that mission of protecting consumers, since a critical component of the funding for resolution plans by associations comes from companies' assessment payments.

Outgoing Chairman Doug Goto Accepts NOLHGA's thanks for his work in 1999 during NOLHGA's 16th Annual Meeting

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NOLHGA JOURNAL

VOL. VI  No. 1

Winter 1999

The NOLHGA Journal is a publication of the National Organization of Life and Health Insurance Guaranty Associations dedicated to examining issues affecting the life and health insurance guaranty system.

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National Organization of
Life and Health Insurance
Guaranty Associations

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A Look at the Federal Antifraud Law

by Joni Forsythe, Counsel,
NOLHGA

One of the projects undertaken by NOLHGA's Legal Committee this year was the investigation of what has come to be known as the Federal Insurance Antifraud Statute.

The Federal Insurance Antifraud Statute is federal legislation designed to target white collar fraud and looting from within the insurance industry. It was signed into law on September 13, 1994, as part of the Violent Crime Control and Law Enforcement Act of 1994.

The Antifraud Statute makes it a federal crime for those engaged in the business of insurance to commit acts that may jeopardize the financial condition of an insurance company. These acts include, among other things, embezzlement, the filing of false financial reports or statements, and the obstruction or corruption of administrative proceedings. In addition, the statute makes it a federal crime for anyone that has been convicted of a felony involving "dishonesty or breach of trust" to work in the insurance industry without the prior consent of the appropriate regulatory officials. More notably, the statute also makes it a federal crime for anyone that is "engaged in the

business of insurance" to permit such prohibited persons to participate in the business of insurance without first obtaining the requisite regulatory consents. This latter provision is particularly disconcerting in light of the array of compliance issues it raises.

On its face, the statute appears to be very expansive in scope and applicability, arguably extending to include just about every person working in the insurance industry. For the purpose of the statute, the term "business of insurance" is broadly defined as "...the writing of insurance, or the reinsuring of risks, by an insurer, including all acts necessary or incidental to such writing or reinsuring and the activities of such persons who act as or are other persons authorized to act on behalf of such persons." As such, this provision would appear to govern "insurers" and others authorized to act on their behalf. For the purposes of the statute, the term "insurer" is broadly defined to include "...any entity the business activity of which is the writing of insurance or the reinsuring of risks, and includes any person who acts as, or is, an officer, director, agent or employee of that business." There are no stated exceptions or immunities, and no grandfathering provisions that would protect persons working in the insurance industry prior to the passage of this law.

Moreover, the statute offers little guidance as to what, if any, affirmative duties are imposed upon those to whom it is deemed applicable. The NAIC has established an antifraud task force which has closely studied this statute and has published formal guidelines for state insurance departments. In the context of those guidelines, the NAIC recommends that insurers implement compliance programs, and has outlined an array of possible components for such programs. Among other things, the guidelines state that prohibited persons must, without exception, be terminated immediately upon discovery of their disqualifying felony conviction, and may not be reinstated until the requisite regulatory consent has been obtained. To the extent the statute is found to create such a duty to terminate, insurers will be faced with fairly complex legal issues, including the possibility of claims for wrongful termination under state law.

NOLHGA's Legal Committee has considered some of the issues raised by the federal statute, and has sent some information regarding the statute to NOLHGA's member guaranty association administrators. ▼

"The Antifraud Statute makes it a federal crime for those engaged in the business of insurance to commit acts that may jeopardize the financial condition of an insurance company."



NOLHGA Annual Meeting Speakers Discuss Protecting Policyholders

by Peter Marigliano
Communications Manager, NOLHGA

During NOLHGA's 16th Annual Meeting in Indian Wells, California, two speakers, Robert Sanderson, of KPMG, LLP, and Larry Pozner, an attorney who represented guaranty associations in litigation against Dain

team working to resolve the Confederation Life insolvency in Canada, asked the question whether consumers could be protected in light of the increasing convergence both in the financial services industry and across borders.

Sanderson noted that consumers need to be "able to sleep at night" and regulators should be able to provide them with at least an assurance that they can do so.

However, Sanderson stated that several factors would challenge regulators responsible for ensuring consumer safety. First, increasing consolidation in the industry will pose challenges of scale for regulators. Secondly, consumers, in their quest for higher returns, may purchase unregulated products, posing political problems for regulators, if entities selling unregulated products were to fail.

Sanderson said that any regulator working to resolve a complex multinational insolvency would face broad tests. One of the key challenges is managing the differing laws and competing interests of various countries. One troubling aspect in this regard according to Sanderson is the increasing codification of laws. This codification, in Sanderson's view, may hamstring regulators. A large multinational insolvency would require regulators to be both flexible and creative in finding solutions to the problems they face. If laws are inflexible and regulators options are pro-

scribed, it will make resolving an insolvency considerably more difficult.

Sanderson also stressed that early communication and access to information should be made available to regulators at the first sign of a problem. With early communication, regulators could prepare for an insolvency and work to come to agreement on issues before the pressure of an actual insolvency made those issues more difficult to resolve.

From the large issues of a multinational insolvency to the small, but no less significant issues of individual policyholders in a regional insolvency, Larry Pozner attempted to put a face on the people who pay – guaranty associations.

Pozner, a Denver-based attorney, was retained by a number of states in their litigation against Dain Bosworth, a brokerage firm that was affiliated with Midwest Life. Over the course of several years, Dain agents advised their clients to purchase products from Midwest Life. Subsequently, ownership of Midwest Life was flipped several times, with each change of ownership making the company weaker and weaker, while Dain failed to inform its clients what it knew about the company's deteriorating financial condition.

After Midwest Life went under, Dain, among other matters, took the position that they should have no responsibility because the guaranty association system

Robert Sanderson

Bosworth, looked at how insurance policyholders are protected. Sanderson examined how consumers could be protected in the insolvency of a large multinational financial services conglomerate, while Pozner examined how policyholders of a small regional insurer, Midwest Life, were protected by guaranty associations.

Robert Sanderson, who led the



Protecting Policyholders

Policyholders, *From Page 4*

covered policyholder losses.

However, the policyholders, often elderly, who placed their life savings with Midwest were not fooled. Time after time in court proceedings, these policyholders explained that the money they received from guaranty associa-

Whether the cases are big or small, multinational or multi-state, the effectiveness of the system will be measured in how well it protects consumers and keeps the promises made by the industry. ▼

Larry Pozner

tions was not really “their” money. “Their” money was lost by Midwest Life. They explained the hardship that the loss of their life savings would have caused if it were not for the guaranty association system, a system which most never even knew existed.

At the end of the day, state guaranty associations settled their claims against Dain, on what they viewed as, favorable terms. According to Pozner, it was the continued willingness of guaranty associations to litigate the case that ultimately brought Dain to the settlement table.

Incoming NOLHGA Chairman Bill Fisher addresses NOLHGA's Annual Meeting

Chuck LaShelle is recognized for his service on NOLHGA's Board of Directors at NOLHGA's Annual Meeting



1999 In Review

1999, *From Page 1*

its largest asset, ranch property in Colorado. After lengthy litigation, the sale of the property closed in 1999, bringing to an

eries of over \$170 million, including \$56.2 million from the Confederation estate, \$42.9 million from National Heritage Life, and \$41 million from Kentucky Central.

NOLHGA Committee Activity

NOLHGA Committees were also active in their work on behalf of the system. Given the potential for havoc brought by the Year 2000 bug, NOLHGA's Year 2000 Insolvency Contingency Plan Committee had a productive year planning for any disruptions the Y2K bug might bring. One key component of the Committee's work this year was the development of an "early response team" concept as one avenue for addressing insolvencies with Y2K-related problems. The Committee has identified a list of the skills that would be needed to address Y2K issues in an insolvency. It has also identified consultants, primarily computer experts, third party administrators, and others that could quickly analyze the insolvent company for Y2K problems.

The Committee also focused on developing a relationship with the regulatory community so that regulators could better understand what NOLHGA was doing to prepare the system for any Y2K disruptions. These communications also served to strengthen relationships in a more general sense, between the guaranty association system and state regulators.

NOLHGA's Communications Committee was also quite active

in 1999. The Committee developed a "Communications Kit For Guaranty Associations" which will help guaranty associations in their interaction with the media and the public. The kit will also be useful background material for state board members new to the guaranty association system.

NOLHGA's Legal Committee developed an internet and e-mail use policy, which will guide NOLHGA as it confronts the increasing use of electronic communications. The Committee also produced a standard Request For Proposal document which is intended to facilitate the transfer of guaranty association covered obligations to assuming carriers.

The Emerging Issues Committee focused on the issue of guaranty association coverage for non-indemnity health plans. During 1999, the committee developed an issue paper that will provide insights to the system as it grapples with calls for guaranty association coverage of non-indemnity providers.

While 1999 will be remembered mostly for Martin Frankel and the Thunor Trust insolvency, NOLHGA and the guaranty system were tested on many other fronts. The continued efficiency of the system in managing a diverse range of insolvencies and issues bodes well for the industry and its policyholders for 2000 and beyond. ▼

Emerging Issues Committee members George Coleman, Merle Pederson and Jean Hasch discuss the implications of guaranty association coverage for non-indemnity health insurance providers

end much of the litigation brought by ASL's former owner,

The Executive Life insolvency has been challenging the system since 1991, and continued to do so in 1999. One of the key victories, from a guaranty system perspective, was an August 3 decision by the Michigan Court of Appeals that the Michigan association was not liable for Guaranteed Investment Contracts held by a pension fund.

In a broader sense, NOLHGA and the system were particularly fortunate with respect to recoveries from various estates. In 1999, the system received recov-



Talking About NOLHGA

NOLHGA, *From Page 2*

Where insolvent carriers wrote business only in one or two states, the affected associations alone sometimes protect consumers, with no assistance from NOLHGA.

NOLHGA's *raison d'être* is the phenomenon of the failures of large life and health companies that wrote business in multiple states. The special challenge for associations in such cases is one of collective action: how to protect consumers quickly and efficiently regarding policies issued in as many as 52 different jurisdictions in a way that satisfies the obligations of associations in each of those jurisdictions? Early in their experience with such insolvencies, the associations and their member companies reached the conclusion that the challenge could best be met through an organization comprising all the associations. To quote another statement from our legal documents: "NOLHGA was created by the various guaranty associations to help them more efficiently perform their statutory duties by coordinating activities in multi-state life and health insurance company insolvencies, improving inter-guaranty association communications, and sharing commonly used resources (project management, legal, actuarial, and financial)."

From this need was born the former Disposition Committee approach, which has evolved into today's Members' Participation Council and task force structure. The current multi-disci-

plinary "working team" approach to staffing insolvencies with the proper mix of outside consultants and NOLHGA staff evolved through the nineties,

"NOLHGA's *raison d'être* is the phenomenon of the failures of large life and health companies that wrote business in multiple states."

along with today's "menu" of technical and strategic considerations employed by task forces. The results of the current approach have, in general, been highly rewarding. The average amount of time needed to provide consumers with claims payments and replacement coverage has steadily diminished; the quality of replacement coverage has increased; the overall financial efficiency of the guaranty system has steadily improved; and the constituencies with which the system deals have developed a high level of confidence in its ability to perform its critical mission.

I believe it was the Nobel prize-winning economist Ronald Coase who described a corporation as a "nexus of contracts." I would paraphrase that description only slightly in describing NOLHGA as a nexus of commitments. In the insolvency of a

multi-state life or health insurer, its members have designed NOLHGA to be the focal point for the analysis and resolution of the statutory obligations of its member associations and their member companies. That goal is achieved by the consultative and cooperative efforts of the associations themselves and their able administrators, through the Task Force/MPC structure; with the support of the industry and NOLHGA's Board; and with the assistance of NOLHGA's staff and top outside consultants from the legal, financial, and actuarial fields.

Clearly, we're talking about participation by a number of very talented individuals. But when we talk about NOLHGA, we talk about not only the list of the people who contribute, but also the ways in which the design and operation of the system itself causes the whole of these individuals' contributions to be ever so much more than the sum of their parts. ▼

UPCOMING EVENTS

December 4-8

**NAIC Winter Meeting
San Francisco, CA**

January 31 - February 1

**NOLHGA Board of Directors
San Diego, CA**

February 23-25

**NOLHGA MPC Meeting
Tampa, FL**

March 11-15

**NAIC Spring Meeting
Chicago, IL**

May 2-3

**NOLHGA MPC Board of Directors
Tysons Corner, VA**

May 17-19

**NOLHGA MPC Meeting
Minneapolis, MN**

NOLHGA



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