

NOLHGA JOURNAL

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

NOLHGA Responds to Eight New Insolvencies

With the announcements of eight new insolvencies in mid-May, NOLHGA and the guaranty association system are responding to their newest challenge. While none of the companies' reserves match the dollar value of some of the larger insolvencies that NOLHGA has contended with over the years, the circumstances that caused the insolvencies may prove equally as challenging to the task force, NOLHGA, the guaranty association system, and the receivers, who must marshal the assets.

The Thunor Trust, a Tennessee-based entity, ultimately con-

trolled seven of the companies through two holding companies. International Financial Corporation, an Oklahoma-domiciled company, controlled three of the companies: First National Life Insurance Company of America (MS); Farmers and Ranchers Life Insurance Company (OK); and International Financial Services Life Insurance Company (MO).

Another holding company, the Franklin American Corporation, a Tennessee-based public corporation with 1490 shareholders and 83 percent owned by the Thunor Trust, controls the other four insurers: Franklin Protective Life Insurance Company (MS); Franklin American Life Insurance Company (TN), which controls Old Southwest Life Insurance Company (AR); and Family Guaranty Life Insurance Company (MS).

According to published reports, a substantial portion of the invested assets of the insurers controlled by the Thunor Trust are missing.

The eighth company, Settlers Life Insurance Company, a Virginia-domiciled insurer, was taken over by Virginia regulators as a result of reinsurance it ceded to First National Life. While the indirect impact on Settlers of First National's problems is serious, Settlers may not be damaged to the same extent as some of the Thunor-controlled companies.

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INSOLVENCIES IN BRIEF

Family Guaranty Life Insurance Company (MS)

States Affected - Mississippi Only
Policyholder Obligations - \$23 Million

Farmers and Ranchers Life Insurance Co. (OK)

States Affected - Oklahoma Only
Policyholder Obligations - \$9 Million

First National Life Insurance Co. of America (MS)

States Affected - AL, AZ, AR, CA, CO, DE, DC, FL, GA, HI, IL, KS, KY, LA, MD, MI, MS, MO, NE, NV, NJ, NM, NC, OH, OK, OR, SC, TN, TX, UT, VA, WA
Policyholder Obligations - \$110 Million

Franklin American Life Insurance Company (TN)

States Affected - AL, AR, FL, GA, IL, KY, LA, MS, NC, OK, SC, TN, VA, WV
Policyholder Obligations - \$54 Million

Franklin Protective Life Insurance Company (MS)

States Affected - AL, AZ, FL, LA, MS, NM, OK, TX
Policyholder Obligations - \$19 Million

International Financial Services Life Ins. Co. (MO)

States Affected - All EXCEPT: IL, IA, ME, MS, NH, NJ, NY, RI, WY
Policyholder Obligations - \$186 Million

Old Southwest Life Insurance Company (AR)

States Affected - Arkansas Only
Policyholder Obligations - Not Yet Available

Settlers Life Insurance Company (VA)

States Affected - AR, DE, GA, IL, IN, KY, LA, MD, MS, MO, NE, NC, ND, OH, SC, TN, VA
Policyholder Obligations - Not Yet Available
(Note: Not part of the Thunor Trust; insolvent due to a reinsurance agreement with First National Life.)

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The System Is Up For The Challenge

As I write this, I am finishing my eighth week as NOLHGA's President. I am only beginning to realize all that I don't know about our system, and to fully appreciate the contributions of those who preceded me.

In my meetings with the Selection Committee and the Board of Directors early this year, I was asked several times for my thoughts on a "peacetime readiness" strategy for NOLHGA. As related elsewhere in this issue (See Page 1), the guaranty association system has mobilized and gone to the front lines with virtually no advance notice, as the result of eight different insolvencies all arising within roughly one week. The speed and effectiveness of the response has been impressive, though not surprising.

I watched the system, as something of an outsider, while it performed spectacularly in many cases over the last few years; so, in a general sense, I knew what could be expected by way of a prompt reaction to the latest challenges. Nonetheless, perspective is everything. Only by participating at close quarters in these cases with all of the constituencies within the system have I begun fully to appreciate just how effective our system is, and more importantly, why it is so effective.

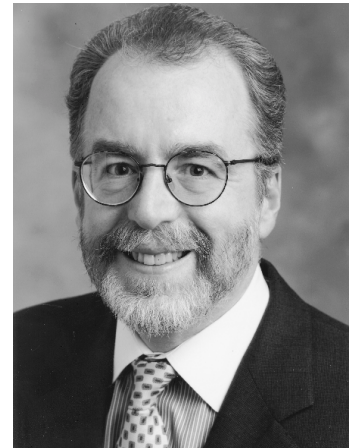
The system's response began in these cases where it frequently does, at the level of state association administrators. Here, the administrators in the states most directly impacted put NOLHGA staff on "early warning" of the

problems, and MPC Chair Peggy Parker (VA) swiftly appointed task forces to address the insolvencies. One, the Thunor Trust task force, is chaired by Chuck LaShelle (TX); the other, the Settlers Life task force, is chaired by Mike Marchman (GA). It has been a genuine pleasure to watch these teams of committed and talented GA administrators, directed by those able (but different!) leaders, develop effective early response strategies.


In the same vein, these new insolvencies have given me a heightened appreciation of the quality of outside professionals -- legal; financial; actuarial; and project management -- who stand ready, willing, and able to support our system as we move with dispatch to find (as Charlie Richardson, of Baker & Daniels says) "warm, safe, dry homes" for policyholders affected by insolvencies.

Last, and not least, the new cases have given me a chance to work closely with NOLHGA's staff in situations where a great many puzzles had to be solved within a very narrow time frame. Without exception, members of the staff have risen to the challenge with professionalism and competence.

I anticipate spending many long hours developing the extensive familiarity with our system that I will need to maximize my personal contribution. But what I have learned already is that the system and the resources behind it work even better now than ever before. ▼



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Communication Key To Y2K Preparedness

by Jack Falkenbach
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Association



By now, we are all aware of the potential problems associated with the Y2K computer problem.

With little more than six months left until January 1, all of those with a stake in the guaranty association system, guaranty associations, insurance departments, and member insurers have, I hope, ensured that their internal systems and those of their ven-

dors, are or will be, Y2K compliant. With most internal issues addressed, NOLHGA's Year 2000 Contingency Plan Committee has been focusing on how the system will respond to an insurer insolvency with substantial Y2K problems.

A key issue identified by the committee was the need for a dialogue between regulators, receivers and guaranty association administrators. Obviously, administrators and insurance departments have somewhat different perspectives regarding potential Y2K problems. In most states, regulators have been focused on identifying those domestic companies that may not be Y2K compliant, and working with them to achieve compliance

or to implement a workable contingency plan. Guaranty association administrators are somewhat more concerned with how potential insolvencies with substantial Y2K problems will be addressed.

In the limited number of meetings between guaranty association administrators and state insurance department representatives, meetings encouraged by this committee, it is clear that most state insurance departments are well along in their identification and monitoring of companies with potential Y2K problems. In some states, insurance departments have been actively working with those companies that are at highest risk to

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"A key issue identified by the committee was the need for a dialogue between regulators, receivers and guaranty associations."

Navigating the E-mail Minefield

by Angela J. Franklin
Assistant Counsel, NOLHGA



"I would love to kiss your covered toes." The Phoenix Gazette recently published a story

about an e-mail user who made a mistake in the address field of an e-mail message intended for his girlfriend and accidentally sent that message to thousands

of on-line computer users.

While this mistake was, at worst, embarrassing, it illustrates how the single click of a mouse could send sensitive and confidential information to thousands of computer users and create serious problems for the sender and his or her company.

In many ways, the legal liability a company would incur related to their employees' use of e-mail is little different from the liability they would bear for any other document produced in the course of doing business.

E-mail, however, poses its own set of problems and responsibilities for companies. NOLHGA is identifying and developing policies and procedures to address issues raised by the use of e-mail at NOLHGA that will minimize NOLHGA and member exposure with regard to legal privileges, confidentiality, privacy, and liability, as well as prevent mistakes like the one mentioned above.

E-mail Policy

NOLHGA is considering an e-mail policy, organized around accomplishing three goals: the

reduction and if possible, elimination of potential legal liability to employees and third parties; the protection of confidential, proprietary information from theft or unauthorized disclosure to third parties; and the protection of NOLHGA's computer systems.

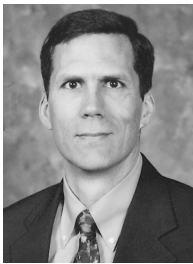
Essential points in the developing policy include a reminder that the contents of the NOLHGA computer systems are the property of NOLHGA, a note that expectations of privacy are very limited, that NOLHGA re-

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Legal Committee Agenda Matches Diverse Challenges

by William P. O'Sullivan
General Counsel, NOLHGA



While the core mission of NOLHGA is assisting its members in fulfilling their statutory obligations, legal concerns are

often the key issues that dictate the cost of and speed with which the guaranty system can respond to insolvencies. The legal issues that confront the system are both diverse and complex. The NOLHGA Legal Committee was formed to provide recommendations and advice on these issues. In carrying out its mission, the Legal Committee formulates recommended positions on legal issues affecting guaranty associations; arranges for the filing of amicus briefs in litigation matters of national import to the guaranty system; prepares comments on interpretations and amendments to model legislation; and coordinates a NOLHGA-sponsored seminar for the purpose of developing and furthering the knowledge of NOLHGA members and their counsel with respect to relevant legal matters.

The following is a summary of 1999 projects being handled by the Committee's subgroups:

Claims Valuation Subgroup

The Claims Valuation Subgroup is seeking to develop general guidelines for measuring guar-

anty association claims in insolvencies. The guidelines will seek to address valuation and related issues with respect to guaranty association claims for administrative expenses, policyholder coverage and unpaid assessments. In addition, this subgroup will provide advice on the use and preparation by guaranty associations of omnibus proofs of claim.

Coverage Issues Subgroup

As insurance products evolve and become ever more complex, the extent of guaranty association coverage continues to be an area of major focus for both industry members and regulators. Two areas that have recently attracted the attention of the NAIC and ACLI are equity-indexed products and non-indemnity health plans. NOLHGA's Coverage Issues Subgroup has worked closely with the ACLI in addressing guaranty association coverage in these areas. With respect to equity indexed products, the subgroup has provided assistance in developing concepts and model act language to clarify the extent of guaranty association coverage.

Uniform Receivership Law Subgroup

The Interstate Compact Commission's adoption of the Uniform Receivership Law (URL) last September has given rise to much legislative activity with respect to state receivership law. Many of the legislative initiatives have been based on the URL. Given this activity, and the strong likelihood that the URL will serve as a model for legisla-

tive activity in this area well into the future, the Legal Committee's URL Subgroup is in the process of preparing a comprehensive review and analysis of the URL. The Subgroup anticipates finalizing its work product by May 31.

The URL Subgroup also will assist NOLHGA in responding to an NAIC initiative to consider amending the Insurers Rehabilitation and Liquidation Model Act to incorporate URL provisions.

Federal Issues Subgroup

While regulation of the business of insurance has been largely left to the states, decisions made at the federal level can have a profound impact on the industry and the guaranty system. As a consequence, NOLHGA's Legal Committee has appointed a Federal Issues Subgroup to track federal matters having an impact on the guaranty system. The Subgroup is now handling three such matters. First, the Subgroup has assisted NOLHGA in preparing a request for a Department of Labor information letter confirming the assignability of ERISA breach of fiduciary duty claims to guaranty associations. As a consequence of providing coverage for guaranteed investment contracts owned by pension plans, several guaranty associations have asserted subrogation rights with respect to claims that a pension plan may have against plan fiduciaries under ERISA. These guaranty associations have encountered strong resistance from plan sponsors. As a consequence, NOLHGA, with support from

this Subgroup, requested an information letter from the DOL on this issue. It is believed that a DOL letter supporting the guaranty associations on this issue will be helpful in resolving differences with plan sponsors.

This Subgroup also is reviewing the Federal Insurance Antifraud Statute to determine possible implications to guaranty associations. This statute, which was part of the Violent Crime Control Law Enforcement Act of 1994, prohibits persons who have been convicted of a felony involving dishonesty or breach of trust from participating in the business of insurance. The statute also prohibits those in the business of insurance from willfully permitting such convicted felons to participate in the business of insurance. The statute provides for substantial fines and prison sentences of up to five years to be imposed for violations. The Federal Issues Subgroup will provide appropriate guidance to NOLHGA and guaranty associations on the application of this statute to their operations and possible precautionary measures, if any, to be taken.

Finally, the Subgroup has been working with various industry trade organizations in considering a proposal to amend the Federal Priority Statute. As a general matter, the Federal Priority Statute provides that claims of the federal government have priority over claims of other persons in insolvency proceedings. Notwithstanding obvious conflicts with the McCarran-Ferguson Act, the federal gov-

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Legal Committee Activity

Legal Committee, *From Page 4*
 ernment has relied on the priority statute to argue that its claims in insurer insolvency proceedings are prior to those of other claimants, including guaranty associations. In addition, the federal government has argued that the priority statute undercuts the application of claims bar dates and other claims filing rules to its claims. These positions have given rise to a great deal of litigation involving the federal government, receivers and guaranty associations. Although the federal government has had relatively little success

in these actions, it appears that these issues will continue to generate expensive and time consuming litigation well into the future. The purpose of the Federal Priority Amendment project is to avoid this litigation by seeking a legislative solution. The proposed legislative solution would simply confirm that insurer insolvency proceedings are exempt from the federal priority statute.

Standard Offering Package Subgroup

In connection with fulfilling their statutory obligations, guaranty associations often solicit offers for the assumption of an insolvent company's covered policy obligations. The NOLHGA task force responsible for a given insolvency will conduct such a solicitation by preparing and distributing an offering package to interested third parties. The offering package typically describes the business to be assumed and the process to be followed in submitting offers for

the business. The offering package is a critical document in efforts to transfer guaranty association covered obligations, and the subgroup has been constituted to standardize and improve the offering packages used by NOLHGA task forces.

Confidentiality Subgroup

The exponential growth of electronic data sharing has raised new issues regarding the confidentiality of information existing in electronic form. This is

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Electronic Communication Raises Liability, Disclosure Concerns

E-mail, *From Page 3*

serves the right to monitor its e-mail, that care should be taken in drafting e-mail, and that inappropriate content is prohibited. The policy also will require acknowledgment by employees that they have read, understood and agreed to abide by the policy.

What is developing as the heart and soul of the policy and procedures is that users must use the same care in drafting e-mail as they would any other business communication. This element is critical to minimizing potential liability. Guiding principles are that e-mail should be truthful and accurate, senders should evaluate whether a particular message needs to be sent by e-mail, and which recipients need to receive the message. Fi-

nally, it is critical that senders be aware that inappropriate material should be avoided, and that anything created or stored on the computer system may, and likely will, be reviewed by others. This last principle is very neatly summed up by Charlie Richardson of Baker & Daniels in a recent *Federation of Regulatory Counsel Insurance Law and Regulation Journal*: "If you wouldn't say it to your grandmother, don't send it via e-mail."

Document Retention

The Microsoft trial focused attention on e-mail circulated by company employees when the videotaped image of Bill Gates squirming in his seat during testimony, seemingly contradicted by his own company's e-mail, was televised on the evening news. E-mail is often over-

looked in company document retention policies. One reason is that disk storage space is inexpensive, unobtrusive, and the default decision is often to simply keep everything. Unfortunately, once five or ten years' worth of e-mail has been stored up, you have got yourself a problem. Why?

First, it can be costly retrieving relevant e-mail documents if the company is sued. The company is under a legal obligation to look for relevant evidence, which may very well be contained on e-mail, and it can be very expensive to go through all those e-mail records looking for relevant documents. Discovery requests for electronic evidence can be crafted in ways that force the company to spend the maximum amount of time and money looking for the evidence. Fur-

ther, if a company deletes old electronic records, including e-mail that could contain evidence, it may be subject to a claim of destruction of evidence. The result could be civil and criminal prosecution.

NOLHGA's approach will be to incorporate e-mail into its document retention policy and develop a policy and procedures to organize the information so that producing pertinent documents will not create an unreasonable burden on NOLHGA. The goal is that the finished e-mail and document retention policies will help NOLHGA safely navigate the information superhighway as we move into the next millennium. ▼



NOLHGA Launches Institutional Memory Project

by Dana Woodward
Manager, Insurance Services,
NOLHGA

The following has happened to everyone. You recall having a document, whether in paper or electronic form, and just when you need it, it eludes you. You've checked all the logical places and scoured the computer trying desperately to remember what the file was called or when it was created...

Ask anyone in business today and they will tell you that the volume of data and records grows every day. The problem everyone is facing is how to control the flow of paper and retrieve information quickly.

In early 1998, the NOLHGA Board directed staff to find a solution to the records retention issue. A Systems Group was formed to study methods by which to achieve institutional memory for the organization. In July 1998, the Systems Group proposed, and the NOLHGA Board approved, the development of an extranet document library. The development of the library is a 2-plus year project to convert NOLHGA's paper files to electronic files. This will allow for easy reference, reuse and sharing of documents.

While researching off-the-shelf products available for creating electronic databases, the group found that current methods use a web browser technology that makes it easier to search and retrieve documents, very similar to surfing the web.

The institutional memory system was unveiled to members on May 19 in Washington, D.C. Members were shown how the system is set up; how documents will be stored in the system; and how to search the system for documents using key words.

The benefits of having an electronic records retention system include:

- * the ability to reference historical data;
- * the ability to access and reuse information easily;
- * the ability to share and collaborate on works in progress;
- * powerful search features;
- * economic storage; and
- * secure backup.

The institutional memory project was divided into four phases. In Phase I, a beta copy of the Lotus Development Corporation's Domino.doc software was tested internally at NOLHGA. After researching software specifically made for records retention, the Systems Group determined that Domino.doc, running on a separate WindowsNT server was the best solution for NOLHGA's needs.

In Phase II, the types of documents to be stored in the system were refined. Three broad categories of documents were defined: primary (those that we should maintain an electronic copy of); trash (duplicates, illegible documents, etc.); and secondary (all other documents).

Currently the project is in Phase III. The system is set up and resides as a node on NOLHGA's local area network. Paper and

electronic files of insolvencies from 1990-1998 are being reviewed, and primary documents are being uploaded to the system. The file review is a long process. If an electronic copy of a primary document is not available, the paper document will be scanned. Secondary documents will continue to be stored in the paper files for pre-1999 insolvencies. An index of the paper files will be included in the institutional memory system.

All documents relating to 1999 and future insolvencies will be stored in the system. In addition, a paper copy of original signed agreements will be maintained on-site at NOLHGA's offices.

The last phase, Phase IV, will provide to guaranty associations and other constituents, direct access to the institutional memory system. Access will be through NOLHGANet via an assigned password. NOLHGA anticipates that member access will be a reality later next year.

Finally, NOLHGA recommends the following for anyone accessing NOLHGANet on the web:

- * 56K modem or faster (ISDN, T1)
- * 64MB RAM
- * 200 MHz or faster processor
- * Recent version of web browser (Internet Explorer or Netscape Navigator).

See you on the web! ▼

NOLHGA's Institutional Memory System will utilize browser-based technology, similar to that used when surfing the World Wide Web.



Communicating On Y2K

Y2K, *From Page 3*

resolve these problems. If the efforts of these states are indicative of the rest, and are successful, the potential magnitude of Y2K problems among life and health insurers may be greatly ameliorated.

While identification and monitoring of companies with Y2K problems is a critical component of Y2K preparedness, both guaranty associations and state insurance departments must be prepared to respond to Y2K problems that exist in insolvencies, even if the insolvency was due to issues unrelated to the Y2K problem.

The committee has identified early notification of NOLHGA by state regulators, regarding companies with substantial Y2K problems, as an important matter.

In the years since NOLHGA's formation, regulators have become extremely cooperative in notifying NOLHGA of regulatory actions as soon as they are taken. This early notification becomes even more critical with regard to impaired companies with Y2K problems. Companies with Y2K problems are likely to have outdated and/or poor systems, and this is likely to impact the quality of data available to receivers and guaranty associations as they work to address

their respective obligations in an insolvency. Additionally, if bad data is carried through from quarter to quarter, it will be necessary to reconstruct records from the point where the Y2K bug first came into play. This could be an extremely costly and time-consuming process. With early communications between regulators, receivers and guaranty associations, this task will be less daunting.

Archiving of static back-up data for companies is a critical component of preparing for potential Y2K problems. Administrators have requested that regulators require companies with potential Y2K problems to backup their data in a static fashion, as

opposed to the more commonly used overlay backup. This will further ensure that receivers and guaranty associations have accurate data, and enable them to address policyholder coverage in the insolvency more quickly.

"Companies with Y2K problems are likely to have outdated and/or poor systems and this is likely to impact the quality of data available to receivers and guaranty associations as they work to address their respective obligations in an insolvency."

Legal Committee, *From Page 5*

sue has particular importance to NOLHGA as it moves forward to implement its institutional memory project. When fully implemented, this project will allow guaranty association administrators to access significant insolvency information from NOLHGA via electronic means. While this easy access to information will be very beneficial to NOLHGA's members, there are concerns about ensuring that protections are in place to safeguard this information from unauthorized or unwelcome third party access. The Confidentiality Subgroup will be making recommendations on protecting NOLHGA's electronic informa-

tion, and in connection with that effort, will be assisting NOLHGA in developing a policy on e-mail and internet use.

Amicus, Legal Seminar and Model Act Subgroups

These three subgroups of the Legal Committee are actively pursuing their standing projects in 1999. The amicus subgroup, which handles requests for NOLHGA amicus support, has already filed a brief in support of the Missouri Guaranty Association in a case arising out of the Executive Life insolvency, and anticipates several additional amicus requests in the near future. The Legal Seminar Planning Subgroup is busy putting

the final touches on what is anticipated to be the best ever NOLHGA Legal Seminar to be held on July 15 and 16 in Snowmass, Colorado. Finally, the Annotated Model Act Subgroup will be publishing the fourth edition of NOLHGA's annotated Life and Health Insurance Guaranty Association Model Act in late October. ▼

While it is impossible to predict the number or magnitude of insolvencies that will have Y2K-related problems, regulators, receivers and the guaranty association system must be prepared to address any that do occur. Keeping the lines of communication between regulators, receivers and administrators open is critical to ensuring that any insolvency is resolved quickly and efficiently. ▼

Thunor, *From Page 1*

The Member's Participation Council has appointed task forces to manage the insolvencies. Chuck LaShelle (TX) has been named chair of the Thunor task force. Also named to the task force were John Colpean (MI), Dan Elrod (TN), William Falck (FL), Rusty Haydel (MS), Dick Horne (AR), Chuck Renn (MO), and Tad Rhodes (OK). Peter Gallanis will serve as the NOLHGA contact.

Consultants named to assist the Thunor task force are: actuarial - Bruce Winterhof, Milliman & Robertson; financial - Tim Hart, Arthur Andersen; legal - Charlie Richardson, Baker & Daniels;

project manager - Fred Buck, Buck & Associates.

The MPC named Mike Marchman (GA) chair of the Settlers Life task force. Frank Gartland (OH), Lowell Miller (NC), Peggy Parker (VA), Phyllis Perron (LA), and Tom Peterson (KY) named as task force members. Holly Wilding will serve as the NOLHGA contact.

Consultants named to assist the Settlers Life task force are: actuarial - Larry Warnock, KPMG Peat Marwick; financial and project management - Bob Tice; legal - Frank O'Laughlin, Rothgerber, Johnson & Lyons, LLP. ▼

UPCOMING EVENTS

June 5-9	NAIC Summer Meeting Kansas City, MO
July 15-16	NOLHGA Legal Seminar Snowmass, CO
July 28-29	NOLHGA Board of Directors Baltimore, MD
August 25-27	NOLHGA MPC Meeting Couer d'Alene, ID
October 2-6	NAIC Fall Meeting Atlanta, GA
October 19	NOLHGA Board of Directors Indian Wells, CA
October 20-22	NOLHGA Annual/MPC Meeting Indian Wells, CA

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