Y4
.C 73/2
91-45

1041
RECEIVED

91Y4
C73/2
91-45

GOVERNMENT
Storage

KANSAS STATE UNIVERSITY
RECEIVED
MAR 30 1970
KANSAS STATE UNIVERSITY

FEDERAL INSURANCE GUARANTY CORPORATION

HEARINGS

BEFORE THE

COMMITTEE ON COMMERCE
UNITED STATES SENATE

NINETY-FIRST CONGRESS

FIRST SESSION

ON

S. 2236

A BILL TO CREATE A FEDERAL INSURANCE GUARANTY CORPORATION TO PROTECT THE AMERICAN PUBLIC AGAINST CERTAIN INSURANCE COMPANY INSOLVENCIES

NOVEMBER 12, 19, 20, 1969; AND FEBRUARY 10, 1970

Serial 91–45

Printed for the use of the Committee on Commerce

KSU LIBRARIES
A11900 964773

U.S. GOVERNMENT PRINTING OFFICE
39–251 WASHINGTON : 1970

AUTHENTICATED
U.S. GOVERNMENT
INFORMATION
GPO

Y4
.C 73/2
91-45

COMMITTEE ON COMMERCE

WARREN G. MAGNUSON, Washington, *Chairman*

JOHN O. PASTORE, Rhode Island
VANCE HARTKE, Indiana
PHILIP A. HART, Michigan
HOWARD W. CANNON, Nevada
RUSSELL B. LONG, Louisiana
FRANK E. MOSS, Utah
ERNEST F. HOLLINGS, South Carolina
DANIEL K. INOUYE, Hawaii
JOSEPH D. TYDINGS, Maryland
WILLIAM B. SPONG, JR., Virginia

NORRIS COTTON, New Hampshire
HUGH SCOTT, Pennsylvania
WINSTON PROUTY, Vermont
JAMES B. PEARSON, Kansas
ROBERT P. GRIFFIN, Michigan
HOWARD H. BAKER, JR., Tennessee
CHARLES E. GOODELL, New York
MARLOW W. COOK, Kentucky

FREDERICK J. LORDAN, *Staff Director*
MICHAEL PERTSCHUK, *Chief Counsel*
S. LYNN SUTCLIFFE, *Staff Counsel*
ARTHUR PANKOPF, JR., *Minority Staff Director*
J. PAUL MOLLOY, *Minority Staff Counsel*

CONTENTS

	Page
Opening statement by the chairman	1
Text of S. 2236	2
Agency comments of the Comptroller General	17

NOVEMBER 12, 1969

CHRONOLOGICAL LIST OF WITNESSES

Cox, Charles K., president, Insurance Co. of North America; accompanied by Edmond Rondepierre, assistant general counsel, Insurance Co. of North America; and Thomas Clark Matthews, Jr., counsel	62
Jacks, Ronald A., president, National Association of Property & Casualty Reinsurers, Washington, D.C.; accompanied by Henry Kramer, president, North American Reinsurance Co	20
Prepared statement of Henry Kramer	24
Lemmon, Vestal, president, National Association of Independent Insurers, Chicago, Ill.; accompanied by George DeWolf, assistant general counsel	37
Maisonpierre, Andre, vice president, American Mutual Insurance Alliance, Washington, D.C	68

NOVEMBER 19, 1969

Jones, T. Lawrence, president, American Insurance Association; accompanied by Melvin L. Stark, manager, AIA Washington office; and Robert N. Gilmore, associate general counsel	100
Stringfellow, William A., general manager, National Association of Mutual Insurance Agents; accompanied by Robert E. Morin, manager, Federal Relations, National Association of Mutual Insurance Agents	237
Worthington, Lorne R., commissioner for the State of Iowa and chairman of the executive committee of NAIC; accompanied by Jon Hanson, executive secretary and director of research of NAIC; Robert E. Dineen, consultant; and T. Nelson Parker, representative in Washington, D.C	128

NOVEMBER 20, 1969

Angevine, Mrs. Erma, executive director, Consumer Federation of America, Washington, D.C	254
Bailey, James E., attorney, representing the American Society of Insurance Management, Washington, D.C	263
Bloom, Richard C., president, National Association of Mutual Insurance Companies; accompanied by Wallace Smith, counsel; and Richard Smith, counsel; and Richard Smock, vice president, legislative services	245
Yolton, John, administrative assistant, United Automobile, Aerospace & Agricultural Implement Workers, Washington legislative office	249

FEBRUARY 10, 1970

Cherington, Paul, Assistant Secretary for Policy and International Affairs, Department of Transportation; accompanied by Richard Walsh, director of operations, automobile insurance study	274
Passer, Dr. Harold, Assistant Secretary for Economic Affairs; accompanied by Walter A. Hamilton, Deputy Assistant Secretary for Domestic Business Policy, Department of Commerce	274

ADDITIONAL STATEMENTS, LETTERS, AND ARTICLES

Page

Bateson, Cornelius C., insurance commissioner, Oregon State Department of Commerce, letter of January 19, 1970 ---- 301
Brown, Hon. Virginia Mae, Chairman, Interstate Commerce Commission, letter of December 19, 1969 ---- 187
Cox, Charles K., president, Insurance Co. of North America, letter of December 2, 1969 ---- 66
Dorsey, Edward and Mrs. Josephine, letter of January 31, 1969 ---- 258
Durkin, John A., commissioner of insurance, State of New Hampshire, press release of June 30, 1969 ---- 281
Groupe, Leonard M., Illinois State Department of Insurance, Bureau of Liquidations, letter of December 16, 1968 ---- 259
Hanson, Jon S., National Association of Insurance Commissioners, letter ---- 158
Hart, Hon. Philip A., U.S. Senator from Michigan, letter of October 24, 1969 ---- 166
Hatfield, Hon. Mark O., U.S. Senator from Oregon, letter of February 11, 1970 ---- 300
Hecker, Sylvia, letter of February 3, 1969 ---- 257
Huening, Mrs. Josephine, letter of June 5, 1968 ---- 258
Huggins, Lyle, president, National Association of Insurance Agents, Inc., letter of February 10, 1970 ---- 299
Kemper, James S., Jr., Kemper Insurance Co., letter of January 26, 1970 ---- 270
Lemmon, Vestal, president, National Association of Independent Insurers, letters of:
  Questions of Hon. Warren G. Magnuson, U.S. Senator from Washington ---- 53
  January 23, 1970 ---- 56
  January 21, 1970 ---- 56
Maisonpierre, Andre, vice president, American Mutual Insurance Alliance, letter of December 22, 1969 ---- 88
Magnuson, Hon. Warren G., U.S. Senator from Washington, letter of December 9, 1969 ---- 56
McHugh, Donald P., vice-president and general counsel, State Farm Mutual Automobile Insurance Co., letter of February 20, 1970 ---- 303
McVey, Willis A., assistant casualty actuary, Casualty Division, Texas State Board of Insurance, memorandum of January 2, 1970 ---- 208
NAIC State Post Assessment Insurance Guaranty Association (model bill) ---- 142
Stafford, Hon. George M., Acting Chairman, Interstate Commerce Commission, letter of November 4, 1969 ---- 167
Wise, Paul S., president, American Mutual Insurance Alliance:
  Letter of January 20, 1970 ---- 271
  Telegram of February 10, 1970 ---- 273
Worthington, Lorne R., chairman, NAIC executive committee, Insurance Department of Iowa, letter January 16, 1970 ---- 203

FEDERAL INSURANCE GUARANTY CORPORATION

WEDNESDAY, NOVEMBER 12, 1969

U.S. SENATE,
COMMITTEE ON COMMERCE,
Washington, D.C.

The committee met, pursuant to notice, at 9:35 a.m. in room 5110, New Senate Office Building, the Honorable Warren G. Magnuson (chairman of the committee) presiding.

Present: Senators Magnuson, Hartke, Hart, Moss, and Spong.

OPENING STATEMENT BY THE CHAIRMAN

The CHAIRMAN. The committee will come to order. I want to make a short opening statement. I appreciate you people being here this morning. We may have some conflict in committee meetings, but we will proceed for as long as we can, until at least 10 o'clock, and then we must go into executive session on some matters of urgency, and we may have to recess the hearings. I hope you will understand.

So, we will begin hearings on S. 2236, which is a bill to create a Federal Insurance Guaranty Corporation to provide, we hope, American consumers protection against property and casualty insurance company insolvencies. Given the hardships which these insolvencies impose upon American policyholders and claimants, it is imperative that this committee provide a means of insuring American consumers against the loss of their insurance. It also seems imperative that this committee aid the State regulators in their examinations for solvency so that situations like State Fire & Casualty and Prudence Mutual can be avoided. Like any insurance activity, insurance company insolvency protection must minimize the risk of insolvency while providing resources to pay off those who have claims.

Now, S. 2236 offers a viable solution for this situation. It provides a nationwide fund for compensating victims and it is set up to provide State regulators expert help so that they can do a better job. I am sure there are many witnesses here who, as we move along with this bill, will suggest some changes. And I hope you will consider this bill as sort of a working paper. We welcome changes, and there may be suggestions or amendments that might improve the bill.

So, we hope that we can have many constructive suggestions and listen to the arguments, even arguments that might be against the bill. There will be some witnesses who will suggest that we abandon this course altogether in favor of some substitute measures, but the committee is basically deeply committed to solving the insolvency problem, and we hope that we can come out of these hearings with some kind of suggested legislation that can help solve this problem.

Staff member assigned to this hearing: S. Lynn Sutcliffe.

The authors of S. 2236 in no way intend to supplant State regulation through proposed Federal insurance guaranty corporations. Our intention is the opposite. We want to give the State regulators assistance in performing as well as possible their roles.

Federal examination power should be and would be exercised sparingly in cooperation with the States as long as they vigilantly regulate on behalf of the policyholder.

Any Federal assumption of regulatory power will only take place if the States abdicate their responsibilities. Those who argue that this bill will displace State regulation have a lower opinion of State regulation than I do. In most cases I think it is pretty good. I will now place in the record a copy of the bill and any agency comments thereon.

(The bill and agency comments follow:)

[S. 2236, 91st Cong., first sess.]

A BILL To create a Federal Insurance Guaranty Corporation to protect the American public against certain insurance company insolvencies

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That this Act may be cited as the "Federal Insurance Guaranty Corporation Act".

CREATION OF CORPORATION

SEC. 2. There is hereby created a Federal Insurance Guaranty Corporation (hereinafter referred to as the "Corporation") which shall guarantee, as hereinafter provided, the contractual performance of participating insurers and which, in connection therewith, shall have the powers hereinafter granted.

BOARD OF DIRECTORS

SEC. 3. The management of the Corporation shall be vested in a Board of Directors consisting of three members, one of whom shall be the Comptroller General of the United States and two of whom shall be citizens of the United States to be appointed by the President, by and with the advice and consent of the Senate. One of the appointive members shall be designated by the President Chairman of the Board of Directors of the Corporation and not more than two of the members shall be members of the same political party. Each such appointive member shall hold office for a term of six years, except that any person chosen to fill a vacancy shall be appointed only for the unexpired term of the member whom he shall succeed: *Provided, however,* That upon the expiration of his term of office a member shall continue to serve until his successor shall have been appointed and shall have qualified. In the event of a vacancy in the office of the Comptroller General of the United States and pending the appointment of his successor, or during the absence or disability of the Comptroller General, the Acting Comptroller General shall be a member of the Board of Directors in the place and stead of the Comptroller General. In the event of a vacancy in the office of the Chairman of the Board of Directors, and pending the appointment of his successor, the Comptroller General shall act as Chairman. A majority of the members shall constitute a quorum for the transaction of business. The members of the Board of Directors shall be ineligible during the time they are in office and for two years thereafter to hold any office, position, or employment in any participating insurer, except that this restriction shall not apply to any member who has served the full term for which he was appointed. No member of the Board of Directors shall be an officer or director of any participating insurer or hold stock in any participating insurer; and before entering upon his duties as a member of the Board of Directors he shall certify under oath that he has complied with this requirement and such certification shall be filed with the Secretary of the Board of Directors.

ADVISORY COMMITTEE

SEC. 4. (a)(1) There is hereby established an Advisory Committee consisting of nineteen members appointed by the Board of Directors. Members of the Committee shall be selected from among representatives of the general public, the

insurance industry, State and local governments including State insurance authorities, and the Federal Government. Of these members of the Committee, not more than six shall be regular full-time employees of the Federal Government, not less than four shall be representatives of the private insurance industry, and not less than four shall be representatives of State insurance authorities.

(2) The Board of Directors shall designate a Chairman and a Vice Chairman of the Committee.

(3) Each member shall serve for a term of two years or until his successor has been appointed, except that no person who is appointed while a full-time employee of a State or the Federal Government shall serve in such position after he ceases to be so employed, unless he is reappointed.

(4) Any member appointed to fill a vacancy occurring prior to the expiration of the term for which his predecessor was appointed shall be appointed for the remainder of that term.

(b) The Chairman shall preside at all meetings, and the Vice Chairman shall preside in the absence or disability of the Chairman. In the absence of both the Chairman and Vice Chairman, the Board of Directors may appoint any member to act as Chairman pro tempore. The Committee shall meet at such times and places as it or the Board of Directors may fix and determine, but shall hold at least four regularly scheduled meetings a year. Special meetings may be held at the call of the Chairman or any three members of the Committee, or at the call of the Board of Directors. A majority of the members shall constitute a quorum for the transaction of business.

(c) The Committee shall review general policies of the Corporation and advise the Board of Directors with respect thereto, assist in obtaining the cooperation of insurers, industry groups, and Federal and State agencies, consult with and make recommendations to the Board with respect to carrying out the purposes of this title, and perform such other functions as the Board may, from time to time, assign. The written reports and recommendations of the Committee shall be made available by the Board to the public.

(d) The members of the Committee shall not, by reason of such membership, be deemed to be employees of the United States, and such members, except those who are regular full-time employees of the Government, shall receive for their services, as members, the per diem equivalent to the rate for grade GS–18 of the General Schedule under section 5332 of title 5, United States Code, when engaged in the performance of their duties, and each member of the Committee shall be allowed travel expenses, including per diem in lieu of subsistence, as authorized by section 5703 of such title for persons in the Government service employed intermittently.

CAPITAL STOCK

SEC. 5. The Corporation shall have a capital stock of $50,000,000 which shall be divided into shares of $1,000 each. The total amount of such capital stock shall be subscribed to by the Secretary of the Treasury. For the purpose of making payments for such stock the Secretary of the Treasury is authorized to use as a public debt transaction the proceeds of the sale of any securities hereafter issued under the Second Liberty Bond Act, and the purpose for which securities may be issued under such Act are extended to include such purchases.

DEFINITIONS

SEC. 6. As used in this title—

(1) The term "insurer" means any enterprise engaged in the business of issuing or reinsuring property, casualty, or surety insurance policies in interstate commerce or engaged in the business of issuing property, casualty, or surety policies which are reinsured (in whole or in part) in interstate commerce.

(2) The term "local insurer" means any enterprise engaged in the business of issuing or reinsuring property, casualty, or surety insurance policies solely within one State.

(3) The term "participating insurer" means any enterprise whose property, casualty, or surety insurance policies are guaranteed under this title.

(4) The term "property, casualty, or surety insurance policy" or "policy" means any contract of property, casualty, or surety insurance, including any endorsements thereto and without regard to the nature or form of the contract or endorsements, insuring against legal liability or loss contingencies, other than those provided for by life, accident and health, or title insurance.

(5) The term "net direct premiums written" means direct gross premiums written on property, casualty, or surety insurance policies, less return premiums

thereon and dividends paid to policyholders on such direct business. For the purposes of this subsection, premiums written on insurance policies issued to self insurers, whether or not designated as reinsurance contracts, shall be deemed "net direct premiums written".

(6) The term "policyholder claim" means (a) a claim of a policyholder or insured within the coverage of a policy, arising out of an occurrence wherein such policyholder or insured suffered damage or is subject to liability for damages within the coverage of the policy, or (b) a claim by a policyholder or insured for return premium arising out of the termination of the policy by reason of insolvency.

(7) The term "Board" means the Board of Directors of the Federal Insurance Guaranty Corporation.

(8) The term "Fund" means the Federal Insurance Guaranty Fund as described in section 10 of this title.

(9) The term "interstate commerce" means trade or commerce among the several States, or between the District of Columbia or any possession of the United States and any State or other possession, or within the District of Columbia.

(10) The term "State" means any State, any possession of the United States, the District of Columbia, and the Commonwealth of Puerto Rico.

(11) The term "State supervisory authority" means the agency or individual of the State of domicile of the insurer having responsibility for regulating the business of insurance within that State.

INCORPORATION; POWERS

SEC. 7. (a) Upon the date of enactment of this title, the Corporation shall become a body corporate and shall be an instrumentality of the United States, and as such shall have power—

(1) to adopt, alter, and use a corporate seal;

(2) to have succession until dissolved by an Act of Congress;

(3) to make contracts, and execute all instruments necessary and appropriate in the exercise of its powers;

(4) to sue and be sued, complain and defend, in any court of law or equity, State or Federal. All suits of a civil nature at common law or in equity to which the Corporation shall be a party shall be deemed to arise under the laws of the United States, and the United States district courts shall have original jurisdiction thereof without regard to the amount in controversy; and the Corporation may, without bond or security, remove any such action, suit, or proceeding from a State court to the United States district court for the district or division embracing the place where the same is pending by following any procedure for removal now or hereafter in effect. No attachment or execution shall be issued against the Corporation or its property before final judgment in any suit, action, or proceeding in any State, county, municipal, or United States court. The Board of Directors shall designate an agent upon whom service of process may be made in any State, territory, or jurisdiction in which any participating insurer does business;

(5) to appoint by its Board of Director such officers, employees, attorneys, agents, adjusters, examiners, and other persons as may be necessary for the performance of its duties, to define their duties, fix their compensation, require bonds of them and fix the penalty thereof, and to dismiss at pleasure such officers or employees. Nothing in this chapter or any other Act shall be construed to prevent the appointment and compensation as an officer or employee of the Corporation of any officer or employee of the United States in any board, commission, independent establishment, or executive department thereof;

(6) to prescribe by its Board of Directors bylaws not inconsistent with law, regulating the manner in which its general business may be conducted and the privileges granted to it by law may be exercised and enjoyed;

(7) to exercise by its Board of Directors, or duly authorized officers or agents, all powers specifically granted by the provisions of this title, and such incidental powers as shall be necessary to carry out the powers so granted;

(8) to make examinations of and to require information and reports from any insurer or local insurer making application for guaranty status, or whose policies are guaranteed under this title; and

(9) to prescribe by its Board of Directors such rules and regulations as it may deem necessary to carry out the provisions of this title.

(b) No individual, association, partnership, or corporation, other than the Corporation, shall hereafter use the words "Federal Insurance Guaranty Corporation" or any combination of such words, as the name or part thereof under which he or it shall do business. Any violation of this subsection shall be punishable by a fine of not exceeding $100 for each day during which such violation is committed.

ADMINISTRATION OF CORPORATION

SEC. 8. (a) The Board of Directors shall administer the affairs of the Corporation fairly and impartially and without discrimination. The Board of Directors shall determine and prescribe the manner in which its obligations shall be incurred and its expenses allowed and paid. The Corporation shall be entitled to free use of the United States mails in the same manner as the executive departments of the Government, and, with the consent of the head of any department or agency of the Federal Government, or of any State government, may avail itself of the use of information, services, and facilities thereof in carrying out the provisions of this title.

(b) The Corporation shall appoint examiners who shall have power, on behalf of the Corporation, to examine any insurer or local insurer making application for guaranty status or whose policies are guaranteed under this title, whenever in the judgment of the Corporation an examination of such insurer is necessary. In making examination of insurers or local insurers the examiners shall have power on behalf of the Corporation to make such examinations of the affairs of all affiliates of such insurers as shall be necessary to disclose fully the relations between such insurers and their affiliates and the effect of such relations upon such insurer. Each examiner shall have power to make a thorough examination of all of the affairs of the insurer and such affiliates and shall make a full and detailed report of the condition of the insurer to the Corporation. All examiners appointed by the Corporation shall cooperate as far as practicable with the appropriate State supervisory authorities in conducting examinations under this title. It is the intent of Congress that any such examinations shall be coordinated with examinations by the appropriate State supervisory authorities and the National Association of Insurance Commissioners. Copies of reports of examinations by examiners appointed by this subsection shall be furnished by the Corporation to the appropriate State supervisory authorities which shall be afforded the opportunity to comment thereon. Copies of any report or statement made to any State supervisory authority by any participating insurer shall be filed with the Corporation within ten days after such reports or statements have been made to such authority. The Corporation may accept any report or statement made to an appropriate State supervisory authority by any insurer or local insurer making application for guaranty status under this title or whose policies are guaranteed under this title.

(c) In connection with examinations of insurers and local insurers, the Corporation or its examiners shall have power to adminster oaths and affirmations and to examine and to take and preserve testimony under oath as to any matter in respect of the affairs or ownership of any such insurer or affiliate thereof, and to issue subpenas and subpena duces tecum, and, for the enforcement thereof, the Corporation may apply to the United States district court for the judicial district or the United States court in any territory or possession in which the principal office of the insurer or affiliate thereof is located, or in which the witness resides or carries on business. Such courts shall have jurisdiction and power to order and require compliance with any such subpena.

(d) The term "affiliate" or "affiliates" as used in the foregoing subsections (b) and (c) means any enterprise related directly or indirectly to the insurance activities of the insurer or local insurer.

(e) In cases of refusal to obey a subpena issued to, or contumacy by, any person, the Board of Directors may invoke the aid of any court of the United States within the jurisdiction of which such hearing, examination, or investigation is carried on, or where such person resides or carries on business, in requiring the attendance and testimony of witnesses and the production of books, records, or other papers. And such court may issue an order requiring such person to appear before the Board of Directors or member or person designated by the Board of Directors, there to produce records, if so ordered, or to give testimony touching the matter in question; and any failure to obey such order of the court may be punished by such court as a contempt thereof. All process in any such case may be served in the judicial district

whereof such person is an inhabitant or carries on business or wherever he may be found. No person shall be excused from attending and testifying or from producing books, records, or other papers in obedience to a subpena issued under the authority of this chapter on the ground that the testimony or evidence, documentary or otherwise, required of him may tend to incriminate him or subject him to penalty or forfeiture; but no individual shall be prosecuted or subject to any penalty or forfeiture for or on account of any transaction, matter, or thing concerning which he is compelled to testify or produce evidence, documentary or otherwise, after having claimed his privilege against self-incrimination, except that such individual so testifying shall not be exempt from prosecution and punishment for perjury committed in so testifying.

(f) If any participating insurer, after written notice is given to it and the State supervisory authority of the recommendations of the Corporation based on a report of examination by an examiner of the Corporation (in cooperation with an examiner of the appropriate State supervisory authority), shall fail to comply with such recommendations within such time as the Corporation deems appropriate in the light of the circumstances of the case, the Corporation may publish such part of such report of examination as relates to any such recommendation not complied with: *Provided*, That notice of intention to make such publication shall be given to the insurer and the appropriate State supervisory authority at least sixty days before such publication is made.

(g) The Corporation may cause any and all records, papers, or documents kept by it or in its possession or custody to be photographed or microphotographed or otherwise reproduced upon film, which photographic film shall comply with the minimum standards of quality approved for permanent photographic records by the National Bureau of Standards. Such photographs, microphotographs, or photographic film or copies thereof shall be deemed to be an original record for all purposes, including introduction in evidence in all State and Federal courts or administrative agencies and shall be admissible to prove any act, transaction, occurrence, or event therein recorded. Such photographs, microphotographs, or reproduction shall be preserved in such manner as the Board of Directors of the Corporation shall prescribe and the original records, papers, or documents may be destroyed or otherwise disposed of as the Board shall direct.

PAYMENT OF GUARANTY

SEC. 9. (a) The Corporation shall assume and perform all the obligations of a participating insurer under property, casualty, and surety insurance policies which are guaranteed under this title, if—

(1) such insurer is determined by a final decision of a court of competent jurisdiction to be insolvent;

(2) the receiver or liquidator appointed by such court gives written notice to the Corporation of such decision; and

(3) such receiver or liquidator makes all books and records (including claim files) available to the Corporation.

Upon compliance with the foregoing with respect to any such insurer, the Corporation shall file forthwith a certificate of assumption with the court having jurisdiction over such insurer.

(b) Upon the filing of a certificate of assumption, all proceedings pending in any court against the insured or the insurer arising out of an occurrence within the coverage of a policy guaranteed under this title shall be stayed automatically for a period of thirty days for the purposes of this title.

(c) The Corporation shall be subject to the same obligations, liabilities, terms, conditions, and waivers of the insurer and shall have available any defense or defenses (including that of policy limits) which would be available to the insurer.

(d) The Corporation is authorized to investigate, examine, adjust, compromise or settle any claim pending against the insured or the insurer on or after the date of the filing of a certificate of assumption. The Corporation is authorized to defend any action pending or brought against the policyholder or the insured on or after the date of the filing of such certificate.

(e) In no event shall any claim for return premium be allowed in excess of 50 per centum of the unearned premiums.

(f) Any person (including any individual, partnership, association, or corporation) having a policyholder claim against the insurer or claim against the insured who also has a claim under State law against a State insurance insolvency or liability security fund growing out of the same insolvency, shall be required to

exhaust first his rights under such State law against such State fund, if any, to the extent available for the satisfaction of his claim before receiving any payment under this title on any such claim, and the liability, if any, of the Corporation to any such claimant under this title shall be limited to the excess, if any, of any such claim not so satisfied under State law from such State fund.

(g) Any person (including any individual, partnership, association, or corporation) having a claim against his insurer under any insolvency protection provision contained in his insurance policy, which claim arises out of the insolvency of a participating insurer, shall be required to exhaust first his rights under this title and/or under any applicable State insolvency or liability security fund, as provided for in subsection (f) hereof, before receiving any payment for such claim from his insurer, and the liability, if any, of his insurer under such policy shall be limited to the excess, if any, of any such claim not so satisfied from such State fund and/or the Fund provided for herein.

(h) The Corporation shall be entitled to valid claim against the insurer, or its liquidator, rehabilitator, conservator, receiver or trustee in bankruptcy, in an amount equal to the liabilities of such insurer paid from the Fund, less the net payments paid into the Fund by such insurer.

FEDERAL INSURANCE GUARANTY FUND

SEC. 10. (a) Funds obtained by the Corporation from the sale of its capital stock, as provided in section 5, and from guaranty fees collected pursuant to subsection (b) of section 13, shall be deposited in the Federal Insurance Guaranty Fund, which is hereby established. The Fund shall be held by the Corporation and used by it for carrying out its guaranty functions under this title, and for operating expenses arising in connection therewith.

(b) Whenever after retirement of the outstanding Treasury shares issued pursuant to section 5 the net asset value of the Fund exceeds 2 per centum of the annual net direct premiums written by all participating insurers, the Corporation shall waive the requirements for fees as herein stated: *Provided*, That such requirement shall be reinstated whenever the net asset value of such fund is less than 2 per centum of the annual net direct premiums written by all participating insurers: *Provided further*, That no distribution or rebate shall be made by reason of the fact that the total amount in fees collected by the Corporation at any time exceeds 2 per centum of such annual direct written premiums. In determining net asset value for the purposes of this subsection, the Board shall include estimated liabilities that may be chargeable to such Fund.

(c) No participating insurer shall be required to pay any fee or assessment under any State insurance insolvency or liability security fund law for any period during which the insurance policies of that insurer are guaranteed pursuant to this title.

(d) The Corporation shall retire as rapidly as practicable, having due regard to the need to maintain at all times the solvency of the Fund, the capital stock of the Corporation which is held by the Treasury.

(e) In the event that the Congress should repeal this title, any moneys remaining in such Fund at that time, after redemption of any outstanding capital stock, repayment of any outstanding loans from the Treasury under section 16 of this title and discharge of all expenses and obligations under this title, shall be returned to the participating insurers pro rata in accordance with the guaranty fees they have paid into the Fund.

(f) In the event that the Congress should reduce the size of the Fund specified in subsection (b) of this section 10, any excess in the Fund above the new statutory limit shall be returned to the participating insurers pro rata in accordance with the guaranty fees they have paid into the Fund.

APPLICATION FOR GUARANTEED STATUS

SEC. 11. Each insurer shall, and each local insurer may, make application to the Corporation for guaranty under this title. Such application shall be in such form and contain such information as the Corporation shall by regulation prescribe. The Corporation shall approve any such application if it finds, after examination, that the applicant is capable of conducting its business in a sound and solvent manner and, in making its determination, shall consider, along with such other factors as it may deem necessary or appropriate, the applicant's capital and surplus, reasonableness of operational expenses, premium writings as related to surplus, adequacy of loss and expense reserves, reinsurance, invest-

ment portfolio and managerial qualifications. Upon approval of any such application, after the imposition of any necessary conditions, the Corporation shall notify the applicant and issue to it an appropriate certificate which shall become effective not earlier than one year after the date of enactment of this title. Upon the taking effect of any such certificate, the contractual obligations of such participating insurer under property, casualty, and surety insurance policies shall be guaranteed by the Corporation. Each participating insurer shall include a statement in each policy to the effect that such policy is guaranteed by the Corporation. The Corporation shall prescribe by regulation the substance of such statement and the form and manner of use. If any such application is not approved by the Corporation, it shall promptly notify the applicant as well as the State supervisory authority, and shall state the reasons therefor. Any insurer or local insurer the application of which has been denied by the Corporation shall, upon written request made to the Corporation within thirty days after receipt of the notification of denial, be granted a hearing as provided in section 14(i) of this title.

PENALTIES

SEC. 12. (a) Any insurer (other than a local insurer) issuing or reinsuring any property, casualty, or surety insurance policy which is not guaranteed under this title shall forfeit to the United States the sum of $1,000 for each and every day that such policy is in effect and is not guaranteed under this title. Such forfeiture shall be payable to the Corporation for its use. The Corporation is authorized to collect any unsatisfied forfeiture claim from the directors and officers of the insurer individually. This subsection shall take effect upon the expiration of one year after the effective date of this title.

(b) Whoever falsely advertises or otherwise misrepresents by any device whatsoever that any property, casualty, or surety insurance policy is guaranteed by the Federal Insurance Guaranty Corporation, or by the Government of the United States, or by any instrumentality thereof, shall be fined not more than $1,000, or imprisoned not more than one year, or both.

REPORTS; GUARANTY FEE

SEC. 13. (a) Each participating insurer shall make to the Corporation reports of condition which shall be in such form, at such time, and shall contain such information as the Board of Directors may require. The Board of Directors may require reports of condition to be published in such manner, not inconsistent with any applicable law, as it may direct. Every participating insurer which fails to make or publish any such report within ten days of its due date shall be subject to a penalty of not more than $100 for each day of such failure, which penalty shall be recoverable by the Corporation for its use.

(b) (1) Each calendar year following the year in which the application of a participating insurer was approved by the Corporation, such participating insurer shall pay to the Corporation a guaranty fee. This fee, which shall be equal to one-eighth of 1 per centum of the net direct premiums written by the participating insurer during the year, shall be assessed semiannually, based on net direct premiums written during the periods January 1 through June 30 and July 1 through December 31.

(2) On or before the last day of the first month following each of the above mentioned semiannual periods, each participating insurer shall file with the Corporation a certified statement showing the net direct premiums written by such insurer during that period. In the event that accurate information is not available at that time, an estimate may be filed: *Provided, however,* That a final certified statement must be filed not later than sixty days from the last day of the reporting period.

(3) The certified statements required to be filed with the Corporation under paragraph (2) of this subsection shall be in such form and set forth such supporting information as the Board of Directors shall prescribe and shall be certified by the president of the insurer or any other officer designated by its board of directors to be, to the best of his knowledge and belief, true, correct, and complete and in accordance with this title and regulations issued thereunder. The assessment payments required from participating insurers under paragraph (1) of this subsection shall be made in such manner and at such time or times as the Board of Directors shall prescribe, provided the time or times so prescribed shall not be later than sixty days after filing the certified statement setting forth the amount of assessment.

(4) Except as otherwise provided in this section, the Board of Directors shall prescribe all needful rules and regulations for the enforcement of this section. The Board of Directors may limit the retroactive effect, if any, of any of its rules or regulations.

(c) The Corporation may (1) refund to a participating insurer any payment of assessment in excess of the amount due to the Corporation, or (2) credit such excess toward the payment of the assessment next bcoming due from such insurer and upon succeeding assessments until the credit is exhausted.

(d) Any participating insurer which fails to make any report of condition under subsection (2) of this section or to file any certified statement required to be filed by it in connection with determining the amount of any assessment payable by the insurer to the Corporation may be compelled to make such report or file such statement by mandatory injunction or other appropriate remedy in a suit brought for such purpose by the Corporation against the insurer and any officer or officers thereof in any court of the United States of competent jurisdiction in the district or territory in which such insurer is located.

(e) The Corporation, in a suit brought at law or in equity in any court of competent jurisdiction, shall be entitled to recover from any participating insurer the amount of any unpaid assessment lawfully payable by such insurer to the Corporation, whether or not such insurer shall have made any such report of condition under subsection (a) of this section or filed any such certified statement and whether or not suit shall have been brought to compel the insurer to make any such report or file any such statement. No action or proceeding shall be brought for the recovery of any assessment due to the Corporation, or for the recovery of any amount paid to the Corporation in excess of the amount due to it, unless such action or proceeding shall have been brought within five years after the right accrued for which the claim is made, except where the participating insurer has made or filed with the Corporation a false or fraudulent certified statement with the intent to evade, in whole or in part, the payment of assessment, in which case the claim shall not be deemed to have accrued until the discovery by the Corporation that the certified statement is false or fraudulent.

(f) Should any participating insurer fail to make any report of condition under subsection (a) of this section or to file any certified statement required to be filed by such insurer under any provision of this section, or fail to pay any assessment required to be paid by such insurer under any provision of this title, and should the insurer not correct such failure within thirty days after written notice has been given by the Corporation to an officer of the insurer, citing this subsection, and stating that the insurer has failed to file or pay as required by law, all the rights, privileges, and franchises of the insurer granted to it under this title shall be thereby forfeited. Whether or not the penalty provided in this subsection has been incurred shall be determined and adjudged after hearing in the manner provided in section 14(i) of this title. The remedies provided in this subsection and in the two preceding subsections shall not be construed as limiting any other remedies against any participating insurer, but shall be in addition thereto.

(g) Any participating insurer which willfully fails or refuses to file any certified statement or pay any assessment required under this title shall be subject to a penalty of not more than $100 for each day that such violations continue, which penalty the Corporation may recover for its own use.

(h)(1) Whenever a change occurs in the outstanding voting stock of any participating insurer which will result in control or in a change in the control of such insurer, the president or other chief executive officer of such insurer shall promptly report such facts to the Corporation upon obtaining knowledge of such change. As used in this subsection, the term "control" means the power directly or indirectly to direct or cause the direction of the management or policies of the insurer. If there is any doubt as to whether a change in ownership or other change in the outstanding voting stock of the insurer is sufficient to result in control or a change in the control thereof, such doubt shall be resolved in favor of reporting the facts to the Corporation.

(2) Whenever such a change as described in paragraph (1) of this subsection occurs, the participating insurer involved shall report promptly to the Corporation any change or changes, or replacement or replacements, of its chief executive officer or of any director occurring in the next twelve-month period, including in its report a statement of the past and current business and professional affiliations of the new chief executive officer or director.

(3) Whenever a participating insurer makes a loan or loans secured or to be secured by 25 per centum or more of the voting stock of another participating insurer, the president or other chief executive officer of the lending insurer shall promptly report such fact to the Corporation upon obtaining knowledge of such loan or loans, except that no report need be made in those cases where the borrower has been the owner of record of the stock for a period of one year or more, or the stock is of a newly organized insurer.

(4) The reports required by paragraphs (1) and (3) of this subsection shall contain the following information to the extent that it is known by the person making the report: (a) the number of shares involved, (b) the names of the sellers (or transferors), (c) the names of the purchasers (or transferees), (d) the names of the beneficial owners if the shares are registered in another name, (e) the purchase price, (f) the total number of shares owned by the sellers (or transferors), the purchasers (or transferees) and the beneficial owners both immediately before and after the transaction, and in the case of a loan, (g) the name of the borrower, (h) the amount of the loan, and (i) the name of the insurer issuing the stock securing the loan and (j) the number of shares securing the loan. In addition to the foregoing, such reports shall contain such other information as may be available to inform the Corporation of the effect of the transaction upon control of the insurer whose stock is involved.

Termination; Enforcement

terminations of guaranty

Sec. 14. (a) Whenever the Board of Directors shall find that (i) a participating insurer or its directors or officers have engaged or are engaging in unsafe or unsound practices in conducting the business of the insurer, (ii) the insurer is in an unsafe or unsound condition to continue operations as a participating insurer, or (iii) the insurer has violated any provision of this title or any rule, regulation, or order issued pursuant to this title, or any condition imposed in writing by the Corporation in connection with the granting of any application or other request by the insurer, or any written agreement entered into with the Corporation, the Board of Directors shall give to the State supervisory authority a statement with respect to such practices or violations for the purposes of securing the correction thereof and shall give a copy of the statement to the insurer. Unless correction shall be made within one hundred and twenty days from receipt of such statement, or such shorter period not less than twenty days fixed by the Corporation in any case where the Board of Directors in its discretion has determined that the insurance risk of the Corporation is unduly jeopardized, or unless within such time the Corporation shall have received acceptable assurances that such correction will be made within a time and in a manner satisfactory to the Corporation, or in the event such assurances are submitted to and accepted by the Corporation but are not carried out in accordance with their terms, the Board of Directors, if it shall determine to proceed further, shall give to the insurer not less than thirty days' written notice of intention to terminate its guaranteed status. Such notice shall contain a statement of the facts constituting the alleged violation or unsafe or unsound practice or condition and shall fix a time and place for a hearing before the Board of Directors or before a person designated by it to conduct such hearing, at which evidence may be produced, and upon such evidence the Board of Directors shall make written findings which shall be conclusive, subject to right of review as hereinafter provided for. If the Board of Directors shall find that any unsafe or unsound practice or condition or violation specified in such statement has been established and has not been corrected within the time above prescribed in which to make such corrections, the Board of Directors may order that the guaranteed status of the insurer be terminated on a date subsequent to such finding and to the expiration of the time specified in such notice of intention. Unless the insurer shall appear at the hearing by a duly authorized representative, it shall be deemed to have consented to the termination of its guaranteed status and termination of such status thereupon may be ordered. Any insurer whose guaranteed status has been terminated by order of the Board of Directors under this subsection shall have the right of judicial review of such order only to the same extent as provided for the review of orders under subsection (i) of this section. The Corporation may publish notice of such termination and the insurer shall give notice of such termination to each of its policyholders at his last address of record on the books of the insurer, in such manner and at such time as the

Board of Directors may find to be necessary and may order for the protection of policyholders. In the event of failure to give the notice to policyholders as herein provided, the Corporation is authorized to give such notice. An order terminating the guaranteed status of any participating insurer shall not affect any guaranteed policy issued by such insurer prior to the date on which the order was issued, but shall be effective with respect to (1) the renewal of such policy, and (2) any property, casualty, or surety insurance policy thereafter issued by such insurer. The procedures contained in this subsection are independent of and supplementary to those provided for in subsections (b) through (e).

CEASE-AND-DESIST PROCEEDINGS

(b) (1) If, in the opinion of the Corporation, any participating insurer is engaging or has engaged, or the Corporation has reasonable cause to believe that such insurer is about to engage, in an unsafe or unsound practice in conducting its business, or is violating or has violated, or the Corporation has reasonable cause to believe that such insurer is about to violate, a law, rule, or regulation, or any condition imposed in writing by the Corporation in connection with the granting of any application or other request by the insurer, or any written agreement entered into with the Corporation, the Corporation may issue and serve upon the insurer a notice of charges in respect thereof. The notice shall contain a statement of the facts constituting the alleged violation or violations or the unsafe or unsound practice or practices, and shall fix a time and place at which a hearing will be held to determine whether an order to cease and desist therefrom should issue against the insurer. Such hearing shall be fixed for a date not earlier than thirty days nor later than sixty days after service of such notice unless an earlier or a later date is set by the Corporation at the request of the insurer. Unless the insurer shall appear at the hearing by a duly authorized representative, it shall be deemed to have consented to the issuance of the cease-and-desist order. In the event of such consent, or if upon the record made at any such hearing, the Corporation shall find that any violation or unsafe or unsound practice specified in the notice of charges has been established, the Corporation may issue and serve upon the insurer an order to cease and desist from any such violation or practice. Such order may by provisions which may be mandatory or otherwise, require the insurer and its directors, officers, employees, and agents to cease and desist from the same, and, further, to take affirmative action to correct the conditions resulting from any such violation or practice.

(2) A cease-and-desist order shall become effective at the expiration of thirty days after the service of such order upon the insurer concerned (except in the case of a cease-and-desist order issued upon consent, which shall become effective at the time specified therein), and shall remain effective and enforcible as provided therein, except to such extent as it is stayed, modified, terminated, or set aside by action of the Corporation or a reviewing court.

TEMPORARY CEASE-AND-DESIST ORDERS

(c) (1) Whenever the Corporation shall determine that the violation or threatened violation or the unsafe or unsound practice or practices, specified in the notice of charges served upon the insurer to paragraph (1) of subsection (b) of this section, or the continuance thereof, is likely to cause insolvency or substantial dissipation of assets or earnings of the insurer, or is likely otherwise seriously to prejudice the interest of the policyholders or the Corporation, the Corporation may issue a temporary order requiring the insurer to cease and desist from any such violation or practice. Such orders shall become effective upon service upon the insurer and, unless set aside, limited, or suspended by a court in proceedings authorized by paragraph (2) of this subsection, shall remain effective and enforcible pending the completion of the administrative proceedings pursuant to such notice and until such time as the Corporation shall dismiss the charges specified in such notice or, if a permanent cease-and-desist order is issued against the insurer, until the effective date of any such order.

(2) Within ten days after the insurer concerned has been served with a temporary cease-and-desist order, the insurer may apply to the United States district court for the judicial district in which the principal office of the insurer is located, or the United States District Court for the District of Columbia, for an injunction setting aside, limiting, or suspending the enforcement, operation, or effectiveness of such order pending the completion of the administrative proceedings pursuant to the notice of the charges served upon the insurer under

paragraph (1) of subsection (b) of this section, and such court shall have jurisdiction to issue such injunction.

(3) In the case of violation or threatened violation of, or failure to obey, a temporary cease-and-desist order, the Corporation may apply to the United States district court, or the United States court of any territory, within the jurisdiction of which the principal office of the insurer is located, for an injunction to enforce such order and, if the court shall determine that there has been such violation or threatened violation or failure to obey, it shall be the duty of the court to issue such injunction.

LIABILITIES OF DIRECTORS AND OFFICERS

(d) (1) Whenever, in the opinion of the Corporation, any director or officer of a participating insurer has committed any violation of law, rule, or regulation, or of a cease-and-desist order which has become final, or has engaged or participated in any unsafe or unsound practice in connection with the insurer, or has committed or engaged in any act, omission, or practice which constitutes a breach of his fiduciary duty as such director or officer, and the Corporation determines that the insurer has suffered or will probably suffer substantial financial loss or other damage or that the interests of the policyholders could be seriously prejudiced by reason of such violation or practice or breach of fiduciary duty, and that such violation or practice or breach of fiduicary duty is one involving personal dishonesty on the part of such director or officer, the Corporation may serve upon such director a written notice of its intention to remove him from office.

(2) Whenever, in the opinion of the Corporation, any director or officer of a participating insurer, by conduct or practice with respect to another insurer or other business institution which resulted in substantial financial loss or other damage, has evidenced his personal dishonesty and unfitness to continue as a director or officer, and, whenever, in the opinion of the Corporation, any other person participating in the conduct of the affairs of the insurer, by conduct or practice with respect to such insurer or other insurer or other business institution which resulted in substantial financial loss or other damage, has evidenced his personal dishonesty and unfitness to participate in the conduct of the affairs of such insurer, the Corporation may serve upon such director, officer, or other person a written notice of its intention to remove him from office and/or to prohibit his further participation in any manner in the conduct of the affairs of such insurer.

(3) In respect to any director or officer of an insurer or any other person referred to in paragraphs (1) and (2) of this subsection, the Corporation may, if it deems it necessary for the protection of the insurer or the interests of the insurer's policyholders or of the Corporation, by written notice to such effect served upon such director, officer, or other person, suspend him from office and/or prohibit him from further participation in any manner in the conduct of the affairs of the insurer. Such suspension and/or prohibition shall become effective upon service of such notice, and, unless stayed by a court in proceedings authorized by paragraph (5) of this subsection, shall remain in effect pending the completion of the administrative proceedings pursuant to the notice served under paragraphs (1) and (2) of this subsection and until such time as the Corporation shall dismiss the charges specified in such notice, or, if an order of removal and/or prohibition is issued against the director or officer or other person, until the effective date of any such order. Copies of any such notice shall also be served upon the insurer of which he is a director or officer or in the conduct of whose affairs he has participated.

(4) A notice of intention to remove a director, officer, or other person from office and/or to prohibit his participation in the conduct of the affairs of an insurer, shall contain a statement of the facts constituting grounds therefor, and shall fix a time and place at which a hearing will be held thereon. Such hearing shall be fixed for a date not earlier than thirty days nor later than sixty days after the date of service of such notice, unless an earlier or later date is set by the Corporation at the request of (a) such director, officer, or other person and for good cause shown, (b) the Attorney General of the United States, or (c) the State supervisory authority. Unless such director, officer, or other person shall appear at the hearings in person or by a duly authorized representative, he shall be deemed to have consented to the issuance of an order of such removal and/or prohibition. In the event of such consent, or if upon the record made at any such hearing the Corporation shall find that any of the grounds specified in such notice

has been established, the Corporation may issue such orders of suspension or removal from office, and/or prohibition from participation in the conduct of the affairs of the insurer, as it may deem appropriate. Any such order shall become effective at the expiration of thirty days after service upon such insurer and the director, officer, or other person concerned (except in the case of an order issued upon consent, which shall become effective at the time specified therein). Such order shall remain effective and enforcible except to such extent as it is stayed, modified, terminated, or set aside by action of the Corporation or a reviewing court.

(5) Within ten days after any director, officer, or other person has been suspended from office and/or prohibited from participation in the conduct of the affairs of an insurer under paragraph (3) of this subsection, such director, officer, or other person may apply to the United States district court for the judicial district in which the principal office of the insurer is located, or the United States District Court for the District of Columbia, for a stay of such suspension and/or prohibition pending the completion of the administrative proceedings pursuant to the notice served upon such director, officer, or other person under paragraph (1) or (2) of this subsection, and such court shall have jurisdiction to stay such suspension and/or prohibition.

(e) Whenever any director or officer of a participating insurer or other person participating in the conduct of the affairs of such insurer, is charged in any information, indictment, or complaint authorized by a United States attorney, with the commission of or participation in a felony involving dishonesty or breach of trust, the Corporation may by written notice served upon such director, officer, or other person suspend him from office and/or prohibit him from further participation in any manner in the conduct of the affairs of the insurer. A copy of such notice shall also be served upon the insurer. Such suspension and/or prohibition shall remain in effect until such information, indictment, or complaint is finally disposed of or until terminated by the Corporation. In the event that a judgment of conviction with respect to such offense is entered against such director, officer, or other person, and at such time as such judgment is not subject to further appellate review, the Corporation may issue and serve upon such director, officer, or other person an order removing him from office and/or prohibiting him from further participation in any manner in the conduct of the affairs of the insurer except with the consent of the Corporation. A copy of such order shall also be served upon such insurer whereupon such director or officer shall cease to be a director or officer. A finding of not guilty or other disposition of the charge shall not preclude the Corporation from thereafter instituting proceedings to remove such director, officer, or other person from office and/or to prohibit further participation in the insurer's affairs, pursuant to paragraph (1) or (2) of subsection (d) of this section.

(f) Except with the written consent of the Corporation, no person shall serve as a director, officer, or employee of a participating insurer who has been convicted, or who is hereafter convicted, of any criminal offense involving dishonesty or a breach of trust. For each willful violation of this prohibition, the insurer involved shall be subject to a penalty of not more than $100 for each day this prohibition is violated, which the Corporation may recover for its use.

PENALTIES

(g) Any director or officer, or former director or officer, of a participating insurer against whom there is an outstanding and effective notice or order (which is an order which has become final) served upon such director, officer, or other person under subsections (d) or (e) above and who (1) participates in any manner in the conduct of the affairs of such insurer, or directly or indirectly solicits or procures, or transfers or attempts to vote any proxies, consents, or authorizations in respect to any voting rights in such insurer, or (2) without the prior written approval of the Corporation, votes for a director or serves or acts as a director, officer, or employee of any insurer, shall uopn conviction be fined not more than $5,000 or imprisoned for not more than one year, or both.

(h) Whenever a participating insurer shall violate any of the penal provisions of this title, such violation shall be deemed to be also that of the individual directors, officers, or agents of such insurer who shall have authorized, ordered, or done any of the acts constituting in whole or in part such violation, and such violation thereof of any such director, officer, or agent, he may be punishable by a fine not exceeding $5,000 or by imprisonment not exceeding one year, or both.

HEARINGS AND JUDICIAL REVIEW

(i) (1) Any hearings provided for in this section or in section 11 of this title shall be held in the Federal judicial district or in the territory in which the principal office of the insurer is located unless the party afforded the hearing consents to another place, and shall be conducted in accordance with the provisions of chapter 5 of title 5. Such hearing shall be public, unless the Corporation, in its discretion, after fully considering the views of the party afforded the hearing, determines that a private hearing is necessary to protect the public interest. After such hearing, and within ninety days after the Corporation has notified the parties that the case has been submitted to it for final decision, the Corporation shall render its decision (which shall include findings of fact upon which its decision is predicated) and shall issue and cause to be served upon each party to the proceeding an order or orders consistent with the provisions of this section. Judicial review of any such order shall be exclusively as provided in this subsection (i). Unless a petition for review is timely filed in a court of appeals of the United States, as hereinafter provided in paragraph (2) of this subsection, and thereafter until the record in the proceeding has been filed as so provided, the Corporation may at any time, upon such notice and in such manner as it shall deem proper, modify, terminate, or set aside any such order. Upon such filing of the record, the Corporation may modify, terminate, or set aside any such order with permission of the court.

(2) Any party to the proceeding, or any person required by an order issued under this section to cease and desist from any of the violations or practices stated therein, may obtain a review of any order served pursuant to paragraph (1) of this subsection (other than an order issued with the consent of the insurer or the director or officer or other person concerned), by filing in the court of appeals of the United States for the circuit in which the principal office of the insurer is located, or in the United States Court of Appeals for the District of Columbia Circuit, within thirty days after the date of service of such order, a written petition praying that the order of the Corporation be modified, terminated, or set aside. A copy of such petition shall be forthwith transmitted by the clerk of the court to the Corporation, and thereupon the Corporation shall file in the court the record in the proceeding, as provided in section 2112 of title 28. Upon the filing of such petition, such court shall have jurisdiction, which upon the filing of the record shall, except as provided in the last sentence of said paragraph (1), be exclusive, to affirm, modify, terminate, or set aside, in whole or in part, the order of the Corporation. Review of such proceedings shall be had as provided in chapter 7 of title 5. The judgment and decree of the court shall be final, except that the same shall be subject to review by the Supreme Court upon certiorari as provided in section 1254 of title 28 of the United States Code.

(3) The commencement of proceedings for judicial review under paragraph (2) of this subsection shall not, unless specifically ordered by the court, operate as a stay of any order issued by the Corporation.

JURISDICTION AND ENFORCEMENT

(j) The Corporation may, in its discretion, apply to the United States district court, or the United States court of any territory, within the jurisdiction of which the principal office of the insurer is located, for the enforcement of any effective and outstanding notice or order issued by the Corporation under this section, and such courts shall have jurisdiction and power to order and require compliance therewith.

DEFINITIONS

(k) As used in this section, (1) the terms "cease-and-desist order which has become final" and "order which has become final" means a cease-and-desist order, or an order, issued by the Corporation with the consent of the insurer or the director or officer or other person concerned, or with respect to which no petition for review has been filed and perfected in a court of appeals as specified in paragraph (2) of subsection (i), or with respect to which the action of the court in which said petition is so filed is not subject to further review by the Supreme Court of the United States in proceedings provided for in said paragraph, or an order issued under paragraph (1) of subsection (e) of this section, and (2) the term "violation" includes, without limitation, any action (alone or with another or others) for or toward causing, bringing about, participating in, counseling, or aiding or abetting a violation.

SERVICE

(1) Any service required or authorized to be made by the Corporation under this section may be made by registered mail, or in such other manner reasonably calculated to give actual notice as the Corporation may be regulation or otherwise provide. Copies of any notice or order served by the Corporation upon any participating insurer or any director or officer thereof or other person participating in the conduct of its affairs, pursuant to the provisions of this section, shall also be sent to the State supervisory authority.

ANCILLARY PROVISIONS; SUBPENA POWER

(m) In the course of or in connection with any proceeding under this section, the Corporation or its designated representative, including any person designated to conduct any hearing under this section, shall have the power to administer oaths and affirmations, to take or cause to be taken depositions, and to issue, revoke, quash, or modify subpenas and subpenas duces tecum; and the Corporation is empowered to make rules and regulations with respect to any such proceedings. The attendance of witnesses and the production of documents provided for in this subsection may be required from any place in any State or in any territory or other place subject to the jurisdiction of the United States at any designated place where such proceeding is being conducted. Any party to proceedings under this section may apply to the United States District Court for the District of Columbia, or the United States district court for the judicial disrict or the United States court in any territory in which such proceeding is being conducted, or where the witness resides or carries on business, for enforcement of any subpena or subpena duces tecum issued pursuant to this subsection, and such courts shall have jurisdiction and power to order and require compliance therewith. Witnesses subpenaed under this section shall be paid the same fees and mileage that are paid witnesses in the district courts of the United States. Any court having jurisdiction of any proceeding instituted under this section by an insurer, or a director or officer thereof, may allow to any such party such reasonable expenses and attorneys' fees as it deems just and proper; and such expenses and fees shall be paid by the insurer or from its assets.

CORPORATION MONEYS; INVESTMENT

SEC. 15. (a) Money of the Corporation not otherwise employed shall be invested in obligations of the United States or in obligations guaranteed as to principal and interest by the United States: *Provided*, That the Corporation shall not sell or purchase any such obligations for its own account and in its own right and interest, at any one time aggregating in excess of $100,000 without the approval of the Secretary of the Treasury: *And provided further*, That the Secretary of the Treasury may waive the requirement of his approval with respect to any transaction or classes of transactions subject to the provisions of this subsection for such period of time and under such conditions as he may determine.

BANKING AND CHECKING ACCOUNTS

(b) The banking or checking accounts of the Corporation shall be kept with the Treasurer of the United States, or, with the approval of the Secretary of the Treasury, with a Federal Reserve bank, or with a bank designated as a depositary or fiscal agent of the United States: *Provided*, That the Secretary of the Treasury may waive the requirements of this subsection under such conditions as he may determine: *And provided further*, That this subsection shall not apply to the establishment and maintenance in any bank for temporary purposes of banking and checking accounts not in excess of $50,000 in any one bank.

LOANS TO PARTICIPATING INSURERS

(c) When the Corporation has determined that a participating insurer is in danger of becoming insolvent, in order to prevent such insolvency, the Corporation, in the discretion of its Board of Directors, is authorized to make loans to such insurer upon such terms and conditions as the Board of Directors may prescribe.

TREASURY LOANS

SEC. 16. The Corporation is authorized to borrow from the Treasury, and the Secretary of the Treasury is authorized and directed to loan to the Corporation on such terms as may be fixed by the Corporation and the Secretary, such funds as in the judgment of the Board of Directors of the Corporation are from time to time required for insurance purposes, not exceeding in the aggregate $500,000,000 outstanding at any one time: *Provided*, That the rate of interest to be charged in connection with any loan made pursuant to this section shall not be less than the current average rate on outstanding marketable and nonmarketable obligations of the United States as of the last day of the month preceding the making of such loan. For such purpose the Secretary of the Treasury is authorized to use as a public debt transaction the proceeds of the sale of any securities hereafter issued under the Second Liberty Bond Act, as amended, and the purposes for which securities may be issued under the Second Liberty Bond Act, as amended, are extended to include such loans. Any such loan shall be used by the Corporation solely in carrying out its functions with respect to such insurance. All loans and repayments under this section shall be treated as public debt transactions of the United States.

EXEMPTION FROM TAXATION

SEC. 17. All notes, debentures, bonds, or other such obligations issued by the Corporation shall be exempt, both as to principal and interest, from all taxation (except estate and inheritance taxes) now or hereafter imposed by the United States, by any territory, dependency, or possession thereof, or by any State, county, municipality, or local taxing authority: *Provided*, That interest upon or any income from any such obligations and gain from the sale or other disposition of such obligations shall not have any exemption, as such, and loss from the sale or other disposition of such obligations shall not have any special treatment, as such, under the Internal Revenue Code, or laws amendatory or supplementary thereof. The Corporation, including its franchise, its capital, reserves, and surplus, and its income, shall be exempt from all taxation now or hereafter imposed by the United States, by any territory, dependency, or possession thereof, or by any State, county, municipality, or local taxing authority, except that any real property of the Corporation shall be subject to State, territorial, county, municipal, or local taxation to the same extent according to its value as other real property is taxed.

FORMS OF OBLIGATIONS

SEC. 18. In order that the Corporation may be supplied with such forms of notes, debentures, bonds, or other such obligations as it may need for issuance under this chapter, the Secretary of the Treasury is authorized to prepare such forms as shall be suitable and approved by the Corporation, to be held in the Treasury subject to delivery, upon order of the Corporation. The engraved plates, dies, bed pieces, and other material executed in connection therewith shall remain in the custody of the Secretary of the Treasury. The Corporation shall reimburse the Secretary of the Treasury for any expenses incurred in the preparation, custody, and delivery of such notes, debentures, bonds, or other such obligations.

REPORTS; AUDITS

SEC. 19. (a) The Corporation shall annually make a report of its operations to the Congress as soon as practicable after the 1st day of January in each year. Such report shall include a statement with respect to the status of the fund established pursuant to section 10, together with such recommendations concerning its adequacy or inadequacy as the Corporation deems necesary or desirable.

(b) The financial transactions of the Corporation shall be audited by the General Accounting Office in accordance with the principles and procedures applicable to commercial corporate transactions and under such rules and regulations as may be prescribed by the Comptroller General of the United States. The audit shall be conducted at the place or places where accounts of the Corporation are normally kept. The representatives of the General Accounting Office shall have access to all books, accounts, records, reports, files, and all other papers, things, or property belonging to or in use by the Corporation pertaining

to its financial transactions and necessary to facilitate the audit, and they shall be afforded full facilities for verifying transactions with the balances or securities held by depositaries, fiscal agents, and custodians. All such books, accounts, records, reports, files, papers, and property of the Corporation shall remain in possession and custody of the Corporation.

(c) A report of the audit for each fiscal year ending on June 30 shall be made by the Comptroller General to the Congress not later than January 15 following the close of such fiscal year. On or before December 15 following such fiscal year the Comptroller General shall furnish the Corporation a short form report showing the financial position of the Corporation at the close of the fiscal year. The report to the Congress shall set forth the scope of the audit and shall include a statement of assets and liabilities and surplus or deficit; a statement of surplus or deficit analysis; a statement of income and expenses; a statement of sources and application of funds and such comments and information as may be deemed necessary to inform Congress of the financial operations and condition of the Corporation together with such recommendations with respect thereto as the Comptroller General may deem advisable. The report shall also show specifically any program, expenditure, or other financial transaction or undertaking observed in the course of the audit, which, in the opinion of the Comptroller General, has been carried on or made without authority of law. A copy of each report shall be furnished to the President and to the Corporation at the time submitted to the Congress.

(d) For the purpose of conducting such audit the Comptroller General is authorized in his discretion to employ by contract, without regard to section 5 of title 41, professional services of firms and organizations of certified public accountants, with the concurrence of the Corporation, for temporary periods or for special purposes. The Corporation shall reimburse the General Accounting Office for the cost of any such audit as billed therefor by the Comptroller General, and the General Accounting Office shall deposit the sums so reimbursed into the Treasury as miscellaneous receipts.

GOVERNMENT CORPORATION CONTROL ACT

SEC. 20. Section 101 of the Government Corporation Control Act, as amended (31 U.S.C. 846), is amended by adding after "Federal Housing Administration", the following: "Federal Insurance Guaranty Corporation".

COMPTROLLER GENERAL OF THE UNITED STATES,
Washington, D.C., August 26, 1969.

B–160321.

Hon. WARREN G. MAGNUSON,
Chairman, Committee on Commerce,
U.S. Senate.

DEAR MR. CHAIRMAN: This is in reference to your letter of June 2, 1969, requesting our comments on S. 2236, a bill to create a Federal Guaranty Corporation to protect the American public against certain insurance company insolvencies.

Whether the Federal Government should undertake, as proposed in the bill, to guarantee the contractual performance of certain insurers issuing or reinsuring property, casualty, or surety insurance policies is a matter of policy for the determination of the Congress and one on which we have no recommendation to make. We do offer certain comments for the consideration of the committee.

BOARD OF DIRECTORS

Section 3 of the bill would provide that the Comptroller General of the United States shall be appointed to the Corporation's Board of Directors consisting of three members, and that, in the event of a vacancy in the office of the Comptroller General or during his absence or disability, the Acting Comptroller General shall be a member of the Board of Directors. The bill also provides in section 19(b) that the Corporation shall be audited by the General Accounting Office in accordance with the principles and procedures applicable to commercial corporate transactions.

The designation of the Comptroller General as a member of the Corporation's Board of Directors is contrary to the policy established in title III of the Budget

and Accounting Act, 1921, which provides, among other things, that the Comptroller General be independent of the executive branch and responsible to the Congress. In regard to audits performed by certified public accountants, the Code of Professional Ethics of the American Institute of Certified Public Accountants, under article 1, states that a member of the Institute will not be considered independent if, during the period of his professional engagement, he "was connected with the enterprise as a * * * director, officer, or key employee." Applying this principle, the presence of the Comptroller General on the Board of Directors might be said to impair the independence of our Office in performing audits of the Corporation.

It is therefore strongly recommended that the committee delete from the bill the proposed designation of the Comptroller General as a member of the Board of Directors and that another member be provided for the Board.

Section 3 would provide that the Directors be appointed for a term of six years. In the interest of continuity of the Board, the committee may wish to provide that the terms of the initial appointment be on a staggered basis. Also, it is noted that no provision is made for compensation of the Board of Directors, such as that included in section 203(i) of S. 688, the bill proposing to establish a Federal Motor Vehicle Guaranty Corporation.

CAPITAL STOCK

Section 5 of the bill would provide for the Corporation to have capital stock of $50 million, the total amount of which would be subscribed to by the Secretary of the Treasury. Under section 10(d), the Corporation would be required to retire such capital stock as rapidly as practicable, having due regard to the need to maintain at all times the solvency of the Federal Insurance Guaranty Fund. However, the bill does not provide for paying dividends or interest on the Government's investment in the capital stock held by the Treasury as is required of some other Government corporations such as the Federal Deposit Insurance Corporation (12 U.S.C. 1823) and the Federal Savings and Loan Insurance Corporation (12 U.S.C. 1725). Accordingly, we suggest that the committee give consideration to providing that the Federal Insurance Guaranty Corporation shall pay interest on the Government's investment in the capital stock of the Corporation, and that such interest be based on the prevailing interest rates of the Treasury. Otherwise, the new program described in the bill will be subsidized by the appropriations made to the Treasury Department for interest on the public debt.

INCORPORATION: POWERS

Section 7(a)(8) of the bill would allow the Corporation to make examinations of any insurer making application for guaranty status, or those insurers whose policies are guaranteed by the Corporation. The bill, however, does not specifically provide for reimbursement to the Corporation for these examinations. Therefore, it is suggested to the committee that specific power be granted to the Corporation to assess fees for such examinations.

TREASURY LOANS

Section 16 of the bill would authorize the Corporation to borrow up to $500 million from the Treasury at an interest rate of not less than the current average rate on outstanding marketable and nonmarketable obligations of the United States as of the last day of the month preceding the making of such loans. We wish to point out that the prescribed minimum interest rate for the Treasury loans does not represent prevailing interest rates on Treasury borrowings. At May 29, 1969, the average interest rate on outstanding marketable and nonmarketable obligations of the United States was 4.943 percent. In contrast, the 7-year and 15-month Treasury notes issued in May 1969 were marketed at a price to yield 6.5 percent and 6.42 percent, respectively. The issue of 26-week Treasury bills on June 23, 1969, were issued at an effective rate of interest of 7.21 percent. Accordingly, the committee may wish to consider modifying this section of the bill to provide that the Corporation pay an interest rate that is related to current interest rates paid by the Treasury. Otherwise, the new program described in the bill will be subsidized by the appropriations made to the Treasury Department for interest on the public debt.

AUDITS

Section 19(a) provides that the Corporation shall make annual reports to the Congress, but does not specify whether the reports are to be made on a fiscal or calendar year basis. Apparently, a June 30 fiscal year is intended, since section 19(f)(2) provides for GAO audits on a fiscal year basis. However, we have been informed (Mr. Maurice G. Herndon, Federal liaison representative for the National Association of Insurance agents) that the insurance industry operates on a calendar year basis. Accordingly, the committee may wish to consider providing for reporting by the Corporation and auditing by the General Accounting Office on a calendar year basis. See 31 U.S.C. 850 for similar provision for the audit of the Federal Savings and Loan Insurance Corporation.

Section 19(b) of the bill provides that representatives of the General Accounting Office shall have access to all books, accounts, records, reports, files, and all other papers, things, or property belonging to or in use by the Corporation pertaining to its financial transactions in performing the financial audit of the Corporation. This is the same authority that the Office has under the Federal Deposit Insurance Act (12 U.S.C. 1827(b)).

Our Office has been unable to fully discharge its audit responsibilities under the Federal Deposit Insurance Act because FDIC has not permitted us to have unrestricted access to the examination reports, files, and other records relative to the banks which it insures. FDIC has denied us unrestricted access to these records because it interprets our access to records authority as being limited to those records pertaining to FDIC financial transactions. We believe, however, that the financial position of FDIC is inseparably linked with the financial condition of the banks that it insures, and that it is essential that we have complete and unrestricted access to all FDIC records so that the potential effect of problems in insured banks upon the financial condition of FDIC can be evaluated. (See Report to the Congress on audit of FDIC for the fiscal year ended June 30, 1968, page 6—B–114831, May 27, 1969.) In view of this problem and if the bill is to receive favorable consideration, we suggest that the committee consider revising S. 2236 to allow our Office access to examination reports, files, and records as well as all financial and other records we consider necessary to carry out our audit responsibilities.

GOVERNMENT CORPORATION CONTROL ACT (GCCA)

Section 20 of the bill provides for including the Corporation as a wholly owned Government corporation under the provisions of the Government Corporation Control Act (31 U.S.C. 846). Certain subsections in S. 2236 could be deleted as they are included in the Government Corporation Control Act. These are subsection 15(b) relating to banking and checking accounts which is contained in 31 U.S.C. 867, and subsections (b), (c), and (d) of section 19 of the bill relating to the auditing of the financial transactions of the Corporation and the reporting thereon by our Office to the Congress which are covered in 31 U.S.C. 850, 851, and 866, respectively.

We bring to your attention the following editorial comments:

1. Throughout the bill the words "this title" and "this chapter" are used in referring to the bill. We suggest using in lieu thereof the words "this act."
2. On page 5, line 3, the word "corporation" apparently should be changed to "cooperation."
3. On page 11, line 9, we suggest deleting the word "free." See 39 U.S.C. 4156.
4. On page 17, line 14, insert a parenthesis after "corporation."
5. On page 22, line 10, the word "Corporation" should be changed to "insurer."
6. On page 25, line 1, "subsection (2)" should be changed to "subsection (a)."
7. The words "of the United States Code" should be changed after "title 5" in line 3 on page 42, after "title 28" in line 15 on page 43, and after "title 5" in line 21 on page 43.
8. On page 48, line 12, the word "pursuant" is misspelled.

Sincerely yours,

ROBERT F. KELLER,
(For the Comptroller General of the United States).

The CHAIRMAN. Our first witnesses today will be Ronald Jacks, president of the National Association of Property & Casualty Re-

insurers, and Mr. Henry Kramer, president of the North American Reinsurance Co.

As I understand it, these gentlemen are engaged in a business that requires daily examination of primary insurance companies. Therefore, the committee welcomes them as experts in this field.

Thank you.

Mr. Jacks, you are first. We will be glad to hear from you.

STATEMENT OF RONALD A. JACKS, PRESIDENT, NATIONAL ASSOCIATION OF PROPERTY & CASUALTY REINSURERS, WASHINGTON, D.C.; ACCOMPANIED BY HENRY KRAMER, PRESIDENT, NORTH AMERICAN REINSURANCE CO.

Mr. JACKS. Mr. Chairman and members of the committee, my name is Ronald A. Jacks, and I am president of the National Association of Property & Casualty Reinsurers. With me is Mr. Henry Kramer, chairman of the Federal Relations Committee of the association and president of the North American Reinsurance Corp., a member of the association. We are happy to accept the committee's invitation to appear before you and give you our views on S. 2236, which would create a Federal Insurance Guaranty Corporation.

NAPCR is an association of professional reinsurers organized as a nonprofit corporation under the laws of the District of Columbia. It is the only such association in the Western Hemisphere, and its members account for a substantial portion of the premiums written by professional reinsurers in the United States. A professional reinsurer is a corporation whose principal business is reinsurance or for whom reinsurance is a substantial and distinct line of business, not essentially related to or considered by the company to be supplemental to the writing of primary insurance.

The principal function of the association is to serve as a forum for the exchange of views among reinsurers on matters affecting the industry and to serve as a vehicle for the industry to express its views on legislative and administrative questions pending before Congress, the executive branch of the Federal Government, and the several States. The association is a relatively new organization, having been organized only about a year and a half ago. In addition to the functions I have noted, we also assist the reinsurance industry in its continuing effort to analyze and be responsive to the evolving needs of the primary companies, who are its clients, and the public generally.

Before turning the Chair over to Mr. Kramer, it would appear appropriate as the leadoff witness in these hearings to briefly describe the historical background in which they occur and briefly delineate what we conceive to be the central issue before this committee.

As the members know, the business of insurance has been regulated by the States for many years. Following the 1944 decision of the U.S. Supreme Court in the *South-Eastern Underwriters* case (*United States* v. *South-Eastern Underwriters Assn., et al.*, 323 U.S. 811 (1944)), holding that the business of insurance was interstate commerce within the meaning of the Federal Constitution, Congress enacted the so-called McCarran-Ferguson Act (15 U.S.C. 1011, et seq.) ceding jurisdiction back to the States to regulate the business and

granting immunity from the Federal antitrust laws to the extent that such activities were effectively regulated by the States.

Since that date, the States have enacted a series of laws designed to carry out the congressional mandate and justify their continued delegation of Federal power. Over the years, both the State regulators and the insurance industry in general have grown increasingly sophisticated and powerful.

In most cases these forces have operated for the public good. However, even supporters of State regulation concede that it can be strengthened, particularly in the area of detecting insolvencies and devising some just means of compensating the innocent victims of such tragedies. Among other things, the power and authority granted regulators in the various States is not uniform or not always what the regulator feels is appropriate for specific situations confronting him from time to time.

Of course, the concern is not that of the regulators alone. The insurance industry also has a large and significant stake in preventing insolvencies. For any failure tends to undermine confidence in the industry and its ability to serve the public.

A number of States and industry representatives have conscientiously sought to meet this crisis by pressing for enactment of State insolvency laws of various types. The National Association of Insurance Commissioners has recently committed itself to the drafting and enactment of a model bill of which I am sure you will hear more later.

The point of all this activity is simply this: That nearly everyone seems to agree there is a genuine problem with respect to detecting and preventing insurance company insolvencies. The difference comes in devising the most effective and acceptable solution.

S. 2236, as we understand it, seeks to correct the situation by creating a Federal Insurance Guaranty Corporation which will be charged with the responsibility of assisting existing State examination of insurance companies, guaranteeing nonlife policies issued by companies engaged in interstate commerce, and assessing those companies to pay for losses arising out of insolvencies not otherwise funded. Participation will be mandatory for such companies and assessments to cover both initial operating funds and subsequent insolvencies will be based on a percentage of each company's "net direct written premiums."

It is significant from our point of view that the bill does not, on its face, seek to displace State regulation in general or periodic examination for solvency in particular. Rather, in its present form, the bill appears to offer funds as well as the assistance of the Federal Government to the States through its provisions for supplemental personnel and the development of common examination standards which can be readily applied nationwide.

Those who oppose the bill—and they are many—argue *inter alia* that this approach "creates a basic dilemma, then seeks to resolve it by an impossible compromise." The dilemma is that "States which have not in the past shown great motivation to establish legal standards and administrative controls adequate to minimize insurer insolvencies would further lose incentive to do so." The "impossible compromise" in this view would be an "aggressive utilization by the

Federal agency of the direct powers conferred on it" to correct this situation. The result, they argue, would be an erosion of State regulation and perhaps eventual supremacy of the Federal Government in the field.

If this analysis is correct, absent its somewhat rhetorical formation, then the all-encompassing issue before this committee is what role the Federal Government should play in bringing about a solution to the problem of potential insolvencies—assuming there is agreement that such a problem exists. Supporters of the bill argue that there is a need for a Federal stimulus to State action and that the Government's involvement can be restrained by legislative limitations on the size and authority of the Federal Insurance Guaranty Corporation.

Presumably those restrictions would apply so long as the States demonstrate that they are willing and able to act. This approach has the obvious advantage of offering assistance to the States which request it, while creating the ever-constant reminder that they must demonstrate the efficacy of their claim to the vitality of State regulation.

Opponents argue either that the States need no help because there is no problem or if it exists it can be solved by "voluntary action" on the part of industry and the States acting in concert. Others argue that there is a need for Federal legislation but that it should be limited to a law "requiring all States to adopt insolvency guaranty laws, establishing minimum standards for such laws, and creating forceful incentives for the States to comply, but which avoids Federal administrative involvement." In their view, such legislation—coupled with a tax on premiums in each States which would be forgiven if the requisite State laws were adopted—would be sufficient to induce cooperation while maintaining the right of each State to develop local alternatives to local needs.

We cannot and do not pass ultimate judgment on these contentions. We do, however, think it clear that: (1) There is substantial, although not total, agreement there is a problem with respect to insurance company insolvencies; (2) the States, by their own admission, through the NAIC have not yet come up with a complete solution and, consequently; (3) there may be a role for the Federal Government in this area such as to encourage State action in which case the question becomes the nature and form of that encouragement and restraints, if any, on its exercise.

This, then, is the perspective in which we and presumably others view these hearings. Ultimately this committee should never lose sight of the fact that it is considering what may be the first step in a fundamental realinement of the role of the Federal and State Governments in the regulation of the business of insurance. Hence, all of the basic questions of federalism are involved in these deliberations—questions on which this committee and the witnesses will differ, but will never recede because they are inherent in the dynamic and rapidly changing society in which we live.

Thank you, Mr. Chairman, for allowing me to serve as an interloctor in this case and to put what we conceive to be the perspective and pivotal issue before the committee.

The CHAIRMAN. We thank you for your testimony. Just thinking out loud, maybe these hearings might have an effect on the States doing the job.

Mr. JACKS. Mr. Chairman, I think they have already accomplished in part that effect.

The CHAIRMAN. That often happens here. Somebody has to take the initiative, and then things start to happen. Of course, if they happen in a correct way, why, then, well and good.

We have many bills in this committee that deal with the very problem you mention: How far should the Federal Government go in this field. Of course, it was the same problem with the banks in the thirties. We finally had to establish two Federal authorities, one for the savings and loans and the Federal Deposit Insurance Corporation. The ones that went down first in that debacle were the so-called State banks. For lack of regulation or many other factors, they had no place to go. Whether it is needed in this field or not is what we are trying to inquire about.

Mr. Kramer, we will be glad to hear from you.

Mr. KRAMER. In the interest of time, I will just comment very briefly on my statement, which supplements what Mr. Jacks said. It is a statement made on behalf of our member companies, not my company alone. I would say that we observe, generally as a practical matter, looking at the whole insurance business, that it is first of all interstate, an interstate business in its character, affecting the entire country, that next of all, there are certain difficulties that do not attend most other businesses. In assisting the insolvency or future insolvency——

The CHAIRMAN. I do not want you to skip—we will put it in the record, but the average layman does not understand much about reinsurance.

Mr. KRAMER. I would be glad to comment on our position. I am speaking for professional reinsurers.

The CHAIRMAN. It is kind of like having a good bench?

Mr. KRAMER. I have heard it referred to as being a bookie's bookie. Reinsurance is a business of insurance of insurance liabilities.

The CHAIRMAN. Or bullpen, I should say.

Mr. KRAMER. We do business exclusively with insurance companies. As such, we are deeply concerned with the health and welfare of insurance companies and, of course, insuring the public. Many of the techniques of insurance and reinsurance are similar, and we have many of the same problems, which gives us an opportunity to understand some of the problems facing the insurance business practically a little bit better than other people.

One of these is the fact that insurance is a business of futures, and this presents certain unique problems in assessing the relevant solvency or ability to pay claims in the future, because events that happen today may not be discharged for a period of some years, and what the value is at that time is inevitably a matter of judgment as well as technique and expertise.

As the members of the committee know, I am sure, this question is a matter of the ultimate responsibility of various State insurance departments which means that for a company that is licensed in 50 States there are 50 separate governmental authorities that have this responsibility and who exercise it. We think that not only does the nature of the insurance business pose certain difficulties with respect to appraising the relative solvency or future solvency of an insurance company or reinsurance company, for that matter, but the business itself is changing, it is changing in several ways. The computer is

taking over. This in itself poses certain technical problems relating to the verification of accounts. The kinds and types of policies that are being issued are changing, becoming broader. Our whole economy is becoming more complex, and, therefore, the nature and character of these future liabilities becomes more complex.

Now, in considering this bill, I wish only to comment on—I do not want to repeat what Mr. Jacks said—but we observe that many States have already recognized the fact that insolvency is a problem because there are State insolvency funds of one kind or another in a number of our States, and we certainly agree that it is in the public interest to see that insurance claims, just insurance claims are paid, and that people are not obliged to suffer the consequences of finding out that a claim against someone is merely that, a claim. There is no indemnity available to them because the company is not there to pay off. We do not regard this as a problem that pervades the industry, but it certainly exists from time to time.

In looking at the bill, we do feel that there are certain dangers or at least it may not be necessary to accumulate——

The CHAIRMAN. I want to preface this. I do hope you realize that up here these are working papers. I have never known of a bill of any importance to go through Congress the way it was written when it was introduced. You have to have a working paper and then you have to get the ideas of people like yourself and Jacks and other people who testify, as to whether the language is right or whether the principle is right. A bill usually states the broad objectives, and then you get down to technicalities of people who should know. We have no pride of authorship in this particular thing. We all realize there is a problem to be met.

Mr. KRAMER. In that spirit, sir, one of the comments we would like to make is we feel it is not necessary to have a preassessment in the sense that you accumulate sufficient funds to discharge any known liabilities in advance. This money can be available on a postassessment basis.

We also observe that the bill provides for or suggests the desirability of having an advisory committee, a great deal of importance with this advisory business because we are dealing with a highly technical business. We believe that a very real portion of this advisory committee are people who are in the insurance business.

(The statement follows:)

STATEMENT OF HENRY KRAMER, PRESIDENT, NORTH AMERICAN REINSURANCE CORP.

Mr. Chairman and members of the committee, It might be helpful if I first define the term "reinsurance" before making a series of general comments about the problem before this Committee and the specific legislation which seeks to resolve it. All insurance companies, at least all those of any significance to the general public, reinsure some parts of their business in one way or another. Reinsurance has been defined as to "insure again." In its simplest form, reinsurance is the process of insuring insurance companies, either on specific risks or entire classes or types of risks. The term "professional" reinsurer describes an insurer whose main, or at least a very substantial part of his business consists of reinsurance as a separate and distinct business objective in itself.

Insurance and reinsurance have many similarities and one of these is relevant to the objective of the proposed legislation under discussion today. Insurance is a business of futures in the sense that a policy is a promise to pay in the event of an unforeseeable contingency in return for an immediate payment of premium.

In order to discharge this unknown future liability, an insurer must have sufficient funds in hand to meet such demands as may be made upon it at the time the insured contingency occurs. When sufficient funds are not in hand, the insurer is insolvent and the problem sought to be solved here by this legislation exists.

The technical problems presented in determining the probable future solvency of an insurer are not as easily determined as in other kinds of businesses, since the unknown character of the future liabilities is precisely that, unknown. Nevertheless, in the course of the history of insurance various techniques and standards have been evolved by which normally acceptable standards of solvency can be enforced. This responsibility today lies ultimately with the various state governments where insurance companies are licensed. As this Committee knows, insurance companies, like other corporations, may be licensed in one or more states and it is common to find the largest companies licensed and actively doing business in all states. Thus, the bulk of the insurance business is under the joint review of fifty separate insurance departments, each with similar, ultimate responsibilities relating to the question of solvency.

However, the problem is not easily susceptible of solution in all cases. There are many reasons for this which would require a rather prolonged discussion. In our increasingly complex society, the number of pertinent factors affecting solvency tax the ability of insurance company managers and, of course, tax the wisdom and abilities of those regulatory examiners charged with the responsibility of seeing that public standards of solvency are maintained.

For example, the increasing computerization of the insurance business is going to present audit problems of an increasing magnitude related merely to verification of figures. The rights of policyholders with respect to actual or potential claims is under constantly changing, and I may say broadening, review by the courts. For these and other reasons, the increasing mechanization and complexity of the business will not permit an increased ability to forecast insolvency than the establishment of arbitrary standards seeking the same result.

As I am sure will be brought out later by others, the states fully recognize this problem and it is our observation that this bill has recognized the continuing interest of the state regulatory officials in coping with this general problem of insolvency.

The trouble remains that if against all expectations a company nevertheless finds itself insolvent, a great many promises to pay are left without any hope of satisfaction. In the sense that the reinsurance companies are members of the whole insurance industry, we see an objective in this bill that we recognize to be in the public interest, especially if it is somewhat modified. For example, many members of the insurance industry feel that as a group they are prepared to recognize the problem and discharge unsatisfied judgments through ratable contributions from within the industry itself. The principle involved is not a scheme for the future but is a reality in a number of states already, notably with respect to automobile insurance. In this connection, many segments of the primary insurance industry feel, and we as reinsurers see no reason to question this opinion, that it is not necessary to have large amounts of funds available at any and all times for the payment of claims against insolvent companies should they occur.

A sound basis for this approach to satisfy all unpaid claims is on a "post-assessment" basis. This contemplates minimum charges on the insurance industry as necessary to support whatever regulatory agency is formed in order to find a satisfactory solution to the solvency question either on a purely state by state cooperation basis, a state plus federal basis, or a fully federal and hence national body. But regardless of its ultimate form we support the basic objective of the bill—the protection of the public.

Turning to the specific sections of the bill, we should like to suggest the following:

1. If the proposed legislation ultimately becomes law, it includes an advisory committee in Section 4, the purpose of which is to assist and guide the Guaranty Corporation in the discharge of its reponsibilities. It is our view that the effectiveness of any program seeking to avoid insolvency will vary more or less in proportion to the broadness of the views that are brought to the problem. Accordingly, the advisory committee is a potentially very important aspect of any legislation of this kind and if asked reinsurers would certainly be willing to cooperate and serve on such a committee.

2. We understand that reinsurance assumed obligations are not intended to be guaranteed. We think this is proper and wholesome, since reinsurance transactions are confined to contracts or policies between corporations or other legal entities authorized to transact an insurance business, and do not indemnify the public who are the object of the protection this bill seeks to afford.

We find no contradiction or unwarranted exception in not guaranteeing assumed reinsurance. As members of the committee probably know, the distinctive characteristics of reinsurance, as differentiated from insurance, have been recognized in insurance statutes for many, many years. In those states that now have insolvency funds of their own, the same principle exists in that such funds do not, without exception, guarantee policy obligations with respect to reinsurance assumed. Moreover, the basic solvency of an insurance company ultimately rests on its own resources and on its own activity. If the continued solvency of a primary carrier appears contingent upon the ability of a reinsurer to pay, this in itself, in our view, is a warning sign of some significance which is, by definition, most effectively dealt with at the primary level.

SUMMARY AND CONCLUSIONS

In summary, we would like to offer the following fundamental points with respect to S. 2236:

1. The business of insurance in the United Stataes is both in fact and law either interstate or international commerce in nature.
2. The multi-state and multi-national aspect of the business makes determination of reliability and solvency at the state level unusually complicated and difficult *under existing conditions.*
3. A method can be devised to meet this need *and not destroy the primacy of state regulation.*
4. The Magnuson bill is one approach to the problem, assuming that in its final form it will maintain existing effective state regulation and create a productive federal-state relationship.
5. Such a bill should provide a pre-assessment for operating funds of a coordinating agency only and provide for a single national post-assessment in the event of losses.
6. Further the bill might be amended to provide:
   (*a*) A strengthening of the role and responsibility of the advisory committee.
   (*b*) Clarification of terminology of the bill in certain technical respects which we shall supply to the Committee staff subsequent to this hearing.

The CHAIRMAN. Has any State provided a method or a guarantee fund to take care of the policyholders in their State if the company should go broke?

Mr. JACKS. There are a number of States who do; yes.

The CHAIRMAN. How do they collect the fund, generally?

Mr. JACKS. In some cases it is a postassessment provision, such as in the recent statutes that have been enacted in Michigan and California. In others, in some areas the insolvency bills or funds are limited to certain lines of insurance and in that case they have been collected as they have gone along as sort of premiums.

The CHAIRMAN. Do the companies pay in a percentage of their business?

Mr. JACKS. In preassessment funds or continuing assessment, yes.

The CHAIRMAN. I am trying to get this clear in my own mind. The banks, for instance, pay in so much to the Federal Deposit Insurance Corporation. The savings and loan people pay in so much to the Federal Home Loan Bank Board and the Rural Credit Administration, but they pay it and not the depositors or in this case the policyholders.

Mr. JACKS. I would think that in most cases where there is a preassessment or a continuing assessment, the policyholders end up bearing the burden of that.

The CHAIRMAN. Do you mean they add it to the premium?

Mr. JACKS. It is a loading in the premium. I would be willing to stand corrected, though.

The CHAIRMAN. If I buy a policy and the stated premium is let's use a figure of $200, when they send me the bill, do they say $202—$2 goes for this?

Mr. KRAMER. No, sir. I think what Mr. Jacks is saying sooner or later under the laws relating to adequacy of premium rates, this must be added to the law.

Mr. JACKS. It is a factor in the rates that is approved by the State commissions. Again this practice, Mr. Chairman, may differ from company to company.

The CHAIRMAN. Just take a commercial bank, a factor in the interest rate they charge is the money paid to the Federal Deposit Insurance Corporation; it is an item of cost, it is not too much, it is a small amount percentagewise, but it is in there some place—the same with the savings and loan. How do they handle it if there is not a preassessment?

Mr. JACKS. I do not think we have had sufficient experience to know.

The CHAIRMAN. And the so-called model bill——

Mr. JACKS. The model bill has not been released yet.

The CHAIRMAN. But that would have to be approved by 50 State legislatures, would it not?

Mr. JACKS. If it was going to be nationwide and effective, yes.

The CHAIRMAN. Which might happen. We may have a uniform system, I do not know, but in the meantime there are insolvencies, are there not?

Mr. JACKS. Yes.

The CHAIRMAN. And they are getting more and more?

Mr. JACKS. That is a matter of judgment.

The CHAIRMAN. It is not for the policyholder?

Mr. JACKS. No. I do not mean to finesse that answer, but there are those who argue that the insolvency problem must be viewed in relation to the dramatic growth of the industry as a whole and as a percentage it is not increasing at an alarming rate.

The CHAIRMAN. What happens when there is open competition?

Mr. JACKS. You mean in terms of insolvency?

The CHAIRMAN. Yes.

Mr. JACKS. Again we have not had enough experience with the combination of the two. I personally happen to think that there is a necessary relationship between open competition and adequate solvency. I would agree with Senator Hart in this regard, and I am speaking for myself here, that they ought to go hand in hand.

The CHAIRMAN. Is my impression wrong—and this is just an impression—that the companies that seem to have the less stability, particularly in the casualty field or auto insurance—now health insurance—seem to be the mail order companies; have I got the wrong impression?

Mr. KRAMER. There is one major error, automobile insurance cannot be sold by mail. In order for a person to buy auto insurance, there is no point in buying if the company is not licensed in the State concerned.

The CHAIRMAN. What about health insurance?

Mr. KRAMER. There is substantial amount of mail-order business in the health insurance business.

The CHAIRMAN. I am not criticizing insurance by mail, but there seems to be more of the, let us say, less stable companies that do direct mail advertising than the more stable companies that use their agents or their agencies or their people in the area or in the State. I do not know why that is, but I guess that is true with all kinds of mail, is it not?

Mr. KRAMER. Actually, health insurance can be sold by mail effectively.

The CHAIRMAN. It may be all right. It seems to me, I have a general impression this is true, I do not pick on any particular company.

Mr. JACKS. I would note for the record, Mr. Chairman, on the other hand, there are a number of very large so-called direct writers in the automobile field who are just extremely successful and reliable companies.

The CHAIRMAN. The growth of health insurance, of hospital care seems to have just expanded fantastically in direct mail. You can sit in your house any time when the mailman brings you only bills and advertisements for health insurance. It is very seldom you get a personal letter any more.

Mr. KRAMER. True. I think if there is a problem in the sale of insurance by mail, it is the sale of insurance by a company that is not licensed in the State where the person is getting the advertisement by mail.

The CHAIRMAN. Is it not true because of this lack of uniformity that often an insurance ad that might go into a nationally circulated publication or direct mail will state these terms are not valid in the States of so and so?

Mr. KRAMER. Yes, sir.

The CHAIRMAN. But there is no question in your mind that the business of insurance is interstate?

Mr. KRAMER. Certainly the bulk of it.

The CHAIRMAN. The bulk of it is interstate. Are there any insurance companies—and I ask this for information—that operate purely intrastate?

Mr. KRAMER. As a practical matter, apart from some rather—I am not a lawyer, sir—but as a practical matter, there are quite a few fairly small ones.

The CHAIRMAN. That operate intrastate?

Mr. KRAMER. Yes, and some of them are very old and quite solvent.

The CHAIRMAN. I think we have some in my State that are purely intrastate in different fields.

Senator Hartke, do you have any questions?

Senator HARTKE. I do not know if this is a proper question for Mr. Kramer, but is there any type of statistical information which is available to give an index of the type of insolvencies that are likely to occur, the numbers that have occurred in the past, the classifications of insolvencies and also any of those that are potentially dangerous at the present time. In other words, what statistical information do we have to back up the information we are trying to develop here for a real comprehensive insolvency protection?

Mr. KRAMER. I think one of the best summaries on the history of it was given in the testimony that attended the introduction of this bill. As to potential or likely insolvency, I must tell you no.

Senator HARTKE. Let me raise this question with you. You are very familiar with the reinsurance field, are you not?

Mr. KRAMER. Yes, sir.

Senator HARTKE. I know of one large insurance company which frankly took risks, so-called hazardous risks, reinsured these, and it became one of the largest insurance companies in the United States. Now, would you have any kind of restrictions on innovation in the field of insurance? Do you envision that there would be regulations for these people? Are they just going to pay a premium to guarantee their particular lot? I do not see how you are going to cover that in a risk business like that.

Mr. KRAMER. I am not sure I follow you.

Senator HARTKE. Let me give you a very simple example. Taking casualty insurance, there are certain people who have a very difficult time in getting automobile insurance; right?

Mr. KRAMER. Yes.

Senator HARTKE. These individuals or corporations or insurance companies that deal in that business, premiums are very high, and yet on the basis of the information that they have, if you had an examination of their portfolio, you would find it very difficult to say that they had any guarantee whatsoever; they could continue in business, isn't that true?

Mr. KRAMER. It might be true and it might not.

Senator HARTKE. That is what I am asking you. Do you have any information on the going concerns at the present time to indicate what you are buying here, what type of risk you are buying.

Mr. KRAMER. You have complete access to all of the data that the States oblige these companies to file, in other words, the statements each year, and the examinations every 3 years and more frequently if the insurance commissioner deems it necessary. This is all a matter of public record.

Senator HARTKE. I understand that. It is not what I am talking about. I understand that the examination of these State reports will not give you any indication of any of the insurance companies which have gone insolvent. Basically the insolvencies have occurred without any real information being revealed by their reports to the State agencies, isn't that true?

Mr. KRAMER. Well, it was there. States do find companies that are about to go insolvent and act.

Senator HARTKE. I understand they do, but by and large the ones that have failed, there was no advance warning given by the States or given by information which was filed with the States, isn't that true?

Mr. KRAMER. Yes, sir.

The CHAIRMAN. I must go in and take over the Commerce Committee executive session before going to the floor, but Senator Hart is on his way and he will continue the hearings. We will go as much as we can today, and will do the best we know how.

Senator HARTKE (presiding). What I am saying is, I have tried to go into the question of the same type of program for pension plans. We ran into the same difficulty of trying to make an assessment of the basic financial stability of these organizations. I was wondering if you have any information whatsoever which at the present time gives you any basis for assessing a fee.

Mr. KRAMER. For assessing a fee?

Senator HARTKE. Yes.

Mr. JACKS. Senator, I think you are driving at two different things. The function of the reinsurer is to provide protection and capacity to a primary company, and he does it on the basis of his assessment of the primary company. First of all he determines whether it is getting an adequate rate, the type of risks it exposes itself to; he makes suggestions on the company's operating ability, on the character and capacity of his executive staff, and after he has gone through all that he may decide he doesn't want to participate in any contractual or treaty relationship with the company, or the coverage that the primary company wants simply exposes the reinsurer to too great a risk.

On the other hand, if he decides that the company is competent and he is undertaking to acquire risks in a normal businesslike manner and getting an adequate rate for it, if in that context you are asking does the reinsurance company have any internal blacklist of companies that may be in financial difficulties, the answer is no. This is a judgmental factor. Each company has its standard.

Senator HARTKE. I understand what you are talking about, but what I am talking about is in terms of this legislation, some type of assessment has to be made. What type of fee is required and what is going to be the allocation of the amount. Is it going to be a blanket amount upon all corporations?

Mr. KRAMER. Our feeling, sir, is first of all you have two items combined in the fee. First of all, the expenses of any agency, whether it involves exclusively the Federal Government or Federal plus State or an interstate compact. That is one item.

The other is the amount of money necessary to discharge these obligations of insolvent companies.

Our feeling is that both of these probably should be assessed on companies in proportion to the kinds of business that they do and the volume of business they do.

Senator HARTKE. I am asking you if there is any statistical information giving you that type of background which would make it possible for you to make such an assessment or whatever you want to call it.

Mr. JACKS. Not a preassessment. If this bill is to become law we would strongly urge, I should think others as well, a postassessment where you levy a charge on the primary companies engaged in interstate commerce in proportion to their share of the market to cover the cost of the insolvency after it occurs.

You see, there is no way really of building a fund in advance to cover insolvency. It is strictly a matter of subjective judgment. It seems to me the most efficient way to handle it if this bill were to be enacted would be to levy a charge in advance only to cover the operating costs of whatever agency or agencies might be created and then wait until insolvencies occur and then charge the companies proportionately.

Senator HARTKE. Senator Spong.

Senator SPONG. I want to apologize to you gentlemen for not being here when you testified, and you may have covered this in your previous testimony.

As I understand it there are three possible approaches to this problem. One is to leave it up to the business and to the States to act voluntarily. Secondly, it would be some legislation wherein the States would be required to act and minimum standards would be set, but the initiative would be with the States and the legislatures of the various States, and, of course, the third would be a wholly Government approach at this level.

Have you gentlemen expressed any opinions on the preference of approach or have you merely observed that this involves great problems so far as Federal-State relationships are concerned and have left it there?

Mr. JACKS. In my opening statement, Senator, I delineated those possible choices and refrained from taking any stand one way or the other. We can't, as a practical matter, at this time make any final judgment for a number of reasons. First of all, we have clients on both sides of the question. Secondly, we have not seen the States' alternative. I think that is critical to any objective determination of the thing.

Senator SPONG. How active have the States been in this area up to now? How many States have actually done something?

Mr. JACKS. I think the latest figure, and I stand corrected by subsequent witnesses, is that there are eight States that have insolvency laws in one form or another. Beyond that, the National Association of Insurance Commissioners, the body that is composed of the 50 State commissioners, has a very active committee working on a task of drafting a model NAIC insolvency bill. I understand that that bill is in its final stages and will be presented to the NAIC at its December meeting in New Orleans. That at least is the state of the art.

Senator SPONG. That is the model bill you were speaking of to Senator Magnuson?

Mr. JACKS. Yes. That is the bill that would have to be enacted by all of the 50 States. Then beyond there it seems to me, I may be again anticipating the question, beyond that it has to be coupled with some multi-State agency, perhaps within the confines of the NAIC, to handle the technical problems involved in what you do with an insolvency that stretches across 20 States. You may appoint one State to act as the receiver, if you will, but, how do you level assessments on a multistate basis? I do not think I am being unfair to the supporters of State legislation to assert that they are going to have to come up with some vehicle for handling an insolvency that stretches across a number of States. Simply getting the model bill enacted is not enough.

Senator SPONG. It might not seem like a ready parallel, but actually the handling of air pollution and the Federal-State relationship is very, very similar when you think about it. What we have ended up doing here is trying to let the States do it, but setting a framework in the standards within which they must operate.

Mr. JACKS. Well, that is why I pointed out in my statement, Senator, that even some of the most dedicated supporters of State legislation, and I am speaking now of Dean Kimball, of the University of Wisconsin Law School and Superintendent Stewart, of New York, who is one of the most outstanding, Commissioner Worthington, of Iowa, all agree that perhaps there is a problem and that there is a need for

some sort of Federal law to establish standards such as you suggest, and to throw the gauntlet back to the States to come up with a workable solution in my view, I am speaking now for myself, that is a preeminently intelligent approach at least when viewed from the State angle. I think it is something this committee may want to give careful consideration to.

Senator SPONG. Thank you.

Senator HARTKE. Let me cut right back to the meat. How can you provide for any type of system here which is a corollary to the Federal Deposit Insurance Corporation? You are starting out on the wrong end. What you are going to first have to create is some type of regulation in the insurance industry. Is that not implicit with what has to go with this bill?

Mr. JACKS. You mean at the Federal level?

Senator HARTKE. Sure.

Mr. JACKS. There are those who would argue that that may never have to come to pass.

Senator HARTKE. You might as well argue in a vacuum. That is a non sequitur, what you are talking about. As a practical matter, I think you would have to address yourselves to that. Quite honestly, you cannot go ahead and make any type of realistic assessment. You are talking basically here of raising $31 million a year under this present bill, and I am not arguing with the merits of it, but you can argue with one-eighth of 1 percent, you raise $31 million a year; it is the estimate. Now you can go up to 1 percent and you going eight times that, so you go up to roughly $250 million a year. If you have a real insolvency in this Nation, that would wipe that amount out in nothing flat. I am quite aware of what you are talking about, your preassessment as far as what is going on and your postassessment, but what you are saying here basically is you are trying to make a judgment—I mean this bill is—without having any uniform system of regulation in the insurance industry, and frankly, if you are going to pass this bill and make it work, you are going to attach Federal regulation to the insurance industry pure and simple.

Mr. JACKS. I think it depends on what you mean by regulation.

Senator HARTKE. Let me make one point clear. I am not doing a graceful minuet as you did, and frankly I do not like graceful minuets. If you are going to sink to the bottom of the sea, I think you ought to rock the bottom instead of sinking quietly. I am not expressing an opinion, I am expressing what I think is a very objective analysis of what happens if you pass this type of legislation.

Mr. JACKS. This may be the first step in the fundamental realinement. If what you are saying is the inevitable result of this bill would be the creation of some Federal regulation——

Senator HARTKE. Not some, make it very clear, you are not going to be able to do this piecemeal any more than you can in the banking business.

Mr. JACKS. With all due respect, Senator, I do not agree. There may be a middle ground. I think that yours is a legitimate conclusion. But, I am not prepared at this time as a matter of hard, cold analysis to say that there cannot be some accommodation between the State and Federal systems.

Senator HARTKE. Let me just come back. Can you give me one example where this is not true in any regulated field on the Federal level?

Mr. JACKS. You mean one example——

Senator HARTKE. Where they have moved hasn't it been total? At this moment I am just being quite honest in my appraisal, and these people like President Johnson used to talk about a creative federalism and President Nixon talks about a new federalism, all the slogans do not solve the problems. The slogans are no good. What is before this committee at this moment—I think everybody ought to face up to the hard facts of reality—is if you are prepared to have this type of legislation, are you prepared to have Federal regulation of the insurance industry, preempting practically all State regulation, except in this one category where you might have more strict regulation on the State level?

Mr. JACKS. I was going to give you an answer to the question, in the atomic energy field, where States seem to be coming up with stronger regulation.

Senator HARTKE. Where?

Mr. JACKS. In Minnesota.

Senator HARTKE. I am not talking about the pure and simple operation of the Government, and that is in this vertical alinement where the States for whatever reason it has been, where the National Government has usurped their power the States have completely abdicated their responsibility, it doesn't make any difference how you assess that, but the fact remains what you have here is an ultimate assumption of the regulation of the insurance industry by the Federal Government. Is that true?

Mr. JACKS. If that is your view, Senator, I don't share it.

Senator HARTKE. I think you will find out—well, all right. Let me ask you, do you favor Federal regulation of the insurance industry?

Mr. JACKS. As an individual or speaking for an association of an industry?

Senator HARTKE. I really don't care how you speak. You are a witness out there. You make up your own mind. You just identify your position.

Mr. JACKS. I will speak for the National Association of Reinsurors. We have not taken a final position whether we favor Federal regulation or not. We do so for a number of reasons. The hard business reason being we have clients on both sides of the question, and we simply are not prepared to take a final stand which will alienate a number of its good customers. But there is another reason.

Senator HARTKE. Let me stop you just there. Is it possible in any type of operation to have the regulators regulate the regulated?

In other words, is it possible to self-regulate yourself? Isn't that an impossibility in all these fields? You know more and more we hear all the sweet talk, and then we hear the accusations about the abuses, and then the industries come on in and say we will regulate ourselves. Is it impossible to regulate yourselves in these fields?

Mr. JACKS. I should think that in the business of insurance that it would be in the ultimate best interest of the public to have a minimal form of regulation, one which seeks to concentrate on guaranteeing the solvency of companies but does not attempt to involve itself with rates, forms and daily trade practices in an inordinate manner.

Senator HARTKE. Let's come back to this one and then I have a nice one for you.

Mr. JACKS. I am not prepared to comment for the association on it at this time, because I think the States frankly have to be given a chance in this area. With or without Federal prodding, the States have to be given a chance to improve their own operations. There are great pressures on the States from the primary companies to open up competition, for example, in the rating field, to allow rates to be filed and used and then put the burden on the Commissioner to come back and show that they are excessive or that they are in some manner inadequate rather than funneling it through a politically appointed commissioner in the first instance. I am waiting, frankly, to see what is going to happen in the next 5 to 10 years, not in the insolvency bill but in general, to see whether the States can respond to the constructive pressures that are put upon them and solve their own internal problems, and if they can do that, then, I think there is a justification to the continued vitality of State regulation.

If they cannot, then I think you are going to find that the demand for Federal regulation is more and more.

Senator HARTKE. Then you are advocating a free, competitive operation; is that what you are saying?

Mr. JACKS. You mean the rating structure? Yes, I think there ought to be open competition and we have supported it in certain areas.

Senator HARTKE. If you have that, then immediately you have to come within the framework of the antitrust laws.

Mr. JACKS. Yes.

Senator HARTKE. And you are willing to come within the framework of the antitrust laws and insolvency regulations, right?

Mr. JACKS. That is a very nice question, and I think the guidance for it is a number of large companies have thought it through very carefully and would say that they tend to favor Federal regulation even though it would mean the loss of some immunity from the antitrust laws. That is a tradeoff that can only be made on the basis of an analysis on the part of each company.

Senator HARTKE. You see where you find yourself in a different position—I am not arguing with you—is the fact I am interested in the companies but I am interested in the public first.

Mr. JACKS. So are we.

Senator HARTKE. That is a difficulty. I am not worried about tradeoffs. What I am saying to you quite honestly, implicit with any type of free competitive situation has to come some form of regulation for insolvency and second, some type of antitrust regulation.

Mr. JACKS. Granted.

Senator HARTKE. That is all I have. I think you people can be very helpful to us.

Mr. JACKS. In what respect?

Senator HARTKE. In coming up with your definitions of these terms of exactly what you would say would be necessary. If you are willing to do this, then I think you ought to move forward. I don't think you are going to stand still. I think something is going to happen.

Mr. JACKS. Meaning what, that you feel that the Federal Government is of necessity going to have to move into this field if this bill is passed?

Senator HARTKE. The old story, the States have failed again. There is no denying that simple fact of life.

Mr. JACKS. That is where we differ.

Senator HARTKE. We can differ. I'm not going to ask you to be self-indicting, but the point is, this is the fact of life.

The net result is something will happen. If you can't read the between the lines, you ought to see that this bill doesn't just come because somebody dreamed and thought it was nice to introduce the bill. My name isn't even on it.

Basically, I feel that something needs to be done. I have gone through the heartaches of trying to do something in this other field. I think much more needs to be done. I don't think you can start an insuring operation unless you know what you're insuring.

Mr. JACKS. I agree entirely. This ought to be a central question, I suggest, for this committee in its initial deliberations, whether, one, there is a role for the Federal Government, and, if you all agree on that, two, what the nature of it should be, and when you talk about the nature of the Federal Government's involvement in this area, then you are necessarily going to have to talk about the potential for complete involvement.

If this committee, with full recognition of that potential, nevertheless decides to recommend this bill, and if the Senate and the House, after all discussions, then we at least know where we have gone. No one can complain that there hasn't been a full, comprehensive recognition of the potential.

I am frankly very glad to see that you bring it out here. I felt that this is a little emphasis that ought to be placed on these hearings.

Senator HARTKE. Let me say before I recess these hearings and go to aviation, which is very important to me—I mean I'm on that committee—I would hope that we just don't bind ourselves into a position where we get no affirmative recommendations as to how to move.

I would think you ought to have some statistical information.

Mr. JACKS. Would you be more precise?

Senator HARTKE. I'm asking you how can you go into a situation now, and make a real determination as to the financial condition of these various insurance companies all across the lot, and with all due respect to the mail-order houses, I think some of the non-mail-order houses, the open-shop operations, are much more dangerous?

Mr. JACKS. Do you want a compendium of the companies that may be insolvent or may be potentially dangerous?

Senator HARTKE. Sure, I think you are going to have to do that. I do not think you can operate in a vacuum here.

Mr. JACKS. Is that the function of the industry?

Senator HARTKE. If you do not do it, we will. It is very simple. I do not care. I would think that the industry itself—yes, I would think they would have a vital interest in trying to come up with the material, the actual statistical and basic factual material upon which an objective decision can be made as far as legislation is concerned. If you do not do that, I will tell you what will happen. You will get regulation based upon the best we can obtain without your information, and then you will cry like mad later on about the Federal Government

moving into a field, not taking certain facts into consideration, and then we will come back and try to correct them and in the meantime a lot of people are going to get hurt. That is typical in legislation. If you do not want to help us, it is all right. But I find too many industries who say we want no Federal regulation, we do not want the Federal Government to participate, which then go ahead and put every roadblock in the way which makes it look as though they have something to hide.

Mr. JACKS. I only raise the very practical problems involved in making a subjective judgment on potential insolvency of the companies in the United States. I do not think it can be done. Frankly, it is not out of the spirit of lack of cooperation. I just have my doubts as to whether it can be done.

Senator HARTKE. It is the old, old story. I am telling you you are going to be hit with the bad apples from the bottom. They may look good on the top, but there are some rotten apples in this basket. You are not going to save yourselves by claiming you cannot be concerned by getting your feet dirty to find this out. You are going to have to walk through the mud with us, I am sorry, and it is not pleasant. The only difference is we are going to go through it some way. I am not speaking for the committee. I just tell you what the very current movement in this country is. Something will be done in this field like many others.

Mr. JACKS. I do not want to be cast in the role of an uncooperative witness, because we certainly have not sought that role. I am trying to speak for my brethren who are to follow, to tell you that you are going to be told that it is difficult, if not impossible, to come up with this. Maybe they can. As you know, the industry is divided upon this. Those who tend to favor the approach that this bill seeks may feel that they can. I am playing Cassandra at this point, because I would not want your enthusiasm to impair what may be the facts to follow.

Senator HARTKE. I am going to recess the hearing and Senator Hart will be here in a few minutes. So, the next witness, if you won't stray too far, I am sure you will be heard this morning.

(A short recess was taken.)

Senator HART (presiding). The committee will be in order.

I am sure that the earlier chairman apologized for the kind of schedule under which we are compelled to operate. The full committee is in executive session. Intermittently, those of us who participate in this hearing will be compelled to return to the executive session. In view of the uncertainty as to how many minutes remain for this subject matter we will ask that the vice president of the American Mutual Insurance Alliance, who is a Washington resident, to permit us to call the witnesses who are scheduled to be heard after him, since both of those men are in Washington from distant points.

The next witness is the president of the National Association of Independent Insurers, Mr. Vestal Lemmon.

The committee appreciates having received your prepared statement. It will be printed in the record in full.

As you go along, if there are any extensions, please feel free to do so.

STATEMENT OF VESTAL LEMMON, PRESIDENT, NATIONAL ASSOCIATION OF INDEPENDENT INSURERS, CHICAGO, ILL.; ACCOMPANIED BY GEORGE DeWOLF, ASSISTANT GENERAL COUNSEL

Mr. LEMMON. Thank you, Mr. Chairman.

I am Vestal Lemmon, president of the National Association of Independent Insurers. Seated with me to my right is our assistant general counsel, Mr. George DeWolf.

Our association consists of more than 350 stock and mutual companies writing over half of the automobile insurance in the United States today. We appreciate this opportunity to make a statement before your committee.

We are entirely in accord with the objective of preventing insurance company insolvencies and cushioning their effect on individual members of the public. However, we are resolutely opposed to the creation of a Federal Insurance Guaranty Corporation for three reasons:

First, it would be inherently so cumbersome and expensive that the supposed cure would be out of proportion to the problem.

Second, it would result in Federal takeover of an area of regulation which the States are quite competent to handle, contravening the trend to return regulatory authority to State and local governments wherever feasible.

Third, it ignores the fact that the States and the insurance industry are taking very adequate steps to further reduce insurance company insolvencies and their consequences to the point of insignificance.

At the outset, I would like to dispel any doubt about who would regulate the property and liability insurance business if S. 2236 is enacted. It would mean Federal regulation of insurance, lock, stock, and barrel. Some may not wish to recognize this inevitable consequence, and may picture the Federal insurance examiner as a cooperative partner of the State regulatory authorities. The Advisory Committee on Economic Regulation to the Department of Transportation, relative to S. 2236, put this palliative in true perspective when it said:

> Inevitably, the Federal agency, to protect the integrity of the fund it must administer, will find it has to reach further and further in the exercise of the powers conferred upon it or to seek even more powers.
>
> Financial supervision is the primary purpose and function of insurance regulation. The needs of financial regulation pervade the legal controls imposed upon insurers. Ultimately, it is inconceivable that the Federal agency charged with faithful administration of a fund derived from people in every state, will be able to tolerate significant discrepancies among the states in capital and surplus requirements, in investment laws, in rate administration, and in examinations of insurers. Comprehensive Federal control will, indeed must, follow Federal financial responsibility.

We support State regulation of insurance as we would support State or local regulation of any function where the job can be done efficiently at a level of government closer to the people. Because we do have 50 State insurance departments, the automobile assigned risk plans and FAIR plans can be tailored to meet the needs of the people in each State. The standards for entry into the business for both companies and agents can be set to reflect local needs and conditions. New innovations in coverage and forms can be developed to meet local needs. Experimentation with various policy forms, rating procedures, experience

credits, et cetera, can be given a trial in a State without extending the plans nationwide and, in fact, different plans can be tried in different States at the same time. Creation and revision of territorial classes is a local matter best handled at the State regulatory level. The flexibility of a State-by-State regulatory system can never be equaled by Federal regulation where a mistake or misjudgment of a regulator applied on a nationwide basis could be ruinous for the insurance industry and the public it serves.

Let me point to a few of the requirements, imposed on the FIGC by the bill itself, to show what an extensive operation is contemplated and what an immense staff would be required.

(*a*) The Corporation is empowered to examine and require information from any covered insurer.

(*b*) It may make such rules and regulations as it deems necessary to carry out the provisions of this act.

(*c*) It shall appoint examiners to examine a company whenever it deems examination necessary.

(*d*) The examiners shall have power to examine all affiliates to disclose fully the relations and the effect of such relations with an insurer, and shall make a full and detailed report.

(*e*) FIGC shall have power to issue subpenas, conduct hearings and take testimony under oath.

(*f*) The Corporation shall assume obligations from the receiver or liquidator of an insured company and shall investigate, examine, adjust, defend, compromise, or settle any claim.

(*g*) It shall evaluate a company's capital and surplus, reasonableness of expenses, premium writings as related to surplus, loss reserves, reinsurance, investments, and management qualifications.

(*h*) Insurers shall make such reports as the Corporation may require.

(*i*) The corporation may suspend a company's guarantee (putting it out of business) if it shall find the insurer or its officers or directors have engaged in an unsafe or unsound practice—whatever that means—or violated any rule, regulation or condition imposed by the corporation.

(*j*) The corporation may issue cease and desist orders.

(*k*) It may remove officers and directors and, for cause, hold them personally liable.

(*l*) It may invest and manage funds.

(*m*) It may make loans to rehabilitate insurers.

This review of the duties imposed on the FIGC makes it clear that a huge bureau will be necessary. The sweeping implications of this legislation are hard to overestimate.

If an FIGC bill becomes law, what would it cost the taxpaying and insuring public? Under the FIGC bill you are now considering, the Federal Treasury would be immediately tapped for $50 million, which funds would be supplemented by assessments on the insurance-buying public. This tax would amount to over $30 million per year which, as I shall detail in a moment, is on the order of 30 times the net, uncompensated insolvency loss to the insured public.

However, there is another wasteful burden of the FIGC which, in the long run, could prove even more onerous to the public than the amassing of this unwarranted fund, and this is the burden of examina-

tion of insurance companies by the Federal Government. The report of the special subcommittee of the NAIC, National Association of Insurance Commissioners, to study the Dodd bill, S. 688, introduced in the last Congress to provide a similar fund for auto insurance only, discussed in detail the cost to the Federal Government of examining insurance companies.

This report, even though limited to the companies writing automobile insurance in the United States, used as a minimum figure for beginning operations, 1,250 examiners. This was based on the number of examiners which were employed by the States, and Senator Dodd at that time claimed that the examination job being done by the States was insufficient.

Based on the salary and benefit levels in effect at that time, the NAIC report indicated personnel cost for the Federal Government would be approximately $27 million during the initial examination period. The report assumed that a permanent staff of 300 field examiners might be sufficient for regular and systematic supervision, provided joint examinations, in cooperation with State examiners, could be relied upon. But that number would be sufficient only if the FIGC relied heavily on reports of State examiners. Based on the precedent of other Federal agencies, we have no doubt that FIGC would actually make its own verification of the accounting statements of the insurance companies, its own verification of the securities held by such companies, its own appraisal of the adequacy of company claim reserves, and all other examination functions. The FIGC would tend to increase this number of examiners in order to check into the adequacy of rates, and reserves and in order to test the quality of the figures reported on the books.

The Federal Deposit Insurance Corporation conducts examinations concurrently with State bank examiners, but FDIC is physically present in conducting the examination. As you know, the FDIC only examines State chartered banks which are insured by it and are not members of the Federal Reserve System.

By way of contrast, the FDIC's practice is to accept reports at face value from the Controller of the Currency, who examines all national banks and all State banks which are members of the Federal Reserve System.

If the FDIC does not accept State examinations without participating in them, we doubt that the FIGC will do so either. Indeed a member of this committee and sponsor of this bill has expressed his opinion that Federal regulation should entirely supplant State regulation. FIGC would not ignore rate examinations for long, as it will certainly be argued that adequate rates are pertinent to solvency.

The NAIC's former estimate of a $20 million per year budget for continuing examination of auto insurance only, now increased to $30 million, seems, therefore, to be still too low to apply to S. 2236. In light of the history of Federal preemption of the regulatory function where joint Federal-State jurisdiction exists, and the legislative history of this proposal, we can only conclude that the FIGC will superimpose on the existing State system a costly duplication of examinations and rate supervisory functions. In practice I would not be surprised to see this $30 million figure doubled. We are talking

about an examination system which may really cost the public something on the order of $60 to $90 million a year.

Now, what is the scope of the problem for which this leviathan is proposed? First, as regards the property insurance industry, there have been remarkably few failures which have had any appreciable effect on the average man. This is because his dwelling fire policy or homeowner's policy must be approved by his mortgagee. We are not aware that any information has been presented to this committee to show that failure of property insurance companies is a significant social problem.

The testimony which has been heard has concentrated on the only segment of the business which has presented problems, and that has been the insolvency of so-called high risk automobile insurers. Testimony regarding the automobile insurance business was presented to the committee considering the Dodd bill, S. 688, in 1967.

Updated testimony has been presented to this committee also. For the Dodd bill hearings, the NAIC undertook an analysis of the figure on insolvent automobile insurers, and the NAIC has now updated its 1960 to 1965 study, bringing it up through the year 1967. The NAIC study indicates that the average losses from automobile insurer insolvencies has declined during the latest period to about $5 million per year, as contrasted with $6 million plus in the previous 5-year period.

This study indicated that the activities of the few unscrupulous or irresponsible insurers are being brought under ever closer surveillance by the State regulatory authorities. The estimated $5 million annual loss in the latest period represents 5 cents per $100 of the premiums written by the American automobile insurance industry. If this burden fell equally on all policyholders, it would cost less per policy than running the presses which print the policies.

To what extent, then, does this 5 cent per $100 premiums become spread through the general insurance premium structure? How unevenly does this burden fall upon policyholders and claimants? All but two of the 50 States now require by law that the uninsured motorists endorsement be added to all auto policies.

I have a chart which I can leave with you. This gives you an indication readily that there are only two States remaining where uninsured motorist coverage is not required by law. It is actually sold in 50 States and required by law in 48.

Senator HART. Why don't you state the two States?

Mr. LEMMON. North Dakota and Maryland. Incidentally, in those two States you have unsatisfied judgment funds. In 36 States by law, of the 50 States, insolvency protection is also covered, by law.

We have been striving long before these bills were conceived to solve this insolvency problem through private insurance means, and we have done this voluntarily and by statute in 36 of the States of the Union to cover the insolvency.

Senator HART. For the record also, I will ask the staff to list the 36 States at this point.[1]

Mr. LEMMON. Some of the States allow the policyholder to reject it, however, and some do not. Based on a review of the States which have had uninsured motorist laws on the books for several years, our

[1] See list in letter on p. 77.

staff estimates that where UM coverage, even with right of rejection, goes into effect, over 90 percent of all insured motorists soon have the coverage on their policies. Indeed, this coverage is available for a nominal premium in every one of the 50 States, so anyone can have this protection. Insolvency protection is now included under the standard UM endorsement in every State in the Nation.

Of the motorists who show sufficient responsibility to carry liability insurance at least 90 percent have UM coverage. Where UM is carried it picks up about 92 percent of liability of insolvent insurers to the UM policyholder. This reduces the insolvent loss to the insuring public with any form of liability insurance to about $1 million per year, or one-thirtieth of 1 percent of—I believe that is more likely one-one hundredth of 1 percent—of premiums written.

We have heard it said that if only one policyholder or claimant suffers from an insurer's insolvency that is one too many. We subscribe to this as something to work toward; an objective. I say, too, that so long as one man, woman or child is killed or maimed on our highways that is also one too many.

But perfection will come only in heaven and, in the practical world of human failing in which we exist, the practical limitations of pushing closer to perfection and the diminishing return on increased efforts to do so must be faced, not only in insurance but in all our worldly endeavors. What practical sense does it make to structure a $60 million per year bureau to deal with an insolvency problem which, with UM benefits, only amounts to $1 million per year, net. This is truly like going to the Mayo Clinic to lance a boil.

Senator HART. I think we disagree on whether this is a boil or potential cancer. In other words, some of us don't buy those figures. Sixty to one would be nothing. Going to Rochester for a boil might be foolish, but it is a question whether the assumptions on which you base those conclusions are valid.

Mr. LEMMON. We use the $5 million from the study made by the National Association of Insurance Commissioners which—and I believe the report has been submitted to your committee.

Senator HART. We will get into that.

Mr. LEMMON. I can substantiate the $1 million figure from the $5 million.

For legislative precedent, the proponents of a Federal Insurance Guaranty Corporation liken it to the Federal Deposit Insurance Corporation. As I have just detailed, the diminishing problem of insurance insolvencies today bears not a shadow of resemblance to the national—in fact the international—emergency of the great depression, which saw the failure of 9,100 American banks. It was out of the desperation of this catastrophe that the FDIC was born. Any inference that like need for an FIGC exists is a fantastic distortion.

But there is a parallel between the FDIC and the proposed FIGC. The FDIC does provide a sorry precedent for the accumulation of a fund out of all proportion to the losses incurred. Aggregate net insurance losses to the FDIC from its inception in 1933 for 35 years through its 1968 report have been $55 million.

Yet it continues to collect assessments from the banks at the rate of over $130 million each year. Its accumulated assessments during this period were $2,543 million, or 46 times its net losses paid. After pay-

ing all losses and operating expenses, the FDIC had, by the end of 1968, accumulated a surplus of almost $3¾ billion. The interest alone on this fund produced $162 million, or over five times the greatest combined losses and expenses suffered by the FDIC in any year. Now, I ask, who charges excessive rates, private or Government insurers?

We would like to cite a much happier precedent. We cite the availability of UM coverage with insolvency protection to all States, up from 26 States in 1966, to anyone who contends the States cannot move quickly to adopt new solutions. This is the most desirable solution to the problem because it results in handling insolvency losses through present insurance channels without the creation of new mechanisms and their attendant administrative expense. Equally important, it results in quicker payment to the claimant.

Secondly, some States have adopted statutes limiting subrogation against insolvent carriers until all other accident liability claims have been paid. This approach is designed to enable an insolvent company to cover the remaining losses suffered by such injured parties. A counterpart measure provides for a waiver of liability against the insured of an insolvent insurer by any party accepting a payment under UM coverage, to the extent of such payment. These are two real gap closers.

Next, we encourage making available higher optional limits of uninsured motorist coverage to all those who wish to buy them.

These are all good methods involving quick payment, and no new mechanics imposed upon the present insurance structure. They are underway and there is no reason to think that efforts to develop practical solutions will stop with these measures. We and the other trade associations have additional ideas under study, and the NAIC is also giving intensive study to the matter.

We have tried to point out that the record of State regulation, while not perfect, is still very good. Some say that Federal regulation could do a better job. They like to cite the FDIC to show how competently a Federal agency examines for solvency. Over the last 2 years for which figures are available, 1967 and 1968, in excess of 28,000 individual examinations were conducted by FDIC officials. Such intensive surveillance has been the hallmark of FDIC operations since its inception. Yet, there have been 473 bank insolvencies recorded under FDIC surveillance, and not all of these can be explained without some embarrassment. For example, take the case involving the Crown Savings Bank of Newport News, Va. In a recently published book entitled "The Regulations," author Louis M. Kohlmerier, Jr., reporter for the Wall Street Journal, exposes that in September of 1964, losses in excess of $940,000 were discovered by the FDIC during an examination of Crown.

However, earlier indications of impropriety by the bank officials had been brought to the attention of the FDIC examiners located both in the State of Georgia and the State of Virginia. In subsequently reviewing the facts of this case, House Banking Subcommittee staff members were quoted by the author as deploring the "lack of communication between the FDIC in Georgia and the FDIC in Virginia; between the FDIC in Virginia and the Federal Reserve Bank in Virginia; and between the FDIC and the Virginia banking authorities.

Because of this breakdown in communication, the action taken by the FDIC was too late."

The moral of this story is twofold: First, Federal agencies are not perfect either, and second, nationwide authority does not guarantee nationwide coordination.

It is not my purpose here to impugn the FDIC or any Federal regulatory agency but, for those who cite shortcomings of State regulators as justifying Federal regulation fairness requires us to point out a few of the more flagrant examples where Federal regulation has not operated with flawless results.

Have the federally regulated railroads avoided insolvencies, and have they made great innovations and forward strikes in expanding their service to the public? Has the Food and Drug Administration cleared any items such as cyclamates for usage and then withdrawn them from the market? And for those who have flown in circles above our major cities, has Government air traffic control kept pace with traffic? And what of the report by the American Bar Association Study Commission's recent critique that the Federal Trade Commission has mismanaged its own resources and is frittering away its appropriations on trivial matters, rather than the important function with which it is charged? And last but closer to home, I am thinking of the State Fire & Casualty Co. case. Did the Federal Government provide adequate controls over the securities industry when it permitted inflated quotations to be published by the National Quotation Bureau?

You will not find perfection in either State or Federal regulation, but you will find solid expertise in the State insurance departments, in the NAIC, and among the experienced State legislators who have dealt with insurance for many years. I submit that the States' track record is good and getting better. There is no problem in insurance insolvencies which cannot or will not be met by State legislation.

Senator HART. I will ask counsel to develop questions which, had my plane gotten in on time, I would have had a chance to review before sitting down here. But I was thinking back to some of the testimony we had in the antitrust hearings on the general subject of insurance, and I just disagree 180 degrees with you on that analysis of that State Fire affair. Assuming, and I am sure it is true—indeed you quote a staff report showing the failure of communication betweeen Georgia and Virginia or some place was responsible in part for the inadequate reaction to a failing bank at Newport News—I remember vividly the testimony we had which showed what I thought was the inadequacy of the existing State regulation in terms of solvency involving the Miami, Fla. failure, where the New Jersey Insurance Commissioner wrote the Florida commission a week or two before the thing was put in receivership and asked what is it like, and the answer was great.

I think that represents a failure of communication, too. So, there is no monopoly on that. I am sure you are right in suggesting that examinations will not insure against insolvency. Why don't we simply have a guarantee fund?

Mr. LEMMON. Senator, the thrust of my whole testimony here is to try to show you and the committee that we in NAII were conscious of this problem long before Dodd introduced his bill, long before the

current bill was introduced, because we recognized that something ought to be done to take care of the innocent victims of automobile accidents. So, we set about putting into coverage at a very nominal charge insolvency protection along with uninsured motorist protection to cover this gap, and being fearful that it might not be sold voluntarily as rapidly as it should—fortunately it did; in the State of Washington, 86 percent were insured for this protection before they all went into effect—but we wanted to be certain they were protected by statute, so we set about to cover it through this mechanism. It should be solved.

It has been pointed out there are two remaining gaps, like the non-car-owning pedestrian who was hit, by waiving subrogation against the insolvent carrier there is always enough residue to take care of this problem. We are trying to take care of this problem, we are constantly working and striving to solve that problem at the State level, and we believe it can be accomplished, we believe it will be accomplished.

Senator HART. I commend you for your concern about this subject of long standing. As you say, before the first Dodd bill was put in, you were concerned and anxious to do something about it, but the harsh fact is since the Dodd bill went in, there have been at least 50 failures.

So, while we sit and talk to each other about our concern and sympathy for the policyholder and the claimant, the urgency of Federal or State legislation in order to avoid failure, 50 have at least occurred in the last 3 years.

Mr. LEMMON. We have been moving in the last 5 or 6 years rapidly toward pushing for enactment of these statutes in the various States, and I think we have been pretty successful.

Senator HART. How many States have guarantee funds?

Mr. LEMMON. Seven I believe. Insolvency funds?

Senator HART. Yes.

Mr. LEMMON. I believe there are seven.

Senator HART. Before asking counsel to develop the questions he has prepared, I noticed as I listened to your testimony you oppose this Federal fund because it wouldn't allow for adjustment for local needs. Now, what exactly is the difference between a fellow in Grand Rapids, Mich. and Punxsutawney, Pa., in terms of reflecting local needs when both of them bought the policy from the same company?

Mr. LEMMON. Their needs extend far beyond the question of insolvency. This UM with insolvency protection takes care of him. If he is insured in Michigan or Pennsylvania, he has his accident in Nevada or any place else.

But the regulation which this bill proposes, as I see it, goes way beyond the insolvency problem. It completely takes over the regulation of every scope of the insurance business. I say, Senator, that your local commissioner in Lansing is more familiar with what the residents of Michigan need than some man in Washington or even the commissioner from Pennsylvania.

Senator HART. UM isn't going to protect the policyholder, is it?

Mr. LEMMON. Sure.

Senator HART. I would ask counsel to develop particularly the figures that we have which indicate a substantially lower cost in the administration of the FIGC than Mr. Lemmon's figures would suggest.

Mr. SUTCLIFFE. If you will bear with me, Mr. Lemmon, let me see if I can discuss with you your conclusions about the losses that the Federal Insurance Guaranty Corporation would prevent.

Now, in examining the NAIC study which you use as a basis for the $5 million figure, I am struck by the way in which that figure was arrived at. To come up with the $5 million figure, the NAIC report used as a base only eight of 14 insolvent insurance companies during that period. The authors of that report then applied their 21-percent ratio to the aggregate of the losses from the remaining six companies and came up with a yearly average figure of $5 million.

Let me have you look at the figures from a different perspective.

I would like to introduce for the record chart C.

(Chart C follows:)

Summary of policyholders and claimant recovery from insolvent auto insurance companies as of September 1968

States	15
Companies [1]	80
Policyholders and claimants:	
Number	239, 897
Amount claimed	$525, 018, 284
Evaluated claims for submission to court for allowances:	
Number	122, 560
Amount	$107, 670, 573
Claims submitted and approved by court:	
Number	80, 105
Amount	$50, 097, 637
Actual assets	$33, 673, 620
Amount paid out as of September 1968	$17, 647, 232

[1] For which data is available.

Source: State insurance department replies to Senate Antitrust and Monopoly Subcommittee questionnaire of June 6, 1968.

Mr. SUTCLIFFE. This summarizes the policyholders and claimant recovery from insolvent auto insurance companies as of September 1968. You will see there a total amount claimed of $525-plus million.

The NAIC assumption is if you apply a 21-percent ratio to the total premiums written—$517 million—you will come up with a figure representing the actual losses that were legitimate.

If you apply that you come up with a yearly loss ratio of about $11 million, not $5 million over a 10-year spread for which we have very complete statistics, although even the $517 million is understated—I will bring that point out later. But complete and accurate as far as we go. That is twice as much as the $5 million figure cited in your testimony.

It is interesting to note that this does not include any loss from premiums. In other words, when a company sends out a notice that it can no longer insure you, you go and buy other insurance; there is a loss from premiums.

Let us go again to the NAIC report which you use as a basis for your information to find out what that figure looks like.

On page 188 of the NAIC report the premium loss for the 10-year period was approximately $111.1 million. This adds an additional $10 million per year to the loss, assuming there are no substantial overlaps between claims and the premium loss. There may be some there.

Let us assume there are some overlaps, and then consider the mutual assessments that you have not plugged into your figures with the statistics we have available which amounted to $3.3 million.

There are figures unavailable in our statistics for 20 companies. In other words, of the 109 insurance companies that have become insolvent, we do not have figures for the claims of 20 of those companies. If you plug in an average written premium for a company of $5 million and apply the 21-percent loss ratio you come up with another additional $21 million.

In summary, I fail to understand how you arrived at the $5 million loss figure, even using the assumptions that you have used, when on the basis of data submitted from the insurance commissioners of the States to the Senate Antitrust Monopoly Subcommittee the minimum loss figure on claims using the 21-percent ratio has to be over $10 million per year, and it is probably more like $20 million.

Again, these are direct loss of claims and do not take into account many other indirect losses.

I would like to have you comment on these developments.

Mr. LEMMON. You are asking me to analyze or verify the figures made by the National Association of Insurance Commissioners.

Mr. SUTCLIFFE. Sir, those are the figures you have relied upon.

Mr. LEMMON. That is the official supervisory body in this country. As I understand it, Mr. Sutcliffe, this study made by the NAIC was made by contacting the commissioners or the liquidators or receivers, whatever the situation might be, to get the estimate of losses outstanding for a particular company in receivership in a given State. From that study these figures were derived.

This 21 percent figure which is for 1966–68—if I read what you are referring to, the data received shows that claimant losses were 21 percent of the premium, virtually the same as the ratio for the insolvent insurers during the period 1960 to 1965.

I suppose it would be a reasonable assumption for them to make that since that ratio was running the same as those more matured insolvencies that work out, that it would be reasonable to use that figure.

I did not make these calculations. I am taking their calculations and I am basing my statement on their calculations which is the official regulatory body in this country.

Mr. SUTCLIFFE. When you take their assumptions and the way in which they calculate and apply it to the total picture you come out with almost twice the yearly average of losses for just the claims alone. It would be helpful if we are to arrive at correct figures for the scope of this problem to have as much information plugged in as possible. That is the only point that I think we wish to make.

Mr. LEMMON. I do not know whether—if there are any missing companies, I do not know whether they supplied them to the insurance commissioner or not. I assume they have.

Mr. SUTCLIFFE. We are trying to obtain as reliable statistics as we possibly can.

Mr. LEMMON. Some of the figures that are seemingly bandied around have been all over the lot. Some have been what was sued for, what was claimed, addendums and all this stuff. Some companies that get into receiverships, generally I have known of many, the courts generally throw a lot of them out without merit. So, you have a lot of adjustments to make.

Mr. SUTCLIFFE. Let me go to the real question which goes to the total cost to administer the FIGC. You mentioned that you estimate a

$60 to $90 million a year cost for administration of that corporation. For the record, if I might introduce on behalf of the committee and Senator Hart and his subcommittee, which has supplied the bases for these charts, a chart showing and comparing the cost of administration for State insurance regulation and for the Federal Deposit Insurance Corporation. This is chart A.

(Chart A follows:)

COMPARISON OF STATE INSURANCE REGULATION WITH BANK REGULATION UNDER FEDERAL DEPOSIT INSURANCE CORPORATION

System	Number of financial [1] institutions (as of Dec. 31, 1968)	Cost of administration and supervision (as of Dec. 31, 1968)	Number of examiners (as of Dec. 31, 1968)	Actual financial loss to public resulting from insolvencies (1934–68)
State insurance regulation	5,000	$40,000,000	1,200	$600,000,000
Bank regulation under Federal Deposit Insurance Corporation	14,000	28,771,737	1,526	12,000,000

[1] Includes life and nonlife insurers, and banks subject to FDIC supervision.

Sources: Best's; Senate Antitrust and Monopoly Subcommittee; State insurance departments and Federal Deposit Insurance Corporation.

Mr. SUTCLIFFE. This chart shows in terms of cost that the Federal Deposit Insurance Corporation which supervises 14,000 financial institutions has a yearly cost of administration and supervision of $28,771,737. The number of examiners 1,526. The actual financial loss to the public resulting from insolvencies between 1934 and 1968 was $12 million. In comparison, then, there is a figure of $40 million per year for State insurance regulation with 1,200 examiners, and financial losses to the public exceeding $600 million for the years 1934 to 1968.

Mr. LEMMON. I do not know what you are comparing here. You are talking about all the regulatory functions of the State supervisory officials or just the examination function?

Mr. SUTCLIFFE. This is the total of taxes and fees that are actually utilized by the State insurance commissioners, but according to your argument one of the basic aspects of regulation is insolvency, and this then would account for the displacement of State regulation by Federal regulation. So, if in fact that is true, the $40 million figure holds. If it is not true, there may be a lower adjustment.

Mr. LEMMON. I would say taking your figures—this is the first time I have seem them, I am a little ill-prepared to comment on them, as you can appreciate—but taking your total State figure of administrative cost of $40 million for State insurance regulation compared with some $29 million for FDIC, FDIC, as I pointed out in my paper, has a very limited function of examination, they have a very limited function as to what they do.

States do many things in supervisory work other than looking at financial statements. It is all embracing. Taking these very figures, if you want to use the State figures and the FDIC, which this bill will do, I think $60 million would be a conservative estimate—maybe more, because you are taking more functions.

Regulation does not stop with examination of companies for solvency only. It never has and never will.

Mr. SUTCLIFFE. You are suggesting, then, that the Federal Deposit Insurance Corporation examinations will be much less complicated

than a Federal Insurance Guaranty Corporation examination; is that correct?

Mr. LEMMON. I said that the FDIC has a very limited scope of activity than the regulatory function of the State insurance authorities.

Mr. SUTCLIFFE. But you do not then subscribe to the fact that that $28 or $29 million figure—you see you brought up as an example the costs of Federal regulation in other areas. The cost of Federal regulation in other areas comes out to $28 or $29 million compared to your $60 to $90 million estimate. There is a disparity which we would like you to explain.

Mr. LEMMON. If you take all these other functions which I think this bill will finally lead you to take; rate regulation, looking into every detail of an insurance company, you are not going to come out with a $30 million figure. You will come out with more.

Mr. SUTCLIFFE. But they only have $31 million a year under the present formulation to operate. How are they going to spend $80 to $90 million?

Mr. LEMMON. You know, they have new taxes each State legislative session, each congressional session, so I do not think that is insurmountable. I do not know where the $600 million comes from. So, I have no comment on that.

Mr. SUTCLIFFE. Let me return to some of the other points that you have made in your statement, if I may.

You state you are opposed to the Federal Insurance Guaranty Corporation because there is no need for a body of experts to help State regulation; is that correct?

Mr. LEMMON. Absolutely. There is no equivocation on that point.

Mr. SUTCLIFFE. This troubles the committee somewhat, and let me bring to your attention again the NAIC staff report in 1968, I believe, pages 216 through 232. In discussing the need—this is the insurance commissioners of the State discussing the need for the experts to help them—they say:

> The actual functions of the Corporation would be to provide State insurance departments with professional expertise and assistance both before and during insolvency proceedings. The Corporation would possess knowledgeable consultants from which the individual commissioners could solicit aid, if and when desired.

Now, the staff report goes on to list other functions which a full-time body of experts could perform. Among those is the Corporation's ability to prevent insolvencies by providing "a vehicle to track interstate adventurers."

Admittedly the type of corporation envisioned by the NAIC staff in their discussion was not a Federal Government corporation but a similar corporation within the existing framework of the National Association of Insurance Commissioners.

In any event, the need for assistance in the insolvency area has been recognized by the National Association of Insurance Commissioners. Could you please comment on that in light of your previous statement?

Mr. LEMMON. There is no question that we are for improving State regulation wherever it is needed.

Mr. SUTCLIFFE. Through a body of experts?

Mr. LEMMON. And we have worked for that in State after State, where we have asked for increased appropriations so there can be

adequate supervision. We have worked for strengthening of the laws so that the commissioner will have the proper tools to regulate for solvency. There is no question about that. I have never embraced this particular facet of NAIC's central office idea, but that would still be State regulation.

I think that each State ought to be fortified, and this is what I am for and what we are for, is to prepare each State with sufficient expertise, with sufficient laws to handle problems within their own States, and most States are doing that today. They are improving each year. They are getting increased pay, better personnel, better grade supervision.

Mr. SUTCLIFFE. Under S. 2236, is it a requirement that the Federal Government examine all insurance companies that apply for guaranty status? Are you aware?

Mr. LEMMON. Is it a requirement?

Mr. SUTCLIFFE. Yes, sir.

Mr. LEMMON. I do not know whether it is a requirement or not. I think that is what will happen.

Mr. SUTCLIFFE. I think there is a basic distinction that perhaps we could bring out between Dodd and S. 2236 because there is no necessity for Federal examination under S. 2236. In fact, S. 2236 allows for the Federal Insurance Guaranty Corporation to concentrate on marginal insurers and avoid duplication of efforts.

Let me say once again this is consistent with the recommendations embodied in the National Association of Insurance Commissioners' report. They said, "The work of the Corporation's staff would not be devoted to the majority of companies whose scrutiny would continue to be conducted under basic NAIC auditing proceedings. The Corporation would concentrate on marginal insurers only. Furthermore, its activities would be integrated with and supplemental to the regular NAIC examination."

Apparently you do not feel that a Federal Insurance Guaranty Corporation could not do that; is that correct?

Mr. LEMMON. I am not saying they could not. I am saying if history is any indication, they will not because, take the Federal Deposit Insurance Corporation in examination of State banks, they have someone physically present, they do not take the State examiner's word, and this is what is going to happen in the insurance company end of it, just as sure as we are sitting here.

Mr. SUTCLIFFE. I am very interested in your discussion of the uninsured motorist coverage. I would like to go over some figures very carefully to understand how you arrived at certain of the conclusions you have made.

You have stated that the loss from insolvencies is 5 cents per $100 of premium.

Mr. LEMMON. Yes, sir.

Mr. SUTCLIFFE. We have had an exchange of views about that. This committee understands it to be more on the order of 10 to 20 cents per $100, and I hope by the end of this hearing we have a firm grasp on what those figures are.

Your contention is that the uninsured motorist coverage picks up 92 percent of the liability of insolvent insurers.

Mr. LEMMON. Yes.

Mr. SUTCLIFFE. Would you please explain to the committee how you determined that 92 percent of the liability of insolvent insurers is picked up by the endorsement? I would like to understand the breakout for BI and PD under all the claims that are made against insolvent insurers because these kinds of breakouts will be absolutely necessary for you to come up with a figure of 92 percent. I would like for you to explain to this committee how that was arrived at and what figures you used, and if we do not have time this morning, at least for the record.

Mr. LEMMON. I do not have time this morning. I will try to file the detailed information.

Certainly, few States required property damage as well as BI. We designed it for BI originally for the very simple reason we wanted to take care of the innocent injured victim of automobile accidents. That was the purpose. That is what it was designed for and that is what it has accomplished.

In getting this 92.2 percent, or whatever it is, we took the BI losses, the bodily injury losses of our normal business, normal passenger car basic limits business, and we found that 92 percent of those losses were under 10–20 limits. The UM covers normally to the statutory limits of 10–20 in most States. Some States are higher and maybe in one or two instances lower. We provide our experience data at the 10–20 point. So 92 percent of the losses are settled within the 10–20.

You would naturally assume that no more of the uninsured motorist claims would run higher excesses than normal business. So you would have 92.2 percent of your liability covered by the UM mechanism.

Mr. SUTCLIFFE. That would assume, of course, a perfect UM coverage?

Mr. LEMMON. No.

Mr. SUTCLIFFE. An ideal compensation of all BI claims that would have been made against a policy holder of an insolvent holder are then directly turned over to the company and are settled or satisfied; is that correct?

Mr. LEMMON. You are talking about a matter of settlement, and I am talking about a matter of coverage. I say the coverage extends to 92.2 percent of those losses.

Mr. SUTCLIFFE. But you have made the assumption of settlement rather than coverage in reducing the figure from $5 million to $1 million.

Mr. LEMMON. That is correct.

Mr. SUTCLIFFE. But you just told me you could not do that. You assumed a settlement coverage—you have assumed a settlement coverage of $4 million. Do you have statistics to show a settlement coverage of $4 million on the basis of the uninsured motorists?

Mr. LEMMON. I said coverage. I did not say settlement.

Mr. SUTCLIFFE. Then how do you take the coverage and translate that into settlement or disposition of assets?

Mr. LEMMON. On your UM coverage, 97 percent of the claims are settled without even final arbitration. That is a pretty good record.

Mr. SUTCLIFFE. How much of the $5 million of claims that you allege per year occur in insolvency situations are settled? How much money? You have come up with the $4 million figure, and that is the figure——

Mr. LEMMON. I would say $4 million, around $4 million.

Mr. SUTCLIFFE. Could you explain to the committee how you arrived at those figures?

Mr. LEMMON. Yes, sir. We provide coverage for the basic limits, 10–20 basic limit. Over that amount is excess. So, your statutory UM would cover all those basic losses. It would not cover the excess losses. Some companies do write the excess.

Mr. SUTCLIFFE. What would it pay? It would cover that. Your argument is it would cover that. What would it pay?

Mr. LEMMON. Up to 10–20 would be $4 million under this illustration.

Mr. SUTCLIFFE. In other words, they pay what the coverage is?

Mr. LEMMON. Sure. Well, you do not mean on a $100 claim they are going to pay $10,000.

Mr. SUTCLIFFE. Let me go on, and if, in reviewing the testimony we want to ask you further questions, we would appreciate the opportunity to develop this further.

Mr. LEMMON. Fine.

Mr. SUTCLIFFE. Despite what the costs are, let's talk about the costs of spreading this loss, whatever that loss is, either $5 or $10 million or more. Under the provisions of S. 2236 the maximum cost to spread the loss is 12.5 cents per $100 of premium. That is figured on the basis of one-eighth of 1 percent of the net direct premiums. I am curious to know, even assuming the UM coverage does spread the risk to the extent you said, how much the uninsured motorist coverage costs the American consumer per $100 of premium written. In other words, can I get an uninsured motorist endorsement to cover insolvency for 12.5 cents per $100 of premium?

Mr. LEMMON. Of course you would be comparing apples and oranges there. The uninsured motorist protection is much broader than insolvency. It covers you against the negligent acts of an uninsured motorist, which is much greater exposure than the insolvency aspect.

Mr. SUTCLIFFE. I realize that, but then if, in fact, you are doing both under the system and you are telling us our system is too expensive, we have to know what the breakout under the uninsured motorist coverage is for the insolvency protection you have afforded, and that is the figure we would like for you to provide.

What is the cost to the American people for the insolvency coverage that you offer under your UM endorsement?

Mr. LEMMON. Under our competitive pricing system it varies by company. Some companies charge different rates than others, and it is bound to be very nominal. The whole uninsured motorist coverage protection is a very nominal cost. It varies by company; it varies by State.

Mr. SUTCLIFFE. It is at least $4 million a year you have told us.

Mr. LEMMON. That is the losses.

Mr. SUTCLIFFE. That is a payout, you say?

Mr. LEMMON. When this is in effect in all the States which it practically is now.

Mr. SUTCLIFFE. Perhaps we can go into that at a further date.

Mr. LEMMON. I will be glad to furnish you the information.

Mr. SUTCLIFFE. If we could have the breakout of what the cost is.

Mr. LEMMON. You mean the loss cost?

Mr. SUTCLIFFE. No. What are you charging the American consumer for the protection that you allegedly are affording him under UM?

Mr. LEMMON. We represent 500 different companies, so they probably have 500 different rates.

Mr. SUTCLIFFE. You cannot average those rates out?

Mr. LEMMON. We can average them, of course.

Mr. SUTCLIFFE. You have had to average those rates out to give us the figure of the $4 million coverage.

Mr. LEMMON. We can take the number of cars and divide it into the number of premiums and that gives you the average rate, sure. But that would be the total now of the uninsured motorist protection as well as insolvency. There is no way to divide this—

Mr. SUTCLIFFE. Could you give us the total revenues for the association you represent under uninsured motorist coverage and the total payout under uinsured motorist coverage with administrative expenses?

Mr. LEMMON. Expense?

Mr. SUTCLIFFE. You want to consider those things in terms of coming up with some kind of net figure.

Mr. LEMMON. Your expenses are not broken out.

Mr. SUTCLIFFE. You must have some 30 percent factor you can apply to come up with a net figure in that area.

Mr. LEMMON. It is so little that I have never heard of American policyholder complain about the charge for UM coverage protection, never.

Mr. SUTCLIFFE. I wonder whether any policyholder in the United States would complain about spending 12.5 cents for every $100 of premium under the Federal Insurance Guaranty Corporation bill. If this is too costly, if this is too expensive, we have to have figures to compare it in terms of what you as an industry are providing. This is all we are asking for.

Mr. LEMMON. I would be against it if it did not cost 1 penny, to be perfectly clear about it.

Mr. SUTCLIFFE. The average uninsured motorist endorsement is considerably above $1. It is considerably above $2. It may be running as much as $8 per policy.

Mr. LEMMON. It could be in some States.

Mr. SUTCLIFFE. Now, we have a lot of things we have to see here as to where these factors plug in. We would like to see them.

Mr. LEMMON. You have got a lot more coverage involved than just the insolvency feature.

Mr. SUTCLIFFE. Fine. We would like to see that broken out if we could.

Senator HART. Thank you very much, and we will look forward to the breakdown of those figures.

Further questions for the National Association of Independent Insurers:

(Full text of letter from Senator Magnuson to Vestal Lemmon, President of the National Association of Independent Insurance and letter of response printed in full following the specific questions and answers below:)

1. In reviewing the NAIC statistics upon which you relied in your testimony, do you still maintain that the year insolvency loss is between 5 and 6 million dollars? If so, would you please explain the bases for this conclusion?

In answer to question #1 of your December 9 letter, my first suggestion would be that the actuaries who prepared the NAIC study are the most logical persons to defend their compilation of the data furnished them by the liquidators as to insolvency losses. Nevertheless, upon reviewing the several estimates of annual insolvency loss which have been submitted to the Committee, considering the adequacy of the data on which they were based, the experience of the personnel evaluating them and the plausibility of the assumptions and interpretations which have been stated in each instance, the NAIC study is the only one in which we are confident of the reliability of the underlying data and the manner in which it was used. A figure between five and six million dollars per year is the best substantiated figure presented to the Committee. The NAIC figures were based on data furnished them by the liquidators and receivers, combined with the states' own records regarding premiums. What source could be better?

It is our belief that UM insolvency protection produced little or no effect on these figures, as UM collections would not be an offset against a claim filed with a receiver. Also, for the period for which the figures were compiled, there was little UM with insolvency protection in effect; the insolvency protection feature is a relatively recent development.

2. Could you please explain in detail how the uninsured motorist endorsement with insolvency protection pays 4 million of the estimated 5 million dollars of yearly losses resulting from insurance company insolvencies?

(a) On what does the NAII arrive at the conclusion that the uninsured motorist endorsement with insolvency protection pays 92% of the insolvency loss? (transcript at 105)

(b) How can the uninsured motorist protection cover 92% of the losses when it does not as a general rule cover property damage loss or loss suffered by non-car owning claimants?

(c) Does the 21% ratio used by the NAIC to calculate actual insolvency loss already take into account the protection afforded by the uninsured endorsements with insolvency protection?

In other words, is the amount of the uninsured motorist endorsement with insolvency protection already included in the insolvency loss formula, thus making any subtraction of UM insolvency protection from an insolvency loss determined by that formula inappropriate?

Our testimony that $4,000,000 of the $5,000,000 claimant insolvency loss would be picked up by UM insolvency protection was based upon a calculation that 80% of third party claims filed by individuals against insolvent insurers could potentially be covered by the insolvency protection under the UM endorsement. We had interpreted the words "loss to claimants" and "average annual claimant losses," which appear in conjunction with the NAIC loss estimates (e.g., page 21, line 28; p. 181, line 44) to refer to third party losses. However, we are now informed that the term "claimant" means a claimant against the receiver. Accordingly, in addition to third party liability claims by individuals a number of other types of claims would be included in the figures receivers furnished the NAIC, such as, (a) collision and comprehensive claims by policyholders, (b) subrogation claims by other insurance companies for collision losses they have paid their insured, (c) claims for return premiums from policyholders and (d) claims by reinsurers for premiums due under reinsurance contracts.

The foregoing information regarding the broader definition of "claimant loss", requires a complete reevaluation, of course, not only of the manner in which UM insolvency protection affects the impact of insolvencies but, in addition, the entire question of on whom the impact falls. Accordingly, we respectfully request that the Committee add the material in this section IV to its records in correction of our previous testimony regarding insolvency protection under the Uninsured Motorist endorsement and in further examination of the subject. If the Committee should desire, we will be glad to return to testify on these matters.

Without a field study of the files of a representative sample of claims in liquidation, there is no way to tell what proportion of the claims before liquidators are from third party claims, from first party coverage on policyholders, for subrogation claims by other insurance companies, for reinsurance premiums due other insurance companies, for return premium to policyholders of the insolvent companies. It would be very helpful if such a study could be undertaken either by this Committee or by the National Association of Insurance Commissioners.

Meanwhile, it is apparent that something less than the total of $5,000,000 to $6,000,000 per annum of insolvency loss is loss to third party claimants; probably substantially less. We should then examine the nature of the other categories of claims, assess their impact on the public and assess the impact of S–2236 on such other claims.

First, regarding claims for return premiums, all solutions proposed to date to the insolvency problem make some acknowledgement of the fact that loss of return premium, although an unfortunate consequence of insolvency, is not of a catastrophic nature which demands a legislative solution. The loss of return premium is not, socially speaking, much different from the loss of any debt or account when a non-insurance firm goes bankrupt. In fact, the loss of return premium may have less impact on most people than would the average bankruptcy loss of an account or merchandise receivable. Thus, in some of the state insolvency plans deductibles are imposed, e.g., Wisconsin with a $200 deductible. In others, loss of premium is excluded from the plan, e.g., California and Michigan. Even under S–2236, only one-half of the premium lost is an allowable claim, so the sponsors obviously do not consider it a serious social problem either!

Second, the part of the "net loss to claimants" represented by subrogation claims of other insurers places no burden on individual policyholders or claimants. The inability of an insurance company to obtain a subrogation recovery against an insolvent insurer constitutes no social problem justifying the creation of an insolvency guaranty fund. The same is true of inability of a reinsurance company to collect premiums due it from the insolvent carrier.

Collision and medical payments claims are more serious than the two previous items. However, even with respect to these claims, the individual may ultimately be reimbursed for his loss by a tort feasor.

The remaining claims are liability claims. We contend that UM with insolvency protection has the potential of reducing the impact of this problem on individuals by 80%. In saying this, we have considered the following points:

1. UM coverage with insolvency protection is now available in all states.
2. All but two of the 50 states now require by law that the UM endorsement be added to all auto policies. These two states have insolvency funds. Some states allow the policyholder to reject UM coverage and some do not. Even in those states where the policyholder may reject it, over 90% of the motorists carrying liability insurance carry the UM endorsement.[1]
3. Most BI liability losses are within the limits of UM coverage.[2]
4. Six states now require that UM coverage also apply to property damage liability claims, with deductibles from $100 to $300 being specified. However, since collision insurance may be carried as a voluntary coverage, and a substantial majority do carry collision, no policyholder need rely on either the solvency or liability of a third party and the third party's insurer to avert major loss from vehicle collisions.
5. With regard to pedestrians who do not own (or whose families do not own) a car, we believe the number of such cases is relatively small, but we have proposed "gap-closer" legislation which would give such claimants priority over insurance companies' subrogation claims, thus reserving sufficient funds to pay most pedestrians in spite of insolvency of the insurer.

In summary, the proportion of uncompensated loss to automobile accident third-party claimants due to insurer insolvencies, which cannot be compensated

---

[1] We have calculated the percentage carrying UM coverage from NAII statistical data on 1967 Calendar Year Earned Car Years. In states where the UM law with right of rejection has been in effect a sufficient length of time so that all policies have been renewed at least once since the law's effective date, the figures indicated 91.26% of the cars insured carried the UM coverage. The states used in the calculation were Alabama, Arkansas, Florida, Georgia, Hawaii, Louisiana, Michigan, Nebraska, North Carolina, Ohio, Pennsylvania, Rhode Island and Wisconsin.

[2] Per NAII records, which include over half of the automobile insurance written in the United States, 92.2% of BI losses incurred are on the basic limits portion of the coverage. "Basic limits" is here defined as $10,000/$20,000. The statistics used are the NAII compilation of 1966 Accident-Year, Countrywide Automobile BI Liability Experience, developed through March 31, 1968.

Uninsured Motorists limits on average somewhat exceed $10,000/$20,000. Minimum UM coverage is never lower than the Financial Responsibility limit, which is constantly being raised by the various states. State trends, including voluntary programs by some companies to offer higher UM limits, make it appear that UM limits will soon be written for amounts which average well in excess of Financial Responsibility Law limits.

for under UM coverage with insolvency protection, is very small. With respect to BI liability, it is something less than 7.8% of such loss (that portion of the loss in excess of the UM limits) and will further diminish as higher UM limits become available. With regard to property damage liability, the insolvency of the third party's carrier can be ameliorated by carrying collision insurance. Most car owners do, in fact, carry collision insurance. This is especially true of newer, more valuable cars, as most of them are financed. Other gaps in protection are very small. Overall, we believe it a reasonable estimate that at least 80% of the third party claimant insolvency loss problem can be solved by UM coverage.

3. How must does the insolvency protection afforded under the UM endorsement cost the American policyholder? If this figure is not available could you please provide the Committee with the following information?

(1) the yearly net direct written premiums collected under the UM endorsement;

(2) the yearly payout under the endorsement to policyholders and to the American Arbitration Association; and

(3) the administrative costs factors for the UM endorsement.

In answer to you question #3, there is no coding of loss data reported by insurance companies to either governmental agencies or to the insurance industry's statistical agents which would segregate UM losses on account of insurers' insolvencies from other UM losses. Accordingly, there is no practical way to obtain this data on a segregated basis.

However, the administrative cost factors and the actual loss factors for the UM endorsement as a whole, as requested in question #3 (3), are available. The NAII statistical service reports for 1966, the last available year with reasonably matured UM loss figures, that the loss ratio for uninsured motorist coverage was 70.8%. The remainder of the premium, 29.2%, would be what the public paid over and above losses to operate the protection system under the UM endorsement. Standard economic theory and accounting practice would call for the application of the 29.2% cost to premiums attributable to the insolvency protection as well as other parts of the undivided-premium UM endorsement package. In fact, there is no reason to assume any difference in normal insurance company expense items, such as commission, taxes, salaries and employee benefits, rent and building operating expenses, fees, accounting, loss experience compilation, equipment, policy issuance, underwriting reports and surveys. There might be some variation in the expense factors regarding claims handling, but which way the factor would vary is not clear. Chances are that if the matter were subjected to cost analysis, the variation of insolvency protection from the overall UM total cost factors would not be great. Accordingly, it seems reasonable to estimate the cost of providing insolvency protection under the UM coverage by applying the approximate figure developed on an overall basis. On this basis, the administrative cost of handling three million dollars in insolvency losses (if that should happen to be the BI component of the five million dollar figure developed by the NAIC, after deducting other types of claims against receivers—see our section IV.) would amount to only $1,280,000. This is, indeed, a modest figure in comparison with even the proponents' estimates of the costs of administering the FIGC.

Net direct earned premiums on UM coverage reported to the NAII statistical service for the aforementioned 1966 year were $64,728,200 and losses incurred were $49,238,598. Unfortunately, the compilation of "written premiums," which you requested, is not ready in time to include with this letter. We will send it to you in a few days.

Information supplied to us by Mr. Edward W. Dippold, Vice President, American Arbitration Association shows that payments to the AAA for UM arbitration were, for the year 1967, $997,027 paid by insurance companies plus $283,630 filing fees paid by claimants. During that year, 8,621 cases were filed for abritration with the AAA. From the standpoint of the cost to society of operating the adjucatory process, this appears to be much less costly per case than the alternative of putting UM claims through the courts. It is also a small figure compared to the total UM premiums shown in previous paragraphs. Again, please bear in mind that the foregoing cases involve very few matters under insolvency protection but, rather, they include all UM coverage arbitrations. Only a small percentage of UM cases are arbitrated and proportionately even fewer cases involving insolvency protection probably reach arbitration.

DECEMBER 9, 1969.

Mr. VESTAL LEMMON,
President. National Association of Independent Insurers,
Chicago, Ill.

DEAR MR. LEMMON: In order to make our hearing record on S 2236 complete, I am submitting for your consideration several questions which the Committee would like your organization to answer. If you could provide the Committee as soon as possible with the answers to the following questions, we would greatly appreciate it:

1. In reviewing the NAII statistics upon which you relied in your testimony, do you still maintain that the yearly insolvency loss is between 5 and 6 million dollars? If so, would you please explain the bases for this conclusion?

2. Could you please explain in detail how the uninsured motorist endorsement with insolvency protection pays 4 million of the estimated 5 million dollars of yearly losses resulting from insurance company insolvencies?

(*a*) On what basis does the NAII arrive at the conclusion that the uninsured motorists endorsement with insolvency protection *pays* 92% of the insolvency loss? (transcript at 105)

(*b*) How can the uninsured motorist protection *cover* 92% of the losses when it does not as a general rule cover property damage loss or loss suffered by non-car owning claimants?

(*c*) Does the 21% ratio used by the NAII to calculate actual insolvency loss already take into account the protection afforded by the uninsured endorsement with insolvency protection?

In other words, is the amount of the uninsured motorist endorsement with insolvency protection already included in the insolvency loss formula, thus making any subtraction of UM insolvency protection from an insolvency loss determined by that formula inappropriate?

3. How much does the insolvency protection afforded under the UM endorsement cost the American policyholder? If this figure is not available could you please provide the Committee with the following information?

(1) the yearly net direct written premiums collected under the UM endorsement;

(2) the yearly payout under the endorsement to policyholders and to the American Arbitration Association; and

(3) the administrative costs factors for the UM endorsement.

If you have any questions when preparing the answers to the above inquiries, please do not hesitate to contact me. Thank you very much for your continuing cooperation as our Committee explores the insurance insolvency problem in the United States. Your testimony and answers to these questions will be most helpful as we consider S. 2236.

Sincerely yours,

WARREN G. MAGNUSON, *Chairman.*

NATIONAL ASSOCIATION OF INDEPENDENT INSURERS,
Chicago, Ill., January 23, 1970.

Hon. WARREN G. MAGNUSON,
Chairman, Committee on Commerce,
U.S. Senate, Washington, D.C.

DEAR SENATOR MAGNUSON: Supplementing my letter of January 21, companies reporting to the NAII as statistical agent had premiums written, for the calendar year 1967, of $89,465,025. This amount would not include their writings in Massachusetts, New York and South Carolina for private passenger cars as these are not available from our statistics. This amount of written premium is equivalent to $82,764,033 of earned premium.

Respectfully yours,

VESTAL LEMMON, *President.*

NATIONAL ASSOCIATION OF INDEPENDENT INSURERS,
Chicago, Ill., January 21, 1970.

Hon. WARREN G. MAGNUSON,
Chairman, Committee on Commerce,
U.S. Senate, Washington, D.C.

DEAR SENATOR MAGNUSON: By letter of December 9, 1969 you asked us to answer three questions, actually seven questions with their subsections, relative to our testimony on November 12, 1969. We will attempt to answer these, and also to

comment on matters which Mr. Sutcliffe, counsel to the Committee, placed in the record by means of charts and comments thereon, which we first saw only upon being shown them at the November 12 hearing.

I.

We were asked to comment on a chart, shown on page 93 of the transcript of the November 12 hearing. We asked that these additional comments, which we have prepared after having more adequate opportunity to examine the exhibit, be placed in the records of the Committee.

A. On page 94 of the transcript, Committee counsel takes the factor which the NAIC study developed, 21%, and implies that this factor would be appropriate to apply against the $525,000,000 "amount claimed" total in the ten years covered by the Senate Committee questionnaire of June 6, 1968. He then arrives at a figure of $11,000,000 average annual loss, contrasted with the $5,000,000 which we have quoted from the NAIC study. Counsel has mistakenly applied the percentage, which the NAIC study determined to be the percentage of actual claimant loss to premiums written, against the questionnaire's figure of *amounts claimed*. Quoting the NAIC Report, page 181 "the data received shows that claimant losses were *21% of the premium*—virtually the same as the ratio for the insolvent insurers during the period 1960–1965."

However, even working with the figures in the Committee staff's exhibit on page 93, we should point out that the claims submitted and approved by courts totalled 50 million dollars, or 5 million dollars per year, approximately the same amount as was arrived at by the NAIC study by a different means (see page 29 of the NAIC booklet).

Looking further at the exhibit, it appears that the $50,097,637 figure may be further reduced by application of the "actual assets" of $33,673,620 shown in the chart and/or the "amount paid-out as of September, 1968." The relationship of these figures to the 50 million dollars is not explained, but it seems that if they are applied to the 50 million dollar figure, the average annual loss to claimants would be well below $5,000,000 per year.

B. Following up the introduction of the chart, Committee counsel, at the bottom of page 94 of the transcript, quotes page 188 of the NAIC report as stating "the premium loss for the ten-year period is approximately $111.1 million." We assume that he meant to cite some other page as we are unable to find any such figure on page 188 of the NAIC booklet on the *Report on the Special Committee on Automobile Insurance Problems*. On November 19, 1969, he again referred to the $111.1 million without citing the source by page or table number, but this time he called it "unearned premiums." (Tr. page 328). Premium loss and unearned premiums are two different things, of course, and any calculation of loss to policyholders which does not recognize this is probably entirely incorrect. This suspicion is given weight by the fact that the $111.1 million for ten years would be more than double the $5 million actual annual loss to policyholders *and* claimants combined, developed from the NAIC study of liquidators' reports.

Aside from the foregoing, there are strong reasons for not considering premium loss as being of equal consequence with loss to claimants, as set out later in this letter (section IV, fifth paragraph), including the fact that S–2236 provides only partial reimbursement of these losses.

C. Continuing on page 95 of the transcript, Committee counsel suggests we should also add in $3.3 million of premium assessments against policyholders of companies which have gone insolvent. Apparently, this covers a ten-year period, and would average $330,000 per year. Here we would comment that, while these assessments are unfortunate, this is a relatively small figure compared to costs of operating the FIGC.

It should also be noted that the number of assessable policies being issued has been declining over the years and continues to decline, due to action by the states and also by abandonment of this method of doing business by automobile insurance companies. But, further, the creation of an FIGC will not do away with assessments against policyholders. The post-loss assessment method of sharing losses between policyholders, while declining in popularity, is a time honored one held out by many academicians and insurance men as the best example of the true concept of insurance risk-spreading. In connection with companies developing operating income by the assessment method it is not at all clear how S–2236 would apply. Would it relieve policyholders of the obligation to pay assessments for which they have contracted (often because of a lower initial premium

charge)? This would be unfair to policyholders paying standard rates to non-assessable companies.

D. In the second paragraph on page 95 of the transcript, Committee counsel makes an assumption that the average written premiums for the twenty insolvent companies, for which figures were not available in the replies to the June 6, 1968 questionnaire, were $5,000,000 each. We find nothing in the record to support this assumption. He then applies the aforementioned 21% figure to this total and arrives at an additional $21,000,000 of loss which, we presume, he would add to the $50,097,637 figure shown in the table, thus increasing the approved claims figure by 40%. Since 20 out of 109 companies is, numerically, only 18.3% of the companies studied, the assumption made is, in effect, that the 20 companies write about double the volume of premiums per company written by the remaining 89. If one were to indulge in assumptions at this point, it would be just as reasonable to assume that these companies would actually be smaller rather than larger. In any event, the assumption of additional loss appears to be completely unsupported, and such speculation should be accorded no weight in the Committee's deliberations.

II.

I was asked to comment on the chart which is shown on page 98 of the transcript. We had not seen this chart prior to the moment it was presented to me at the hearing by Mr. Sutcliffe and, accordingly, could not comment on it fully at the time. We would like, now, to add the following comments regarding the chart and the related testimony.

In summary, we must comment that the figures presented on the chart as comparable are, in each case, not comparable and are highly misleading.

A. The FDIC Examining Staff does not have the responsibility for examining all 14,000 banking institutions. This number includes all national banks, all state banks which are members of the Federal Reserve System and also the state banks which are not members of the FDIC. (Source: *FDIC 1968 Annual Report*, Table 101). Banks in the first two categories are examined by the Controller of the Currency, and banks in the latter category are examined by state banking officials only. The number of banks subject to examination by the FDIC is only 7,850 and these have about one-fifth as much in assets as the banks examined by the Controller of the Currency. (Source: *FDIC 1968 Annual Report*, Table 101 and 108). Accordingly, the inference that the entire banking industry of 14,000 banks is examined by 1,526 FDIC examiners at a cost of $28,771,737 is completely misleading and untrue.

B. The $12,000,000 shown as actual financial loss to the public resulting from insolvencies of banks (1934–1968) is not explained. Is this loss to depositors from uninsured banks? Is it loss to depositor from insured bank before the FDIC reimburses depositors? Is it loss to depositors in excess of the FDIC per account limit? In its 1968 Report the FDIC indicated accumulated loss and loss expenses of $55,000,000. How does the $12,000,000 figure square with this? As the government can only pay out money which it receives from the public, it is misleading to exclude the $55,000,000 from any table comparing the financial burden on the public due to bank insolvencies with the financial burden resulting from insurance company insolvencies.

Of course, we believe that any mention of the financial burden on the public attributable to protecting against bank insolvency is incomplete without mention of the tremendous cost burden of operating the extensive examination operations. For the period of time in the table, this amounted to $362,000,000 for the FDIC alone. Probably even greater examination expenses were incurred by the Controller of the Currency since he examines about an equal number of banks, but they are banks whose assets aggregate about five times those of FDIC examined banks.

C. The chart includes the number of insurance institutions, administrative expenses, purported losses and examiners involved in state regulation of life insurance, which is not an appropriate subject for comparison here, since it is not proposed under S–2236 that life insurance be included in the FIGC. Further, we are not shown the source of the $600,000,000 insolvency figure attributed to the insurance industry and are not aware that such a figure has ever been substantiated by any well founded study presented to this Committee or to anyone else. The NAIC booklet (pp. 46 and 47) shows that during the 1930s life insurance policyholders suffered $180,000,000 in loss. However, this includes the depression years 1930–33, and during this period bank depositors' losses were 3½ billion (Ibid, p. 46). Since then, life insurance company losses have been

miniscule. The studies of the fire and casualty industry go back to 1958 and show $50,000,000 in losses to claimants. There seems to be no credible basis for estimating fire and casualty losses prior to this date. The $600,000,000 figure, therefore, appears to be pure speculation.

D. The 1,200 state examiners, shown in the table, are not as high a percentage of the total number of persons employed by the state insurance departments as the 1,526 examiners employed by the FDIC are in proportion to its total personnel. State insurance departments have many employees who deal with such matters as rate regulation, policyholders' complaints, licensing of insurance agents, etc., whereas FDIC is engaged almost entirely in examination. The chart, however, uses the entire cost of state regulation of $40,000,000—not just the cost of 1,200 examiners, thereby creating an inference that state costs per examiner are higher than federal costs. This, again, is an incorrect and misleading inference.

III.

In answer to question #1 of your December 9 letter, my first suggestion would be that the actuaries who prepared the NAIC study are the most logical persons to defend their compilation of the data furnished them by the liquidators as to insolvency losses. Nevertheless, upon reviewing the several estimates of annual insolvency loss which have been submitted to the Committee, considering the adequacy of the data on which they were based, the experience of the personnel evaluating them and the plausibility of the assumptions and interpretations which have been stated in each instance, the NAIC study is the only one in which we are confident of the reliability of the underlying data and the manner in which it was used. A figure between five and six million dollars per year is the best substantiated figure presented to the Committee. The NAIC figures were based on data furnished them by the liquidators and receivers, combined with the states' own records regarding premiums. What source could be better?

It is our belief that UM insolvency protection produced little or no effect on these figures, as UM collections would not be an offset against a claim filed with a receiver. Also, for the period for which the figures were compiled, there was little UM with insolvency protection in effect; the insolvency protection feature is a relatively reecnt development.

IV.

Our testimony that $4,000,000 of the $5,000,000 claimant insolvency loss would be picked up by UM insolvency protection was based upon a calculation that 80% of third party claims filed by individuals against insolvent insurers could potentially be covered by the insolvency protection under the UM endorsement. We had interpreted the words "loss to claimants" and "average annual claimant losses," which appear in conjunction with the NAIC loss estimates (e.g., page 21, line 28; p. 181, line 44) to refer to third party losses. However, we are now informed that the term "claimant" means a claimant against the receiver. Accordingly, in addition to third party liability claims by individuals a number of other types of claims would be included in the figures receivers furnished the NAIC, such as, (a) collision and comprehensive claims by policyholders, (b) subrogation claims by other insurance companies for collision losses they have paid their insured, (c) claims for return premiums from policyholders and (d) claims by reinsurers for premiums due under reinsurance contracts.

The foregoing information regarding the broader definition of "claimant loss", requires a complete reevaluation, of course, not only of the manner in which UM insolvency protection affects the impact of insolvencies but, in addition, the entire question of on whom the impact falls. Accordingly, we respectfully request that the Committee add the material in this section IV to its records in correction of our previous testimony regarding insolvency protection under the Uninsured Motorist endorsement and in further examination of the subject. If the Committee should desire, we will be glad to return to testify on these matters.

Without a field study of the files of a representative sample of claims in liquidation, there is no way to tell what proportion of the claims before liquidators are from third party claims, from first party coverage on policyholders, for subrogation claims by other insurance companies, for reinsurance premiums due other insurance companies, for return premium to policyholders of the insolvent companies. It would be very helpful if such a study could be undertaken either by this Committee or by the National Association of Insurance Commissioners.

Meanwhile, it is apparent that something less than the total of $5,000,000 to $6,000,000 per annum of insolvency loss is loss to third party claimants; probably substantially less. We should then examine the nature of the other categories of claims, assess their impact on the public and assess the impact of S–2236 on such other claims.

First, regarding claims for return premiums, all solutions proposed to date to the insolvency problem make some acknowledgement of the fact that loss of return premium, although an unfortunate consequence of insolvency, is not of a catastrophic nature which demand a legislative solution. The loss of return premium is not, socially speaking, much different from the loss of any debt or account when a non-insurance firm goes bankrupt. In fact, the loss of return premium may have less impact on most people than would the average bankruptcy loss of an account or merchandise receivable. Thus, in some of the state insolvency plans deductibles are imposed, e.g., Wisconsin with a $200 deductible. In others, loss of premium is excluded from the plan, e.g., California and Michigan. Even under S–2236, only one-half of the premium lost is an allowable claim, so the sponsors obviously do not consider it a serious social problem either!

Second, the part of the "net loss to claimants" represented by subrogation claims of other insurers places no burden on individual policyholders or claimants. The inability of an insurance company to obtain a subrogation recovery against an insolvent insurer constitutes no social problem justifying the creation of an insolvency guaranty fund. The same is true of inability of a reinsurance company to collect premiums due it from the insolvent carrier.

Collision and medical payments claims are more serious than the two previous items. However, even with respect to these claims, the individual may ultimately be reimbursed for his loss by a tort feasor.

The remaining claims are liability claims. We contend that UM with insolvency protection has the potential of reducing the impact of this problem on individuals by 80%. In saying this, we have considered the following points:

1. UM coverage with insolvency protection is now available in all states.
2. All but two of the 50 states now require by law that the UM endorsement be added to all auto policies. These two states have insolvency funds. Some states allow the policyholder to reject UM coverage and some do not. Even in those states where the policyholder may reject it, over 90% of the motorists carrying liability insurance carry the UM endorsement.[1]
3. Most BI liability losses are within the limits of UM coverage.[2]
4. Six states now require that UM coverage also apply to property damage liability claims, with deductibles from $100 to $300 being specified. However, since collision insurance may be carried as a voluntary coverage, and a substantial majority do carry collision, no policyholder need rely on either the solvency or liability of a third party and the third party's, insurer to avert major loss from vehicle collisions.
5. With regard to pedestrians who do not own (or whose families do not own) a car, we believe the number of such cases is relatively small, but we have proposed "gap-closer" legislation which would give such claimants priority over insurance companies' subrogation claims, thus reserving sufficient funds to pay most pedestrians in spite of insolvency of the insurer.

In summary, the proportion of uncompensated loss to automobile accident third-party claimants due to insurer insolvencies, which cannot be compensated for under UM coverage with insolvency protection, is very small. With respect to BI liability, it is something less than 7.8% of such loss (that portion of the loss in excess of the UM limits) and will further diminish as higher UM limits

---

[1] We have calculated the percentage carrying UM coverage from NAII statistical data on 1967 Calendar Year Earned Car Years. In states where the UM law with right of rejection has been in effect a sufficient length of time so that all policies have been renewed at least once since the law's effective date, the figures indicated 91.26% of the cars insured carried the UM coverage. The states used in the calculation were Alabama, Arkansas, Florida, Georgia, Hawaii, Louisiana, Michigan, Nebraska, North Carolina, Ohio, Pennsylvania, Rhode Island and Wisconsin.

[2] Per NAII records, which include over half of the automobile insurance written in the United States, 92.2% of BI losses incurred are on the basic limits portion of the coverage. "Basic limits" is here defined as $10,000/$20,000. The statistics used are the NAII compilation of 1966 Accident-Year, Countrywide Automobile BI Liability Experience, developed through March 31, 1968.

Uninsured Motorists limits on average somewhat exceed $10,000/$20,000. Minimum UM coverage is never lower than the Financial Responsibility limit, which is constantly being raised by the various states. State trends, including voluntary programs by some companies to offer higher UM limits, make it appear that UM limits will soon be written for amounts which average well in excess of Financial Responsibility Law limits.

become available. With regard to property damage liability, the insolvency of the third party's carrier can be ameliorated by carrying collision insurance. Most car owners do, in fact, carry collision insurance. This is especially true of newer, more valuable cars, as most of them are financed. Other gaps in protection are very small. Overall, we believe it a reasonable estimate that at least 80% of the third party claimant insolvency loss problem can be solved by UM coverage.

V.

In answer to your question #3, there is no coding of loss data reported by insurance companies to either governmental agencies or to the insurance industry's statistical agents which would segregate UM losses on account of insurers' insolvencies from other UM losses. Accordingly, there is no practical way to obtain this data on a segregated basis.

However. the administrative cost factors and the actual loss factors for the UM endorsement as a whole, as requested in question #3 (3), are available. The NAII statistical service reports for 1966, the last available year with reasonably matured UM loss figures, that the loss ratio for uninsured motorist coverage was 70.8%. The remainder of the premium, 29.2%, would be what the public paid over and above losses to operate the protection system under the UM endorsement. Standard economic theory and accounting practice would call for the application of the 29.2% cost of premiums attributable to the insolvency protection as well as other parts of the undivided-premium UM endorsement package. In fact, there is no reason to assume any difference in normal insurance company expense items, such as commission, taxes, salaries and employee benefits, rent and building operating expenses, fees, accounting, loss experience compilation, equipment, policy issuance, underwriting reports and surveys. There might be some variation in the expense factors regarding claims handling, but which way the factor would vary is not clear. Chances are that if the matter were subjected to cost analysis, the variation of insolvency protection from the overall UM total cost factors would not be great. Accordingly, it seems reasonable to estimate the cost of providing insolvency protection under the UM coverage by applying the approximate figure developed on an overall basis. On this basis, the administrative cost of handling three million dollars in insolvency losses (if that should happen to be the BI component of the five million dollar figure developed by the NAIC, after deducting other types of claims against receivers—see our section IV.) would amount to only $1,280,000. This is, indeed, a modest figure in comparison with even the proponents' estimates of the costs of administering the FIGC.

Net direct earned premiums on UM coverage reported to the NAII statistical service for the aforementioned 1966 year were $64,728,200 and losses incurred were $49,238,598. Unfortunately, the compilation of "written premiums," which you requested, is not ready in time to include with this letter. We will send it to you in a few days.

Information supplied to us by Mr. Edward W. Dippold, Vice President, American Arbitration Association shows that payments to the AAA for UM arbitration were, for the year 1967, $997,027 paid by insurance companies plus $283,630 filing fees paid by claimants. During that year, 8,621 cases were filed for arbitration with the AAA. From the standpoint of the cost to society of operating the adjudicatory process, this appears to be much less costly per case than the alternative of putting UM claims through the courts. It is also a small figure compared to the total UM premiums shown in previous paragraphs. Again, please bear in mind that the foregoing cases involve very few matters under insolvency protection but, rather, they include all UM coverage arbitrations. Only a small percentage of UM cases are arbitrated and proportionately even fewer cases involving insolvency protection probably reach arbitration.

We hope you will find this letter a complete response to your questions at the hearing and your letter of December 9, and that you will place it in the Committee's records. However, if we can furnish further information, please let me know.

Respectfully submitted.

VESTAL LEMMON, *President.*

Senator HART. Our next witness is the president of the Insurance Co. of North America, Mr. Charles K. Cox.

STATEMENT OF CHARLES K. COX, PRESIDENT, INSURANCE CO. OF NORTH AMERICA; ACCOMPANIED BY EDMOND RONDEPIERRE, ASSISTANT GENERAL COUNSEL, INSURANCE CO. OF NORTH AMERICA, PHILADELPHIA; AND THOMAS CLARK MATTHEWS, JR., WASHINGTON COUNSEL

Mr. Cox. Senator Hart, and gentlemen: I am president of Insurance Co. of North America. INA is one of the largest underwriters of property and casualty insurance, writing substantially all lines of insurance throughout the United States, and in many foreign countries. We are also one of the principal domestic reinsurers, affording reinsurance facilities to a broad clientele including some of the largest and some of the smallest primary insurance companies in the country.

INA is vitally interested in matters affecting the insuring public, and the integrity of our industry. The continued existence of a private enterprise insurance industry is dependent upon a very high degree of public confidence in the ability of insurance companies to meet their obligations.

I welcome this opportunity to express my views on Senate bill 2236 which bears directly on that subject.

INA shares your committee's concern about injury to the insuring public resulting from insolvency of insurance companies. As licensed insurers, we operate within an extensive system of regulation which has this aspect of public protection as one of its primary purposes. I believe that no legislation, and no reasonable system of regulation, whether State or Federal, can be devised to absolutely eliminate the possibility of insurer insolvencies. It would surely not be in the public interest to devise a system affording easy entry into the insurance market, and also assuring that no matter how inefficient, how badly managed, or how misused, no such company should ever fail.

I am certainly not saying we are in favor of easy entrance. We are very much in favor of improving standards for entrance into the insurance industry.

As with other private industries, the risk of failure exerts a healthy influence on management. We would not support an effort to eliminate that risk. However, we do support the effort to prevent injury to the insuring public resulting from such failures.

Under ordinary business practices, and under the present system of State regulation, the great majority of impending failures are detected in sufficient time to rehabilitate the company or to wind up its affairs in an orderly fashion. There remains, however, the possibility that an insurance company may reach insolvency in such a way that policyholders or claimants are left with unsatisfied claims. In this latter case, INA shares the view of the sponsors of this bill that there is a need to make available to the insuring public a means of protecting itself against such unsatisfied claims.

There are a number of ways in which such protection could be afforded.

It is possible to devise insurance contracts which protect the policyholder against such loss. Under such contracts, the policyholder looks to the insurer of his choice to protect him against the possibility of an uncollectable claim against an insolvent company. A present ex-

ample of this farm of protection exists in the insolvency provisions of the uninsured motorist coverage.

It is legally permissible for private reinsurers to issue reinsurance contracts which would respond notwithstanding insolvency of the primary company, or which would respond for the full obligation of the primary company in the event of insolvency.

And as a matter of fact, those contracts are in existence.

It would be possible for insurers to establish a common fund which would respond in the event of insolvency of any of the participants.

It would be possible for States to establish either voluntary or compulsory funds, financed by company contributions or through the taxing authority, and which would respond in the event of insolvency of any participating company.

It would be possible for the Federal Government to establish either a voluntary or a compulsory fund, financed by company assessment or through taxing authority, and which would respond in the event of insolvency of any participating company.

By its very nature, the circumstance which causes the Federal Government to consider legislation in this area is the exception rather than the rule. In order for this type of public injury to occur, there must first be a failure of the ordinary management process within the company, and there must also be a failure of the State regulatory system to detect the potential insolvency and to exercise its statutory responsibilities to rehabilitate, or, if necessary, to liquidate the company. I do not minimize the damage suffered by those who are caught by such a contingency, or the need for protection against such damage. I do want to emphasize that it is a contingency with which we are dealing, and the corrective mechanism adopted should be one appropriate to the contingent nature of the problem.

It is my firm belief that private industry can and does provide very substantial protection to the public against financial loss resulting from insurance company insolvencies. It does so in several ways; for example, by managing its own business so as to minimize the possibility of insolvency. The industry also provides uninsured motorist coverage as part of every standard policy so that each solvent company protects its policyholders against insolvencies of other companies.

In addition, INA and other professional reinsurers also provide the public with a real measure of protection with their continual surveillance of the companies they reinsure.

The industry should be encouraged to continue to make every effort to protect the public against insolvencies, and to expand such protection where possible. It is also my belief that the existing system of State regulation affords substantial protection to the public against injury resulting from insolvencies; California, for example, has an outstanding record in this field. There are some others.

A Federal program for the protection of the public would be desirable if it were structured in such a way as to reflect the contingent nature of the problem and to permit full effectiveness of private and State protective systems. While I am completely sympathetic toward the approach set forth in S. 2236, in its present form, I would like to discuss several alternatives which I believe would better achieve these objectives.

I propose that a postinsolvency assessment plan be substituted for the standing fund contemplated by the bill. Based on present premium volume, as I understand it, the standing fund would amount to approximately $500 million.

The accumulation of such a large fund is inconsistent with the contingent nature of the exposure. It would impose an immediate added cost to present policyholders to provide for the possible future indemnification of a different group of policyholders.

The existence of such a large fund would create substantial administrative expense—I do not know the figure—and, quite frankly, it has been my observation that when a large fund lies idle in the hand of a government agency for any considerable period, it is likely to become the subject of new legislation to divert the fund to other more immediate uses.

I find the same thing in my own household.

To some extent, similar effects could materialize under a post-insolvency assessment program; however, they are much less likely.

A post-insolvency assessment is consistent with the contingent nature of the exposure, and is also compatible with the operations of the industry. By their nature, these companies are in the business of assuming obligations to respond in money indemnification upon the happening of some future contingency.

The second fundamental change which I have proposed is that the Federal fund should not be universally compulsory. As I have previously stated, there are a number of devices which the industry could employ to afford protection against insolvency, and there are a number of programs which could be adopted at the State level. Accordingly, I am proposing alternatives under which every company would be required to be a member of some insolvency protection program acceptable to the Federal regulatory authority. These programs might take the form of reinsurance contracts, or voluntary pools, or State pools. This provision would permit maximum utilization of private resources to provide this protection, and would allow for future expansion of private capabilities in this area. The use of voluntary pools would also bring to bear, to the public benefit, the special capability of professional insurers to detect potential insolvency situations at a very early stage; and professional reinsurers, too.

As under the present S. 2236, participation in the Federal program would exempt a company from participation in a State program. Companies could therefore elect to provide this protection through participation in voluntary pools, purchase of special reinsurance, participation in State pools, or participation in the Federal program.

It might be argued that such an option would result in the gravitation of those companies most likely to face insolvency to the Federal program. If that should be true, I do not see that it is a disadvantage. On the contrary, if a system could be devised under which those companies most likely to face insolvency could be identified and compelled to obtain insolvency protection, there would be no need to impose the system on all companies. Indeed, I assume that the Federal regulatory official charged with administration of the program would adopt standards which would enable him to identify those companies requiring the greatest scrutiny and to avoid needless examination of those clearly meeting the standard. On the other hand,

identification of a company as a participant in the Federal plan might become such a substantial market advantage that all companies would seek to be so identified.

The third substantial change which I propose is that the Federal fund be constructed as a "last resort" fund, to be utilized only after all private sources and all available State funds have been exhausted. Again, this would be appropriate to the contingent nature of the exposure, and would encourage maximum expansion of private industry capacity to provide this coverage.

It is my understanding that one provision of S. 2236 would have the effect of preempting any private insolvency protection, and that the provision was included to prevent an undesirable effect of subrogation under the present uninsured motorist coverage. Specifically, if one automobile policyholder has a valid claim against another, but is unable to collect because the other driver's insurance company is insolvent, the policyholder is paid by his own company. The company making the payment is subrogated to the claim of its policyholder against the other driver. As it pursues this claim, the driver who was insured in the company which became insolvent is left without protection. This is, of course, one kind of injury which you and we are seeking to prevent.

There are several possible ways of dealing with this problem. One would be to eliminate the right of subrogation. This, however, presents inconsistencies in matters of principle, as when the negligent driver was underinsured, or self-insured, or simply uninsured.

I currently have under study a proposal which I believe may offer a more satisfactory solution. Under this proposal the company providing the insolvency protection would condition its right of subrogation by agreeing to accept an assignment of the defendant's claim against his insolvent insurance company, whether collectable or not. This would prevent injury to the policyholder arising out of the insolvency of his insurance company without affecting the right of subrogation against a defendant who had elected to be self-insured.

The insolvency protection afforded by uninsured motorist coverage is one example of the ability of the industry to deal with this problem. There are other private methods which do exist or which could be developed. I feel that Federal legislation should encourage maximum utilization of these capabilities.

In summary, I concur with the sponsors of Senate bill 2236 that there is a need to provide the insuring public with a means of protecting itself against the contingency of insurance company insolvency, and I believe there is a vital role to be played by the Federal Government in this area. With the changes I have proposed, I would support the bill.

I thank the committee for this opportunity.

Senator HART. Thank you, Mr. Cox, for a very thoughtful and constructive statement. The notion that the risk of failure has a healthy influence on management, I am sure is true.

Mr. COX. It is, indeed.

Senator HART. Would you agree that at least the one feature of this guarantee bill that we are considering, that provision which enables the Commission to put a poorly managed company out of business even before if folds by revoking the guarantee status, would provide an incentive for good management, too?

Mr. Cox. Yes; I think I would agree with that, Senator. I think that the companies that would be affected most would not be the poorly managed, because the poorly managed normally find some solution; it may be merging with another company or selling out. It is the dishonestly managed that we would be concerned with here.

Senator HART. Would the provision in the bill which makes directors of insolvent companies personally liable for gross mismanagement have a constructive influence?

Mr. Cox. It certainly should.

Senator HART. Do you have any figures that would help us on this question of how much of the present insolvency loss is picked up by the standard uninsured motorist endorsement?

Mr. Cox. I am sorry, Senator, I do not.

Senator HART. Would it be possible to get it?

Mr. Cox. We will do our very best to get it for your committee.

Senator HART. If you are able to do it, it will be received in the record.

(The information requested follows:)

INSURANCE CO. OF NORTH AMERICA,
Philadelphia, Pa., December 2, 1969.

Hon. WARREN G. MAGNUSON,
Chairman, Committee on Commerce,
U.S. Senate,
Washington, D.C.

DEAR SENATOR MAGNUSON: In the course of my November 12 appearance before your committee, Senator Hart asked if we could develop answers for two questions. The questions and our answers are as follows:

1. Is it possible to determine the proportion of insolvency losses in the country which are covered by the insolvency provisions of the uninsured motorist coverage?

It is not possible to answer this question from statistical sources. It would first be necessary to know the actual amount of automobile liability claims against insolvent companies, and then the amount paid under uninsured motorist coverage. These factors could be determined only by interviewing claimants and only after sufficient time had elapsed to complete liquidation of the companies and resolution of the outstanding tort claims. The coverage has not been in existence long enough to develop significant information at this time even by the interview method.

As an alternative, I have inquired into the feasibility of determining what proportion of all uninsured motorist losses represent insolvency claims. I find that this is not available through statistical sources, and that no provision is being made for statistical coding of such losses in the future. The reason is that the total cost of uninsured motorist coverage averages approximately $4 to $5, and the highest cost anywhere is approximately $12. With a premium so small, it is not economically feasible to code and classify separate kinds of losses. Losses attributable to insolvency are expected to be a very small part of all losses paid under uninsured motorist coverage, and would therefore account for a proportionately small part of the total uninsured motorist premium. Again, the coverage is too new to permit development of significant data even through the interview method.

2. What provision is made under uninsured motorist coverage to reimburse the policyholder who must retain counsel to prosecute his claim against his own company?

None. Claims submitted under uninsured motorist coverage are handled as a third party claim would ordinarily be handled, and, as you probably know, more than 95% of these claims are settled without litigation. In the vast majority of cases, the policyholder will recover these claims without retaining counsel. In those cases where the issues of liability or damages are in dispute, and settlement cannot be negotiated, the policyholder will be required to establish his claim as he would ordinarily do against the negligent party. If a state provided for recovery of costs of litigation against a negligent party, these costs would be included in

the uninsured motorist recovery. This expense is in no way related to the insolvency of the other party's insurer, and the problem is in no way related to the insolvency problem.

You also extended an invitation to comment on questions which were addressed to other witnesses, and I would like to offer such a comment.

At several points, a question was asked substantially as follows: If open-competition rating laws were widely adopted, would it not be essential to provide insolvency protection to protect those policyholders and claimants of companies which fail under increased competition? As I stated in my prepared testimony, I believe there is a need for a system through which the insuring public can protect themselves against loss due to insolvency of an insurer, even at the present rate of insolvencies, or for that matter at a rate of insolvencies less than we presently contemplate. The question implies, however, that the increased competition which may be expected under an open-competition type rating law will produce a greater number of insolvencies. I do not agree with this implication. It is quite possible that increased competition will bring about the economic failure of inefficient companies, however, it does not follow that these failures will materialize in the form of insolvencies, leaving unpaid policyholders and claimants.

In my opinion, quite the contrary is true. INA has long advocated a form of regulation which would minimize the emphasis on statistical justification and prior approval of rates and which would concentrate the regulatory effort on oversight of actual market practices and examination of companies for solvency. The prior approval system is both wasteful and inefficient. If it is not accompanied by effective oversight of market practices and examination of companies, it is virtually meaningless. If the oversight and examination functions are in fact effective, the prior approval procedures are redundant.

The prior approval form of rate regulation, placing extreme emphasis on statistical experience, and precluding companies from charging rates which they believe to be adequate, creates underwriting restrictions and shortage of market, which in turn produce insurers specializing in "substandard" risks, and marginal companies. The risks written by such companies are "substandard" only because the normal market was precluded from charging a rate at which they would be willing to write such risks (although that rate may have been lower than that charged by the substandard specialists).

Wide adoption of a California type rating law would not increase the incidence of insolvencies and, by permitting the normal market to absorb a wider range of risks, would minimize the formation of the marginal type of company which is most likely to become insolvent.

Thank you again for the opportunity to present my views to your committee.

Very truly yours,

CHARLES K. COX,
President.

Senator HART. Is it fair, oversimplifying it, to say that you—I am not sure it is fair to ask a witness if any oversimplified statement is a fair statement—are you suggesting a voluntary membership in the guarantee fund, or at least some type of alternative coverage which is acceptable to the fund?

Mr. COX. I am suggesting that the Federal Government establish standards which, if met, would enable the statutory requirements to be fulfilled.

Sentator HART. Whether that would involve the creation of a guaranty corporation or not?

Mr. COX. The guarantee corporation would be in existence but not all companies would be required to belong to it or participate in it.

Senator HART. Presumably, the company that was not required to participate would be sound and hence in less need of the kind of expert assistance which some of us visualize the guaranty corporation able to provide. At least there might be, assuming the validity of the notion of the expert pool being available, a less satisfactory dollar return on the investment in establishing the corporation if that skill in the pool were not available except to those who were required to participate?

Mr. Cox. I would not think it would be less satisfactory. I would think it would enable the Federal regulator to concentrate his attention on these companies that needed it.

Senator HART. The committee would welcome any suggestions you have for solving or responding to some of the other problems that are connected with this uninsured motorist endorsement, such as the need to hire your own lawyer sometimes to prosecute your claims against your own company. Any cure for that problem?

Mr. Cox. I would like to have the opportunity to submit an amplification of our views on the subject.[1]

Senator HART. We would welcome it.

Thank you very much again for your thoughtful testimony.

We now return to the witness who was kind enough to step aside for a minute to hear the out-of-town witnesses: the vice president of the American Mutual Insurance Alliance, Mr. Andre Maisonpierre.

STATEMENT OF ANDRE MAISONPIERRE, VICE PRESIDENT, AMERICAN MUTUAL INSURANCE ALLIANCE, WASHINGTON, D.C.

Mr. MAISONPIERRE. Thank you, Mr. Chairman.

Mr. Chairman, I would like the opportunity of reading our statement. It is a brief statement. Attached to our statements there are a member of appendixes——

Senator HART. Which will be ordered printed in full.

Mr. MAISONPIERRE. My name is Andre Maisonpierre, and I am a vice president of the American Mutual Insurance Alliance, a voluntary association of more than 100 mutual property and casualty insurance companies writing insurance in all 50 States and the District of Columbia (app. A). Our companies write in excess of $2.8 billion in insurance in the lines which would be covered by S. 2236.

We very much appreciate the opportunity of expressing our views on S. 2236. Although we share the concern which the bill sponsors have regarding the effects of insurance company insolvencies, we oppose the bill as unnecessary and inappropriate to the problem it purports to resolve.

INTRODUCTION

S. 2236 approaches the insurance company insolvency problem on the assumption that neither the State insurance regulators, legislatures, nor companies have acted to mitigate this problem. The fact is that a great deal has been done in the past. Recent developments complement that which has been done in the past, and an entirely new program, such as S. 2236, is unnecessary.

STATE ACTIONS RELATED TO INSURANCE COMPANY INSOLVENCIES

We believe that States have acted, and are acting, forcefully to prevent insolvencies through stronger regulatory controls and authority, increased capital and surplus requirements, and increased jurisdiction over the operations of holding companies and unauthorized insurers. State insurance departments continue to develop methods

[1] See letter on p. 66.

to detect potential failures due to incompetent management, and to plug the loopholes through which unscrupulous operators have occasionally succeeded in infiltrating the business.

Realizing that some failures will occur, the industry and State regulators have acted to protect the insurance-buying public from the consequences of these few inevitable insolvencies.

UNINSURED MOTORIST COVERAGE

Over the past 4 years, through legislation and voluntary action on the part of the insurance industry, a contractual form of insolvency protection has been made available to auto insurance purchasers in all jurisdictions. This was accomplished by extending the uninsured motorist provision, already incorporated in most automobile liability policies, to include coverage against insolvencies. More than 90 percent of the automobile liability insurance policies in effect today provide this protection.

The insolvency coverage operates in this manner: An insured driver is injured by a negligent motorist. The negligent motorist's insurance company becomes insolvent and is unable to pay the liability claim. At that point, the injured person's own insurance company takes the place of the insolvent insurer and pays its own policyholder for his injury, up to the limits of the State's financial responsibility law.

The Alliance, and other major segments of the industry, are continuing our efforts to make certain that this protection be automatically provided to all insured motorists.

Since 1966, the Alliance has sought publicly to have legislation enacted in every State which would require that every auto liability policy sold in the State contain insolvency coverage. To date, 34 States have enacted such legislation (app. B).

In the meantime, since January 1967, both the stock and mutual rating bureaus have voluntarily added the insolvency coverage to their filings on behalf of member and subscriber companies. Most major nonbureau companies likewise include the coverage voluntarily, even in those States where it is not required by law.

In order to make this approach even more effective, the Alliance is seeking legislation in every State which would prohibit uninsured motorist carriers from subrogating against the remaining assets of the insolvent company. This would conserve the funds of the insolvent company for the benefit of persons who do not have available the uninsured motorist coverage, and to pay the company's other obligations.

We also advocate that such legislation prohibit subrogation against the policyholders of an insolvent carrier. As a practical matter, the right of subrogation against the insolvent company's policyholders is seldom exercised anyway, because the possibility of making significant recoveries by this method is minimal.

The position of the Alliance parallels that of the National Association of Insurance Commissioners, which encourages the enactment of uninsured motorist coverage legislation with insolvency protection and without right of subrogation against the estate of an insolvent carrier or its insured.

STATES' POST-INSOLVENCY ASSESSMENT PLANS

While continuing our efforts to stimulate the enactment of legislation providing for mandatory uninsured motorist coverage with insolvency protection, the Alliance recognizes that the economic consequence of insurance company insolvency affects a broader spectrum of American citizens than just those purchasing automobile insurance. Accordingly, the Alliance proposed and supported legislation designed to extend protection to non-car-owning pedestrians, to property insurance policyholders, and to all claimants and insureds of insolvent property and casualty insurers.

Our proposal calls for the enactment at the State level of legislation creating an insolvency program in which all licensed carriers in that State are required to participate.

If an insolvency occurs, these carriers, through an assessment, provide funds out of which claimants and policyholders of the insolvent carrier are compensated. A model bill (app. C) was drafted and, in the few months remaining in State legislative sessions in 1969, this type of legislation was enacted in New Hampshire, California, Michigan and Wisconsin.

The States of New York, New Jersey and Maryland already had enacted insolvency fund legislation in prior years. (See app. D.) We believe these plans can be enacted in other States within a reasonable period.

These programs, called "postinsolvency assessment plans," close those gaps which may remain to protect the public from insurance company insolvency problems. Some 26 State legislatures will be in session in 1970, and nearly all States will be in session in 1971. Contact with State insurance regulators, State legislators and other State officials indicates a growing interest in the enactment of postinsolvency assessment funds. If the States do take action within a reasonable period, as we believe they will, there is no need for a Federal Insurance Guaranty Corporation.

S. 2236 WOULD REPLACE STATE REGULATION OF INSURANCE BY FEDERAL REGULATION

The Alliance's major objection to S. 2236 is that it would ultimately replace State regulation of insurance by Federal regulation. As the bill clearly indicates, the fund's governing board is given the responsibility to insure company solvency through strict regulation. The primary function of insurance regulation is to insure that the companies will remain solvent without, at the same, taking advantage of the public which it serves. Thus, it is axiomatic that whoever regulates for solvency also regulates the total insurance industry.

As we have already indicated, we do not claim that State insurance regulation is perfect. However, the advocates of Federal regulation of insurance tend to compare the defects of State regulation with a hypothetical Federal regulatory system which, we know from experience, is not attainable. There is nothing in the history of the Federal regulatory system to install any confidence that Federal regulation of insurance will be, on the whole, more efficient than the present State regulatory system. The fact is that recent serious criticism of a number of Federal regulatory agencies would seem to confirm our fear of

having the regulatory authority over the insurance industry pass from the State to the Federal Government.

In the meantime, S. 2236 would impose upon the industry dual regulation—State and Federal—with all of its conflicting pressures, demands, and irrational decisions.

S. 2236 would require the establishment of a vast Federal bureaucracy, which would duplicate the efforts of State administrative agencies. Such duplication would not only be wasteful in the huge amount of dollars expended, but would also be extremely detrimental from the viewpoint of the misuse of manpower.

Competition between the States and the Federal agency for trained personnel would be inevitable. State insurance departments might be deprived of experienced manpower during the establishment of a sufficiently strong Federal bureaucracy to oversee the industry. The resulting vacuum would encourage unscrupulous management manipulations by those who operate best in such a regulatory vacuum.

Frankly, there is no way to create a Federal Insurance Guaranty Corporation without providing strong regulatory powers to the corporation management. Historically, the involvement of Federal funds in a project or a program has irresistably led to increased Federal involvement in the regulation of that project or program. Thus, your committee should recognize that approval of this legislation will transfer the authority to regulate insurance from the States to the Federal Government.

S. 2236 WOULD UNNECESSARILY TAX CONSUMERS

In addition, there are other objections to S. 2236. Although section 10(b) provides that assessments on the companies will cease once the fund has reached 2 percent of assessable premiums, our projections indicate that this 2 percent will never be reached.

We estimate a conservative premium growth at a compound rate of 9 percent per year annually.

Applying the required tax of one-eighth of 1 percent of premiums collected, the gap between the collected funds and the 2 percent maximum lid would widen every year. Thus, the statutory shutoff point would never be reached, and the public through the companies, would forever have to bear such a tax. (See app. E.)

This situation is very analogous to that of the Federal Deposit Insurance Corporation. It has been suggested, in fact, that the Federal Insurance Guaranty Corporation would play a similar role toward the insurance industry as the Federal Deposit Insurance Corporation plays toward the banking business. Without detracting from the fact that the FDIC has given stability to the banking industry, it has been an extremely expensive operation from the standpoint of the American public. The fact is that, since its inception, the FDIC has collected upward of $4 billion from the American consumer, while paying out $55 million in net losses.

For every dollar which the FDIC has paid to the public because of bank insolvencies, it has collected $76. In addition, it has cost over $5 in administrative expenses alone to return each dollar in loss to the public.

Just in 1968 the FDIC collected from the American consumer close to $300 million. It paid out slightly less than $1.5 million in net losses,

but spent $29 million—almost 20 times the net amount of losses—to administer the program.

As was recently repoted in a Journal of Commerce article, "It (FDIC) has done an excellent job maintaining confidence in banks, especially small banks. It is being overpaid, which is another way of saying that it is too expensive, based upon its own figures." There is every reason to believe that whatever public confidence would be purchased through a Federal Insurance Guaranty Corporation, it would be purchased at a very heavy price. (See app. F.)

STATE INSOLVENCY PLANS ARE MORE EFFICIENT THAN S. 2236

It has been claimed that the establishment of a single fund would be much more efficient than the establishment of 50 separate insolvency plans. If efficiency is to be measured by cost, we question the validity of this argument.

It has been estimated that the cost of managing a Federal Insurance Guaranty Corporation would be upward of $36 million. When compared to the administrative expense of the FDIC, we believe this to be a conservative figure.

On the other hand, the cost of operating State post-insolvency assessment plans is negligible, since they call for no additional administrative personnel, and do not become active until after an insolvency has taken place, thereby avoiding the administrative costs necessary to maintain a program which may never be used.

We believe that State plans are more efficient, if judged by the criteria of public convenience. Any member of the public will have to deal with only one plan—the one located in his State—under the supervision of his State insurance regulator.

Far more confusing to the individual would be the labyrinth of local, State and regional agencies between himself and a Federal corporation. In truth, one program might be operationally more convenient for the insurance industry, but the purpose of such plans is to serve the public, and not the insurance companies.

If efficiency is to be measured by concern over dislocation, then again, State plans must be judged considerably more efficient than a Federal Insurance Guaranty Corporation. State plans fit directly into the present regulatory pattern. The Federal Insurance Guaranty Corporation, on the other hand, will totally disrupt such a regulatory pattern.

Finally, an efficient insolvency plan should provide incentives for sound financial supervision of insurers. Post-insolvency assessment plans do this by giving legitimate insurance companies a financial incentive to assist State regulators in identifying and dealing with the borderline operators.

State plans also put pressure on the State regulator to move in promptly and prevent insolvencies, since he will otherwise have to impose the consequences of his failure to do so on the suriving companies and on the policyholders of his State.

A Federal Insurance Guaranty Corporation, on the other hand, would create a powerful counterincentive to effective action on the part of State regulatory officials, and companies. States which have not taken effective action in the past to minimize insurer insolvencies, would be even less motivated to do so under a Federal insolvency plan.

This is true because insolvency losses in those States would be paid for by funds collected largely from the people of other States.

Instead of moving in promptly to deal with a company in questionable financial condition, there might be a tendency to procrastinate and avoid calling in the Federal Government, in the hope that somehow the crisis could be averted.

The inevitable tendency of such a system would be for the Federal administrators of the fund to make more and more aggressive use of the direct supervisory powers contemplated under S. 2236. The Federal agency, in order to protect the integrity of the fund it must administer, would feel impelled to encroach more and more into the legal and administrative functions of State regulatory officials.

The inevitable result, we believe, would be to superimpose Federal supervision of insurance on the existing pattern of State regulation. In short, the whole concept is detrimental to the overriding goal of promoting sound financial supervision, and destructive of the concept of federalism, as well.

Viewed from any point, we believe that State postinsolvency assessment plans provide a very efficient solution to closing any gaps in the insolvency problem which remain today.

CONCLUSION

In conclusion, we want to stress that the opposition of the American Mutual Insurance Alliance to S. 2236 is predicated upon the fact that the problems which it would attempt to solve are being solved right now at the State level. We do not believe that there is any justification for the imposition of Federal regulation on a business presently being adequately regulated by the States.

Our association pledges its continued effort toward the enactment of State postinsolvency assessment plan legislation aimed at closing the remaining gap in the insurance insolvency problem area. (See app. G.)

APPENDIX A

ALLIANCE MEMBERS

Abington Mutual Fire Insurance Company, Herbert I. Perry, President, 536 Washington Street, Abington, Massachusetts 02351.

Amalgamated Casualty Insurance Company, Charles F. Hoelzer, President, 405—4th Street, N.W., Washington, D.C. 20001.

American Hardware Mutual Insurance Company, R. S. Hanson, President, P.O. Box 435, Minneapolis, Minnesota 55440.

American Manufacturers Mutual Insurance Company, James S. Kemper, Jr., President, New York, New York, (Exec. Offices, 4750 Sheridan Rd., Chicago, Illinois 60640).

American Mutual Insurance Company of Boston, R. E. Roberson, President, Wakefield, Massachusetts 01880.

American Mutual Liability Insurance Company, R. E. Roberson, President, Wakefield, Massachusetts 01880.

American Mutual Reinsurance Company, Roy H. Heyen, President, One East Wacker Drive, Chicago, Illinois 60601.

Atlantic Mutual Fire Insurance Company of Savannah, Fred Wessels, Jr., President, P.O. Box 187, Savannah, Georgia 31402.

Attleboro Mutual Fire Insurance Company, R. Burton Forbes, President and Treasurer, P.O. Box 270, Attleboro, Massachusetts 02703.

Austin-St. Paul Mutual Insurance Company, M. E. Sugden, President, 84 South Sixth Street, Minneapolis, Minnesota 55402.

Automobile Mutual Insurance Company of America, De Forest W. Abel, Jr., President, P.O. Drawer 6008, Providence, Rhode Island 02904.
Bakers Mutual Insurance Company of New York, Peter G. Metz, President, 75 Maiden Lane, New York, New York 10038.
Barnstable County Mutual Fire Insurance Company, Irvin K. Besse, Vice President-Secretary, Hallet Street, Yarmouthport, Mass. 02675.
Brethren Mutual Insurance Company,[1] Paul D. Horst, President, 100 West Washington Street, Hagerstown, Maryland 21740.
California Mutual Insurance Company, Charles E. Bancroft, President, P.O. Box 1438, Ventura, California 93001.
Capitol County Mutual Fire Insurance Company, E. H. McDonald, President, P.O. Box 2328, Fort Worth, Texas 76101.
Central Mutual Insurance Company, F. W. Purmort, Jr., President, P.O. Box 351, Van Wert, Ohio 45891.
Chicago Mutual Liability Company, Herbert J. Choice, President, 2 North Riverside Plaza, Chicago, Illinois 60606.
Church Mutual Insurance Company, W. W. Schuster, President, 1004 First Street, Merrill, Wisconsin 54452.
Cincinnati Equitable Insurance Company, W. E. Hutcheson, Secretary-Treasurer, 6 East Fourth Street, Cincinnati, Ohio 45202.
Citizens Mutual Insurance Company, Peter C. Jacobs, President, P.O. Box 506, Janesville, Wisconsin 53545.
Citizens Security Mutual Insurance Company,[1] S. A. Broughton, President, Red Wing, Minnesota 55066.
Consolidated Mutual Insurance Company, Norman Lustig, President, 345 Adams Street, Brooklyn, New York 11201.
Dorchester Mutual Fire Insurance Company, John N. Tulley, President, P.O. Box 2044, Boston, Massachusetts 02106.
Druggists Mutual Insurance Company, V. M. Parsons, President, P.O. Box 370, Algona, Iowa 50511.
The Economical Mutual Insurance Company,[2] W. W. Foot, President & General Manager, Kitchener, Ontario, Canada.
Employers Mutual Casualty Company,[1] Robb B. Kelley, President, P.O. Box 712, Des Moines, Iowa 50303.
Employers Mutual Fire Insurance Company, J. M. Sweitzer, Chairman, 2000 Westwood Drive, Wausau, Wisconsin 54401.
Employers Mutual Liability Insurance Company, J. M. Sweitzer, Chairman, 2000 Westwood Drive, Wausau, Wisconsin 54401.
Exchange Mutual Insurance Company, J. R. Shaw, President, P.O. Box 1071, Buffalo, New York 14240.
Factory Mutual Liability Insurance Company of America, De Forest W. Abel, Jr., President, P.O. Drawer 6008, Providence, Rhode Island 02904.
Farm Bureau Mutual Insurance Company of Michigan, Nile L. Vermillion, Executive Vice President, 4000 North Grand River Avenue, Lansing. Michigan 48904.
Farmers Mutual Fire Association of West Virginia,[1] R. H. Hinzman, Secretary-Treasurer, P.O. Box 1467, Fairmont, West Virginia 26555.
Farmers Mutual Insurance Company, Walter J. Fayle, Secretary-Manager, P.O. Box 849, Santa Rosa, California 95402.
Federated Mutual Implement and Hardware Insurance Company, C. I. Buxton, II, Chairman of the Board & President, 129 East Broadway, Owatonna, Minnesota 55060.
Fitchburg Mutual Fire Insurance Company, W. Bruce Adams, President, 781 Main Street, Fitchburg, Massachusetts 01420.
Florists' Mutual Insurance Company, Olin A. Wetzel, President, P.O. Box 428, Edwardsville, Illinois 62025.
Gore Mutual Insurance Company,[2] Duncan McIntosh, Vice President and Managing Director, Galt, Ontario, Canada.
Grain Dealers Mutual Insurance Company, Howard M. Betts, President, 1752 North Meridian Street, Indianapolis, Indiana 46202.
Granite Mutual Insurance Company, Arthur H. Sprague, President, P.O. Box 460, Barre, Vermont 05641.
Greater New York Mutual Insurance Company, Alexander E. Rosenthal, President, 770 Broadway, New York, New York 10003.
The Hamilton Mutual Insurance Company of Cincinnai, Ohio, Richard E. Felts, President, 1520 Madison Road at Victory Parkway, Cincinnati, Ohio 45206.

Footnotes at end of Appendix A.

Hardware Dealers Mutual Fire Insurance Company, John W. Joanis, President, 1421 Strongs Avenue, Stevens Point, Wis. 54481.
Hardware Mutual Casualty Company, John W. Joanis, President, 1421 Strongs Avenue, Stevens Point, Wis. 54481.
Hardware Mutual Insurance Company of the Carolinas, Ralph N. Farmer, President, P.O. Box 2008, Charlotte, N.C. 28201.
Hingham Mutual Fire Insurance Company, Thomas Bates, Chairman of Board, 49 Main Street, Hingham, Massachusetts 02043.
Holyoke Mutual Fire Insurance Company, Raymond B. Morrison, President, 39 Norman Street, Salem, Massachusetts 01970.
Ideal Mutual Insurance Company,[1] E. P. Lalley, President, 261 Madison Avenue, New York, New York 10016.
Indiana Lumbermens Mutual Insurance Company, Norman M. Newberg, President, P.O. Box 1985, Indianapolis, Indiana 46206.
Indiana Union Mutual Insurance Company, Charles T. Coats, President, 3190 North Meredian Street, Indianapolis, Indiana 46207.
Interboro Mutual Indemnity Insurance Company, E. A. Cook, President, P.O. Box 229, Mineola, New York 11501.
Industries Mutual Insurance Company,[1] T. Merkert, Manager-Treasurer, 507 South 72nd Street, Omaha, Nebraska 68114.
Iowa Kemper Mutual Insurance Company, Edward C. Jones, President, P.O. Box 551, Mason City, Iowa 50402.
Iowa Mutual Tornado Insurance Company, W. M. Treimer, President, P.O. Box 1336, Des Moines, Iowa 50305.
Iowa National Mutual Insurance Company, J. C. Rice, President, P.O. Box 111, Grand Rapids, Iowa 52406.
Jamestown Mutual Insurance Company, John H. Carr, President, P.O. Box 880, Jamestown ,New York 14701.
Jewelers Mutual Insurance Company, I. W. Anderson, Secretary-Treasurer, 104 East Wisconsin Avenue, Neenah, Wisconsin 54956.
Kyoei Mutual Fire and Marine Insurance Company,[2] Shotaro Ochiai, Manager, General Planning Department 3, 1-Chome Shiba-Tamura-Cho Minato-Ku, Tokyo, Japan.
Liberty Mutual Fire Insurance Company, Frank L. Farwell, President, 175 Berkeley Street, Boston, Massachusetts 02117.
Los Angeles Mutual Insurance Company, James L. Belsha, President, 610 South Broadway, Los Angeles, Calif. 90014.
The Lumber Mutual Fire Insurance Company of Boston Massachusetts, D. L. Rollins, President, 575 Technology Square, Cambridge, Massachusetts 02139.
Lumbermens Mutual Casualty Company, James S. Kemper, Jr., President, 4750 Sheridan Road, Chicago, Illinois 60640.
The Lumbermens Mutual Insurance Company, Dale G. Roth, Vice President and Secretary, P.O. Box 459, Mansfield, Ohio 44901.
Lutheran Mutual Fire Insurance Company, Fred C. Schmitt, Secretary, 77 West Washington Street,, Chicago, Illinois 60602.
Lynn Mutual Insurance Company, Andrew M. Innes, President, 12 Monument Square, Concord, Massachusetts 01742.
Madison County Mutual Automobile Insurance Company, Ladimir J. Aubrecht, Secretary-Treasurer, 100 St. Louis Street, Edwardsville, Illinois 62025.
MAPFRE, Mutual Insurance Company,[2] Ignacio Hernando de Larramendi, Director General, Mutualidad de Seguros, Avenida de Calvo Sotelo, 25 Madrid–4, Spain.
Merchants and Businessmen's Mutual Insurance Company, J. Axe Miller, President, P.O. Box 1633, Harrisburg, Pennsylvania 17105.
Merchants' and Manufacturers' Mutual Insurance Company, Carl J. Eichar, President, P.O. Box 35, Mansfield, Ohio 44901.
Merrimack Mutual Fire Insurance Company, E. C. Nichols, President, 305 North Main Street, Andover, Massachusetts 01810.
Michigan Millers Mutual Insurance Company, S. L. Baker, Chairman of the Board, Box 60, Lansing, Michigan 48901.
Michigan Mutual Liability Company, Ralph J. Ladd, President, 28 West Adams Avenue, Detroit, Michigan 48226.
Middlesex Mutual Assurance Company, Everett G. Patterson, President, 200 Court Street, Middletown, Conn. 06457.

Footnotes at end of Appendix A.

Middlesex Mutual Insurance Company, Andrew M. Innes, President, 12 Monument Square, Concord, Massachusetts 01742.
The Millers Mutual Fire Insurance Company of Texas, Ed B. Collett, President, P.O. Box 2269, Fort Worth, Texas 76101.
Millers Mutual Insurance Association of Illinois, Nelson K. McBrien, Executive Vice President, 320 Easton Street, Alton, Illinois 62002.
Minnesota Mutual Fire and Casualty Company, J. H. Laidlaw, President, 407 South Fourth Street, Minneapolis, Minnesota 55415.
Montgomery Mutual Insurance Company,[1] Homer E. Rowland, President, 900 Olney-Sandy Spring Road, Sandy Spring, Maryland 20860.
Mountain States Mutual Casualty Company, Sherburne P. Anderson, President, P.O. Box 249, Albuquerque, New Mexico 87103.
Municipal Mutual Insurance Company of West Virginia, Michael Di Fabbio, Executive Vice President, P.O. Box 310, Wellsburg, West Virginia 26070.
Mutual Assurance Company for Insuring Houses from Loss by Fire, J. Morgan Denison, Secretary-Treasurer, 240 South Fourth Street, Philadelphia, Pa. 19106.
Mutual Fire Insurance Company of West Virginia,[1] Blaine W. Engle, Secretary, P.O. Box 2067, Clarksburg, West Virginia 26301.
National Grange Mutual Insurance Company, Kenneth P. Colby, President, P.O. Box 540, Keene, New Hampshire 03431.
National Mutual Church Insurance Company, Miss M. J. Van Treese, Secretary, 1603 Orrington Avenue, Suite 1320, Evanston, Illinois 60201.
New Castle Mutual Insurance Company, W. L. Coates, Jr., President, 1007 Washington Street, Wilmington, Delaware 19801.
New Jersey Manufacturers Insurance Company, Vincent E. Hoyer, President, P.O. Box 2708, Trenton, New Jersey 08607.
Norfolk and Dedham Mutual Fire Insurance Company, Robert L. Freeman, President, 222 Ames Street, Dedham, Massachusetts 02026.
North Star Mutual Insurance Company, W. E. Anderson, Secretary, Cottonwood, Minnesota 56229.
Northwestern Mutual Insurance Company, F. J. Orth, Chairman of the Board, 217 Pine Street, Seattle, Washington 98101.
The Ohio Hardware Mutual Insurance Company,[1] G. E. King, Secretary-Treasurer, P.O. Box 459, Mansfield, Ohio 44901.
Pawtucket Mutual Insurance Company, A. W. Benson, President, P.O. Box 820, Pawtucket, Rhode Island 02862.
Pennsylvania Lumbermens Mutual Insurance Company, Frank Braceland, Jr., President, 231 South Broad Street, Philadelphia, Pa. 19107.
Pennsylvania Millers Mutual Insurance Company, F. J. Gager, President, 72 North Franklin Street, Wilkes-Barre, Pa. 18703.
Perth Insurance Company,[2] H. G. Livingstone, President-Manager, Stratford, Ontario. Canada.
The Philadelphia, Contributorship for the Insurance of Houses From Loss by Fire, Walter L. Smith, Jr., Secretary-Treasurer, 212 South Fourth Street, Philadelphia, Pa. 19106.
The Portage la Prairie Mutual Insurance Company, E. M. Brown, General Manager, Portage la Prairie, Monitoba, Canada.
Preferred Mutual Insurance Company, Robert R. Hoadley, President, New Berlin, New York 13411.
Retail Lumbermens Mutual Insurance Co. of Wisconsin, Marvin R. Gumm, Executive Secretary, P.O. Box 3098, Milwaukee, Wisconsin 53218.
Richland-Knox Mutual Insurance Company, Malcolm S. Black, Executive Vice President, 680 Park Avenue, West, Mansfield, Ohio 44906.
Saskatchewan Mutual Insurance Company,[2] J. B. Hammill, Managing Director, Saskatoon, Saskatchewan, Canada.
The Shelby Mutual Insurance Company of Shelby, Ohio, Paul H. Dubuc, President, 19 Mansfield Avenue, Shelby, Ohio 44875.
Sierra Mutual Fire Insurance Company, Hardy Kuykendall, Sr., Secretary-General Manager, 3699 Park Boulevard, San Diego, California 92103.
Skaraborgs Lans Brandstodsbolag,[2] Bentgt Nyström, Box 32, Mariestad, Sweden.
Southern Mutual Insurance Company, Roy T. Scoggins, President, P.O. Box 792, Athens, Georgia 30601.
Texas Employers' Insurance Association, Walton O. Head, Chairman of the Board and President, P.O. Box 2759, Dallas, Texas 75221.

Footnotes at end of Appendix A.

Traders and Mechanics Insurance Company, Harold K. Bartlett, President, 36 John Street, Lowell, Massachusetts 01852.
Tri-State Mutual Insurance Company,[1] R. H. Swanson, President, 111–115 South Freeman, Luverne, Minnesota 56156.
Union Mutual Insurance Company of Providence, F. N. Folsom, President, P.O. Box 6187, Providence, R.I. 02904.
Utica Fire Insurance Company of Oneida County, New York, Howard W. Chappell, Executive Vice President, P.O. Box 851, Utica, New York 13503.
Utica Mutual Insurance Company, Victor T. Ehre, President, P.O. Box 530, Utica, New York 13503.
Utilities Mutual Insurance Company, George T. Norton, Vice President & General Manager, 56 Pine Street, New York, New York 10005.
Waseca Mutual Insurance Company, J. E. Rutledge, President, 203½ North State Street, Waseca, Minnesota 56093.
The Wawanesa Mutual Insurance Company,[2] M. C. Holden, President-Managing Director, 207 Donald Street, Winnipeg 1, Manitoba, Canada.
Wayne Mutual Insurance Company, Ralph H. Gresser, Secretary, 220 North Market Street, Wooster, Ohio 44692.
Wisconsin Mutual Insurance Company, D. C. Lynn, President, P.O. Box 974, Madison, Wisconsin 53701.

[1] Denotes National Associate Member.
[2] Denotes International Associate Member.

Appendix B

List of States Requiring Uninsured Motorist Coverage With Insolvency Protection

1. Arkansas
2. California
3. Connecticut
4. Delaware
5. Florida
6. Georgia
7. Idaho
8. Illinois
9. Indiana
10. Iowa
11. Kansas
12. Kentucky
13. Louisiana
14. Massachusetts
15. Michigan
16. Minnesota
17. Mississippi
18. Missouri
19. Nebraska
20. Nevada
21. New Hampshire
22. North Carolina
23. Oklahoma
24. Oregon
25. Pennsylvania
26. South Carolina
27. South Dakota
28. Tennessee
29. Texas
30. Vermont
31. Washington
32. West Virginia
33. Wisconsin
34. Wyoming

Appendix C

American Mutual Insurance Alliance Draft Bill Company-Operated Post-Assessment Insolvency Pool

(State) Insurers Insolvency Pool Act

Section 1. *Title.* This Act shall be known and may be cited as the (State) Insurers Insolvency Pool Act.

Section 2. *Purpose.* The purpose of this Act is to provide a remedy for covered claims under property and casualty insurance poicies when the insurer has become insolvent subsequent to the effective date of this Act and is unable to perform its contractual obligations. To this end, there is hereby created the (State) Insurers Insolvency Pool which shall consist of three account: (1) Workmen's Compensation account; (2) Automobile account; and (3) all other covered insurance account. The Pool shall be responsible (a) for the investigation, adjustment, compromise, settlement and payment of covered claims; (b) for the investigation, handling and denial of non-covered claims; and (c) for the management and investment of funds administered by the Pool. The members of the Pool shall be responsible (a) for payment of assessments levied pursuant to Section 8; (b) for adherence to the rules of the plan approved pursuant to Section 7; and (c) other obligations imposed by this Act.

SECTION 3. *Definitions.* (a). "Insurer" or "company" means any corporation or organization licensed to engage in the writing of property or casualty insurance policies in this state, including the exchanging of reciprocal or inter-insurance contracts between individuals, partnerships and corporations. [Consideration may be given in each state to excluding farmers, county, township, assessment mutual insurers.]

(b) "Property and casualty insurance policies" or "policy" means any contract, including endorsements thereto and without regard to the nature or form of the contract or endorsement, which provide coverages as enumerated in Sections ——, of the (State) General Statutes except:

(1) Life insurance and annuities (being that class of insurance referred to in Section ——— of the (State) General Statutes).

(2) Accident and health insurance except where written as part of an automobile insurance contract (being that class of insurance referred to in Section —— of the (State) General Statutes).

(3) Title insurance (being that class of insurance referred to in Section —— of the State) General Statutes).

(4) Mortgage guaranty insurance (being that class of insurance referred to in Section ——— of the (State) General Statutes).

(5) Credit insurance (being that class of insurance referred to in Section——— of the (State) General Statutes).

(c) "Net direct written premiums" means direct gross premiums written on property or casualty insurance policies, less return premiums thereon and dividends paid or credited to policyholders on such direct business. Premiums written by any authorized insurer on policies issued to self-insurers, whether or not designated as reinsurance contracts, shall be deemed net direct written premiums.

(d) "Commissioner" means the Commissioner of Insurance of this state.

(e) "Insolvency Pool" or "Pool" means the Insurers Insolvency Pool established pursuant to Section 7 of this Act.

(f) (1) "Covered claims" means a claim which:

(a) Arises out of a property or casualty insurance policy issued by an insurer which was authorized to do an insurance business in this state either at the time the policy was issued or when the insured event occurred; and

(b) Is within any of the classes of claims under subsection (2) below.

(2) A claim shall not be paid unless it arises out of an insurable event under a property or casualty insurance policy and it is:

(a) The claim of a policyholder or insured, who at the time of the insured event was a resident of this state; or

(b) The claim of a person having an insurable interest in or related to property which was permanently situated in this state; or

(c) A claim under a liability or workmen's compensation insurance policy when either the insured or third party claimant was a resident of this state at the time of the insured event.

(3) A covered claim shall not include any claim in an amount of $200 or less, not the first $200 of any claim in excess of that amount.

(4) A covered claim shall not include that portion of any first party claim which is in excess of the applicable limits provided in the policy or $_____, whichever is less.

(5) A covered claim shall not include that portion of any third party claim, other than a workmen's compensation claim, which is in excess of the applicable limits provided in the policy $_____, whichever is less.

(6) A covered claim shall not include any obligation to insurers, insurance pools, underwriting associations or any person which has a net worth greater than $1,000,000 at the time of the insured event.

(g) "Insolvent insurer" means an insurer which was licensed to issue property or casualty insurance policies in this state until determined insolvent by a court of competent jurisdiction of the insurer's domiciliary state, and which adjudication was subsequent to the effective date of this Act.

(h) "Affiliate" or "affiliates" means any enterprise related directly or indirectly to the insurance activities of the insurer.

SECTION 4. *Property and Casualty Insurers Subject to Act.* Every insurer authorized on or after the effective date of this Act to write property or casualty insurance policies in this state shall be a member of the Insolvency Pool and shall be liable for assessments pursuant to Section 8 of this Act and shall also be responsible for the other obligations imposed pursuant to this Act.

SECTION 5. *Determination of Insolvency; Notice of Insolvency.* Upon the determination of a court of competent jurisdiction of the state of domicile of an in-

surer that such insurer is insolvent, the Commissioner of this state shall promptly give notice thereof, by first class mail, to: (a) all persons known or reasonably expected to have or be interested in claims against the insurer, at such person's last known address; (b) all insureds of the insolvent insurer, at such insured's last known address and (c) all insurers subject to this Act. The Commissioner may also require each agent of the insolvent insurer to give prompt written notice, by first class mail, at the insured's last known address, to each insured of the insolvent insurer for whom he was agent of record. If the insurer be domiciled in this state, notice shall also be given by publication in a newspaper of general circulation published in the county where the insurer had its principal office, not less than once per week, for four weeks, and by publication elsewhere in this state as the court may direct.

SECTION 6. *Obligations of the Insolvency Pool.* In the event of the determination of insolvency of a licensed insurer after the effective date of this Act, the coverage afforded by property and casualty insurance policies issued by such insurer shall, with respect to covered claims, and for a period of (a) 30 days from the date of such determination, or until (b) policy expiration date if less than said thirty days, or until (c) such policy has been replaced by the insured within said thirty days, become the obligation of the Pool. The Pool shall be deemed to be the insurer for such period with respect and to the extent of such claims with all the rights, duties and obligations of the insolvent insurer, and the Pool is hereby authorized to investigate, adjust, compromise and settle covered claims, or to investigate, handle and deny non-covered claims.

SECTION 7. *Creation of Insurers' Insolvency Pool by Plan.* (a). There is hereby created the (State) Insurers' Insolvency Pool, a not for profit legal entity with the right to sue and be sued. The Pool shall adopt, and the Commissioner shall approve, a reasonable plan, not inconsistent with the provisions of this Act, fair to insurers and equitable to their policyholders, pursuant to which all admitted insurers become members of the Pool. All members of the Pool shall adhere to the rules of the Plan.

(b) If, for any reason, the Pool fails to adopt a suitable Plan within six months following the effective date of this Act, or if at any time thereafter the Pool fails to adopt necessary amendments to the Plan, the Commissioner shall adopt and promulgate, after hearing, such reasonable rules as are necessary to effectuate the provisions of this Act. Such rules shall continue in force until modified by the Commissioner or superseded by a plan of operation adopted by the Pool and approved by the Commissioner.

(c) In accordance with the Plan, the Pool may designate insurers to act on behalf of the Pool to carry out the purposes of this Act, but a member may decline such designation. The Commissioner may disapprove such designation. The Plan may provide a procedure under which pending claims or judgments against the insolvent insurer, or its insureds, are assigned to the member companies designated to act for the Pool. The assignee-insurer is hereby authorized to appear and defend a claim in a court of competent jurisdiction or otherwise and to investigate, adjust, compromise and settle a covered claim or to investigate, handle and deny a noncovered claim, and do so on behalf of and in the name of the Pool. If an assignee-insurer pays the covered claim it shall be reimbursed by the Pool or be entitled to set off said payment against future assessments. The unreimbursed claim of such an insurer against the Pool shall be an admitted asset of the insurer. Insureds entitled to protection of this Act shall cooperate with the Pool and the assignee-insurer.

(2) The Pool shall have no cause of action against the insured of the insolvent insurer for any sums it has paid out. The Pool shall be subrogated to the rights of any insured or claimant, to the extent of a covered claim, to participate in the distribution of assets of the insolvent insurer to the extent that the Pool has made payment. Any claimant or insured entitled to the benefits of this Act shall be deemed to have assigned to the Pool, to the extent of any payment received, his rights against the estate of the insolvent insurer. The Pool shall receive the benefit of any reinsurance contracts or treaties entered into by the insolvent insurer which cover any of the liabilities incurred by the insolvent insurer with respect to covered claims. After determination of insolvency of any insurer, the Pool shall be a party in interest in all proceedings involving policies insured or assumed by the Pool with the same rights to receive notice and defend, appeal and review as the insolvent insurer would have had if solvent. All moneys recovered under this section or any other section shall be added to the assessments collected under Section 8.

SECTION 8. *Assessments.* (a) For the purposes of administration and assess-

ment under this Section, the Pool shall be divided into three separate accounts: (1) Workmen's Compensation Insurance account; (2) Automobile Insurance account; and (3) all other covered insurance account. Separate assessment shall be made for each account. No assessment shall be levied for any account as long as the assets held in such account are sufficient to cover all estimated payments for liquidation in process under the account.

(b) To the extent necessary to secure the funds for the respective accounts of the Pool for the payment of covered claims and also to pay the reasonable costs to administer the Pool, the Commissioner, upon certification of the Pool, shall levy assessments in the proportion that each insurer's net direct written premiums in this state in the classes protected by the account bears to the total of said net direct written premiums received in this state by all such insurers for the preceding calendar year for the kinds of insurance included within such account. Assessments shall be remitted to and administered by the Pool in the manner specified by the approved Plan. Each insurer so assessed shall have at least thirty days written notice as to the date the assessment is due and payable. Every assessment shall be made as a uniform percentage applicable to the net direct written premiums of each insurer in the kinds of insurance included within the account in which the assessment is made. The assessments levied against any insurer shall not exceed in any one year more than 1% of that insurer's net direct written premiums in this state for the kinds of insurance included within such account during the calendar year next preceding the date of such assessments. If sufficient funds from such assessments, together with funds previously raised, are not available in any one year in the respective account to make all the payments or reimbursements then owing to insurers designated to act for the Pool, the funds available shall be pro-rated and the unpaid portion shall be paid as soon thereafter as funds become available. Assessments shall be included as an appropriate factor in the making of rates.

(c) The Pool may exempt any insurer from an assessment if an assessment by the Pool would result in such insurer's financial statement reflecting an amount of capital or surplus less than the sum of the minimum amount required by any jurisdiction in which the insurer is authorized to transact insurance.

(d) Any necessary and proper expenses incurred by an insurer in the investigation, adjustment, compromise, settlement, denial or handling of claims assigned to it shall, upon proper vertification under the rules of the Pool, entitle the insurer to reimbursement. Any insurer whose employee serves on the staff of the Pool may set off from its assessment any necessary and proper expenses incurred by the insurer resulting from said service of its employee. An insurer which ceases to engage in the business of writing property or casualty insurance policies in this state shall have no right to a refund of any assessment previously remitted to the Pool.

SECTION 9. *Procedure to Determine Covered Claims.* Except for (a) voluntary settlements or compromises between a claimant and an assignee-insurer (on behalf of the Pool), or (b) a final judgment, other than a default judgment, against the insured or insurer in a court of competent jurisdiction rendered prior to the determination of insolvency of the insurer, the proof and allowance of a covered claim shall be governed by [cite relevant section of statute relating to proof and allowance of claims in a liquidation proceeding].

SECTION 10. *Paid Claims as Proper Claims Against Insolvent Estate.* As respects insolvent insurers incorporated in this state, the receiver, liquidator or statutory successor shall allow as a proper claim on the assets of the insolvent company amounts paid under the provisions of this Act by or on behalf of the Pool on or with respect to covered claims, and any statute of this state relating to the rights and duties of such receiver, liquidator or statutory successor is deemed amended to so provide. As a condition of an insurer doing business in this state, all property and casualty insurance policies issued or renewed on or after the effective date of this Act shall be deemed to provide that the insurer appoints the Pool as its agent as respects investigation, adjustment, compromise and settlement of covered claims and to reimburse the Pool for any payment made under the terms of this Act, and that such appointment and obligation shall be binding on any receiver, liquidator or statutory successor appointed to liquidate or wind up its affairs.

SECTION 11. *Other Insurance.* Any person (including any individual, partnership, association or corporation) having a claim against his insurer under any insolvency provision contained in his insurance policy, which claim arises out of the insolvency of a participating insurer, shall be required to exhaust first his rights under such policy and his rights to recover such claim under the provisions

of this Act shall be reduced accordingly. Any amount paid a claimant in excess of the amount authorized by this Act may be recovered by action brought by or on behalf of the Pool.

SECTION 12. *Duties of Commissioner.* The Commissioner shall sue for and recover, on behalf of the Pool any assessment not paid when due. He may, after notice and hearing, revoke the certificate of authority to transact business in this state of an insurer, a member of the Pool, which (a) shall fail to pay an assessment when due as provided in this Act and after demand having been made, or (b) otherwise fails to comply with the plan as approved pursuant to Section 7 of this Act. Any action taken by the Commissioner shall be subject to judicial review as provided in Section 2 of the (State) General Statutes.

SECTION 13. *Insolvency Pool Subject to Examination.* The Pool shall be deemed a company or insurer within the scope of Section —— relating to examinations.

SECTION 14. *Insolvency Pool: Limitation on Taxability.* The Pool shall be exempt from all license fees, income, franchise, privilege, occupation or other taxes levied or assessed by the state, any municipality, county or other political subdivision of the state, except state, county, or municipal taxes upon the real or personal property of the Pool, which is to be assessed and taxed in the same manner as real property and personal property of other non-exempt persons.

SECTION 15. *Insurers Solvency Board; Organization and Powers.* (a). There shall be in the Insurance Department an Insurers Solvency Board which shall consist of seven members. The Commissioner of Insurance shall be a member of the Board and shall be its chairman and chief executive. The remaining six members, who shall not be considered employees of the Insurance Department, shall be appointed as follows:

(1) The Commissioner shall compile a list of the three stock insurers most likely to incur the largest assessment, per insurer, for each of the accounts under Section 8, and he shall also compile a list of the three non-stock insurers most likely to incur the largest assessment, per insurer, for each of the accounts under said Section 8. The Commissioner shall solicit from the said eighteen insurers the names of eighteen individuals as nominees for membership to the Insurers Solvency Board. [Persons who are nominated for the Board shall reside in this state—(optional)]. The Commissioner shall thereupon certify said nominations in writing to the Governor separately for stock and non-stock insurers and separately for each account.

(2) From the nominations so received for each such account, the Governor shall appoint one stock member and one non-stock member.

(3) Any member may be removed from office by the Governor when, in his judgment, the public interest may so require. In the event of such a removal, the Governor shall file with the Secretary of State a statement of the cause of the removal.

(4) Each member so appointed shall serve for a term of three years and until his successor has been appointed and qualified, and in case of a vacancy for any reason in the office of any such member, the Governor shall appoint a member to fill the unexpired term of such vacant office from the nominations as heretofore described.

Reasonable expenses of the members of the Insurers Solvency Board, incurred in attending meetings, shall be paid out of the State Treasury on certification of the Commissioner of Insurance upon the audit and warrant of the Treasurer. The Insurers Solvency Board shall hold its regular meetings at such time and places as shall be fixed by the Board. The Board shall meet at any time, on call of the Commissioner of Insurance. The Commissioner shall call a meeting, upon not less than two days notice, upon the written request of any two members of the Board. The Board may by resolution provide for a shorter notice of a meeting by telegraph, telephone or otherwise. The Board shall keep a record of all its proceedings and shall appoint a secretary and such other officers as it deems necessary, who need not be members of the Board. For the purpose of considering questions before it, the Board shall have access to all the books, records, reports and papers in the department, including all confidential communications, and the members of the Board shall hold such communications as confidential.

(b) The Insurers Solvency Board shall have power, by affirmative vote of four of its members, to examine, without previous advance notice, the assets, conditions and affairs of any insurer when the Board believes that said insurer's further transaction of business may be hazardous to its policyholders or to its creditors, or to the public. Examinations by the Insurers Solvency Board shall be conducted by independent certified public accountants and the expenses thereof shall be borne by the (State) Insurers Insolvency Pool.

Said examination may extend to general agencies, management entities or affiliates of said companies with respect to matters affecting said companies. Said report of examination shall be furnished to the Commissioner and held confidential until a hearing shall have been held or waived, pursuant to Section ——. A refusal by a company, a general agency, a management entity or affiliate of a company to submit its books, papers, accounts, records or affairs to such examination shall be so reported to the Commissioner and shall constitute grounds for suspension, rehabilitation, liquidation or conservation of the insurer within the purview of Section —— or for the license revocation of the agency, as the case may be.

The Board may also so examine the affairs of such an insurer after formal adjudication of insolvency to assist in the conservation of assets, and said Board shall furnish its report to the Commissioner and also to the (State) Insurers Insolvency Pool.

(c) The Insurers Solvency Board shall have power by an affirmative vote of four of its members, to make recommendations to the Commissioner upon any matter germane to the solvency, liquidation, rehabilitation or conservation of companies or persons engaged in the business of writing property or casualty insurance policies in this state.

(d) Reports and recommendations under this Section shall not be considered public documents. There shall be no liability on the part of, and no cause of action shall arise against, member insurers, the Pool or their agents or employees, the Governor, the Commissioner or his authorized representative, for any statements made by them in any reports or recommendations made hereunder.

SECTION 16. *Non-Duplication of Recovery.* It is not the purpose of this Act to provide or permit duplicate recoveries of covered claims under this Act and an insolvency fund or its equivalent of any other State. In the construction and application of this Act with respect to a covered claim which may be recoverable under his Act and under an insolvency fund or its equivalent in another state, the sole recovery

(a) with respect to a workmen's compensation claim, shall be under the insolvency fund or its equivalent of the state of residence of the claimant;

(b) with respect to a first party claim of an insured for damage to or destruction of property with a permanent location, shall be under the insolvency fund or its equivalent of the state where such property is permanently situated;

(c) with respect to any oher covered claim, shall be under the insolvency fund or its equivalent of the state of residence of the insured.

SECTION 17. *Termination. Distribution of Fund.* (a). The Commissioner shall by order terminate the operation of the (State) Insurers Insolvency Pool as to any kind of insurance afforded by property or casualty insurance policies with respect to which he has found, after hearing, that there is in effect a statutory or voluntary plan which:

(1) is a permanent plan which is adequately funded or for which adequate funding is provided; and

(2) extends, or will extend to the (State) policyholders and residents protection and benefits with respect to insolvent insurers not substantially less favorable and effective to such policyholders and residents and the protection and benefits provided with respect to such kind of insurance under this Act.

(b) The Commissioner shall by the same such order authorize discontinuance of future payments by insurers to the (State) Insurers Insolvency Pool with respect to the same kinds of insurance; provided, that assessments and payments shall continue, as necessary, to liquidate covered claims of insurers adjudged insolvent prior to said order and the related expense not covered by such other plan.

(c) In the event the operation of any account of the (State) Insurers Insolvency Pool shall be so terminated as to all kinds of insurance otherwise within its scope, the Pool as soon as possible thereafter shall distribute the balance of moneys and assets remaining in said account (after discharge of the functions of the Pool with respect to prior insurer insolvencies not covered by such other plan, together with related expenses) to the insurers which are then writing in this state policies of the kinds of insurance covered by such account, and which had made payments into such account, pro-rata upon the basis of the aggregate of such payments made by the respective insurers to such account during the period of five years next preceding the date of such order. Upon completion of such distribution with respect to all of the accounts specified in Section 8, this Act shall be deemed to have expired.

SECTION 18. This Act shall take effect on _____, 1970.

APPENDIX D

COMPARISON OF ENACTED STATE INSOLVENCY PLANS

	Types of insurance included	Insurers included	Timing	Contact with the State	Amount of coverage	Excluded from coverage
California	All except life, title, surety, disability, mortgage, mortgage guaranty, ocean marine.	All licensed insurance except those writing excluded types.	Unpaid obligation of insolvency insurance incurring prior to or within 30 days after liquidation appointed, coverage continued until policy expires, is replaced or canceled.	Workmen's compensation benefits under California law, other obligations if policyholder or claimant a California resident.	$100 deductible (except workmen's compensation). Maximum $500,000 (except workmen's compensation).	Unearned premium obligated under reinsurance contracts. Obligation to insurance pools, underwriting associations.
Michigan	Workmen's compensation, auto, "basic property" (2901) multiperil (homeowner's; farm, commercial).	All licensed insurance except life.	Unpaid obligation of insolvency insurance incur. prior to or within 30 days after receiver appointed. Coverage continued until policy expires, is replaced or canceled but not for more than 30 days after receiver appointed.	Policyholder or claimant Michigan resident.	$200 deductible Maximum ½ of 1 percent of premium in State (except workmen's compensation). Maximum $150,000 basic property or commercial multiperil claim.	Unearned premium. Obligation to insurance pools, underwriting associations. Persons with net worth greater than 1/10 of 1 percent of premium.
New Hampshire	Auto	Auto	Policy issued prior to adjudication of insolvency or receiver appointed.	Policyholder a New Hampshire resident.	Maximum (1) Bodily injury, liability 25–50. (2) Property damage liability, $25,000. (3) Medical pay $5,000.	Claims cognizable under UM coverage.
Wisconsin	All except variable annuity and variable life insurance.	All licensed insurance except fraternal, assessment, mutual, nonprofit service plans.		Claim of residence policyholder, insured or beneficiary. Claim of owner of property in Wisconsin. Liability or workmen's compensation claim if (1) Insured or 3d party residence. (2) Personal injury suffered in State or by residence. (3) Property damaged situated in state.	$200 deductible	
Maryland	Auto liability and property damage.	Auto liability and property damage.	File claim with court handling insolvency. 6 months to give notice of valid additional claim to insurance commissioner.	Policyholder or 3d party resident.	Up to individual policy limits.	
New Jersey	Auto liability	Auto liability	Notice to insurance commissioners within 2 years of insolvency or 2 years of date of accident whichever is later. Unpaid obligation via court must go back to have commission named.	do	$100 deduct up to individual policy limits.	

	Types of insurance included	Insurers included	Timing	Contact with the State	Amount of coverage	Excluded from coverage
New York	Auto, fire, extended coverage, water damage, theft, glass, boiler and machinery, elevator, animal, collision, fidelity, insurety, credit, ocean, and inland marine. Only applies to real property as used predominantly for residential.	All licensed insurance other than life.	----------	Policyholder or 3d party resident.	Maximum $1,000,000	
Minnesota	Workmen's compensation.	Workmen's compensation.		Workmen's compensation benefits under Minnesota law.		
North Carolina	do	do		Workmen's compensation benefits under North Carolina law.		
Pennsylvania	do	do		Workmen's compensation benefits under Pennsylvania law.		

APPENDIX E

PROJECTION OF FUTURE GROWTH OF FEDERAL INSURANCE GUARANTY CORPORATION

[In millions]

	Total premium [1] (1)	2 percent maximum (2)	Factor (3)	(1) × (3) (4)	Cumulative of (4) (5)	Difference (2) less (5) (6)	Difference each year (7)
1968	$25,000	$500	.00125	$31.3	$31.3	$469	
1969	27,250	545	.00125	34.1	65.4	480	$11
1970	29,703	594	.00125	37.1	102.5	491	11
1971	32,376	648	.00125	40.5	143.0	505	14
1972	35,290	706	.00125	44.1	187.1	519	14
1973	38,466	769	.00125	48.1	235.2	534	15
1974	41,928	839	.00125	52.4	287.6	551	17
1975	45,701	914	.00125	57.1	344.7	569	18
1976	49,815	996	.00125	62.3	407.0	589	20
1977	54,298	1,086	.00125	67.9	474.9	611	22

[1] Premium growth is at a compound rate of 9 percent per year.

Note: Col. 5 represents the build up in the insolvency fund if there is a tax of 1/8 of 1 percent of premiums collected each year and no expenses or insolvency loss payments are made. Col. 6 represents the gap between the maximum growth of the insolvency fund (no losses) and the 2 percent maximum lid proposed.

APPENDIX F

FINANCIAL ANALYSIS OF FEDERAL DEPOSIT INSURANCE CORPORATION, INCOME AND EXPENSES

[In millions]

	Income			Expenses				
Year	Total	Insurance assessment	Investments and other sources	Total	Net losses and expenses	Interest on capital stock	Administration and operating expenses	Net operating surplus
1968	$295.0	$132.4	$162.6	$30.4	$1.4		$29.0	$264.6
1967	263.0	120.7	142.3	30.4	6.0		24.4	232.6
1966	241.0	111.7	129.3	25.0	5.2		19.8	216.0
1965	214.0	102.2	112.4	24.4	6.7		17.7	190.2
1933–64 (inclusive)	3,116.1	2,077.9	1,100.6	332.7	35.9	$80.6	216.2	2,845.8
Total (1933–68)	4,192.11	2,544.9	1,647.6	332.9	55.2	80.6	307.1	3,749.6

Source: Federal Deposit Insurance Corporation Annual Report of the Corporation, 1968, p. 28.

APPENDIX G

AMERICAN MUTUAL INSURANCE ALLIANCE'S BOARD OF DIRECTORS' STATEMENT ON S. 2236 AND INSURANCE COMPANIES INSOLVENCY, ADOPTED MAY 27, 1969

A. The Alliance will vigorously oppose the enactment of S. 2236, to create the Federal Insurance Guaranty Corporation.

B. The Alliance believes that the scope of the insurance insolvency problem has not been viewed in the proper perspective, that it has been grossly exaggerated by some, and that the problem does not approach the magnitude of a national social problem requiring the drastic measures proposed by the Magnuson bill. However, we believe that the insolvency of a company does present serious human problems which should be eliminated or at least more fully alleviated. Therefore, we believe the Alliance position on insolvency legislation should be expanded to meet current pressures at the state level and particularly those in Washington.

The Alliance should take the following affirmative position on insolvency legislation:

(1) Continue to propose and actively support at the state level uninsured motorist coverage with insolvency protection. Further, the Alliance should recommend that the uninsured motorist laws prohibit subrogation by the uninsured motorist coverage carrier against the estate of an insolvent company or against the insured of an insolvency company, thereby leaving additional funds which may be paid to other claimants.

(2) Because of the current pressures at the state level and the serious threat

of enactment of the proposed Magnuson bill, we do not believe the above position is adequate. Therefore, we recommend that the Alliance *advocate and support affirmatively* post-assessment insolvency plans in all states similar to the Alliance post-assessment insolvency bill with the following modifications:

(*a*) Expand the scope of the Alliance model post-assessment insolvency bill to cover all property and casualty lines excluding only accident and health insurance, life insurance, title insurance, mortgage guarantee insurance, and credit insurance. We believe this expansion to be necessary because insolvencies are not limited to particular lines of insurance and the hardship imposed on individuals because of an insolvency is no less disastrous under a property insurance policy than it would be under a casualty insurance policy.

(*b*) Include in the Alliance post-assessment insolvency bill a provision for automatic termination of further state assessments upon adoption of a federal insolvency program whether by Congressional legislation or otherwise. We believe this to be necessary to prevent possible future concurrent jurisdiction.

C. The Alliance should consider and develop some type of national insolvency protection system under industry operation and control, with such Congressional legislative authorization as may be necessary.

Senator HART. Thank you very much.

I would like to raise only one point with you. Counsel, I am sure, has others. You have that section in there that discusses the cost of the Federal Deposit Insurance Corporation?

Mr. MAISONPIERRE. Right, sir.

Senator HART. We can only make our individual guesses as to how much the American consumer may have been saved by the existence of the corporation. It is pure guess.

Leaving aside that point—I am not trying to crowd you on that one—you do not indicate the current cost that the American consumer who is an insurance purchaser now pays in the form of fees and taxes on companies. I am told it amounts to close to a billion dollars, and our figures show that the States, then, provide only 40 million for their insurance regulation activities. Is that not a figure which should be included when you make the comparison of the FDIC?

Mr. MAISONPIERRE. May I comment in two parts on this, Mr. Chairman?

First, as to the estimation of how much the American public is saved through the activities of the FDIC, we do have a number of uninsured banks in this country.

Senator HART. Not very many.

Mr. MAISONPIERRE. I beg your pardon?

Senator HART. Not very many.

Mr. MAISONPIERRE. This is correct; but we still have a number of them. These banks are not subject to any type of Federal regulation. They are subject to State regulation. These uninsured banks had no insolvencies in 1968.

I will go further; they had no closing of these banks in 1968 as a result of financial difficulties. There were none in 1967, and there was only one in 1966. So there does not seem to be a general pattern of insolvency in the banking industry regardless of the FDIC.

As to the other part of your question, Mr. Chairman, the insurance industry, the property and casualty industry for which I can speak, provides a very substantial support to the running of State governments through the method of State premium taxation.

In fact, in a very substantial number of States, premium taxation represents the third-largest support for running State government.

Understandably, approximately 4.5 to 5 percent of net taxes collected from the companies for the regulation of the business—for the running——

Senator HART. What percentage?

Mr. MAISONPIERRE. 4½ to 5 percent. I can provide for the committee a State-by-State analysis.

Senator HART. No, just for this discussion I wanted to hear.

Mr. MAISONPIERRE. However, if the States were to be prevented from taxing premiums, as they do today, the State would have to look to some other sort of taxation, and the consumer would have to pay for these taxes through some other source. So I do not think it is fair to compare the taxes paid by the companies to the operation of the FDIC because these taxes are going for the running of the total State government program.

Senator HART. Mr. Sutcliffe?

Mr. SUTCLIFFE. Mr. Maisonpierre, you mentioned at the present time you felt that the States had sufficient authority and were exercising that authority to prevent certain problems of insolvency. Let me run through a couple of things to find out for our purposes what the State insurance regulators can do.

What can a State insurance regulator do to prevent the management of an insurance company from paying exorbitant attorneys' fees to a principal of that company?

We have an example of this, as you are aware, and I just want to know what the State insurance director at the present time can do to prevent that?

Mr. MAISONPIERRE. It is difficult to generalize about the powers of the State regulators.

Mr. SUTCLIFFE. Let us use the example of the State regulator in Illinois, who has, I think, probably the broadest powers in the United States, so that we start with the most favorable example we can.

Mr. MAISONPIERRE. I feel that Illinois does not have the broadest powers; but it does have some pretty broad powers since the enactment of legislation in 1967, I believe.

The conduct of company management and its payments of fees is part of a department's examination of the total operation of the company.

Mr. SUTCLIFFE. Mr. Maisonpierre, is that always broken out? Does the examiner always look to what the legal fees paid out are? We have one example in the State of Illinois, which seems to be doing a good job of regulating; they did not break out the payment of attorneys' fees to the principals of the company in the Prudence Mutual situation.

Mr. MAISONPIERRE. I recognize this was not broken out in this particular case. Although I cannot speak for the Illinois Director, I am sure that from now on he will require the companies to break these out.

Mr. SUTCLIFFE. Will the 49 other State directors do the same?

Mr. MAISONPIERRE. I believe that every insurance commissioner or director learns from each solvency. The other commissioners will be very much interested in finding out what the insurance director's investigation of the Prudence Mutual Co. case turns up, and they will analyze this and will set in motion new regulatory patterns within

their States to prevent companies from using certain loopholes presently existing.

Mr. SUTCLIFFE. Is the communication network such that every insurance commissioner will learn from the problems that a single insurance commissioner has?

Mr. MAISONPIERRE. I believe there is no area today which is of greater interest to commissioners than that involving insolvency, to some extent thanks to this committee.

Mr. SUTCLIFFE. Let me turn to your statements on the uninsured motorist endorsement. Has the Alliance you represent always favored the uninsured motorist endorsement? And if it has not, would you explain to this committee the basis for any opposition that you have had to the uninsured motorist endorsement? This may have to go back to an organization that was in existence prior to the formulation of the American Mutual Insurance Alliance.

Mr. MAISONPIERRE. If I recall correctly, Mr. Sutcliffe, and this goes beyond my days with the Alliance, because we must recognize that the uninsured motorist coverage was introduced in the early 1950's, there was a concern on the part of the Alliance companies that—through the uninsured motorist coverage we were giving really what you might call a free ride to the uninsured motorist himself. He did not participate in any way in the cost of the damage which he creates.

In addition, we felt that the uninsured motorist coverage might act as a deterrent to people getting insurance. This was in the early 1950's. We have since wholeheartedly endorsed the uninsured motorist coverage.

As far as the insolvency protection being added to the uninsured motorist coverage, we have wholeheartedly endorsed this protection indeed.

Mr. SUTCLIFFE. Does this insolvency protection under the UM endorsement cover as a general rule, property damage? Or is it only coverage for bodily injury?

Mr. MAISONPIERRE. At this stage it does cover primarily bodily injury. It covers up to the limits of the financial responsibility laws.

Mr. SUTCLIFFE. What are those limits usually? Is it $10,000? Is that correct? Just for the record.

Mr. MAISONPIERRE. They have been $10,000. A number of States have been upgrading their limits, and I would be glad to submit for the record a list of the financial responsibility limits.

(The information requested follows:)

AMERICAN MUTUAL INSURANCE ALLIANCE,
Washington, D.C., December 22, 1969.

Hon. FRANK E. MOSS,
Senate Commerce Committee, New Senate Office Building,
Washington, D.C.

DEAR SENATOR MOSS: When the American Mutual Insurance Alliance testified on S. 2236, we were asked for information relating to both the financial responsibility limits which had been established in the different states, as well as the subrogation provisions under the uninsured motorist laws of the different states.

In lieu of submitting a narrative answer to these questions, we thought that it would be better to devise an appropriate chart. The chart is attached.

Sincerely,

ANDRE MAISONPIERRE,
Vice President.

UNINSURED MOTORISTS CHART

State	Limits	Right to reject	Required deviations from standard wording	Statutory insolvency provision: Included	Statutory insolvency provision: Cutoff period (years)	Statutory right of subrogation in insolvency provision: Tortfeasor	Statutory right of subrogation in insolvency provision: Insolvent insurer
Alabama	10/20	Yes		No		No	No.
Alaska	15/30	Yes		No		No	No.
Arizona	10/20	Yes		No		No	No.
Arkansas	10/20	Yes	(1)(2)	Yes	1	Yes	Yes.
California	15/30	Yes		Yes	1	Yes	No.
Colorado	15/30	Yes		No		No	No.
Connecticut	[3] 20/20	No		Yes	None	(4)	(4).
Delaware	10/20	Yes		Yes	1	Yes	Yes.
Florida	10/20	Yes	(2)(5)	Yes	1	Yes	Yes.
Georgia	[6] 10/20/5	Yes	(1)(2)	Yes	None	Yes	Yes.
Hawaii	10/20	Yes		No		No	No.
Idaho	10/20	Yes		Yes	1	Specific prohibition.	Yes.
Illinois	10/20	No		Yes	None	(7)	(7).
Indiana	10/20	Yes		Yes	2	Yes	No.
Iowa	10/20	Yes		Yes	1	Yes	Yes.
Kansas	10/20	Yes		Yes	2	Yes	No.
Kentucky	10/20	Yes	(1)	Yes	1	Yes	Yes.
Louisiana	5/10	Yes	Arbitration is optional.	Yes	1	Yes	Yes.
Maine	20/40	No		No		No	No.
Massachusetts	5/10	No		Yes	1	(3)	(7).
Michigan	10/20	Yes		Yes	None	Specific prohibition.	Yes.
Minnesota	[3] 10/20	No		Yes	None	Yes	Yes.
Mississippi	5/10	Yes	(1)	Yes	1	Yes	Yes.
Missouri	10/20	Yes		Yes	2	Yes	Yes.
Montana	10/20	Yes		No		No	No.
Nebraska	10/20	Yes	(2) (5)	Yes	1	Specific prohibition.	Yes.
Nevada	15/30	Yes	(1)	Yes	None	No	No.
New Hampshire	[3] 15/30	No		Yes	3	(7)	(7).
New Jersey	[8] 10/20/5	Yes		No		No	No.
New Mexico	[9] 10/20/5	Yes		(10)	None	Yes	No.
New York	10/20	No	Administered by MVAIC	No		Yes	No.
North Carolina	[11] 5/10/5	Yes		Yes	3	Yes	Yes.
Ohio	12. 5/25	Yes		No		No	No.
Oklahoma	[12] 5/10	Yes	Arbitration is optional.	Yes	1	(7)	(7).
Oregon	5/10	No	(2)	Yes	2	Yes	No.
Pennsylvania	10/20	No		Yes	6	Specific prohibition.	Yes.
Rhode Island	10/20	Yes		No		No	No.
South Carolina	[6] 10/20/5	No	(1)	Yes	None	Yes	No.
South Dakota	10/20	Yes		Yes	None	Yes	Yes.
Tennessee	10/20	Yes	(1)	Yes	1	Yes	Yes.
Texas	10/20	Yes		Yes	None	Specific prohibition.	Yes.
Utah	10/20	Yes		No		No	No.
Vermont	10/20	No		Yes	1	Yes	Yes.
Virginia	[13] 20/30/5	No	(1) (2)	(10)	None	Yes	No.
Washington	15/30	Yes		Yes	3	Specific prohibition.	Yes.
West Virginia	[14] 10/20/5	No	(1)	Yes	None	do	Yes.
Wisconsin	[3] 15/30	Yes		Yes	None	Yes	No.
Wyoming	10/20	Yes		Yes	None	Specific prohibition.	Yes.

[1] Arhitration not permitted.
[2] Workmen's compensation benefits not allowed to be excluded or set off.
[3] Up to BI limits.
[4] UM insurer prohibited from subrogating against tortfeasor if tortfeasor assigns his rights as insured against insolvent insurer to UM insurer.
[5] Medical payments coverage benefits not allowed to be set off. Absent a specific statutory prohibition of subrogation, the insurer has the contractual rights afforded by the Trust Agreement in the UM Coverage.
[6] $200; P.D. deductible.
[7] UM insurer not entitled to recovery against tortfeasor in excess of recovery against insolvent insurer.
[8] $100; P.D. deductible.
[9] $250; P.D. deductible.
[10] There is no statutory insolvency provision. However, the prescribed endorsement for the State contemplates such coverage.
[11] $100; P.D. deductible; up to 15/30/5 if BI limits are that much.
[12] But larger amounts may he offered and purchased if desired.
[13] $200; P.D. deductible; up to policy limits.
[14] $300; P.D. deductible.

Mr. SUTCLIFFE. With a property damage claim, then, the person has to go against his own first party coverage if he has those first party coverages; is that correct?

Mr. MAISONPIERRE. Are you talking about a property damage claim?

Mr. SUTCLIFFE. Yes.

Mr. MAISONPIERRE. In the majority case the property damage claim is not covered.

Mr. SUTCLIFFE. And he goes to his own insurance company for that?

Mr. MAISONPIERRE. To his collision coverage; yes.

Mr. SUTCLIFFE. Is there usually a deductible in that PD coverage as a general rule?

Mr. MAISONPIERRE. There is a deductible. Generally under the collision coverage there is a deductible of $50 or $100.

Mr. SUTCLIFFE. He makes that claim to his insurance company, the first party coverage, and then he makes the other claim—what does he have to show when he makes the other claim?

Mr. MAISONPIERRE. There is no claim in the uninsured motorist coverage for property damage, and this is one of the gaps in which we are trying to close.

Mr. SUTCLIFFE. Under bodily injury, he has to go for bodily injury coverage to his own company. This is correct.

Mr. MAISONPIERRE. This is correct.

Mr. SUTCLIFFE. What does he have to show?

Mr. MAISONPIERRE. Under the uninsured motorist coverage he must show that the third party was uninsured or he was hit by a hit-and-run driver or, in some instances, that the other company is insolvent.

Mr. SUTCLIFFE. What about the liability of that third party? Does he have to show that?

Mr. MAISONPIERRE. He must demonstrate just the same as he has to demonstrate the liability of a third party against—any third party carrier. In other words, the claim is not against the company. The claim remains against the individual, and he must show the negligence of of the individual and not the negligence of the company.

Mr. SUTCLIFFE. I just want to make sure I understand this. If the company feels he was contributorily negligent, what do they do? Because under our system, contributory negligence would cancel out his right to recover.

Mr. MAISONPIERRE. Are we talking about the practice? In practice, the companies will waive contributory negligence. As you know, today the theory of contributory negligence has been weakened very considerably.

Mr. SUTCLIFFE. Are you telling me it is not an either/or situation? They are following the practice of contribution of 60-percent fault plus 40-percent fault, and they will allow for a settlement of the 20-percent difference?

Mr. MAISONPIERRE. The company will handle the claim made by its own policyholder in exactly the same manner as it would handle the claim made by a third party.

Mr. SUTCLIFFE. Who defends the claimant, to show that he was not contributorily negligent?

Mr. MAISONPIERRE. Who defends the claimant?

Mr. SUTCLIFFE. This would be the claimant under the uninsured motorist endorsement.

Mr. MAISONPIERRE. The claimant has his attorney. Let me point this out.

Mr. SUTCLIFFE. His attorney is who?

Mr. MAISONPIERRE. The policyholder has his own attorney. The claimant has his own attorney. Under the uninsured motorist coverage, in the overwhelming majority of States, the matter does not have to go to litigation. The policy itself calls for compulsory arbitration.

Mr. SUTCLIFFE. Is there any appeal from that compulsory arbitration, any right of appeal?

Mr. MAISONPIERRE. I do not believe so. Let me point this out. The Alliance companies—I believe all the Alliance companies, provide in the policy that the arbitrator will be the American Arbitration Association, which is certainly above being influenced by any party.

Mr. SUTCLIFFE. Right. I wasn't questioning the influence. I was just wondering whether there was a right of appeal in this arbitration situation.

Mr. MAISONPIERRE. Excuse me. If I may also point out that which Mr. Lemmon has indicated, that about 97 percent of the cases are settled without the assistance of arbitration.

Mr. SUTCLIFFE. Is this because—why don't you suggest to me why this settlement occurs? Is this normal practice?

Mr. MAISONPIERRE. Because the companies lean over backwards and pay their policyholders, recognizing that the policyholder has already been put through a lot of misery by not—by having faced the insolvency question.

Mr. SUTCLIFFE. You mention that the right of subrogation against a policyholder is seldomly exercised in practice. We're talking about in practice now. Is this because there is seldom any significant amount of payout under the endorsement?

Mr. MAISONPIERRE. Because the significant recovery against an uninsured motorist will be meaningless, really. Motorists without protection—insurance protection—would not be able to pay the judgment, and it would cost the companies more to pursue their right of subrogation against the uninsured motorist himself.

Mr. SUTCLIFFE. What about in the insolvency situation?

Mr. MAISONPIERRE. This is the same thing.

Mr. SUTCLIFFE. The same thing?

Mr. MAISONPIERRE. This is the same thing, because again, the motorist himself has no insurance upon which he can fall back.

Mr. SUTCLIFFE. But you have a liability limit of $10,000. You wouldn't go—if you had to pay out the $10,000, the normal thing is you couldn't recover that amount from the individual?

Mr. MAISONPIERRE. It would be very difficult. It would also create a great deal of ill will.

Mr. SUTCLIFFE. We have gone through this with some of the other witnesses, and I would like just to ask you if you have any figures on your income and outgo under the UM endorsement, whether you can break out from that what the insolvency protection costs. We need these figures to determine the most efficient way of providing the American people protection against the apparently inevitable insolvency of insurance companies, particularly inevitable in light of the trend towards open competition?

Mr. MAISONPIERRE. I don't have—we do not have any figures, but let me say this: You have noted that I stayed away from the con-

troversy over the amount of insolvency. I have done this because although I strongly believe in the accuracy of the NAIC report, to the extent——

Mr. SUTCLIFFE. Which part of that report?

Mr. MAISONPIERRE. Its statistical analysis. To the extent that the NAIC itself will appear before this committee, I believe it is proper for the NAIC to justify its own figures, and not for an outsider to do so.

Assuming an annual $5 million insolvency loss, and about a hundred million policyholders of automobile, we can fairly see what the cost will be for policies. The cost would be about five million into 100 million per policy.

Mr. SUTCLIFFE. We have to be provided the $4 million figure. This is what we need, the breakout on the coverage to substantiate the $4 million figure.

Mr. MAISONPIERRE. I believe the NAIC figures are well substantiated.

Mr. SUTCLIFFE. The NAIC has not provided us with the $4 million figure breakout on UM coverage?

Mr. MAISONPIERRE. We have made no analysis of this. I could point this out. At the time the Mutual Rating Bureau, which is the rating branch of the mutual industry, voluntarily rolled on the insolvency protection to the uninsured motorist coverage, it did not add any increase to the cost of the coverage.

Mr. SUTCLIFFE. That suggests two things to me. One, in a reading of the case law, the solvency protection, because of the imposition of uninsured language of the standard endorsement, was being imposed anyway, that may be why there was no necessity for raising it.

No. 2, we would like to have from your Association, the income and outgo of uninsured motorist, because if they were able to absorb that amount of money, it suggests that there is something extremely interesting about that UM endorsement.

Mr. MAISONPIERRE. It suggests to us that the insolvency losses were so minimal in comparison to the total losses of the industry, that they could only be absorbed as part of the losses, looking in retrospect, and that the industry did not feel any factor had to be included for future losses.

Mr. SUTCLIFFE. So we could have all arguments presented, there would be one other explanation, I guess. And that would be that the losses were in existence but there was an ability to avoid payment of those losses. So just for the record, we have the three alternatives before us to evaluate, and consider, for further discussion. Because that could be the third alternative in this exchange that we have had on this point.

I would like to turn, if I could, for a moment to another matter. Under your proposed State-insolvency assessment plan, who would actually make the settlement of the claims?

Mr. MAISONPIERRE. The companies themselves.

Mr. SUTCLIFFE. The companies in the pool?

Mr. MAISONPIERRE. Yes. I might say we have an example of that going on right now. Since enactment of the post assessment legislation in California, there has been a company that has gone insolvent, and it might be desirable to indicate what happened in that case.

The company became insolvent. The pool governing committee, of course, with the approval of the commissioner, who is chairman of

the pool, requested one of the more substantial companies in California, Farmer's Exchange, to take over the handling of the claims in the name of the pool.

Mr. SUTCLIFFE. Is this large, in the sense of the business that it was writing in that State?

Mr. MAISONPIERRE. It writes a very substantial amount of business in the State. This was a small insolvency. The Farmer's Exchange has, in turn, taken over further handling of the claims against the insolvent company. Insofar as the claimants are concerned, the only difference, really, is instead of being visited by a representative of the Key Exchange, they are visited by a representative of the Farmer's Exchange.

As far as the policyholders of the company are concerned, another insurance company in California has bought out the outstanding policies of Key, and so they are continuing to be insured at no extra cost to them.

Mr. SUTCLIFFE. We will want to study that example very closely, and if you have any further information on that case, I would appreciate your bringing it to the attention of the committee.

Under the AMIA plan, would a minimizing of payouts from the assets of the insolvent insurance company minimize the possible post-assessment? Is there an incentive for the pool to settle their claims at the lowest possible rate, in order to prevent drawing upon the post-assessment situation? If so, is the consumer adequately protected in this situation, since, as you suggest, the insurance companies are in charge of this distribution?

Mr. MAISONPIERRE. The companies are in charge of distribution, but the insurance commissioner is the chairman of the pool, No. 1. No. 2, the public is protected by the present system, the court system, the law system, under which we are operating. And insofar as the public is concerned, I can see no difference, that it would be affected any differently by the pool than it would be under the present system, without a pool.

Mr. SUTCLIFFE. I have another statement from NAIC that I would like your comment on, if I may.

In the staff report, on page 217, they said this about the individual State guaranty fund approach, and they didn't distinguish between post-assessment and pre-assessment, apparently:

> The individual State guaranty approach is not aimed at solving all the problems. local and interstate, that arise between the time the company starts to weaken and, if the situation cannot be reversed, the time when the battle is lost.

The point is, it wasn't a complete solution, and we are looking for a complete solution. Do you have any comment on this?

Mr. MAISONPIERRE. I am not exactly sure what the NAIC means in its report. Under a postassessment plan, the State insurance commissioner would be under—there would be an incentive, shall we say, for the insurance commissioner, to speed up the legal ramifications, to declare a company insolvent for two reasons:

No. 1, he would want to see the claimants and policyholders protected, and the pool would come into effect only after this had been done.

No. 2, he would want to insure that the assets of the company would be protected as much as possible, and this applies particularly in a case of a potential insolvency involving questionable manipulations.

Mr. SUTCLIFFE. Let me see if I can understand the interrelationship between the UM endorsement with insolvency protection and your postassessment plan.

Suppose a man went to a company for payment under his endorsement on a $2,000 claim, but he accepted $200—he didn't want to hire a lawyer or fight, or whatever the reasons, that is not important—could that man then go to the pool for the recovery of the remaining $1,800 of his alleged claim? Could he go there again, or is he precluded from proceeding against the pool because he accepted the uninsured motorist settlement?

Mr. MAISONPIERRE. I do not understand why this man would take $200 on a $2,000 claim. If he has a $2,000 claim, and he feels he is due $2,000, he would take $2,000.

Mr. SUTCLIFFE. Let me give you one possible answer.

Perhaps in the particular area he is located, the contingent fee arrangement is so high, he is almost money ahead to take the $200. That is just one suggestion.

I really didn't mean to throw that out. Simply, if he makes a settlement, can he go against the pool for what he still thinks he is owed, or is he foreclosed?

Mr. MAISONPIERRE. The pool acts as excess over the uninsured motorist coverage.

Mr. SUTCLIFFE. But the uninsured motorist coverage is different; in other words, if he has a claim above $10,000, OK.

Mr. MAISONPIERRE. This is right.

Mr. SUTCLIFFE. But this is the claim below $10,000.

Mr. MAISONPIERRE. His claim below $10,000 is covered by the uninsured motorist protection.

Mr. SUTCLIFFE. If he has accepted the $200, could be go against the pool?

Mr. MAISONPIERRE. If he accepted the $200 settlement, he must have a weak case.

Mr. SUTCLIFFE. I want to know if under the provisions of the bill, he is prohibited from going to the pool alleging they gave me $200 and I have $1,800 more coming.

Mr. MAISONPIERRE. Under our model bill, the pool only comes in and pays where the uninsured motorist coverage does not pay, and fills the gap. We have called this a gap closure.

Where you and I seem to have some problem here, is, I happen to believe and to know that the companies are paying full value on the uninsured motorist claims.

Mr. SUTCLIFFE. The figures—they were simply to show the discrepancy. We could say he was cantankerous and he settled for $1,990 and he went to the pool for $10.

I want to know how it works.

Mr. MAISONPIERRE. Under the program, the losses would be paid by the uninsured motorist coverage. The pool would only come into play when the uninsured motorist coverage does not cover—does not legally cover—the loss.

Mr. SUTCLIFFE. Above the $10,000?

Mr. MAISONPIERRE. Above the $10,000 or property damage.

Mr. SUTCLIFFE. Fine; that answers my question, then.

How many States at the present time prohibit subrogation either against the estate of the insolvent insurer or the policyholder?

Mr. MAISONPIERRE. I do not have the exact figure, but I will be glad to furnish it.

Mr. SUTCLIFFE. Do you have an order of magnitude? Less than 10?

Mr. MAISONPIERRE. This is contained in the NAIC report, and I would be glad to furnish it to the committee.

Mr. SUTCLIFFE. Perhaps we will be able to find that out from the next witness.

Do you oppose the present riot reinsurance program for urban properties?

Mr. MAISONPIERRE. No, sir; we do not. We support the program.

Mr. SUTCLIFFE. Does your association support participation in almost a dual role with the Federal Government in that program?

Mr. MAISONPIERRE. We support State participation for a number of reasons; the most important one being that we believe that the Federal reinsurance program is highly allied to the State responsibility, keeping the law and order in the State, that the State responsibility cannot be passed on to the Federal Government.

If a State has a financial interest in the loss, it will provide better law and order in the State.

Mr. SUTCLIFFE. Is this a fair example of a duality of regulation with the State and Federal Government, or does it have absolutely no bearing on the argument that you are making about the inability or the compatibility of those two?

Mr. MAISONPIERRE. I see very little relationship here, because the Federal Government does not regulate——

Mr. SUTCLIFFE. But they are involved?

Mr. MAISONPIERRE. They are involved; but they do not regulate the industry. The power given to the Federal Government is given to the Federal Administrator.

Mr. SUTCLIFFE. Your quarrel is with the way the present FIGC bill is written; in other words, the concept doesn't bother you?

Mr. MAISONPIERRE. Yes, it does; because under the Federal reinsurance program, the Administrator has really no power over the operation of the companies. He has a certain power—he has no power over each individual State plan for that matter.

Mr. SUTCLIFFE. So, you would be willing to accept the Federal Insurance Guaranty Corporation would provide nothing but a fund to protect policyholders?

Mr. MAISONPIERRE. I would question whether such a program would be advisable, because I believe that a fund such as——

Mr. SUTCLIFFE. I would question that, too.

Mr. MAISONPIERRE. I think you need to have the power granted to the board for such a fund.

Mr. SUTCLIFFE. Can you tell us anything about the dual Federal-State involvement with the flood insurance program?

Mr. MAISONPIERRE. The flood insurance program is basically a Federal program, not a State program.

Mr. SUTCLIFFE. There is no State involvement at all?

Mr. MAISONPIERRE. There is no State money involved, and it is a Federal program, a contract between the companies and the Federal Government. It is made directly with the Federal Government.

Mr. SUTCLIFFE. And the State insurance regulator really has no interest?

Mr. MAISONPIERRE. They are not involved.

Mr. SUTCLIFFE. In your testimony, you state that the American Insurance Alliance will work for passage in 50 States of mandatory unisured motorist insolvency endorsement; is that correct?

Mr. MAISONPIERRE. Mandatory uninsured motorist endorsement with insolvency protection.

Mr. SUTCLIFFE. And a postinsolvency assessment plan in combination.

Mr. MAISONPIERRE. Right.

Mr. SUTCLIFFE. Will other segments of the industry present a united front in this approach, and if not, what are the prospects for the passage of your particular program?

Mr. MAISONPIERRE. I can't speak for the rest of the industry. Frankly, I don't know what one segment of the industry's position is on this matter.

Mr. Lemmon has indicated that his association is studying some gap-closing mechanism.

Mr. SUTCLIFFE. This is what prompted the question, because we didn't hear about the combination of the postinsolvency assessment plan in the testimony by the National Association of Independent Insurers, and I am just wondering if we are going to have three, four, or five different positions; whether or not the feasibility of approach you outlined is realistic.

Mr. MAISONPIERRE. I cannot answer for——

Mr. SUTCLIFFE. We do not want to go into the unrealistic.

Mr. MAISONPIERRE. I can't answer for the position of other insurance associations. I do know this, as you know, we proposed our model bill late in 1969; late in the 1969 legislative session.

I think we have had some rather remarkable results, to the extent that some industrial and large and important States, such as Michigan and California, have acted on this program.

We have also contacted State insurance regulators, and we have received excellent reception for our type of program, not necessarily our model bill.

The NAIC is in the process of developing draft legislation which hopefully it will present to this committee when it testifies on the 19th, which unquestionably will be presented to the full membership of the NAIC at its next meeting in December.

I believe, beginning next year, there will be a strong movement, both within the industry and by the regulators and by legislators, who are also concerned about this in the enactment of the type of legislation which we have proposed.

Mr. SUTCLIFFE. I have just one more question, and then we can all go to lunch, after Senator Hart, I am sure, finishes his questions.

You state that the changes in the UM endorsement with the insolvency provision coupled with the enactment in 50 States of a post-insolvency assessment plan would close the remaining gaps in the insurance insolvency problem area. I have a question about one gap that I fail to see how you are closing, and that is the problem of assessability.

Now, I would like to show you a chart which sort of presents the assessability problem.

(The chart referred to follows:)

CHART B.—CLAIMS AND ASSETS DATA FOR PENNSYLVANIA MUTUAL INSURANCE COMPANY INSOLVENCIES FOR WHICH COMMONWEALTH HAD TO ADVANCE MONEYS FOR INITIAL ADMINISTRATION EXPENSES (INFORMATION AS OF DEC. 31, 1968)

Company	Placed in liquidation	Claims estimated by Pennsylvania Insurance Department		Actual value of assets at liquidation date [1]	Moneys advanced by Commonwealth for initial expenses	Potential value of other assets [2]	Potential recovery from assessable Policyholders		Claims payout		Administration expenses
		Number	Amount				Number	Amount	Number	Amount	
1. Commonwealth Mutual	February 1964	1,500	$2,995,037	$829	$42,158	$5,900	100,000	[3]	0	0	$135,533
2. Empire Mutual	January 1967	1,300	5,691,428	19,860	16,202	2,131,497	118,250	[3]	1	$111	111,551
3. Home Mutual	February 1968	400	481,676	306	10,350	34,304	64,748	[3]	0	0	11,865
4. Springfield Mutual	December 1962	61	29,940	74	387	30,770	1,200	[3]	0	0	2,984
5. Sylvania Mutual	March 1967	40	140,910	0	885	84,914	3,000	[3]	0	0	885
6. Wilton Mutual	June 1966	54	43,987	28	909	27,990	4,000	[3]	0	0	2,156
7. Wissahickon Mutual	May 1966	980	2,327,216	13	9,320	188,433	13,500	[3]	0	0	18,555
Total (7)		4,335	11,710,194	21,110	80,211	2,503,808	304,698	[3]	1	111	283,299

[1] Cash, bonds, and other securities.
[2] Agents premium balances outstanding, reinsurance recoverables, and other receivables.
[3] Data not available.

Source: Pennsylvania Department of Insurance at Feb. 4, 1969, to Senate Antitrust and Monopoly Subcommittee questionnaire of June 6, 1968.

Mr. SUTCLIFFE. This describes the assessability problem in the Commonwealth of Pennsylvania during selective years for which we had information. It indicates there were 304,898 policyholders from seven different assessable mutuals faced with assessments and $11.7 million in claims.

Today, only $111 have been paid. All assets of the companies have gone to administrative expenses and I believe the Commonwealth of Pennsylvania has had to advance over $80,000 for claims of administration up to this time.

It appears that there is significant exposure to the members of policyholders for these assessable mutuals.

I would simply like you to explain how your proposals will close the gap of the assessability or the assessable mutual problem.

Mr. MAISONPIERRE. We recognize that there is this gap. We are working on this.

I might say legislation was enacted in Illinois at the last session, which provides for relief of assessability to the extent that no assessment would be collected against any policyholder if the assessment is less than $500.

Our problem here, of course, is we need to recognize one thing, that assessable mutual companies do fulfill a very desirable role in the economy of the State. These are generally small county mutual companies, and many of them are very sound companies. It would be one thing to say that no policyholders can be assessed after insolvency has been declared. We think this would destroy, probably, the basic integrity of these companies. They would probably have to go out of existence, and we recognize they fulfill a very important role.

The Illinois approach is a good approach. We have endorsed it in Illinois. We are going to be assessing in greater detail, the effect of such an approach on assessable mutuals that have become insolvent in the past, and the effect on policyholders.

If we believe the Illinois approach will protect the policyholder, we will wholeheartedly endorse this program.

If this program does not work, we will seek out another program.

Senator HART. Thank you very much.

I want to thank all of the witnesses for being patient with the kind of schedule that we had to follow.

We will adjourn to resume at 10 o'clock in the morning of the 19th.

(Whereupon, at 1:25 p.m. the committee was adjourned to resume on November 19, 1969.)

FEDERAL INSURANCE GUARANTY CORPORATION

WEDNESDAY, NOVEMBER 19, 1969

U.S. SENATE,
COMMITTEE ON COMMERCE,
Washington, D.C.

The committee met, pursuant to recess, at 10 a.m. in room 5110, New Senate Office Building, Hon. Philip A. Hart presiding.

Present: Senators Hart, Moss, and Baker.

Senator HART. The committee will be in order.

Today we resume hearings on S. 2236, a bill to create a Federal Insurance Guaranty Corporation. This bill is intended to protect people who, without such protection, would suffer when property and casualty insurance companies become insolvent.

Such protection would be afforded through a national guaranty fund which indemnifies policyholders and claimants. The bill would provide also public protection by assisting States in their examination for solvency, and hence reduce the incidents of insolvency.

Last week, I think the hearings left unresolved many issues. The committee is still uncertain about the efficacy of alternative proposals for remedying insolvency problems.

For example, do uninsured motorist endorsements containing provisions reduce significantly insolvency losses? If so, at what cost to the consumer?

Would 50 State post-insolvency assessment plans successfully pick up those people not covered by the uninsured motorist coverage? At what cost? Why, as is suggested, is it inevitable that S. 2236 will lead to Federal regulation? Should the bill combine a pre- and post-assessment approach?

These are just some of the issues on which we would like to have comment and which I think remain unresolved. We will begin the hearings today with testimony from the American Insurance Association, then from the National Association of Insurance Commissioners, and we will close today, hearing from the National Association of Mutual Insurance Agents.

I anticipate the pleasure of receiving the testimony from all of our witnesses. I hope the committee will have a deeper insight into the insolvency problem and the role Federal legislation can play in meeting the problem.

I welcome the president of the American Insurance Corp., Mr. T. Lawrence Jones, who is accompanied by Mel Stark, the manager of the Washington office of AIA, and Robert N. Gilmore, associate general counsel.

STATEMENT OF T. LAWRENCE JONES, PRESIDENT, AMERICAN INSURANCE ASSOCIATION; ACCOMPANIED BY MELVIN L. STARK, MANAGER, AIA WASHINGTON OFFICE, AND ROBERT N. GILMORE, ASSOCIATE GENERAL COUNSEL

Mr. JONES. May I say at the outset that we have had a group in our Association working on this problem for over 4 years. I say that with deference because we are aware that the chairman has been working on the problem longer than that, and probably much of your early work was what stimulated our early work, but if I can proceed through the whole of our statement, it details this 4½-year work. At the outset I will say to the chairman that our conclusion is, we support this legislation as a preferable solution to a very difficult problem and urge its enactment.

My name is T. Lawrence Jones and I am president of American Insurance Association, an organization of insurance companies writing all kinds of property and casualty insurance throughout this country.

Our member companies have a premium volume of over $7 billion. We are pleased to have this opportunity to appear before the Senate Commerce Committee to present our views on the general problem of insurance company insolvency, and more particularly, on S. 2236.

This bill, introduced by Senator Magnuson and cosponsored by Senators Dodd, Hart, Hollings, Inouye, Moss, and Pastore, would create a Federal Insurance Guaranty Corporation for the purpose of protecting the American public against insurance company insolvencies.

Public officials, legislators and the insurance industry itself have been concerned with the problem of insurance company solvency for many years. As could be expected, the intensity of concern has varied substantially as the number of company insolvencies rose and fell and as reports of insurance company liquidations increased and decreased.

Regardless of the understandable ups and downs of public concern, American Insurance Association is convinced that there is a real problem to which a solution must be found.

Some years ago the insurance industry held to the position that all measures by which insurance companies collectively helped, in one way or another, to defray the losses of insolvent insurance companies were unsound.

It was argued that these measures put weak companies on a parity with strong ones and tolerated, if not encouraged, bad management. It was further argued that these plans removed incentives on the part of agents and brokers to be sure that they were placing their business with responsible and reputable insurance companies.

We cannot disagree with the logic of these arguments, but times have changed. Today, such arguments are outweighed by social considerations and we believe the prime consideration is that the public must be protected in the event of an insurance company insolvency.

In addition, the nagging insolvency problem damages the industry as a whole and each company suffers in public esteem.

There has been considerable debate as to the size of the problem. Some have endeavored to treat it as *de minimis*. It is our view that the figures should speak for themselves, but in any event we have concluded that one insurance company insolvency is one too many, especially if there is no way to reimburse the victims of that insolvency.

The only question open for discussion, in our judgment, is what solution will best serve the public interest.

American Insurance Association has been seeking the best solution over a period of years and with renewed intensity since the introduction in January 1967 of S. 688, providing for a Federal Motor Vehicle Insurance Guaranty Corporation.

Until recently the discussion has centered on automoble insurance. In fact, the earlier bills, such as S. 688, would have provided protection only against the insolvency of automobile insurers. The focus on automobile insurance suggested to some the desirability of expanding the uninsured motorist coverage specifically, to include insurance company insolvencies.

All States except Maryland and North Dakota, now have mandatory uninsured motorist laws. Most of these laws are specifically applicable in cases where the insurer is insolvent but, even in those States where the law is silent as to coverage in case of insurer insolvency, there is a strong likelihood that the laws would be construed to apply.

In fact, practically all auto insurers today have voluntarily included provisions in their uninsured motorist coverage making the coverage specifically applicable to insolvencies.

American Insurance Association has never regarded the uninsured motorist endorsement with coverage for insolvency as either an adequate or effective answer to insurance company insolvencies.

These uninsured motorist laws are confined to automobile insurance and therefore do not provide protection to other claimants and policyholders who may be the victims of an insurer insolvency.

Even in the area of automobile accidents they do not protect the noncar-owning pedestrian who has the misfortune of being injured by a motorist whose insurance company has become insolvent.

The uninsured motorist insolvency coverage is an obvious example of placing the financial burden of insurance company insolvency where it does not belong. It is not a valid solution and we doubt whether anyone today will seriously contend otherwise.

A number of States have endeavored to meet the problem by the enactment of laws providing for State security or insolvency funds. These laws were originally enacted to protect employees under State workmen's compensation laws.

Most of these laws were enacted during the 1930 depression years. Legislators were concerned that workers injured in industrial accidents might find their workmen's compensation benefits endangered by insurance company insolvencies.

Most of these workmen's compensation security funds were of the preinsolvency assessment type—for example they required the collection of funds by assessing insurers prior to a insolvency.

Two of them—Maryland and Minnesota—are post-assessment insolvency funds, which means insurers are assessed only after the insolvency has occurred.

The security-fund solution for automobile liability insurance companies was first enacted by the State of New York in 1947. This law, Section 333 of the New York Insurance Law, was amended in 1969 to make the New York security fund applicable to all property and casualty lines other than workmen's compensation which continues to have its own security fund law.

In the 1950's Maryland and New Jersey enacted automobile liability insurance security fund laws of the preinsolvency assessment type. In subsequent years, some State legislatures, from time to time, considered insolvency fund legislation but no additional States enacted these laws until the renewed interest this year when California, Michigan, New Hampshire and Wisconsin enacted post-insolvency assessment laws and, as noted above, New York expanded its law to cover other property and casualty lines.

In addition, New York has also placed a much needed ceiling of $200 million on the fund. This year Maryland amended its law to make the fund applicable to automobile physical damage insurance.

This renewed interest in State insolvency fund legislation has been caused by a recent flurry of insolvencies, some of which have been widely publicized.

In addition, the introduction of legislation in Congress, patterned after the Federal Deposit Insurance Corporation Act with strong support in both the Senate and House of Representatives, has rekindled interest in legislation at the State level.

The position of American Insurance Association on State preinsolvency assessment funds and State postinsolvency assessment funds is clearcut. Neither, in our judgment, provides a sound solution to the problems and we do not think the public interest is well served by such legislation.

The preinsolvency assessment type of law creates a fund in anticipation of some possible future insolvency. The proliferation of such funds in each of the 50 States to protect policyholders and claimants from insolvencies in a business which is transacted across State lines would be difficult to justify from the standpoint of efficient and sound public administration.

In the years following the Southeastern Underwriters Association decision by the U.S. Supreme Court in 1944, it was recognized that a sure way to encourage Federal action would be for a number of States to enact preinsolvency security fund laws.

It did not make sense then, and it makes no sense today, to have 50 States amassing such funds, administering them and making payments to claimants and policyholders. If one accepts the hypothesis that preinsolvency funding is more effective and equitable than post-insolvency laws, then clearly one fund is preferable to the establishment of 50 funds.

There is valid concern that these State preinsolvency funds which tend to reach amounts far in excess of foreseeable needs will be diverted to other purposes. This fear has been ridiculed by some public officials, but the plain fact is that such diversion has happened in the past few years. Twice, the New Jersey Automobile Security Fund moneys have been diverted into the New Jersey Claim and Unsatisfied Judgement Fund. So this is not a fanciful fear; it is a real possibility.

A major weakness in the State preinsolvency fund legislation is that it is solely a "bail-out" remedy. It does absolutely nothing to bolster and strengthen regulatory procedures in order to prevent insolvencies. Some have even suggested that these preinsolvency funds may accelerate the number of insolvencies because State regulatory authorities may become complacent and less diligent in exercising their supervisory functions, knowing that the funds will take care of policy-

holders and claimants. We disagree with that view. There are far too many other discomforting consequences which will beset an insurance commissioner in the event of an insolvency—including market restrictions, loss of jobs, loss of tax revenue and all the other heartaches associated with a liquidation proceeding. While regulatory bodies will not relax their vigilance in regulating to preserve solvency, these security fund laws in no way help to prevent insolvencies. The industry has long held the view, and I believe it does today, that any solution to the insolvency problem which provides financial assistance to policyholders and claimants must be accompanied by additional affirmative regulatory procedures to prevent insolvencies. American Insurance Association still holds to that proposition.

The postinsolvency assessment law avoids, or at least lessens, some of the defects inherent in preinsolvency assessment fund laws. Large sums are not accumulated and thus do not remain idle and unproductive long before they are needed. Also, since no funds are accumulated, there is no enticing opportunity for diversion to other purposes. However, like the preinsolvency laws, postinsolvency assessment laws do not make any sound and workable contribution to the prevention of insolvency.

The postinsolvency assessment plan has other serious defects. It exposes insurers to unknown liabilities which could occur at a time when they might be least able to sustain such additional liabilities, even though there are annual limitations on assessments.

There is no way the postinsolvency assessment plan can soften the patent inequity of placing the total economic burden on solvent and well-managed insurers. The postinsolvency law, as we have noted, does nothing to prevent insolvencies and then compounds this inadequacy by making the strong and reputable companies pay for the sins of the mismanaged and weak, including a number whose management might have engaged in highly questionable, if not at times clearly fradulent, practices.

The postinsolvency assessment concept is embodied in model State legislation being proposed by the American Mutual Insurance Alliance. The AMIA model bill, as we understand it, places some regulatory power in an insolvency board composed of the insurance commissioner and representatives of insurance companies, thereby recognizing that something more than a financial rescue is needed. Whether it is a proper responsibility for the private sector to become involved in this kind of industry policing, is debatable. It is noteworthy that up to the present time, no postinsolvency assessment law has bestowed any such authority on insurance companies.

I note, parenthetically, that there are three laws that provide that an industry group is in the position to make reports and recommendations, but certainly this is not the power to examine, or to take action against another company, and it would not be what we would call policing, or not what we would call a workable contribution toward preventing insolvency.

Summarizing our views on State security fund laws, American Insurance Association is completely opposed to a solution which would establish security funds in each State by means of an annual assessment on insurers. We are also opposed to the postinsolvency assessment plan although we recognize that it is probably the least objectionable

remedy available at the State level. An additional reason that these State postinsolvency assessment laws are less objectionable than some of the other State proposals, is that they can be effectively meshed into a national solution should a national plan prove to be the ultimate answer.

Since the American Insurance Association companies have recognized the shortcomings of the conventional State-oriented solutions, we have explored alternatives to the Federal Deposit Insurance Corporation approach in order to see if we could develop a national plan which could be administered largely, if not solely, by the industry.

In this phase of our work, we were guided by the following basic criteria:

1. Any such plan must provide additional safeguards to prevent insolvencies; bailout alone would be unacceptable.
2. It should include a private guaranty facility, national in scope.
3. In order to avoid further echelons of regulation, the role of State and Federal regulation should be as little as legally possible.
4. All insurers should be compelled or strongly induced to participate in the facility.

Within the context of these criteria, we studied the concept of a private facility along the lines of the National Association of Securities Dealers which is authorized by the 1938 amendments to the Securities Exchange Commission Act of 1934 to regulate over-the-counter brokers. Such a plan would have contemplated one or more private facilities guaranteeing the policies of its members. All insurers would be required to belong to a facility which would have certain examination powers over its members.

In the course of our study of this proposal we were advised by counsel that a purely private facility without Federal legislation could present problems. It was recommended to us that it might be necessary to have some Federal supervisory power over the private facility and that members of the facility should have the right to appeal the action of the facility to the supervising Federal body. It was further suggested that it might be necessary to have some exemption from the Federal antitrust laws. Part of the reasoning for this suggestion was that the activities of the facility would include the policing of the insurers and this could be construed to constitute, "boycott, coercion and intimidation" which are expressly excluded from the scope of the exemption contained in the McCarran-Ferguson Act.

If it were necessary to obtain Federal legislation to permit the operation of a private insurance guarantee facility, three practical questions had to be answered.

1. Could we reasonably anticipate that the Congress would favorably consider legislation authorizing a private facility to exercise a policing function, albeit a limited one?
2. Would the Congress be likely to expand the present antitrust exemption even for such a worthy purpose as providing policyholder and claimant security against insolvencies?
3. Against the background of the highly successful Federal Deposit Insurance Corporation Act, is there any reasonable likelihood that the Congress would consider a different approach in the insurance area?

We have endeavored to analyze realistically and objectively these

three questions and have concluded that they must be answered in the negative.

One other consideration has affected our view of the private facility approach. Some of our member companies do not believe that private insurers should become involved in the policing of their competitors. Even if there were no Federal legislative problems, they would be opposed to a private facility with policing powers. Additionally, we should reiterate that American Insurance Association is opposed to any solution which does not make a workable contribution to the prevention of insolvencies.

Although we have concluded that the private facility approach is not feasible, if we could be convinced that it did not necessitate far-reaching Federal legislation, we would be willing to reexamine our position. The one caveat would be the practicality and propriety of any device requiring competitors to police one another.

We have examined other variations of the private facility approach, including the private insurance guarantee corporation proposal outlined in the June 16, 1969 automobile insurance study background memorandum, prepared by the staff of the National Association of Insurance Commissioners' Central Office for consideration by the NAIC Special Committee on Automobile Insurance Problems.

We believe that our comments with respect to a private facility suggested by present regulation of over-the-counter brokers by National Association of Securities Dealers is applicable to the proposal suggested by staff of the NAIC central office.

The Economic Regulation Advisory Committee to the Department of Transportation Auto Insurance and Compensation Study under date of July 8, 1969, submitted a report to the Department of Transportation on S. 2236. This advisory committee suggested its own proposal in lieu of S. 2236. Their plan would provide for the enactment by the Congress of a law providing for the imposition of a "substantial Federal general revenue tax on insurance premiums derived within each State." It would further provide that the tax be forgiven in full as to States which have in effect an insolvency guarantee law meeting certain criteria specified in the Federal law. The purpose of this proposal is to apply maximum pressure on "State legislatures and regulators to have adequate legal requirements and adequate administrative supervision of insurers." The proposal contemplates the possibility of State enactment of insolvency fund laws similar to the New York law or a postinsolvency assessment law such as those enacted in four States this year.

This plan has all the weaknesses of the State insolvency measures and it is hard to see what it does to improve State regulatory machinery to prevent insolvencies.

We have great respect for the members of this advisory committee, but we cannot convince ourselves that a tax threat proposal of this sort is a workable solution.

We come now to S. 2236, the consideration of which is the reason for the hearings of your committee.

S. 2236 is patterned on the highly successful Federal legislation establishing the Federal Deposit Insurance Corporation which insures

the deposits of all its member banks. The bill establishes a corporation to be known as the Federal Insurance Guaranty Corporation, to which practically all insurers are required to belong. Only a small number of insurers would not be required to join since very few companies are not in one way or another engaged in interstate commerce.

Each insurer would pay an annual fee equal to one-eighth of 1 percent of its net direct premiums. These fees would be continued only to the extent it would be necessary to keep the net asset value of the fund at an amount not less than 2 percent of the annual direct premiums written by all participating insurers. Before this cutoff, the corporation would have to retire the outstanding Treasury shares amounting to $50 million, which supply the initial financing.

The FIGC would be empowered to settle or adjust any claim against an insolvent member insurer. Claims for return premiums would not be allowed in excess of 50 percent of unearned premiums. The bill would require claimants to exhaust their claims against State insolvency funds before receiving payments from FIGC. No further fees or assessments under any State insolvency laws would be permitted for any period during which the insurance policies or that insurer are guaranteed under this legislation.

In the case of insolvency protection under the uninsured motorist endorsement, a policyholder would first have to exhaust his remedies against any applicable State insolvency fund and then against the Federal Insurance Guaranty Corporation before receiving any payment from his insurer.

It is clear, therefore, that the bill seeks to establish a single program for providing payments to those who have claims against an insolvent insurance company.

The bill grants broad examination powers to the corporation. All such examinations are required to be coordinated as far as practicable with appropriate State supervisory authorities and the National Association of Insurance Commissioners. It authorizes the corporation to terminate the guaranteed status of an insurer if it finds:

1. That the insurer is engaging in unsafe or unsound practices;
2. The insurer is in unsafe or unsound condition, or
3. The insurer has violated this law or any rule or regulation issued under it.

The Corporation also has power to bring cease-and-desist proceedings if it believes an insurer is engaging in unsafe or unsound practice or is violating the law.

American Insurance Association, as previously stated, recognizes that a problem exists and a solution must be found. We have shared with this committee our analysis and conclusions with respect to the various proposals which are under consideration. It is our view that S. 2236, patterned after the Federal Deposit Insurance Corporation Act, is clearly preferable to all other proposals and we endorse this legislation.

It should be noted that S. 2236 provides a sure way to protect members of the public against the possibility of insurance company insolvency. It also prohibits the proliferation of State insolvency funds which, in our judgment, is a totally unacceptable solution. Finally,

unlike all the other solutions under discussion, S. 2236 strengthens the regulatory process. It should prove to be especially helpful in preventing the interstate shifting of company assets, which has been beyond the reach of State regulatory power and which has been such a significant factor in a number of insolvencies.

We disagree with those who contend that this legislation portends the end of State regulation or that it diminishes the important role of State regulation. On the contrary, we believe it complements and supplements State supervision. It will, in fact, strengthen State regulation by removing a long-standing source of criticism.

We have reached our decision supporting S. 2236 only after the most careful study. We are well aware that in varying degree, a number of segments of the industry are opposed to this legislation. We also know that the National Association of Insurance Commissioners has adopted a resolution against this legislation. Our decision to support this bill reflects our considered judgment that the FDIC approach offers the most effective and workable solution to the insolvency problem of a business which is extensively transacted across State lines.

(The attachments follow:)

MANDATORY UNINSURED MOTORIST PROVISIONS (COMPILED BY THE LAW DEPARTMENT OF THE AMERICAN INSURANCE ASSOCIATION), OCTOBER 1969

State	Limits (thousands of dollars)	Property damage exclusion	May insured reject coverage?	Uninsured motorist fee	Applicable where insurer insolvent?	Unusual features
Alabama	10/20		Yes [1]	None	No provision	
Alaska	15/30		do	do	do	
Arizona	10/20		do [1]	do	do	
Arkansas	10/20		do	do	Yes	
California	15/30		do	do	do	(b)(h).
Colorado	[2] 15/30		do [1]	do	No provision	
Connecticut	(a)20/20		No	do	Yes	(n).
Delaware	10/20		Yes [1]	do	do	
Florida	10/20		do [1]	do	do	
Georgia	(m)10/20	$250	do [1]	do	do	(e)(h)(j).
Hawaii	10/20		do	do	No provision	
Idaho	10/20		do [1]	do	Yes	
Illinois	10/20		No	do	do	
Indiana	10/20		Yes [1]	do	do	
Iowa	10/20		do [1]	do	do	(j).
Kansas	10/20		do [1]	do	do	(n).
Kentucky	10/20		do [1]	do	do	(h)(q).
Louisiana	5/10		do	do	do	(n).
Maine	20/40		No	do	do	
Massachusetts	5/10		do	do	do	
Michigan	10/20		Yes [1]	$35	do	(o).
Minnesota	(u)10/20		(p)	None	do	
Mississippi	5/10		Yes [1]	do	do	(e)(j).
Missouri	10/20		do [1]	do	do	
Montana	10/20		do [1]	do	No provision	
Nebraska	10/20		do [1]	do	Yes	
Nevada	15/30		do [1]	do	do	(e)(h)(j)(q)
New Hampshire	[2] (a)15/30		No	do	do	
New Jersey	10/20	100	Yes [3]	do	No provision	
New Mexico	10/20/5	250	do [1]	do	do	
New York	10/20		No	do	do	(h).
North Carolina	(k)10/20/5	100	Yes	do	Yes	(g)(k).
Ohio	[2] 12. 5/25		do [1]	do	No provision	
Oklahoma	(r)5/10		do [1]	do	Yes	(s)(t).
Oregon	10/20		No	do	do	(c)(h).
Pennsylvania	10/20		do	do	do	
Rhode Island	10/20		Yes	do	No provision	
South Carolina	10/20/5	200	No	$50 maximum [4]	Yes	(d) (e) (f) (g) (h) (j).
South Dakota	10/20		Yes [1]	None	do	
Tennessee	10/20		do [1]	do	do	(e) (q).
Texas	10/20		do [1]	do	do	
Utah	10/20		do [1]	do	No provision	
Vermont	10/20		No	do	Yes	
Virginia	[3] (a)20/30/5	200	do	$50 [4]	No provision	(e)(g)(h).
Washington	15/30		Yes [1]	None	Yes	
West Virginia	10/20/5	300	No	do	do	(e)(j).
Wisconsin	(r)10/20		Yes [1]	do	do	
Wyoming	10/20		do [1]	do	do	

[1] If rejected, insurer need not offer coverage on renewal unless requested.
[2] Effective Jan. 1, 1970.
[3] Insured must elect to accept or reject offer of coverage in writing.
[4] Fund distributed to insurers after deduction of administration expense.
(a) Insured may require limits equal to his liability limits.
(b) Failure to file evidence of financial responsibility under financial responsibility law creates rebuttable presumption that vehicle was uninsured.
(c) Coverage not required in policy covering trucks of combined weight and load capacity of more than 6,000 operated by employees covered by workmen's compensation.
(d) No charge to be made for coverage.
(e) Arbitration provision prohibited.
(f) Insurer must give notice of termination of policy.
(g) Insurer may defend uninsured motorist.
(h) Also covers cases where insurer denies liability.
(j) Requires contact in hit-and-run cases.
(k) Person who carries liability limits of at least 15/30 is entitled to 15/30 coverage.
(m) Insured vehicle and contents only.
(n) Arbitration optional with insured.
(o) All policies to contain notice that coverage was explained and that insured may reject.
(p) Coverage may not be rejected for policies covering private passenger vehicles or pickup trucks. May be rejected as to others.
(q) "Uninsured motor vehicle" includes vehicle insured in lower limits.
(r) Insurer may make higher limits available.
(s) If agreement by arbitration is not reached within 3 months from demand for arbitration, insured may sue tort feasor
(t) Inapplicable to motor carriers whose drivers are covered by workmen's compensation.
(u) After 1970 insured may require limits equal to his liability limits.
Note. Copyright 1969 American Insurance Association.

WORKMEN'S COMPENSATION SECURITY FUNDS

Arizona.—Uninsured Employers and 2nd Injury Special Fund.—§ 23–1065, Revised Statutes—Fund is maintained by a tax not to exceed 2% of premiums; also in no-dependency death cases, carriers shall pay $1,150 into fund. § 23–907B authorizes payments out of special fund plus a 10% penalty on employer.

Connecticut.—2nd Injury & Compensation Assurance Fund—§§ 31–354 and 31–355–Gen. Stats.—1% of compensation paid during preceding year with payments to cease when fund reaches $100,000 and to be resumed when it falls below $100,000.

Maryland.—§§ 85–89, Art. 101, Maryland Code-Post-insolvency assessment, pro-rata, upon all insurers not to exceed 1% of workmen's compensation premiums written during preceding calendar year.

Minnesota.—§§ 79–28, 79–29, Minn. Stat. 1965. Assessment of other carriers for the payment of unpaid workmen's compensation awards of insolvent company. Pro-rata assessment in any one year in no case to exceed 1% of workmen's compensation premiums written during the preceding calendar year.

New Jersey.—Sec. 34:15–103 ff. Revised Statutes of 1937. 1% of net written premiums payable bi-annually until fund, over and above liabilities, equals 5% of workmen's compensation loss reserves of all stock carriers as of December 31 next preceding; payments to be resumed when said fund falls below this figure.

New York.—Art. 6–A (§§ 106–109) of Workmen's Compensation Law. One percent of net written premiums payable until fund, less liabilities, equals 5% of New York Workmen's Compensation loss reserves of all stock carriers as of December 31 next preceding, or equals $2,300,000, whichever sum is greater. Payments are resumed when fund is reduced below this amount. Payments to be made quarterly.

North Carolina.—Art. 3, Chap. 97, §§ 97–105–97–117, Gen. Stats. One percent of net written premiums payable bi-annually until fund over and above liabilities equals 5% of workmen's compensation loss reserves of all stock carriers as of December 31 next preceding; payments to be resumed when said fund falls below this figure.

Oregon.—Direct Responsibility Employer's Adjustment Reserve § 656.614, Oregon Rev. Stats.-Pro-rata assessment upon (DRE) employers sufficient to pay unpaid claims because of insolvency of surety or guarantor of employer.

Pennsylvania.—Act No. 470, Laws of 1937. One percent of net written premiums payable annually until fund, over and above liabilities, equals 5% of workmen's compensation loss reserves of stock carriers as of June 30 next preceding. Payments are to be resumed when the fund falls below this amount.

United States Longshoremen's and Harbor Worker's Act.—Special Fund—§§ 18 (b) and 44—$1,000 paid into Fund by employer in each no-dependency death case.

Wisconsin.—Workmen's Compensation Law, Sec. 102.65. One percent of earned premiums payable annually until fund, over and above liabilities equals 5% of the loss reserves of all stock carriers for the payment of benefits under said section as of December 31 next preceding. Payments are to be resumed when fund falls below this amount. Payments into stock fund are not to be discontinued unless said fund consists of at least $25,000 over and above its known liabilities. This fund has now been consolidated with the mutual and reciprocal funds and transformed into a temporary fund for payment of assessments into the newly created post assessment Insurance Security Fund which has broad coverage, including workmen's compensation (S. B. 525) Chapter 144, Laws of 1969.

BROAD GUARANTEE PROVISION'S INCLUDING WORKMEN'S COMPENSATION

California.—Act 14.2 Sec. 1063 ff. of the Insurance Code. Provides for creation of California Insurance Guarantee Association to which all insurers, with certain exceptions life, title, etc. must belong. Workmen's compensation writers included as a separate category. Post insolvency assessment limited to 1% of net direct premium written in particular category (Chapter 1347, Laws of 1969, effective August 31, 1969).

Michigan.—Secs. 7833 and 7901 ff. (compiled Laws of 1948, added by Act No. 277, Laws of 1969) creates Property and Casualty Guaranty Association to which all insurers, except life, must belong. Workmen's compensation writers included as a separate category. Post insolvency assessment limited to 1% net direct premium written in previous calendar year in particular category.

Wisconsin.—Described above.

INSOLVENCY FUND LEGISLATION AS OF NOV. 7, 1969

State	Bill No.	Brief summary	Status
California	House 1310	Creates the Insurance Guarantee Association, which will assess all insurers other than life or title; post-assessment, maximum 1 percent in year.	Law.
Florida	Senate 920	Would have created security funds for casualty, property, surety and workmen's compensation insurance, preassessment.	Died.
	Senate 1523	Would have required insurers to pay 1 percent of premiums on postassessment basis where insurer is insolvent, to defray losses to claimants.	Do.
Maryland	Senate 199	Makes the Motor Vehicle Liability Security Fund applicable to physical damage.	Law.
Michigan	House 3166	Would create the Property and Casualty Insurance Insolvency Fund, which would assess upon insurers the amount needed to pay for transfer by reinsurance or coinsurance of all policies in force on residents, and for cost of adjustment and payment of claims, postassessment.	No action.
	House 3216	Would create the Michigan Casualty Assessment Association consisting of all insurers writing automobile and workmen's compensation insurance; the association to assume obligations of any casualty insurer declared insolvent; postassessment, maximum 1 percent in year.	Do.
	House 3699	Creates an insolvency pool, and requires all insurers writing casualty, property, and workmen's compensation insurance to assume obligations of insurer declared insolvent; postassessment, maximum 1 percent in year.	Law.
New Hampshire	House 668	Creates the New Hampshire Automobile Assessment Association to which all automobile insurers must belong. Upon determination that an insurer is insolvent, the insurance commissioner shall assess all members of the association for payment of all bodily injury liability, property damage liability, medical payments, uninsured motorists, auto physical damage claims, and claims for unearned premiums.	Do.
New York	Senate 3534	Broadens the Motor Vehicle Liability Security Fund to cover all property liability lines, payments to cease when fund reaches $200,000,000.	Do.
Wisconsin	Senate 525	Creates a security fund; postassessment, maximum 2 percent in year.	Do.
U.S. Congress	H.R. 1087	Creates the Federal Motor Vehicle Insurance Guaranty Corp., based on the Federal Deposit Insurance Corporation Act.	No action.
	H.R. 1376	do	Do.
	H.R. 2656	do	Do.
	H.R. 3671	do	Do.
	H.R. 6475	do	Do.
	S. 2236	Would create the Federal Insurance Guaranty Corp., applicable to all lines other than life, accident, and health and title, preassessment.	Heqrings scheduled for Nov. 12, 19, and 20.
	H.R. 13428	do	No action.

PROPERTY AND LIABILITY SECURITY FUNDS

California.—California Insurance Guaranty Association to which all insurers, except those writing exclusively surety, credit, ocean, marine, life, title and certain other lines, must belong for purpose of providing each member with insolvency insurance. Post assessment, not more than 1% of net direct premium written in category (compensation, auto, other) in the State (Chapter 1347, Laws of 1969).

Maryland.—Motor Vehicle Security Fund—for payment of allowed claims of injured parties and policyholders arising out of motor vehicle accidents by reason of insolvency or inability of insurer to meet its insurance obligations. Preassessment ¼ of 1% net direct written auto liability and physical damage premiums. (§ 482A of Art. 48A, Annotated Code of Maryland)

Michigan.—Property & Casualty Guaranty Association maintained by all authorized insurers, except life, which shall discharge obligations of insolvent insurers arising out of contracts issued or payable to residents. Policy contracts covered: Auto insurance, workmen's compensation, basic property insurance, homeowners, farm owners and commercial multiple peril. Post-assessment not to exceed 1% of net direct premiums during previous calendar year. (Act 277, Acts of 1969)

New Hampshire.—Auto Assessment Association to which all auto insurers are required to belong. Post insolvency assessment for payment to residents of bodily injury liability, property damage, medical payments, U.M., physical damage and claims for unearned premiums. Maximum assessment in any calendar year shall not exceed 3% of total amount of all net direct premiums written by all licensed auto insurers having such business in the State in said calendar year. (Chapter 349, Laws of 1969, effective June 30, 1969)

New Jersey.—Motor Vehicle Liability Security Fund for purpose of securing the benefits under policies of motor vehicle liability insurance by reason of the default of an insurer which becomes insolvent—½% of direct gross motor vehicle premiums; ceases when net value of Fund reaches $6,000,000; resumes when Fund falls below such amount. (§§ 39:6–92—39:6–104 NJSA)

New York.—Property & Liability Insurance Security Fund to be used in payment of allowed claims of residents by reason of the inability due to insolvency of an authorized insurer to meet its insurance obligations under generally all property and liability lines. Pre-assessment: 1% net direct written premiums until Fund reaches $200,000,000. (§ 334 N.Y. Insurance Law, as amended by Chapter 189, Laws of 1969)

Wisconsin.—Wisconsin Insurance Security Fund—Applicable generally to all lines. Fund divided into three separate accounts, life, disability and all other covered insurance, for purpose of paying claims of residents arising out of policy issued by authorized insurer and which claim has been approved in the liquidation of the insurer issuing the policy. Post assessment, maximum 2% of the assessable premiums (Chapter 144, Laws of 1969, effective 8/22/69)

Senator HART. Thank you very much, Mr. Jones. Shortly after you began your statement, we were joined by the distinguished Senator from Utah, Mr. Moss, and by the able Senator from Tennessee, Mr. Baker. Mr. Baker has had to go to the floor in connection with the judicial nomination, and hopes to be back later.

Mr. JONES. I am glad to see Senator Moss again.

Senator HART. There is no need to tell you that your conclusion is encouraging to those of us who propose this particular bill; and unlike those of us who introduced the bill you speak from a background of knowledge.

As you outlined the stages you went through in reaching the conclusion that a Federal system such as the bill proposes is best, I was impressed, and I think the readers of the Record will be, of your identification of the other alternatives and your analysis of them.

I just have a couple of questions. One would be to ask your judgment on the basic question, a question to which you make reference in the very opening portion of your testimony, just how much money has the American consumer lost by reason of insurance company insolvency? Does your association—we have had various estimates of losses—does your association have a figure based upon your research?

Mr. JONES. Yes, Senator, we do. It is in working paper form. I don't have it with me. I could furnish it to you later.

Senator HART. If you will provide for the record the estimate you make as to the losses caused by insurance company insolvency.

Mr. JONES. I think we could give you at this time some of the figures from memory from those working papers, if you would be interested in them.

Senator HART. Yes, and if they need to be corrected, will you do it?

Mr. STARK. We would be glad, as Mr. Jones said, to supply a more definite working paper. The figures we have seen that accompany the estimate of loss with respect to the proposal that S. 2236 involves itself with, are significant. We think the figure of $200 million does, in a round sum, represent a reasonable and conservative figure as to what was actually lost in the last 10 years.

We believe it is difficult to pinpoint this; there are a number of elements involved. What did the individual actually lose by virtue of an insolvency? One of the great imponderables is that you cannot define this when the seizure of assets take place by virtue of liquidation and there is a fractional amount of money to be distributed. There is a tremendous discounting going on in the effort to liquidate, so that many claims that have a reasonable value take a certain level which in the context of a solvent insurer settling those claims would have a value of x dollars and finally wind up with an x minus figure. I think this has to be taken into account to reach some estimate of what the loss actually was, not what was paid out. This is a development we will try to address ourselves to and bring the committee more information on at a later date.

Senator HART. We would appreciate for the record receipt of your analysis on this question. I am sure it will be useful.

(The information requested follows:)

ANALYSIS OF LOSSES TO THE AMERICAN PUBLIC FROM PROPERTY-CASUALTY INSURER INSOLVENCIES 1958–69

I

In the quarter-century since the passage of the McCarran-Ferguson Act of 1945, 224 property and casualty insurance companies have become insolvent.[1] Some 135 of these insolvencies have occurred during the 12 years beginning in 1958, as the following table shows:[2]

Year:	*Number of insolvencies*	Year—Continued	
1958	5	1965	22
1959	4	1966	15
1960	6	1967	19
1961	8	1968	4
1962	19	1969	4
1963	10		
1964	19	Total	135

II

Before turning to an aggregate estimate of the direct and indirect losses to the American public from these insolvencies, it is necessary to indicate that these losses are difficult to fix, for the following reasons:

First, it is impossible to determine how many persons with legitimate first or third party claims against an insurer fail to pursue them when the company becomes insolvent. Many policyholders with *return premium claims* may simply abandon them, either from gratitude that their losses are not greater or from the conviction that the amounts due them are not worth the delay and expense of recovery proceedings.[3] Policyholders with other, larger *first party claims*[4] may absorb the losses themselves rather than undertake the additional expense of prosecuting these claims. Finally, *third party claimants* against policyholders of the insolvent companies (under automobile bodily injury and property damage coverages and other liabilitity policies) may give up their claims when they

[1] *Sources:* 1945–1957—*An Analysis of Insurance Company Insolvencies and the Public Interest*, an unpublished doctoral dissertation prepared by Halim E. Bishara at the University of Wisconsin in 1961; 1958–1969—tables prepared by the staff of the U.S. Senate Judiciary Subcommittee on Antitrust and Monopoly and inserted at pp. 6–15 of the Record of the Automobile Insurance Study Oversight Hearings held by the Senate Commerce Committee on May 6, 1969; and *Best's Reports*.

[2] *Sources:* U.S. Senate Judiciary Subcommittee on Antitrust and Monopoly: *Best's Reports*.

[3] Dr. Richard M. Heins of the University of Wisconsin School of Commerce, summarizing the findings of the Bishara thesis, supra, told the December 1962, meeting of the NAIC Subcommittee on Insolvencies that the average length of the liquidation period for insurers failing between 1850 and 1959 was 11½ years.

[4] Namely, claims under automobile comprehensive, collision and medical pay coverages, fire and extended coverage or homeowners' policies, etc., and claims for out-of-pocket expenses.

discover that they must compete with thousands of other claimants for a possible share of the limited assets of the defunct insurer.

Second, it is impossible to fix the reasonable value of unliquidated third party claims against an insolvent insurer when (1) the question of the legal liability of an insured to a claimant is decided not by a jury or by customary negotiation of the parties, but by a liquidator anxious to winnow out as many borderline claims as possible; and (2) these claims must of necessity be related to the assets available to pay them.

If there are very few assets available for payment of a large number and dollar amount of claims, liquidators are inclined to disallow claims in which the legal liability of the insured is doubtful, and heavily discount the remaining claims in evaluating them for submission to court for allowance. The discounting of claims in many instances will be related not to their reasonable value, but rather to the size of the asset pool all claimants must share.[5] There is virtually no way of computing the losses to legitimate claimants resulting from this process. However, Senate Antitrust and Monopoly Subcommittee data on 80 insolvent automobile insurers from 15 states demonstrates graphically the attrition that takes place in claims against insolvent insurance companies.

This data reveals that as of September, 1968, 239,897 policyholders and claimants had filed a total of $525,018,284 in claims against the 80 insurers. Of these claimants, 122,560 had been permitted by the liquidators to submit $107,670,573 in claims to the courts for allowance. The courts, in turn, had allowed 80,105 claims totaling $50,097,637. Available to pay these and later claims, plus legal and administrative expenses, were $33,673,620 in actual assets. Of the total, $17,647,232[6] was paid out to claimants as of September, 1968.

Third, it is impossible to determine until the end of liquidation proceedings what proportion of an insolvent insurer's assets will be consumed in defraying the legal and administrative expenses of the liquidation rather than in paying claims. This fact makes it extremely difficult to estimate in advance the ultimate policyholder and claimant loss.

The magnitude of this problem is illustrated by a Senate Antitrust and Monopoly Subcommittee table which shows that as of September, 1968, the liquidators of 76 insolvent automobile insurers in 15 states had expended $11,286,584 in administrative and legal expenses in order to pay a total of $18,815,432 in claims.[7]

---

[5] Senate Antitrust and Monopoly Subcommittee figures show that seven Pennsylvania mutual auto insurers which failed during the 1958–69 period had total actual assets at the time of liquidation of $21,000. Assets of four of these companies were as follows: $0, $13, $28 and $74.

[6] An additional $1,168,200 in auto bodily injury and property damage claims were paid out of New York State insolvency funds.

[7] Of this total, $1,168,200 in auto bodily injury and property damage claims were paid out of the New York Stock Public Motor Vehicle Liability Security Fund and the New York Motor Vehicle Liability Security Fund. The state-by-state breakdown is as follows:

Comparisons of claims paid with administrative expenses paid for insolvent auto insurers in liquidation, as of September 1968

State	[a] Companies	Claims paid	Administrative expenses paid
Pennsylvania	19	$8,113	$706,735
Illinois	17	2,192,108	[b]
Texas	7	3,077,082	1,023,526
Indiana	6	789,646	1,446,087
Maryland	4	354,961	1,105,538
Arkansas	3	----------	30,000
Missouri	2	75,943	155,000
California	4	815,000	608,354
Michigan	3	4,686,406	1,571,659
Florida	3	396,012	268,912
Wisconsin	2	1,060,303	642,156
West Virginia	2	263,256	519,906
Tennessee	1	108,915	56,431
Minnesota	2	----------	349,716
New York	1	4,987,687	2,802,564
Total (15 States)	76	18,815,432	11,286,584

[a] For which data is available.
[b] Not available.

Source: State insurance department replies to Senate Antitrust and Monopoly Subcommittee questionnaire of June 6, 1968.

Fourth, in the case of 19 insolvent mutual insurers whose 652,939 policyholders have been assessed for more than $49 million, it is impossible to determine until the end of their liquidation proceedings, if at all, (1) what proportion of the assessments will be collected and thus become assets available for the payment of claims and expenses; and (2) what proportion of any collected assessments will be consumed in defraying collection, legal and administrative expenses rather than in the payment of claims.

Fifth, while some direct losses—like first party non-return of unearned premium and non-payment of physical damage claims and third party property damage claims—can be estimated with reasonable accuracy, other direct losses from insurer insolvencies cannot be accurately measured. These losses include the economic impact of an insurance company's failure to provide its policyholder with promised legal defense and the cost to the policyholder of uninsured judgments against him in suits by third parties, judgments which in many cases he cannot hope to satisfy during his lifetime.

Sixth, the *indirect* costs of insurer insolvencies cannot be quantified. These costs include loss of confidence by the public in the private insurance mechanism and in the ability of government to prevent future insurance company insolvencies; the emotional costs of unsatisfied judgments, pending assessments and unpaid claims; and the lost benefit of tax dollars used unproductively in the prosecution of litigation stemming from insolvencies and in paying the costs of lengthy liquidation proceedings.

Seventh, and finally, there is a paucity of data on which to base an accurate estimate of total direct and indirect losses from insurer insolvencies. For many of the 135 companies becoming insolvent since 1958, there is no data available. For others, data is fragmentary, particularly in the area of first party claims. For those which have been in liquidation for several years, the data is incomplete, and for those recently failed, claims data is still being gathered.

Thus, no estimate of the losses, direct and indirect, from the 135 insolvencies covered by this study can pretend to be completely accurate. Many assumptions must be made to fill gaps in available data, and certain relationships derived from figures available for some companies must be projected for other companies for which similar data is lacking.

Because of the obvious pitfalls of attempting to quantify in dollar terms all the losses caused by insurer insolvencies, dollar figures have been used only where there were credible statistical bases for such figures. In all other instances, there has been only an attempt to indicate, by comparison or proportion, the general magnitude of the losses involved. These general estimates have been clearly labeled as such, and qualified as they must be in the interest of fairness.

III

Of the 135 property-casualty insurance companies which have become insolvent since 1958, there is solid data available on only 88 of them. These 88 companies were property-casualty companies writing automobile insurance and the data dealing with them was prepared by the Senate Antitrust and Monopoly Subcommittee.[8] The first part of this section will treat the direct losses from these 88 insolvencies which can be reasonably quantified. These losses consist of non-return of unearned premium and non-payment of claims other than those for return premium.

The 88 companies wrote a total of $517,415,614 in direct gross automobile insurance premiums, in addition to premiums for other lines of insurance, during the years they were in business. The following figures represent the quantifiable losses from the automobile business written by these companies.

Upon receipt of an automobile insurance policy premium for a year's coverage, the insurer must place the entire premium in its unearned premium reserve, so that it will be proportionately available for return to the policyholder if either the insurer or the insured decides to cancel the policy during the coverage period. Not until that period has expired has the insurer "earned" the premium paid.

On a statutory basis, at any given point in an automobile insurer's calendar year, approximately 50 percent of all its premium income is considered unearned, assuming, of course, a steady, even flow of such income over the 12-month period. This figure represents an average balance between premiums earned and the unearned premium reserves required to be posted.

---

[8] See *supra* [1].

The proportion of the 88 insurers' auto premium volume that was unearned when they became insolvent was developed as follows: First, each insurer's total auto premium volume was divided by the number of years the company was in business. The resulting annual average auto premium was treated as the auto premium volume for the company's final year of operation.[9] The total average annual auto premium for the 88 companies was found to be $98,224,035. Then, the 50 percent unearned premium factor above was applied to this total, producing an estimated unearned premium loss to the policyholders of these companies of $49,112,017.

Losses to persons making claims against these 88 insolvent insurers for other than unearned premiums were derived from the total average annual auto premiums of $98,224,035 referred to above. On the assumption that the automobile insurance losses incurred by these 88 insurers during their final years of operation approximated the permissible automobile insurance loss ratio of 65 percent, this factor was applied to the premium volume figure above to produce a total of $63,845,623 in losses to claimants for other than return premium against these 88 insurers.

Thus, the preliminary total for direct losses from the automobile insurance writings of these insolvent insurers is as follows:

Nonreturn of unearned premium	$40, 112, 017
Nonpayment of claims other than those for return premium	63, 845, 623
Preliminary total	112, 957, 640

From this preliminary total must be subtracted the assets available or already used to pay the losses, less administrative and legal expenses paid.

As noted on page 3 above, Senate Antitrust and Monopoly Subcommittee data on 80 of the 88 insolvent companies shows that these companies had actual assets of $33,673,620 available to pay 239,897 claims totaling $525,018,284. Of these assets, as of September, 1968, $17,647,232 had been paid out to claimants, and $11,286,584[10] had been used to cover administrative and legal expenses, so that there remained $4,739,804 for the payment of the remaining claims.[11]

The total of the $17,647,232 paid out to claimants and the $4,739,804 available for future payments is $22,387,036. The subtraction of this figure from the preliminary direct loss total of $112,957,640 yields an estimated total of $90,570,604 in quantifiable direct losses from the automobile insurance writings of the 88 insolvent insurers covered by the Senate Antitrust and Monopoly Subcommittee data.

The 88 companies above were among 111 fire and casualty companies writing automobile insurance which failed during the 1958-69 period.[12] An additionoal 24 property-casualty companies not writing automobile insurance[13] also failed during this period.

Estimating the direct losses from the remaining 47 companies and from the other business of the 88 auto insurers is difficult not only because of the reasons outlined in Section II above, but also because data is either unavailable or too fragmentary to be useful. Accordingly, the following analysis is predicated on a series of rational assumptions and parallels aimed at conservatively stating the likely losses from the remaining 47 insolvencies and from the other business written by the 88 auto insurers discussed above.

Turning first to the 23 fire and casualty companies writing automobile insurance for which data from the Senate Antitrust and Monopoly Subcommittee was not available, a rough estimate of the direct losses from their collapse can be achieved by the techniques employed in the analysis of the 88 companies above.

---

[9] These averages, in the vast majority of cases, are far lower than the actual final year auto premium writings of these companies. Most of the 88 insurers wrote their largest premium volume in their final years of operations. The averaging approach was taken to avoid any possibility of overstating the unearned premium losses from these insolvencies.

[10] Including $1,713,785 in legal fees and $5,563,163 in salaries and wages.

[11] As noted above, as of September 1968, out of $525,018,284 in claims filed by 239,897 policyholders and other claimants, liquidators had evaluated 122,560 claims totaling $107,670,573 for submission to the courts for allowance. The courts had approved 80,105 of these claims for a total of $50,097,637. It is clear that the assets of the companies are insufficient to meet even these claims, much less those evaluated and approved later. There is no way of estimating what proportion of more than $49 million in assessments against the policyholders of 19 mutual insurers among the 88 will be collected and become available for the payment of claims against the companies. See pages 5 and 12.

[12] 109 of these companies failing between 1958 and 1968 are listed at pp. 6 and 7 of the Commerce Committee hearing record, supra [1]. The last two failed in 1969. They are State Fire and Casualty (Florida) and Prudence Mutual (Illinois).

[13] See table on Page 1 of this study.

However, it is necessary to have an average annual premium base to which to apply the 50 percent unearned premium factor and the 65 percent permissible loss ratio factor. If it is granted that data on 88 of the 111 companies is sufficiently representative to justify projections for the remaining 23, an average annual auto premium *per company* among the 88 can be derived and applied to the remaining 23.

Thus, the total average annual auto premium for the 88 companies ($98,224,035) divided by 88 yields a per company average annual auto premium of $1,116,182. If this is multiplied by 23, it produces an average annual auto premium for these companies of $25,672,186.

Application of the 50 percent unearned premium factor to this product yields an unearned auto premium loss of $12,836,093 for these companies, and application of the 65 percent permissible loss ratio yields an auto claims loss (other than unearned premium) of $16,686,921. Thus, the total direct automobile insurance loss attending the collapse of these 23 companies appears to be at least $29,523,014.

This technique cannot be applied with the same degree of certainty to the 24 insolvent property-casualty insurers not writing automobile insurance. First, the annual premium volume of the insolvent property-casualty companies not writing automobile insurance was probably lower than that of similar companies writing such business. Second, the permissible loss ratio for fire business is about 58 percent, rather than 65 percent as in automobile insurance. Finally, many fire policies are written for terms longer than one year, sometimes for as long as five years, so that the unearned premium factor must be lowered substantially. An unearned premium factor of 20 percent is appropriately conservative.

Proceeding completely without data, and assuming an annual average per company fire premium volume of only $250,000 (more than 75 percent less than that for the companies above writing automobile insurance), the results for the 24 property-casualty companies could be as follows: Total average annual fire premiums volume, $6,000,000 ($250,000×24); total claims loss, $3,480,000 ($6,000,000×.58); total unearned premium loss, $1,200,000 ($6,000,000×.20); total of all losses, $4,680,000.

An additional area of direct losses that needs attention is the other business written by the 111 property-casualty companies whose automobile insurance writings have been treated above.

The great majority of the premium volume of these 111 companies was derived from automobile insurance business. A reasonable estimate of the proportion derived from this source would be 90 percent. Taking the total average annual automobile insurance premium volume of these 111 companies, $123,896,221 ($98,224,035 for 88 companies plus $25,672,186 for 23 companies), and assuming that all the other business they wrote was fire insurance, the following results appear:

If the $123,896,221 in average annual auto insurance premium volume was 90 percent of the total, it would appear that the average annual premium volume in other lines was $13,766,247. Application of the permissible fire loss ratio of 58 percent to this amount yields a claims loss (other than unearned premium) of $7,984,423, and application of a 20 percent unearned premium factor yields an unearned premium loss from this business of $2,753,249. The total of the measurable direct losses from the other lines of business written by these 111 companies thus is $10,737,672.

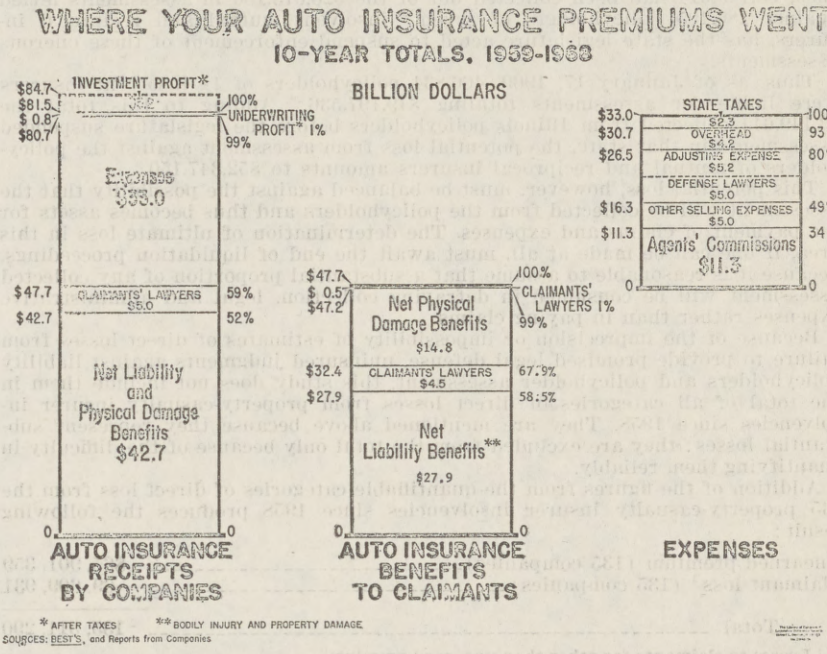
Other areas of direct loss from these 135 insolvencies are either more difficult or nearly impossible to quantify. These areas, as noted on page 5 above, include losses stemming from an insurer's failure to provide its policyholders with promised legal defense and from uninsured liability judgments against these policyholders.

The magnitude of the losses from failure to provide promised legal defense can be gauged from the attached chart, prepared by the Library of Congress' Legislative Reference Service for the Senate Antitrust and Monopoly Subcommittee. The chart shows that the nation's automobile insurers spent $5 billion, or 6.1 percent, of the $81.5 billion in automobile premiums they collected from 1959 through 1968 in defending their policyholders against third-party claimants.

If the 6.1 percent figure were applied to the $517,415,614 in auto premiums written by the 88 high-risk automobile insurers included in the Senate Antitrust and Monopoly Subcommittee data,[14] the result would be a staggering $31,562,352.

[14] See page 117.

However, some of the premiums of the 88 companies included in the Antitrust and Monopoly Subcommittee data were written as early as 1952, and the defense cost factor may have been different at that time. In addition, a $31,562,352 total would not reflect the probability that in all but the final few years of their operations, most of the 88 companies fulfilled their promise of defense to their policyholders.



A more likely estimate of the loss to policyholders from failure to provide legal defense would result from applying the 6.1 percent factor to the average annual auto premiums written by the 111 auto insurers covered by this study. The average annual auto premium figure developed above is $123,896,221. Application of the 6.1 percent factor would produce a policyholder loss from the failure of these 111 auto insurers to provide promised legal defense of $7,557,669.[15]

Turning to the cost of uninsured judgments against the liability policyholders of insolvent insurers, there is no way, short of a case-by-case search of claim and court records, to determine the dollar total in this area of direct losses. An idea of the severity of this element of direct losses can be obtained from Antitrust Subcommittee data[16] which shows that as of the spring of 1967 at least 45,335 of the 179,250 policyholders of 17 insolvent auto insurers faced third-party claims against them totaling more than $98 million. The insolvent companies had just over $11 million to satisfy not only these claims but also nearly $5 million in first party claims.

As indicated on page 5 above, it is also difficult to measure the ultimate loss resulting from the assessment of policyholder of insolvent mutual insurers.

Senate Antitrust and Monopoly Subcommittee data[17] shows that 19 of the insolvent insurers in this study were "assessable" mutual or reciprocal insurers

---

[15] This figure would not reflect the fact that the great majority of liability suits arising from automobile accidents take longer than a year to settle or lap over from one year to another as cost items.

[16] See tables inserted at p. 6852 of Volume 12 of the Subcommittee's hearing on the Insurance Industry (1965), and the Commerce Committee hearing record, *supra* [1].

[17] See p. 13 of Commerce Committee hearing record, *supra* [1].

domiciled in five states.[18] The 652,939 policyholders of these companies knowingly or unknowingly agreed when they became insureds to subject themselves in the event of the insurer's insolvency to assessment, regardless of whether or not they had claim outstanding or unearned premiums due them.

As January 17, 1969, these policyholders had assessments levied against them totaling $69,270,686. These assessments are enforceable by the courts, and there is no recourse against their collection. Only in Illinois, where as of January 17, 1969, $3,149,614 had been collected out of the $20,073,150 in assessments levied against 186,105 policyholders of seven[19] insolvent mutual and reciprocal insurers, has the state legislature acted to suspend enforcement of these onerous assessments.

Thus, as of January 17, 1969, 466,834 policyholders of 14 insolvent insurers were liable for assessments totaling $49,197,536.[20] Adding to this total the $3,149,614 collected from Illinois policyholders before the legislature suspended assessments in that state, the potential loss from assessment against the policyholders of mutual and reciprocal insurers amounts to $52,347,150.

This potential loss, however, must be balanced against the possibility that the assessment will be collected from the policyholders and thus becomes assets for the payment of claims and expenses. The determination of ultimate loss in this area, if one can be made at all, must await the end of liquidation proceedings, because it is reasonable to assume that a substantial proportion of any collected assessment will be consumed in defraying collection, legal and administrative expenses rather than in paying claims.

Because of the imprecision or impossibility of estimates of direct losses from failure to provide promised legal defense, uninsured judgments against liability policyholders and policyholder assessment, this study does not include them in the total of all categories of direct losses from property-casualty insurer insolvencies since 1958. They are mentioned above because they represent substantial losses; they are excluded from the total only because of the difficulty in quantifying them reliably.

Addition of the figures from the quantifiable categories of direct loss from the 135 property-casualty insurer insolvencies since 1958 produces the following result:

Unearned premium (135 companies)	$65,901,359
Claimant loss[1] (135 companies)	69,609,931
Total	[2]135,511,290

[1] Losses to claimants for other than unearned premium.

[2] Total is gross loss less (1) $17,647,232 paid out to claimants against 88 companies writing automobile insurance and (2) $4,739,804 of these companies' assets available for payment of additional claims against them. It does not take into account assets available to liquidators of 47 of the 135 insolvent companies. Data on such assets was unavailable. However, asset data for 88 of the companies indicates that total would not be reduced significantly by the subtraction of the 47 companies' assets. Total also does not reflect any payouts by state insolvency funds or under insolvency clause of uninsured motorist endorsement to auto insurance policies. Such payouts to date have been negligible.

The addition of ultimate losses from other categories of direct loss would greatly increase this total, even before *indirect* losses are considered. These indirect losses are impossible to measure in dollar terms, but are no less significant or severe for this reason.

In addition to the financial costs of unsatisfied judgments or unpaid claims, claimants and policyholders alike must suffer the psychological and emotional costs of insurer insolvencies—worries about unpaid hospital and physicians' bills, the uncertainty of any recovery from liquidators, the anxiety of protracted litigation, and the baleful prospect of court action to enforce assessments or attach possessions for the satisfaction of uninsured judgments.

The executive and judicial branches of the governments of states in which insolvencies occur must shoulder the administrative and legal burdens of liquidating the defunct insurers.[21] These burdens consume countless millions of taxpayers' dollars urgently needed for other state services.

---

[18] California (1); Illinois (5)*; Indiana (1); Maryland (2); and Pennsylvania (10). (*Two of the seven companies listed under Illinois in the Commerce Committee hearing record failed prior to 1958.)

[19] Two of the seven companies listed under Illinois in the Commerce Committee hearing record. *supra* [1], failed prior to 1958.

[20] Of this total $250,000 had been collected from among the 5,006 assessable policyholders of an insolvent Indiana insurer as of Janauary 17, 1969.

[21] Beyond the scope of this study are additional costs to government, policyholders and claimants stemming from the rehabilitation or conservation of nearly insolvent insurers.

Finally, insurance company insolvencies shake the confidence of the American public in both the private insurance mechanism and the ability of government to prevent future insolvencies.

In conclusion, it is clear that the failure of 135 property-casualty insurance companies since 1958 has cost the American public at least $135 million in measurable direct losses. If other direct losses and all indirect losses resulting from these insolvencies could be measured in dollar terms, the total would be in excess of $200 million.

Respectfully submitted.

AMERICAN INSURANCE ASSOCIATION.

Senator HART. It heightens the need to do something about it, though. You in your testimony analyzed the proposals that involve the industry supervising the examinations and practices of insurance companies. You indicate the reasons you think this is not a satisfactory approach.

I will ask you a question that may raise a reason in addition to those which you assign for rejecting this approach. Isn't it possible that under an industry-managed examination certain insurance companies would resist the liquidation of a high risk company or any changes in that company to prevent insolvency because of resulting market restrictions that might focus attention on selective underwriting practices?

Mr. JONES. I wouldn't like to say that is true now. It might have been true at an earlier period. I think our companies have straightened out the problem associated with the high risk companies and have developed affiliates which are recognized by the State insurance departments on a different rating basis and that more and more we are providing markets that meet the need ourselves through affiliates of strong companies.

That might have been a condition at one time, but beginning in 1964 I think the industry has begun to develop companies tailored to meet the motorist's needs that do present a much higher risk. On that basis insurance departments recognized a separate rating basis.

Senator HART. You speak as one who supports this bill.

Mr. JONES. Yes, sir.

Senator HART. And reflect companies which may not be included in the suggestion that was contained in my question. But for those companies that urge open competition, isn't it fair for me to raise with respect to that approach the possibility that is contained in my question?

Mr. JONES. It is a very fair question, Senator, because you can find evidence in the record that existed prior to this time to support your question. Yes. I would like to suggest that that problem is improving, but it is a fair question. I would have to say that some of our companies and some of our strongest companies have just gotten around last year and this year to developing affiliate companies that could meet the market for the higher risk driver.

We may have been a little slow in responding in some respects, but we have.

Senator HART. For the umpteenth time but just for the sake of putting it in the record at an appropriate point I am one of those who feel that you just can't have open competition unless you are going to apply Federal antitrust principles to a particular field. Senator Moss.

Senator Moss. Thank you, Mr. Chairman, and thank you, Mr. Jones, for a very fine statement. I appreciated hearing the part that I heard orally and I have tried to skim through the back part that I missed as you began.

I had two or three questions about this uninsured motorist insolvency protection. How long has this been available, this uninsured motorist insolvency endorsement?

Mr. JONES. With the insolvency provision?

Senator Moss. Yes.

Mr. JONES. The insolvency provision has only been added in the last two, two-and-a-half or three years. We feel that it is very likely the courts would have held that without us adding the insolvency provision to the uninsured motorist coverage, the uninsured motorist endorsement would have covered the insolvency situation anyway, but about 2 years ago we started writing it into our policies.

Senator Moss. Has this been picking up then over a period of time?

Mr. JONES. The interesting thing, sir, is when we added it we didn't add anything to the premium, and the material as we accumulated it from the companies don't separately identify anything as being picked up in this way, that any insolvencies being picked up are distinguished from motorists that had no insurance. It is a cumbersome process in any sense. If you take the situation of the State Fire Casualty which has been before this committee, it was a long time before there was a declaration of insolvency.

So you might have a claim against a company that is not able to respond and it may be a long time before it is declared insolvent, and I don't know that you would be acting properly with regard to your stockholder and policyholder interest if you paid it before there was a declaration of insolvency.

So it is a very unresponsive delayed sort of thing involved with a lot of other procedures. There are some other reasons why we feel it is not a proper answer to picking these up. I don't think anyone can really say how much of it is picked up through the uninsured motorist. Through our related rating organizations, we are unable to identify the situation.

Senator Moss. Would you say there wasn't any change in premium when you put this endorsement on?

Mr. JONES. No, we didn't increase it, and it had no impact on the loss ratios as reported to us after we added it on.

Senator Moss. What is the percent of cost or payout resulting attributable to the insolvency protection under the UM coverage?

Mr. JONES. We aren't identifying it and it didn't seem to have any impact on the loss ratios. We are unable to tell you. We don't separate on uninsured motorist endorsement payment that was based on the fact of insolvency.

Senator Moss. So, as near as you can measure it, it hasn't made any appreciable difference then in payouts?

Mr. JONES. No, sir, not discernible.

Senator Moss. Thank you very much. This is an interesting field, and I am pleased that your study has led you to endorse this bill. I don't have very good technical background in this insurance field, but the problem is there and I can see it, and it seems to me that this was a way to meet it.

With the backing of the organization you represent, I think this endorsement is very significant.

Senator HART. I am reminded as I go through the statement you have here, you discuss the recommendation made by the Department of Transportation's Economic Regulation Advisory Committee.

Mr. JONES. What is your reaction to the argument that the study committee makes against S. 2236? The argument is, the bill would create a counterincentive to effective State regulation because it encourages State laxness and then provides for Federal displacement of a lax State administrator.

I said in my statement that we have great respect for those people, and I must respectfully say we come to just the opposite conclusion. You and I both have people looking over our shoulders. Yours are the voters. Mine are the member companies.

I guess none of us ask for additional people to look over our shoulders. We probably seek to have the least number. This is very much in the tradition of our check and balance system of our Federal Government. You would have here an organization that was very much an associate of yours that would be making examinations together but they are looking over your shoulder. This cannot help but be a further incentive to the insurance commissioners to really do a very effective job, it would seem to me.

We are aware that some of the critics of the bill say that they regard this as a back door method to Federal regulation, and we must say in all sincerity to you that we think it is a very direct and front door method to strengthen State regulation and to support it.

Senator HART. Thank you for saying it. Let me say the sponsors view it exactly the same way.

Mr. JONES. It is very forthright cooperation with the State regulatory authorities and with the uniform national system. A Federal corporation is different from a Federal agency, as you very well know from your work in the Senate. We can't help but believe that it is a complement, that it strengthens it, it supports it.

Senator HART. Mr. Sutcliffe.

Mr. SUTCLIFFE. Mr. Jones, I have just a few questions.

In your statement you conclude that the public interest is not served by the pre- or post-insolvency assessment fund at the State level.

Could you elaborate a bit on why the public interest is not served?

Mr. JONES. One, preassessment would cause the unnecessary accumulation of numerous funds. That concept is not preferable to the Federal Insurance Guaranty Corporation preassessment approach where all of those who are receiving the guaranty of protection of their policies are paying for that guaranty or protection as they go along.

The postassessment concerns us because it represents a blank check put in the hands of the State regulatory process, and you are unable to report a blank check into your financial statements or your balance sheet.

It is a commitment you cannot estimate. It is a contingent liability that you can't assess or report. Let me check with my colleagues for a minute. I am sure they can add something to this.

Mr. GILMORE. Mr. Sutcliffe, I think one other point that we could make to what Mr. Jones has just said is neither the preinsolvency assessment approach or the postinsolvency assessment approach on a

State level make any additional contribution to preventing insolvency.

This is one of the basic tenets that we adopted in our whole approach to this problem. We did not want to go solely for a rescue mission or a bailout remedy. We wanted to make some additional contribution to preventing insolvency.

Mr. SUTCLIFFE. It might be argued that there is a prevention capability because of the authority given to an insurance pool to foster examination beyond the normal triennial examination of the State insurance department.

Is it your opinion then that that particular examination power would never be exercised by the industry itself?

Mr. GILMORE. I am not saying that it would never be exercised by the industry itself. That is not our position. We have reservations on the propriety of putting this missing function in the hands of industry. I think that is one of the major points of our statement.

But above and beyond that, we have been advised that to have a solution to the insolvency problem which would envisage a private facility with some policing functions like the National Association of Security Dealers, then that would require Federal legislation and might even require some further exemption to the McCarran-Ferguson Act.

Mr. SUTCLIFFE. Is it your position that all insolvencies could be prevented? In other words, you stress the prevention capability——

Mr. JONES. Do you mean the Federal Insurance Guaranty Corporation could prevent all insolvencies?

Mr. SUTCLIFFE. Any vehicle for examination and supervision.

Mr. GILMORE. I would say that is highly undesirable. As you gentlemen probably know we regard ourselves as an overregulated industry and certainly we don't want any more regulation in that sense.

It would stifle adjustment and development to changing social conditions. I don't think that it is your purpose, and that is the reason this needs to be backed up with a payment in those cases where you didn't prevent. That is the reason we think favorably of the guaranty fund—really this is an application of the insurance principle to prevent insolvency.

Mr. SUTCLIFFE. But there are prevention approaches that can be taken that aren't being taken at the present time?

Mr. GILMORE. Very definitely.

Mr. STARK. I would like to add that I don't think we will ever completely eliminate insolvencies any more than the FDIC has through the fine process of assistance in the banking industry.

The point is that larceny and fraud can be accomplished in the face of the strongest kind of regulation in any kind of business. The fact is that insolvencies occur for many reasons in all kinds of businesses, some of them by virtue of the competive nature of the economy.

Mr. SUTCLIFFE. Are they likely to increase with the desire on the part of a large segment of the insurance industry for open competition?

Mr. STARK. I wouldn't say that this is necessarily an unlikely situation, but I think our letting the competitive process work itself out under competitive pricing laws plus the fact that examination procedures might be strengthened, could have an impact at the outset on marginal insurers. There are marginal insurers all over the country who are barely alive with their heads above water.

The qualification tests to be imposed by the FIGC in conjunction with the insurance commissioners may cause a shakeout of a nature that was identified when the FDIC was established in the 30's. There was at the outset a rather unusual number of banks that failed. Much of this traceable, of course, to the preceding severity of the economic depression, but a great deal of it due to the examination process.

I think this is a possibility. In the interest of the American consumer and the public, I think this is a desirable-mechanism at a place where the incidences of insolvencies can be eliminated to the greatest extent.

Mr. JONES. In our study, the insolvencies have indicated to us that they were primarily caused by deliberate mismanagement or dishonest management. The thing we don't think the industry can stand is another State fire and casualty situation where they just went off with the assets of a very respected and old company. That is the kind of thing we would hope could be prevented.

We are not convinced that competitive factors caused very many of the insolvencies, but that is the kind of thing I hope we don't try to direct, to prevent insolvencies resulting from competitive factors.

That would stifle the industry too much. But if such things do occur, it is in the interest of the industry that all those people who suffer as a result of it are compensated by this Guaranty Corporation Act.

Thus, we can keep the competitive climate and still not have our American citizens suffer from the result of those operations.

Mr. SUTCLIFFE. On page 8 of your statement you object to the post-insolvency assessment funds because they do nothing to prevent insolvencies and then compound this inadequacy by making strong reputable companies pay for the sins of the mismanaged and weak.

Doesn't S. 2236 make strong reputable companies or their policyholders pay for the sins of the weak? What are the distinguishing points? You have mentioned already the prevention capability. Are there any other distinguishing points between that statement and the approach taken in the Federal Insurance Guaranty Corporation?

Mr. JONES. Well, under the Federal Insurance Guaranty Corporation—the people who have their insurance policies guaranteed are paying for it while it is being guaranteed.

Mr. SUTCLIFFE. So that it would be the second point of distinction in addition to the prevention capability?

Mr. JONES. Yes.

Mr. SUTCLIFFE. Are there any other points of distinction?

Let me throw out one to you and see if it makes any sense. Under a national scheme with a payment or assessment on the net direct premiums written, is the corporation able to function much the way any other insurance operations function in that there is a broad spreading of the risk?

Mr. JONES. Yes, indeed, and those that were mismanaged participate along with those that were well managed, and hopefully we can prevent the deliberate mismanagement.

Mr. STARK. If I may add, Mr. Sutcliffe, you are suggesting the classic operation of the insurance principle for this measure. You have funds in hand, you know what you are going to have, you know how to handle the budget by virtue of a level application of income in the course of a year or following years. This gives an opportunity for an organization to have not only the funds in hand for its administra-

tive purposes but also for its best estimate of losses, and to be able to plan accordingly. Is that the thrust of your question?

Mr. SUTCLIFFE. My thoughts were not that sophisticated. I was thinkinging in layman's terms about the insurance approach of collecting a fund and having it available. I didn't mean to suggest a postassessment vehicle within the framework of S. 2236 may not be something to consider.

Mr. JONES. The postassessment approach that has offended our companies is that they get called in and asked to contribute or told what the contribution is going to be, and people that cause the contribution to be made haven't contributed a cent to this.

They feel some resentment when this occurs, that the company that went insolvent contributed nothing toward the loss that was placed on them.

Mr. SUTCLIFFE. So a combination preassessment/postassessment plan may be something that your Association would accept within the framework of S. 2236?

Mr. JONES. Well, yes, but we think the limit was wisely placed on this fund, and we think the bill as drafted has the proper answer, to go ahead and create up to 2 percent of those premiums being written.

At the present time that would be somewhere between $400 million and $500 million for the whole Nation and all coverages. New York State alone contemplates going to $200 million, and Florida has a very large figure in mind, $100 million. So, this is a very realistic figure and not too much of an accumulation.

Mr. SUTCLIFFE. In the statement, you mention that the Federal Deposit Insurance Corporation has been highly successful. Not at this time, but for the record, could you extrapolate for us the way in which you envision the Federal Deposit Insurance Corporation and its operations vis-a-vis the projected Federal Insurance Guaranty Corporation?

In other words, if you are making the comparison between the highly successful FDIC number one, show us why you believe it is highly successful, and number two, extrapolate for us the relationship between FDIC or your projection of the relationship between FDIC and FIGC.

Mr. JONES. We will be happy to do this.

I might add for the benefit of the committee and I think Senator Hart even questioned this, that some of our senior executives of our member companies have the opportunity of serving on boards of directors of banks. I know that a number of them have taken the occasion to discuss with the president of the bank on whose board they serve what they felt and thought about the Federal Deposit Insurance Corporation, and universally there was a very favorable response.

They certainly gained the impression from the banks with which they were associated that the relationship between the bank and the FDIC was a satisfactory relationship and a well regarded relationship.

We will be happy to develop this for you.

Mr. STARK. I think it might be wise at this time to say that we have been developing some information on a comparative analysis basis of the costs of FDIC administration and costs of FIGC administration in trying to come up with some related figure that had some validity.

We heard some figures mentioned last week in other testimony. I think we are in a position at this time to say that the figures and the information we will submit to you at a later date will indicate a

reasonable outside figure for administration of FIGC that will be in the neighborhood of $15 million annually.

Senator HART. We will certainly welcome the analysis.

(The information to be furnished follows:)

ADMINISTRATIVE COST OF PROPOSED FEDERAL INSURANCE GUARANTY CORPORATION

The bill (S. 2236) creating the Federal Insurance Guaranty Corporation (FIGC) is patterned after the legislation creating the Federal Deposit Insurance Corporation (FDIC)—the Act of June 16, 1933, 48 Stat. 168, 12 U.S.C. §§ 1811 *et seq.*, known since 1950 as the Federal Deposit Insurance Act.

The purpose, functions and financing methods of the two corporations are quite similar. Like the FDIC, the FIGC has two primary purposes—the *prevention* of insolvency and the *indemnification* of its victims. Again like the FDIC, the FIGC would achieve these purposes through initial qualification and continued examination of guaranteed members and through the payment of losses from a fund accumulated by assessment of the membership. Finally, again like the FDIC, the FIGC would be self-sustaining, financing its activities through assessment of its members in proportion to their business volume.

For more than 35 years, the Federal Deposit Insurance Corporation has been a vital underpinning of America's dual federal-state banking system. It has served to maintain public confidence in the banking institution and to protect depositors' funds against the risk of bank failure. With assets totaling nearly $4 billion, the FDIC now provides up to $20,000 protection for each of more than 191 million accounts containing more than $296 billion. This protection is available to depositors in 97 percent of America's banks.

Because of the similarity of the purposes, functions and financing techniques of the FDIC and the FIGC, we believe it is possible to estimate the outside annual cost of administering and operating the FIGC by comparison to the FDIC.

Accordingly, the administrative and operating expenses of the FDIC have been analyzed in the context of the Corporation's relationship to other Federal banking agencies and the state banking authorities and the results of this analysis have been applied to the FIGC and its likely relationships with the various state insurance departments.

On the basis of this analysis, it is our conclusion that it would cost, at the most, less than $12 million a year to administer and operate the Federal Insurance Guaranty Corporation.

Carrying out the comparison with the FDIC in nearly all respects, this estimate of the FIGC's cost would permit maintaining a central headquarters and 14 regional offices;[1] paying a staff of 800; conducting examinations of 3,000 guaranteed insurers; doing research and data processing; collecting assessments; contributing to the Civil Service retirement fund and making F.I.C.A. payments; investing the corporation's assets; and other miscellaneous overhead items.

It is our conclusion that the cost of administering and operating the FIGC will approach $11.3 million only after many years, if at all. This conclusion is based on the following reasonable assumptions:

(1) The states will continue to be the primary regulators of the insurance business, and the FIGC will serve only to complement and supplement state examination for insurer solvency;

(2) the states will maintain or increase their current efforts to prevent insurer insolvencies;

(3) the FIGC will forego, for those applicant companies meeting certain strict criteria, examinations for qualification as guaranteed insurers;

(4) the FIGC will adopt, again according to strict criteria, a flexible schedule of examinations of guaranteed insurers that will permit it, in cooperation with the states, to concentrate its attention on companies most in need of supervision; and

(5) the FIGC will not reach its maximum level of staff and operating capability for several years.

No attempt is made to arrive at an estimate of the FIGC's annual losses and expenses allocable to the liquidation of insolvent insurers and the indemnification of the victims of insolvencies. However, on the basis of an FIGC membership

[1] The FDIC has 14 regional offices to handle the examination of the approximately 7,500 insured institutions it regularly supervises. The FIGC, with only 3,000 members, might be organized with seven regional offices located in the seven zones into which the National Association of Insurance Commissioners has divided the country.

of 3,000, a current premium volume in applicable lines in excess of $23 billion, and an FIGC assessment rate of one-eighth of one percent of net direct written premiums, the FIGC will have an annual income of at least $28.7 million. After the deduction of $12 million at the most in administrative and operating expenses, at least $16.7 million would be available for guaranty losses and expenses and for the early retirement of the initial Treasury loan of $50 million. This excess of income over operating expenses would appear clearly adequate for all but the most dire of contingencies.

Below is a detailed summary of the steps taken in reaching the estimate of the outside annual cost of administering and operating the FIGC:

The bill (S. 2236) proposing creation of the FIGC provides that every property and casualty insurer whose policies are either issued or reinsured in interstate commerce must belong to the Corporation. According to the Insurance Information Institute, there are approximately 3,000 property and casualty insurance companies operating in the United States. This data is based on the reports of the various state insurance departments, and thus includes the vast majority of the so-called "county mutuals" operating in limited geographical areas. Of the 3,000 companies, approximately 1000 issue policies in interstate commerce, and thus would automatically become members of the Corporation. Of the remainder, the National Association of Property and Casualty Reinsurers estimates that at least 99%, if not 100% to some extent reinsure their policies in interstate commerce. Thus, it would appear that if present trade practices were continued, virtually all U.S. property and casualty insurance companies would be required to belong to the FIGC.

Assuming an FIGC membership of 3,000 companies, an estimate was made as to the force of examiners and supervisory personnel needed to evaluate the solvency and insurability of the Corporation's membership. This estimate was developed by analyzing the functions of the FDIC in relation to other federal bank supervisory agencies and their state counterparts and applying the results of this analysis to the likely relationships between the FIGC and the various state insurance departments.

To assure the solvency of the 13,822 banks it insures, the FDIC has statutory authority to examine all of them. In actual practice, however, the FDIC utilizes the reports of other Federal banking authorities to gauge the condition of its 4,716 nationally-chartered bank members and its 1,261 state-chartered Federal Reserve member banks. This practice avoids duplication of effort and expense.

With 5,977 of its insured banks under the supervision of other Federal bank supervisory agencies, the FDIC regularly examines only the 7,511 state-chartered insured banks which do not belong to the Federal Reserve System, and 334 insured mutual savings banks. The FDIC generally examines these institutions at least once during each twelve-month period, but more often if required by circumstances.

The FDIC is empowered to conduct its examinations of insured banks independently of state banking agencies. In more than half the states, however, the FDIC regularly examines jointly or concurrently with the state authorities to reduce the burden of examination activity for the banks as well as for the examiners. S. 2236 appears to contemplate a similar relationshp between the FIGC and the state insurance departments.

In 1968, the FDIC employed 1,243 field examiners in its 14 regional offices and 20 review examiners in its Washington headquarters to assess the liquidity and insurability of the approximately 7500 institutions referred to above. The Corporation employed an additional 263 clerical and professional personnel in its examination division, for a total of 1,526 persons engaged directly or indirectly in the business of examining insured banks. Thus, the ratio of regularly examined banks to examination personnel under the FDIC is approximately 5 to 1.

This ratio undoubtedly would be higher if the FDIC did not have the benefit of the 1500 examiners employed by the various state banking authorities. As noted above, FDIC examiners work jointly or concurrently with state examiners in more than half the states.

It is of interest to note that the ratio of FDIC examination personnel to state examination personnel is approximately one to one.

Returning to the FIGC and its likely membership of 3,000 property and casualty insurance companies, and applying the FDIC ratio of insured institutions to examination personnel (5 to 1), it would appear that the FIGC might employ in its examination division a maximum of 600 persons.

The insurance departments of the 50 states employ approximately 1,200 examiners to measure the solvency of the 3,000 property-casualty insurance companies and the 2,000 life insurance companies licensed to do business in the United States.

Superficially, it would appear that about three-fifths of these examiners (720) would be needed to examine the 3,000 property and casualty insurance companies. However, it takes somewhat longer to examine a property-casualty insurer than it does a life insurer of equivalent asset size, and some adjustment must be made in the simple ratio of number of companies to number of examiners. Allowing for an adjustment of approximately 80 examiners, it could be said that roughly 800 of the states' 1200 examiners are engaged in the examination of property and casualty insurers.

If the one-to-one ratio of FDIC examination personnel to state bank examiners were applied to the relationship between the FIGC and the state insurance departments, it would appear that the FIGC should have 800, rather than 600, persons in its examination division. However, we believe the lower maximum figure is sufficient, for several reasons.

First, as noted above, it is reasonable to assume that in qualifying insurers for guaranteed status, the FIGC may rely on state examination reports as a measure of the condition of some insurers whose soundness and solvency are very well established. Under this procedure, of course, the FIGC would retain its authority to examine such insurers after they had been certified.

Second, while the FIDC examines its insured banks approximately once a year, the great majority of the states currenly examine property and casualty insurers only once very three years. It is reasonable to assume that this procedure is sufficient for the overwhelming majority of insurers, and that it would not be considered necessary to staff the FIGC for annual examinations of all guaranteed carriers. However, it is assumed that there would be the need for close supervision, in cooperation with state authorities, of marginal insurers.

Third, it would appear that the FIGC would serve primarily to complement and supplement state examination for insurer solvency. The states should be able to supervise effectively the majority of insurance companies, and it should be necessary for the FIGC to play only a supporting role. Assuming such a supporting role for the FIGC, it would not seem necessary to have as many federal as state personnel examining property and casualty insurers.

Turning again to the FDIC, it was determined that in 1968 approximately 75 percent (1,526 out of 2,055) of its total personnel were engaged directly or indirectly in the examination of insured banks. Applying a similar percentage to the FIGC, it would appear that the total staff of the new Corporation would number approximately 800.

The FDIC's 1968 administrative and operating expense per employee ($29 million divided by 2,055 employees) was $14,111. If this average is applied to the estimated maximum of 800 employees of the FIGC, it would appear that the total outside annual administrative and operating cost of the new Corporation would be approximately $11.3 million.

Respectfully submitted.

MELVIN L. STARK,
Manager, American Insurance Association,
Washington Office.

Mr. SUTCLIFFE. Just a couple of other questions for the committee's information.

You mentioned the National Association of Security Dealers operation. Is there any kind of regulation for solvency in that operation? I am not familiar with it. How does it compare to the projected Federal Insurance Guaranty Corporation?

Mr. STARK. Mr. Gilmore may have something to add to this, but I want to say there is such a vast difference in the entity you are dealing with. You are dealing with salesmen who have a limited handling of funds, with reserves and other financial situations, totally different from insurance companies.

Whatever does go on, I do not think they would require the kind of internal policing that we envision could occur with insurance companies looking over insurance companies to find out what is going on.

Mr. SUTCLIFFE. There is no ability for one company to effectively put another company out of business?

Mr. STARK. No, I don't think that is true, and, of course, the SEC has the final word in the event of an appeal. That is written in the statute, as to what can happen in the event a member does appeal.

Mr. GILMORE. I don't have much to add to that. I think the only analogy we were trying to develop was in the policing area. This was an example where the Federal Government some years ago—30 or more years ago—bestowed upon a private facility, the NASD, some policing powers over the brokers—and required all the over-the-counter brokers to belong to some such facility.

I think there is actually only one. This is the analogy we were using as a starting point to see if there was some place for a private facility in the area of insurance company solvency. I don't really know, but I don't believe the NASD provides for insolvent protection. It could be, but I don't have information on that.

Mr. JONES. The reason we went to this was that we began to study if there was a type of private facility that we could create. We went to our counsel and we said if we took this approach, what can we do, and counsel said the only analogy they knew of was the National Association of Security Dealers where actually a governmental power was put in the hands of an outside private group.

Mr. SUTCLIFFE. But when you use the word "we" to whom do you refer?

Mr. JONES. When we do this you mean? Our committee. We have had a committee for over 4 years called the Committee on Insolvency in the American Insurance Association, and there are executives on this that have been in the industry for a great number of years and have brought experience and they have had some very long meetings.

We have kicked these things around and have given the staff instructions for research and other work to do. That is whom I am referring to when I say "we"; it is our committee.

Mr. SUTCLIFFE. I have no further questions.

Senator HART. Gentlemen, is there something you would like to add in light of the questions?

Mr. JONES. No, sir. We appreciate the opportunity and we thank you for your consideration.

Senator HART. I thank you very much for a very, I think, thoughtful and certainly flatfooted testimony. Flatfooted is probably the wrong word. Explicit testimony.

Speaking for the National Association of Insurance Commissioners is the chairman of the Iowa State Insurance Commission, Lorne R. Worthington.

STATEMENT OF LORNE R. WORTHINGTON, COMMISSIONER OF INSURANCE FOR THE STATE OF IOWA AND CHAIRMAN OF THE EXECUTIVE COMMITTEE OF NAIC; ACCOMPANIED BY JON HANSON, EXECUTIVE SECRETARY AND DIRECTOR OF RESEARCH OF NAIC; ROBERT E. DINEEN, CONSULTANT TO NAIC; AND T. NELSON PARKER, REPRESENTATIVE OF NAIC IN WASHINGTON, D.C.

Mr. WORTHINGTON. Gentlemen, I would like to have accompany me Mr. Jon Hanson, executive secretary and director of research of

NAIC; Mr. Robert E. Dineen, consultant to NAIC; and Mr. T. Nelson Parker, representative of NAIC in Washington, D.C.

Mr. Chairman, my name is Lorne R. Worthington. I serve as insurance commissioner for the State of Iowa. Today I am appearing before this committee on behalf of the National Association of Insurance Commissioners, which is usually referred to as the NAIC.

Having its inception in and regular meetings since 1871, the NAIC is the oldest voluntary association of State regulatory officials in the United States. Numbering among its members are the principal insurance regulatory authorities of the 50 States, the District of Columbia, and the territories of the United States. I am chairman of the NAIC Executive Committee and of its Special Committee on Automobile Insurance Problems.

I. The Need for Guarantee Fund Legislation

(A) The magnitude of the insolvency problem.—The concept of a Federal Guaranty Corporation, backed by a stringent Federal regulatory and examination structure, has been premised on the belief that during a 10-year period starting in 1958 policyholders and claimants have lost over $200 million attributable to automobile insurer insolvencies. This alleged loss figure, however, is based upon conjecture rather than upon credible fact.

In contrast, based upon relevant factual information obtained from liquidators of the insolvent insurers, a recent study places actual insolvency losses to policyholders in a truer perspective. For example, in the period 1966–68, the average annual loss to claimants was less than $5.4 million, which results in a current rate of loss of 49 cents per $1,000 of premium (based upon approximately $11 billion of auto premiums in 1969 compared to a rate of 60 cents per $1,000 of premium for the period 1960–65.

(Figures developed by studies of the Texas Insurance Department conducted in cooperation with the NAIC Special Committee on Automobile Insurance Problems. For the detail of these studies, see Report of the Special Committee on Automobile Insurance Problems, NAIC annual meeting, June 16, 1969, p. 29 et seq. See also id. at 180–182.) An exaggerated impression of losses attributable to insolvencies if often obtained by totaling amounts "claimed" by policyholders and third-party claimants in liquidation proceedings.

But, as experienced liquidators know, claimants typically demand amounts greater than that to which they believe themselves entitled to allow room for negotiation and compromise.

Many claims lack merit and many are doubled up due to both the policyholder and third-party claimants making overlapping claims. Thus, when claims are finally adjudicated, the total allowance is only a fraction of what is claimed.

For comparative purposes, we note that the Federal Savings & Loan Corp. charges 83 cents per $1,000 of S. & L. deposits for something less than 100 percent coverage.

When the amount of total automobile insurance written is considered, the small magnitude of policyholder and claimant losses due to insolvencies attests to the basic strength of the existing system rather than justifying calls for fundamental regulatory changes.

(B) The nature of the insolvency problem and the need for guarantee fund legislation.—Although the insolvency problem is not great when viewed on a national basis, the consequences may nevertheless cause quite severe hardship for those individuals involved. An individual who cannot recover justified recompense for injuries and loss is little consoled or helped by the fact that he is only one of a few who find themselves in such plight.

Furthermore, every insurance company failure undermines public confidence in and the value of the insurance institution whose very existence is the result of the public's desire and need to be and feel secure from risk.

Let there be no mistake as to the position of the NAIC. At its 1967 meeting, the NAIC stated that it:

> Believes that every promise to every policyholder should be kept fully. No policyholder should ever have to accept anything less than full performance of his contract. (Two proceedings of the NAIC 599, 1967.)

More recently at the NAIC June 1969 meeting in Philadelphia, a position statement said:

> While the statistics have been interpreted by some in such a manner as to greatly overstate the magnitude of the problem, let it clearly be understood that it is the position of the NAIC that no person should suffer as a result of the insolvency of an insurer and that we stand ready to supplement our past actions with present actions to assure this end. (Two proceedings of the NAIC, 1969.)

There is an emerging consensus for establishing some type of guaranty fund or funds to resolve the insolvency problem. Three States adopted this approach in prior years. In June 1967, the NAIC recommended guaranty funds or assessment mechanisms as possible alternatives. (2 id. at 600, 1967.)

Last June, the NAIC lent further support to these measures, as well as recommending that serious consideration be given to the establishment of a non-Federal interstate facility aimed against insolvencies. In recent months, four more States have enacted guaranty fund legislation.

In addition, the widespread availability of uninsured motorist coverage with the insolvency clause has substantially contributed toward lessening the insolvency problem. This coverage is akin to guaranty fund protection in certain circumstances.

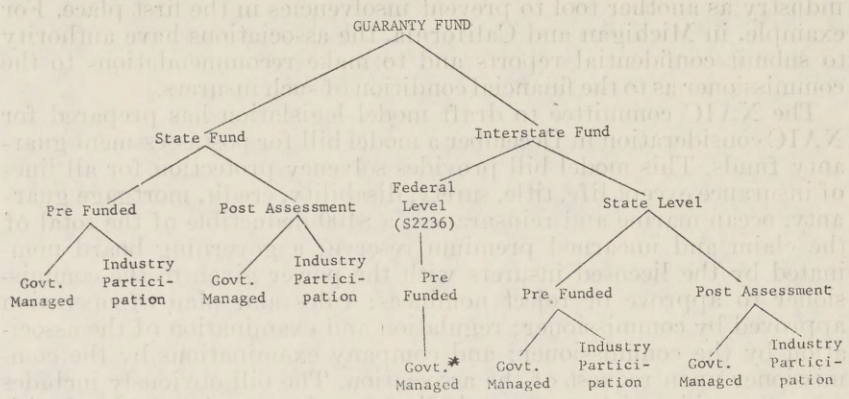
Since it is sold nationwide, in effect, we already have a form of guaranty protection—hence, the recognition that guaranty fund legislation is merely the next evolutionary (and not particularly large) step to closing the gap. Thus, there is vigorous discussion as to what type of guaranty fund would best serve the public need as distinguished from a dialog as to whether or not such need exists.

II. Alternative Types of Guaranty Fund Legislation

Alternative approaches under discussion include various types of State funds of either a prefunded or postassessment basis with or without industry participation in the program's management in varying degrees.

Also, there is substantial discussion about some type of interstate fund at either the State level (presumably using the facilities of the NAIC) or under the aegis of Federal Government.

Hereto, there are questions as to the pre or post nature of the fund as well as to the degree of industry participation in the fund management. The following chart graphically summarizes some of the various alternatives.



*Re advisory committee with industry participation.

(Commerce Committee staff note: The representation of S. 2236 in the above chart is not entirely accurate. There is industry participation in the Federal Insurance Guaranty Corporation by way of an Advisory Committte (with industry representaton) to the Board of Directors.)

A. STATE FUNDS

Prior to this year, Maryland, New Jersey, and New York enacted insolvency funds. Each is established on a prefunded basis through periodic contributions with a ceiling on the fund size. Each is administered by the Insurance Department. In recent months, a different pattern has developed. California, Michigan, New Hampshire, and Wisconsin have adopted the postassessment approach. That is, instead of accumulating funds in advance, funding the insolvency protection is to be achieved by assessing insurers upon the actual occurrence of liquidation.

Both approaches have their advocates. The prefunders maintain that any security arrangement should be immediately credible, should be able to provide adequate security without needless delay to accumulate funds, and should not be exposed to the vagaries of collection after the fact. On the other hand, the postassessors argue that sufficient sums of money can be assessed quickly, and made available by the time a court and liquidator actually settle or approve claims. Furthermore, this approach obviates the necessity for accumulating large sums of money which may not be needed and which might prove to be a tempting target for other legislative purposes.

With the exception of Wisconsin, the postassessment States have attempted to utilize the existing knowledge and expertise of the industry in administering the insolvency program subject to the control and supervision of the commissioners. For example, in California and Michigan, an association is created whose membership consists

of all insurers doing business in the State who write coverages included within the scope of the act.

California, Michigan and New Hampshire legislation, in addition to performing the guaranty function, seeks to utilize the expertise of industry as another tool to prevent insolvencies in the first place. For example, in Michigan and California, the associations have authority to submit confidential reports and to make recommendations to the commissioner as to the financial condition of such insurers.

The NAIC committee to draft model legislation has prepared for NAIC consideration in December a model bill for postassessment guaranty funds. This model bill provides solvency protection for all lines of insurance except life, title, surety, disability, credit, mortgage guaranty, ocean marine and reinsurance; a $100 deductible of the total of the claim and unearned premium reserve; a governing board nominated by the licensed insurers with the power given to the commissioner to approve or reject nominees; rules and plan of operation approved by commissioner; regulation and examination of the association by the commissioner; and company examinations by the commissioner upon request of the association. The bill obviously includes more than this quick summary indicates and a copy is submitted with this statement for your information.

The concept of using an industry association, functioning under the insurance commissioner, is not a new one. It is used on a nationwide basis in the automobile assigned risk area. More recently Congress sanctioned this concept in adopting the FAIR plan approach which is designed to provide city property owners, particularly the poor, ready access to adequate insurance coverage.

In this connection, it is interesting to note that one large industry group—American Mutual Insurance Alliance—has proposed and supports model postassessment legislation including active industry participation in assisting the commissioner in preventing insolvencies. This is a very interesting development in light of the industry attitude of noninvolvement and opposition to guaranty funds as recently as several months ago.

(It may well be that the industry now foresees the general adoption of guaranty fund legislation throughout the country. It may have decided that it would rather have a voice in the drafting of this legislation than to continue bitter end opposition. Such a course would mean that it would have legislation thrust upon it which would be wholly unsatisfactory to it. The recent words of Mr. Hamer H. Budge, Chairman of the SEC, addressed to the Association of Stock Exchange Firms comes to mind. He said, "It seems to me that the Government's course should and must of necessity be determined at least in large measure by the willingness of the industry through self-regulation to accept the responsibilities and shoulder the burdens."

("I would assume that the course taken by the Government will be in direct ratio to the willingness and ability of the self-regulators of the industry to do those things which must be done.")

B. INTERSTATE GUARANTEE FUND

Currently, vigorous discussion and study is being focused on an alternative approach—namely an interstate guarantee fund. One form of this approach is a Federal insolvency fund such as that embodies in S. 2236, which will be discussed later.

A second form under consideration is the creation of a non-Federal interstate corporation and guarantee fund. The responsibility for managing, staffing, and operating the interstate corporation would rest with the industry subject to the regulatory control and close scrutiny by the States through the NAIC. Through this facility, the expertise of the industry could be utilized in performing a variety of functions including (1) the guarantee function when a member insurer becomes insolvent; (2) assisting States in the prevention of insolvencies; and (3) assisting in the prosecution of those who fraudulantly use insurance companies. The latter activity would add a deterrence to future adverse conduct.

There is nothing radical about the relationship between a quasi-private-public corporation and the regulatory activities of a governmental agency. For example, in the securities business, Congress not only created the SEC as the Federal enforcement agency but also it enacted the legislative framework setting the stage for the National Association of Securities Dealers. By this means Congress adopted the public policy of harnessing the expertise and facilities of the securities industry for self-regulation. Similarly, the use of surplus lines associations, such as the one in California, serves as a precedent for using a quasi-private-public organization to achieve a regulatory purpose.

C. CONSIDERATION OF ALTERNATIVES

The NAIC is currently studying and weighing these various alternatives to meeting the insolvency gap problem. Its special committee on automobile insurance problems, supported by the background studies and discussion of the NAIC Central Office, is in the process of reaching conclusions in preparation for making detailed recommendations to the NAIC as a whole at the December meeting. At the moment, we are studying alternative model statutes—on the pre-funded and on the post-assessment basis. The statute for a post-assessment plan has been written and will be presented for NAIC approval in December. We are also developing model legislation for an interstate program but this may not be completed by the December meeting. Of course, any interstate facility would be integrated with the activities of those States already having adopted a program.

Several States have either enacted or have some type of guarantee fund legislation in the "hopper." What's important to note here is the fact that both individual States and the NAIC are actively engaged in solving the problem and that such solutions can be achieved without doing violence to the traditional and effective pattern of insurance regulation.

III. Appraisal of State Action

Proponents of Federal intervention in the insolvency area are quick to allege shortcomings of State efforts. Too often, however, such critics suffer from viewing the problem in a narrow perspective which, in turn, impedes reaching a valid judgment in determining the best solution.

A. DEFINITION OF THE PROBLEM

What is the real problem or broad issue with which we are confronted? It is more than just the manner of treatment for insolvent insurers. No one questions the essential role which insurance plays in today's economic and social environment in terms of protecting an individual as a driver, as a passenger, as a pedestrian, as a property owner, from the potentially catastrophic consequences of motor vehicle accidents.

Protection can be afforded for losses resulting from death, injuries, and illness; for damages to real property; for loss of or damage to personal property (including the automobile itself) and for economic disaster resulting from legal liability. But obviously the insurance mechanism can only perform its function to the extent that persons involved are covered. Thus, the crucial problem with which we are regulators, you as legislators, and the public as consumers must be concerned is that of maximizing (to the extent feasible and consistent with other public policy objectives) the protection afforded to the motoring public—that is, increasing the number of persons insured vis-a-vis those not insured and enhancing the strength and adequacy of such coverage once issued.

When an insurer becomes insolvent, it cannot fully perform its function of providing insurance protection. Thus the insolvency problem is just one part of the overall problem of affording protection to as many persons as possible. An accurate appraisal of State performance requires viewing such performance in this broader perspective.

B. EVOLUTIONARY REGULATORY RESPONSE

Both the States and the industry have used a variety of approaches, programs, and contracts to combat the broad problem of uninsured motorists. For example, when experience proved that there were practical limits on how many people would buy automobile insurance voluntarily, the States responded by enacting the financial responsibility laws, and later the safety responsibility laws, and compulsory insurance in three States. These moves markedly increased the number of insured cars. As supplementary gap closing measures, unsatisfied judgment statutes and the New York Vehicle Accident Indemnification Corp. were also adopted.

When insurers became reluctant to insure poor risk drivers, assigned risk plans were developed and have been put into effect on a country-wide basis. These have been and are being liberalized to make broader coverage available to virtually all drivers. Furthermore, when drivers found their insurance being canceled or not renewed, reasonable restrictions were imposed on arbitrary cancellations and refusals to renew. The NAIC in June 1969 urged even more action by the States to limit arbitrary cancellations and refusals to renew.

As more and more people acquired insurance, it became quite common for insured persons to be involved in accidents with drivers who had not displayed a similar sense of responsibility. Hence, the States fostered the development by the industry of the uninsured motorist (UM) coverage which is now available in every State. Subsequently, UM coverage was expanded to embrace within the definition of uninsured motorist those persons whose insurers became insolvent. Coverage

under the expanded definition is now mandatory in more than 30 States and such expanded coverage is available in every State. Seven States have gone one step further by enacting various types of State guarantee funds.

The implementation and continuous development of the financial responsibility and compulsory insurance laws, the assigned risk plans, UM coverage with the insolvency clause and State insolvency funds demonstrates that State insurance regulation has conducted a vigorous and continuing attack on the broad problem of maximizing insurance protection to the public. The insolvency problem is only one facet of the broader issue. It constitutes a residual gap. Nevertheless, even just a few insolvencies create a real problem requiring solution. The recent activity at the State level and in the NAIC demonstrates a firm conviction on the part of State insurance regulators that they have the responsibility, the ability, and the willingness to come to grips with and to solve this residual problem.

It does not appear justifiable for Congress to appear with an instant Federal solution to a residual problem when the States and the industry are dealing with the basic problems of protecting the public. If and when the States show that they are unwilling or unable to remedy this residual gap—which would be in vivid contrast to what is actually happening today—then, and only then, should serious consideration be given to Federal intervention.

C. A FEDERAL PARALLEL

Congress should be among the first to recognize that not every problem can be solved at one time or immediately by legislative activity. For example, it was not until 1933 that the Securities Act was passed. This had to be followed by the Securities Exchange Act of 1934, the Public Utility Holding Act in 1935 and the Investment Company and Investment Advisors Acts in 1940. Even though these acts were preceded by years of study and deliberations, nevertheless, they still have been found to lack perfection. To wit: Although the over-the-counter market existed when the Federal securities laws came into being in the 1930's and early 1940's, it was not until 1964 that the Securities Exchange Act of 1934 was amended to bring this market under Federal supervision. Here we see an elapse of 30 years since the first congressional legislation. Furthermore, following numerous studies of the securities industry, other amendments are being proposed and presumably some will be enacted.

This is a typical illustration of the evolutionary process of legislation and regulation. In complicated areas such as the securities or the insurance business, not all problems can be foreseen or instantaneously solved. No one claims that the failure to solve everything back in the 1930's demonstrates that the Federal Government has been so remiss in meeting its responsibility to warrant the loss of its jurisdiction to regulate. Congress and the SEC have been vigorous in providing a legislative and regulatory framework to protect the public interest. What they have been unable to solve today, they seek to solve tomorrow.

Similarly, State legislatures and insurance regulatory agencies, through the evolutionary process, have steadily reduced the problem of an uninsured, unprotected public. Since the magnitude of the insol-

vency problem has been relatively small and since in most States insolvencies have been few and far between, it is understandable why the States in the past concentrated on other aspects of the broader problem. As these are being solved, the current State and NAIC activity in the insolvency area indicates that the process of evolutionary response to public need has not diminished.

IV. The Federal Insurance Guaranty Corporation

Now, let's take a closer look at S. 2236, including some of its potential ramifications. This bill would create a Federal Insurance Guaranty Corporation. In practical effect, virtually all property, casualty and surety insurers would be required to particiapte and hence be subject to the bill's regulatory provisions.

A. REGULATORY PROVISIONS

1. Examinations.—The Corporation would have extensive examination and reporting powers over insurers applying for guaranty status and those who have achieved such status (Sec. 7(a)(8). It is empowered to appoint examiners to examine insurers whenever the Corporation deems necessary, to examine the affairs of all affiliates, to administer oaths and take testimony and to make full and detailed reports to the Corporation (Sec. 8(b)(c)). Many insurers writing various types of property and casualty insurance either directly or indirectly engage in the life insurance business, typically through affiliates. Since it would be difficult if not impractical to examine only one part of an insurer's business in passing upon the question of its solvency and financial condition, life insurers may indirectly be brought within the statute's embrace. It can fairly be anticipated that a Federal guaranty fund with Federal examinations would ultimately be extended into areas far beyond any "residual gap" in the automobile insurance coverage. An insurer's refusal to comply with the Corporation's recommendation based on an examination report would authorize the Corporation to publish the relevant part of the report. Although S. 2236 expresses the intent that such examinations should be coordinated with those of the States and the NAIC, their position would clearly be subordinate—for example, copies of any report or statement to the State regulatory authority must be filed with the Corporation, but they do not have to be accepted by it (Sec. 8(b)).

The establishment of a Federal corps of examiners as contemplated in S. 2236 would tend to substantially weaken rather than strengthen the examination process which is the heart of the regulatory system.

Competent insurance examiners are highly trained specialists who must have at least 5 years examination experience to become "Senior Examiners." Experienced men have always been in short supply, and it is only reasonable to expect that a new Federal agency would of necessity have to recruit from State insurance departments in order to build a staff of examiners. The present system of "convention" or "zone" examinations which is the product of nearly 100 years of evolutionary progress by the States working together through the NAIC could well be destroyed. This, of course, would affect the entire industry, including life insurance, and could well create additional insolvencies.

2. Reporting.—In addition to examination reports, the Corporation would also receive from participating insurers "reports of condition" in such form, at such times and including such information required by it. Furthermore, the Corporation can compel the insurer to publish such reports (Sec. 13(a)). Changes in the outstanding voting stock which result in change of control of the insurer must be reported (Sec. 13(h)).

3. Licensing.—Before granting guaranty status—which virtually all insurers must obtain in order to continue doing business—the Corporation is authorized to examine the applying insurer as to its capability "of conducting its business in a sound and solvent manner * * *" (Sec. 11). In making this determination, among other things, the Corporation should consider capital and surplus, reasonableness of operating expenses, premium writings as related to surplus, adequacy of loss and expense reserves, reinsurance, investment portfolio, and managerial qualifications. The guaranteed status can be withheld if the insurer doesn't meet Corporation imposed conditions (Sec. 11). Furthermore, the Corporation may terminate guaranty States—which, in effect, precludes a company from doing business—if it finds that (1) the insurer, its directors or officers have or are engaged in unsafe or unsound practices; (2) the insurer is in an unsafe or unsound condition; or (3) the insurer has violated the statute, a regulation thereunder or conditions imposed by the Corporation (Sec. 14(a)). In other words, the power to grant, withhold or terminate guaranty status is very much akin to a State's licensing power.

In short, S. 2236 grants to a new Federal agency the power to examine; to compel, receive and publish reports; and to (in effect) license and terminate an insurer's license to do business. In addition, the Corporation would have the authority to remove company directors and/or officers when, in its opinion, they have engaged in certain types of specified conduct (Sec. 14(d)). Thus, S. 2236 vest broad and pervasive regulatory power over the operations and conduct of the insurance business, regulatory power which essentially duplicates that of the States.

In addition, this bill would seem to completely replace rather than merely duplicate State functions in the liquidation area.

(The Corporation would assume and perform all obligations under guaranteed policies of an insurer determined by the court to be insolvent, if the court appointed received gives notice and makes all books and records—including claim files—available to the Corporation. Then the Corporation would file a certificate of assumption with the court. Thereafter proceedings against the insured or insurer would be stayed for 30 days. The Corporation is authorized to investigate, examine, adjust, compromise or settle any claim and to defend any action after filing the certificate of assumption. (Sec. 9.))

(Thus, it appears that S. 2236 removes the handling of the liquidation proceedings from the control of the liquidator and the supervising State court. The bill does not provide for court approval of the findings of the Corporation and its adjusters as to the validity of claims and the amounts allowed. The liquidators, whose function is apparently reduced to merely holding the assets of the defunct insurer, presumably must recognize by way of subrogation any claim filed by the Corporation. Years of experience and tested procedures at the State level for the equitable distribution of assets of an insolvent insurer

would be replaced by a new and untried Federal mechanism. Furthermore, unless numerous regional offices are established by the Corporation throughout the country, in disputed cases claimants would be required to file their claim, submit proof, produce witnesses and testimony, et cetera, in Washington rather than at the local level.)

B. APPRAISAL OF STATE VERSUS FEDERAL SOLUTION TO THE INSOLVENCY PROBLEM

1. Efficiency.—The proposed Guaranty Corporation with its pervasive Federal regulatory controls and Federal assumption of liquidation activities, presupposes that a Federal agency by its very nature is efficient, economical, and well-funded. Not all Federal agencies meet these standards. It is a common complaint among Federal administrators that their agencies are substantially understaffed, underfunded, and unable to fully perform all their functions. One can read in the daily papers illustrations of the absence of perfection in the performance of various duties ranging from neglect, delay, omissions, over zealousness, and even being taken in by fraudulent schemes from time to time. A Federal regulatory solution is not a panacea.

State insurance regulators cannot claim perfection. We have our problems and shortcomings. Regulatory problems which continue to arise must be met. What is important to note, however, is that (1) such problems are not unique to State insurance regulation but rather extend to the Federal arena as well and (2) State insurance regulators are acting vigorously to meet unresolved problems. Furthermore, State regulation is decentralized although coordination is provided where needed through the machinery of the NAIC. It is closer to the public, it is economical, in the main it is effective, and it is in existence. As we know, there is increasing emphasis and interest at all levels of government for further dispersion of regulatory authority and power back to the States. The enactment of S. 2236 would be a move in the opposite direction.

2. Cost.—From a cost standpoint, a serious question exists as to the desirability of a federally administered guaranty system with a dual examination and regulatory capacity paralleling that of the States. As the Texas study pointed out, for an agency to do everything the proposed Federal corporation is supposed to do, there would have to be a substantial budget. For example, the Federal Deposit Insurance Corporation's annual budget is in the neighborhood of $20 million. The FDIC examines no national banks nor State banks who are members of the Federal Reserve System. Nor is it involved in the detailed work of settling insurance claims in a liquidation proceeding.

In contrast, the Federal Insurance Guaranty Corporation would have the power to examine virtually all property and liability insurance companies. An annual administrative budget of something in excess of $30 million appears to be a realistic minimum. This annual administrative cost would be approximately six times greater than the amount of the average annual loss attributable to insolvent automobile insurers. One must question the wisdom of adopting an approach leading to such a "cost-benefit ratio."

C. THE BASIC ISSUE

I would like to quote now from the "Statement of the Advisory Committee on Economic Regulations to the Department of Transportation."

S. 2236 creates a basic dilemma, then seeks to resolve it by an impossible compromise. It would create a Federal Guaranty Fund by levying a tax on all policyholders throughout the country. It then provides for Federal administration of the insolvency fund and Federal participation with state insurance supervisors in the financial supervision of insurers and in the administration of insolvent insurers. It evidences a purpose to preserve the pattern of existing state regulation, yet at the same time recognizes that the administrators of the Federal fund cannot rely entirely upon state regulation.

Actually, the bill would create a dramatic counterincentive to the fullfillment of the objective of sound financial supervision of insurers. States which have not in the past shown great motivation to establish legal standards and administrative controls adequate to minimize insurer insolvencies would further lose incentive to do so. This is true because insolvency losses in those states would be paid for from the Federal fund derived largely from the people of other states. The only control offsetting this economic counter-incentive would be the aggressive utilization by the Federal agency of the direct powers conferred upon it by the bill. This, however, automatically results in the superimposition of a system of Federal supervision on the existing pattern of state regulation. Inevitably, the Federal agency, to protect the integrity of the fund it must administer, will find it has to reach further and further in the exercise of the powers conferred upon it or to seek even more powers. Financial supervision is the primary purpose and function of insurance regulation. The needs of financial regulation pervade the legal controls imposed upon insurers. Ultimately, it is inconceivable that the Federal agency charged with the faithful administration of a fund derived from people in every state will be able to tolerate significant discrepancies among states in capital and surplus requirements, in investment laws, in rate administration, and in examinations of insurers. Comprehensive Federal control will, indeed must, follow Federal financial responsibility. Hence S. 2236 manages to create two powerful incentives in conflict with each other and with prevailing attitudes toward federalism: First, it creates an incentive to the states to do an inadequate job of supervision and control of insurers and second, it creates an incentive for the Federal agency to become even more involved in that task.

The authority to examine, compel and receive reports, license and refuse to license constitutes the fundamental underpinnings to the entire system of State insurance regulation. S. 2236's duplication of this regulatory effort not only would be expensive to the public but also over a period of time would lead to industry demand for regulation by only one level of government. Let there be no mistake or misunderstanding, this bill involves a broad, complex, and fundamental issue—i.e., State versus Federal regulation of the entire insurance business. If enacted, it would, in pratcical effect, go a long way toward resolving the issue without even confronting and discussing the issue on its merits. This is surely a draconian solution for a residual gap problem in the automobile insurance area.

V. Conclusion

Although the magnitude of the insolvency problem has been overstated, nevertheless the problem is a very real one which deserves and is receiving the attention of both the NAIC and the individual States. There is an emerging concensus for guaranty fund legislation at the State level. Three types are under consideration—a prefunded plan, a postassessment plan, or an interstate non-Federal fund. There is no support among the commissioners for the enactment of S. 2236.

S. 2236 would superimpose an additional layer of duplicative and costly regulation at taxpayer expense—on an already intensively regulated industry. The creation of a Federal group with extensive regulatory powers would erode the effectiveness and could ultimately destroy the time-tested system of State insurance regulation.

In the opinion of the NAIC, the State guaranty fund system would be far better in protecting the public interest, both with respect to solving the insolvency gap problem, as well as in dealing with how the insurance business can best be regulated.

Some have questioned whether the necessary insolvency protection would be afforded in every State if the States were left alone. The Economic Regulation Advisory Committee to the Department of Transportation Automobile Insurance and Compensation Study has squarely opposed the concept of a Federal Insurance Guaranty Corporation. At the same time, however, the committee of which I am a member recommended an alternative approach if the States do not do the job—i.e., Federal legislation creating powerful incentives or compulsion for the States to adopt insolvency guaranty laws. Such legislation could be achieved by imposing a substantial Federal tax on premiums in each State failing to adopt insolvency legislation which meets Federal statutory minimum standards. In a sense, this is "forcing" legislation patterned after the McCarran Act.

Many commissioners question the need of using Federal power to galvanize the States and the business into acting. They argue that seven States have already acted, four in recent months. Other States are blueprinting activity for the next legislative session. The NAIC Special Committee on Automobile Insurance Problems is close to submitting its recommendations complete with model bills to implement them. The industry's adamant and unanimous opposition to any type of guaranty fund legislation of 1 or 2 years' age no longer exists. It is recognized by most that the question is not any longer whether guaranty fund legislation should be passed but rather what form it should assume. Some portions of the industry not only do not resist the concept of guaranty funds but have, in fact, drafted suggested model legislation as well as having expressed interest in a non-Federal interstate fund. Thus, recent months have witnessed a radically changed climate and a gathering momentum to get the insolvency problem resolved. Since this is the case, Federal action—even of the "forcing" type—seems to be superfluous.

Based on our experience, the various points raised in this statement, current State, and NAIC activity, et cetera, the NAIC is firmly opposed to the enactment of S. 2236. We favor State guaranty funds and will shortly have State model legislation available for action by those States which have not yet adopted guaranty fund legislation.

We are convinced that given time, the NAIC and the States will continue to meet the challenge and close the insolvency gap which even now has been narrowed to include a very small percentage of our populace. We ask, therefore, that you give us time and that you not act precipitously and thereby destroy the historic pattern of State regulation of insurance.

Senator HART. This is an obvious reaction, a comment. It is interesting that back to back two very opposite points of view are stated this morning to the committee voiced in both cases by men well informed in the field and both speaking with complete conviction and sincerity.

That is why sometimes if you are the third party you almost have to toss a coin.

You would agree that you are in direct disagreement with Mr. Jones?

Mr. WORTHINGTON. I think that is quite obvious, yes.

Senator HART. You note that the identification test, State and Federal action, quite relevant in our system of things, but the important point, and I'm not suggesting you were discounting it at all, is not whether we shall turn to the Federal Government or rest with the State. The important point is how shall we best protect the public, and it is against that inquiry that we should evaluate which of the two methods is the more likely to achieve that end.

While we talk this year, there have been two insurance insolvencies, State Fire was mentioned this morning, Prudence Mutual is another—this happened while we sat and talked about who will do it.

We have been talking about the need of this kind of legislation for a good many years now. I am not suggesting that the increased concern at the State legislative level and among commissioners and companies is occurring only because a few years ago there were filed in the Congress bills that would move the Federal Government into the business, but it is pretty clear that the impetus for the State activity was stepped up markedly after the Federal Government started talking seriously about doing it itself in cooperation with the States.

Mr. WORTHINGTON. I think, Senator, we agree with the conclusion that you made, and that is that there is a problem and the NAIC and the State insurance commissioners stand ready to work to resolve that problem. The question that used to be a question that was discussed as to whether or not there was in fact a problem is one that we are pretty generally agreed on at this point.

We recognize the problem and we are here saying now that we feel that we can solve the problem within the traditional confines of State regulation. As a matter of fact, for 30 percent of the people in the country, it has already been solved through either post- or preassessment guarantee fund association. We have reason to believe that the legislatures which meet in January will adopt our model State post-assessment guarantee bill by June of next year. Nearly all the States in the country that have legislatures meeting can have a form adopted of guarantee legislation, which may be before the House and Senate can act on the bill that is before us today.

Senator HART. Would that solution be as complete and protective of the public interest as the establishment of the Federal guarantee fund?

Mr. WORTHINGTON. We are in a position today where we can describe in terms for you the proposed model plan which will be presented to the NAIC with the understanding that this bill has thus for received only the approval of a subcommittee, and will be considered by its parent committee, the Laws and Legislation Committee, and by the total NAIC.

So, there may be some changes made in it between now and the 6th of December. I would like to say that this bill does provide, we think, the same kind of protection without the cost to either the policyholder or to the insurance companies that S. 2236 would involve. Let me just briefly try to tell you what is involved in the bill.

Senator HART. Commissioner, we want to hear it, but would it be possible for you, with the explanation having been made that it is

simply the result of subcommittee action that may be changed, to send us a copy of the bill as it came out of the subcommittee for the record now?

Mr. WORTHINGTON. Yes, I think we can.

Senator HART. We will receive that.

(The draft bill follows:)

NAIC STATE POSTASSESSMENT INSURANCE GUARANTY ASSOCIATION MODEL BILL

Section 1. *Title.* This Act shall shall be known and may be cited as the (state) Insurance Guaranty Association Act.

Section 2. *Purpose.* The purpose of this Act is to provide a mechanism for the payment of covered claims under certain insurance policies to avoid excessive delay in payment and to avoid financial loss to claimants or policyholders because of the insolvency of an insurer, to assist in the detection and prevention of insurer insolvencies, and to provide an association to assess the cost of such protection among insurers.

Section 3. *Scope.* This Act shall apply to all kinds of direct insurance, except life, title, surety, disability, credit, mortgage guaranty, and ocean marine insurance.

Comment: This bill focuses on property and liability kinds of insurance and therefore exempts those kinds of insurance deemed to present problems quite distinct from those of property and liability insurance. "Credit insurance" as used here is intended to mean insurance on accounts receivable.

Section 4. *Construction.* This Act shall be liberally construed to effect the purpose under s. 2 which shall constitute an aid and guide to interpretation.

Section 5. *Definitions.* As used in this Act. [Optional (1) "Account" means any one of the three accounts created by s. 6.]

Comment: This definition should be used by those states wishing to create separate accounts for assessment purposes.

For a note on the use of separate accounts for assessment see the comment after section 6. f this definition is used, all subsequent subsections should be renumbered.

(1) "Association" means the (state) Insurance Guaranty Association created under s. 6.

(2) "Commissioner" means the Commissioner of Insurance of this State.

(3) "Covered claim" means an unpaid claim, including one for unearned premiums, which arises out of and is within the coverage and not in excess of the applicable limits of an insurance policy to which this Act applies issued by an insurer, if such insurer becomes an insolvent insurer after the effective date of this Act and (a) the claimant or insured is a resident of this state at the time of the insured event; or (b) the property from which the claim arises is permanently located in this state. "Covered claim" shall not include any amount due any reinsurer, insurer, insurance pool, or underwriting association, as subrogation recoveries or otherwise.

Comment: The subcommittee feels that the claims covered by the Association should include all claims, including unearned premiums, arising from the policies of the insolvent insurer. A state may wish to exclude unearned premiums, in which case "excluding" should be substituted for "including" in the first line. However, recovery from this state's Association should be limited to persons having sufficient contacts with the state. The subcommittee does not feel that coverage should be extended to elements of the insurance industry which know or reasonably can be expected to know the financial condition of various companies.

The meaning of the term "residence" should be determined by the law of each state. This is especially true in relation to corporations, for the subcommittee feels "the residence" of a corporation should not necessarily be equated with its domicile.

(4) "Insolvent Insurer" means (a) an insurer authorized to transact insurance in this state either at the time the policy was issued or when the insured event occurred and (b) determined to be insolvent by a court of competent jurisdiction.

(5) "Member insurer" means any person who (a) writes any kind of insurance to which this Act applies under s. 3, including the exchange of reciprocal or inter-insurance contracts, and (b) is licensed to transact insurance in this state [, except (at the option of state)].

Comment: A state may wish to exempt from the act certain kinds of companies, such as farmer, county, township, or assessment mutuals, fraternals, or non-profit service plans.

(6) "Net direct written premiums" means direct gross premiums written in this state on insurance policies to which this Act applies, less return premiums thereon and dividends paid or credited to policyholders on such direct business. "Net direct written premiums" does not include premiums on contracts between insurers or reinsurers.

(7) "Person" means any individual, corporation, partnership, association or voluntary organization.

Comment: In some states it may be necessary to add reciprocals and insurance exchanges to this definition.

Each state will wish to examine its own statutes to determine whether this definition and the others listed above should be deleted and to determine whether additional definitions are necessary.

Section 6. *Creation of the Association.* There is created a non-profit unincorporated legal entity to be known as the (state) Insurance Guaranty Association. All insurers defined as member insurers in s.5(5) shall be and remain members of the Association as a condition of their authority to transact insurance in this state. The Association shall perform its functions under a plan of operation established and approved under s.9 and shall exercise its powers through a board of directors established under s.7.

[Alternate Section 6. *Creation of the Association.* There is created a non-profit unincorporated legal entity to be known as the (state) Insurance Guaranty Association. All insurers defined as member insurers in s.5(6) shall be and remain members of the Association as a condition of their authority to transact insurance in this state. The Association shall perform its functions under a plan of operation established and approved under s.9 and shall exercise its powers through a board of directors established under s.7. For purposes of administration and assessment, the Association shall be divided into three separate accounts: (a) The workmen's compensation insurance account; (b) The automobile insurance account; and (c) The account for all other insurance to which this Act applies.]

Comment: Although the Association is created here as a "non-profit unincorporated legal entity," each state will wish to examine its law to determine whether some alteration in this terminology is desirable.

The alternate section 6 should be used if a state, after examining its insurance market, determines that separate accounts for various kinds of insurance are necessary and feasible. The major consideration is whether each account will have a base sufficiently large to cover possible insolvencies. Such separate accounts will permit assessments to be generally limited to insurers writing the same kind of insurance as the insolvent company. If this approach is adopted the alternate provisions for sections 8(1)(c) and 8(2)(f) and new provision 5(1) should also be used.

Section 7. *Board of Directors.*

(1) The board of directors of the Association shall consist of not less than five (5) nor more than nine (9) persons serving terms as established in the plan of operation. The members of the board shall be selected by member insurers subject to the approval of the commissioner. Vacancies on the board shall be filled for the remaining period of the term in the same manner as initial appointments. If no members are selected within 60 days after the effective date of this Act, the commissioner may appoint the initial members of the board of directors.

(2) In approving selections to the board, the commissioner shall consider among other things whether all member insurers are fairly represented.

(3) Members of the board may be reimbursed from the assets of the Association for expenses incurred by them as members of the board of directors.

Comment: The number of members on the board of directors may be left open to some extent, as it is here, or it may be specified. The same holds true for the terms of office. A state may also wish to provide that a majority of the members of the board represent domestic insurers.

Section 8. *Powers and Duties of the Association.*

(1) The Association shall:

(a) Be obligated to the extent of the covered claims existing prior to the determination of insolvency and arising within 30 days after the determination of

insolvency, or before the policy expiration date if less than 30 days after the determination, or before the insured replaces the policy or causes its cancellation, if he does so within 30 days of the determination, but such obligation shall include only that amount of each covered claim which is in excess of $100 and is less than $300,000, except that the Association shall pay the full amount of any covered claim arising out of a workmen's compensation policy. In no event shall the Association be obligated to a policyholder or claimant in an amount in excess of the obligation of the insolvent insurer under the policy from which the claim arises.

Comment: The obligation of the Association is limited to covered claims unpaid prior to insolvency, and to claims arising within 30 days after the insolvency, or until the policy is canceled or replaced by the insured, or it expires, whichever is earlier. The basic principle is to permit policyholders to make an orderly transition to other companies. There appears to be no reason why the Association should become in effect an insurer in competition with member insurers by continuing existing policies, possibly for several years. It is also felt that the control of the policies is properly in the hands of the liquidator. Finally, one of the major objections of the public to rapid termination—loss of unearned premiums with no corresponding coverage—is ameliorated by this bill since unearned premiums are permissible claims against the Association.

The deductible amount ($100) and the maximum ($300,000) represent the subcommittee's concept of practical limitations.

(b) Be deemed the insurer to the extent of its obligation on the covered claims and to such extent shall have all rights, duties, and obligations of the insolvent insurer as if the insurer had not become insolvent.

(c) Assess insurers amounts necessary to pay the obligations of the Association under par. (a) subsequent to an insolvency, the expenses of handling covered claims subsequent to an insolvency, and the cost of examinations under s.13 and other expenses authorized by this Act. The assessments of each member insurer shall be in the proportion that the net direct written premiums of the member insurer for the preceding calendar year bears to the net direct written premiums of all member insurers for the preceding calendar year. Each member insurer shall be notified of the assessment not later than 30 days before it is due. No member insurer may be assessed in any year an amount greater than 2% of that member insurer's net direct written premiums for the preceding calendar year. If the maximum assessment, together with the other assets of the Association, does not provide in any one year an amount sufficient to make all necessary payments, the funds available shall be pro-rated and the unpaid portion shall be paid as soon thereafter as funds become available. The Association may exempt or defer, in whole or in part, the assessment of any member insurer, if the assessment would cause the member insurer's financial statement to reflect amounts of capital or surplus less than the minimum amounts required for a certificate of authority by any jurisdiction in which the member insurer is authorized to transact insurance. Each member insurer may set off against any assessment, authorized payments made on covered claims and expenses incurred in the payment of such claims by the member insurer.

[Alternate (c) Allocate claims paid and expenses incurred among the three accounts separately, and assess member insurers separately for each account amounts necessary to pay the obligations of the Association under par. (a) subsequent to an insolvency, the expenses of handling covered claims subsequent to an insolvency, the cost of examinations under s.13 and other expenses authorized by this Act. The assessments of each member insurer shall be in the proportion that the net direct written premiums of the member insurer for the preceding calendar year on the kinds of insurance in the account bears to the net direct written premiums of all member insurers for the preceding calendar year on the kinds of insurance in the account. Each member insurer shall be notified of the assessment not later than 30 days before it is due. No member insurer may be assessed in any year on any account an amount greater than 2% of that member insurer's net direct written premiums for the preceding calendar year on the kinds of insurance in the account. If the maximum assessment, together with the other assets of the Association in any account, does not provide in any one year in any account an amount sufficient to make all necessary payments from that account, the funds available shall be pro-rated and the unpaid portion shall be paid as soon thereafter as funds become available. The Association may exempt or defer, in whole or in part, the assessment of any member insurer, if the assessment would cause the member insurer's financial statement to reflect amounts of capital or surplus less than the minimum amounts required for a certificate of

authority by any jurisdiction in which the member insurer is authorized to transact insurance. Each member insurer may set off against any assessment, authorized payments made on covered claims and expenses incurred in the payment of such claims by the member insurer if they are chargeable to the account for which the assessment is made.]

Comment: The maximum assessment per year may be varied from state to state depending on the size of the base. The figure used should produce sufficient funds to handle any possible insolvency, keeping in mind that the total amount may not be needed in one year.

The 2% maximum used here would have produced in 1968 on a nation wide basis, from the kinds of insurance to which this Act applies, approximately $500,000,000. For a note on the use of alternate sections for separate accounts see the comment after section 6.

(d) Investigate claims brought against the Association and adjust, compromise, settle, and pay covered claims to the extent of the Association's obligation and deny all other claims and may review settlements, releases and judgments to which the insolvent insurer or its insureds were parties to determine the extent to which such settlements, releases and judgments may be properly contested.

(e) Notify such persons as the commissioner directs under s.10(2)(a).

Comment: The liquidation statutes of the state may describe the persons to be notified by the liquidator, but since this assocition provides a distinctive service, the commissioner may wish to require a separate notification by it.

(f) Handle claims through its employees or through one or more insurers or other persons designated as servicing facilities. Designation of a servicing facility is subject to the approval of the commissioner, but such designation may be declined by a member insurer.

(g) Reimburse each servicing facility for obligations of the Association paid by the facility and for expenses incurred by the facility while handling claims on behalf of the Association and shall pay the other expenses of the Association authorized by this Act.

(2) The Association may:

(a) Employ or retain such persons as are necessary to handle claims and perform other duties of the Association.

(b) Borrow funds necessary to effect the purposes of this Act in accord with the plan of operation.

(c) Sue or be sued.

(d) Negotiate and become a party to such contracts as are necessary to carry out the purpose of this Act.

(e) Perform such other acts as are necessary or proper to effectuate the purpose of this Act.

(f) Refund to the member insurers in proportion to the contribution of each member insurer to the Association that amount by which the assets of the Association exceed the liabilities, if, at the end of any calendar year, the board of directors finds that the assets of the Association exceed the liabilities of the Association as estimated by the board of directors for the coming year.

[Alternate (f). Refund to the member insurers in proportion to the contribution of each member insurer to that account that amount by which the assets of the account exceed the liabilities, if, at the end of any calendar year, the board of directors finds that the assets of the Association in any account exceed the liabilities of that account as estimated by the board of directors for the coming year.]

Comment: The subcommittee feels that the board of directors should determine the amount of the refunds to members when the assets of the Association exceed its liabilities. However, since this excess may be quite small, the board is given the option of retaining all or part of it to pay expenses and possibly remove the need for a relatively small assessment at a later time. For the notes concerning the use of the alternate section for separate accounts, see the comment after section 6.

Section 9. *Plan of Operation.*

(1)(a) The Association shall submit to the commissioner a plan of operation and any amendments thereto necessary or suitable to assure the fair, reasonable, and equitable administration of the Association. The plan of operation and any amendments thereto shall become effective upon approval in writing by the commissioner.

(b) If the Association fails to submit a suitable plan of operation within 90 days following the effective date of this Act or if at any time thereafter the Association fails to submit suitable amendments to the plan, the commissioner shall, after notice and hearing, adopt and promulgate such reasonable rules as

are necessary or advisable to effectuate the provisions of this Act. Such rules shall continue in force until modified by the commissioner or superseded by a plan submitted by the Association and approved by the commissioner.

(2) All member insurers shall comply with the plan of operation.

(3) The plan of operation shall:

(a) Establish the procedures whereby all the powers and duties of the Association under S. 8 will be performed.

(b) Establish procedures for handling assets of the Association.

(c) Establish the amount and method of reimbursing members of the board of directors under S. 7.

(d) Establish procedures by which claims may be filed with the Association and establish acceptable forms of proof of covered claims. Notice of claims to the receiver or liquidator of the insolvent insurer shall be deemed notice to the Association or its agent and a list of such claims shall be periodically submitted to the Association or similar organization in another state by the receiver or liquidator.

Comment: On the general subject of the relationship of the association to the liquidator, the subcommittee takes the position that since this is a model state bill, it will be able to bind only two parties—the association and the in-state liquidator. Nevertheless, the provisions should be clear enough to outline the requests being made to out-of-state liquidators and the requirements placed on in-state liquidators in relation to out-of-state associations.

(e) Establish regular places and times for meetings of the board of directors.

(f) Establish procedures for records to be kept of all financial transactions of the Association, its agents, and the board of directors.

(g) Provide that any member insured aggrieved by any final action or decision of the Association may appeal to the commissioner within 30 days after the action or decision.

(h) Establish the procedures whereby selections for the board of directors will be submitted to the commissioner.

(i) Contain additional provisions necessary or proper for the execution of the powers and duties of the Association.

(4) The plan of operation may provide that any or all powers and duties of the Association, except those under ss. 8(1)(c) and 8(2)(b), are delegated to a corporation, association, or other organization which performs or will perform functions similar to those of this Association, or its equivalent, in two or more states. Such a corporation, association or organization shall be reimbursed as a servicing facility would be reimbursed and shall be paid for its performance of any other functions of the Association. A delegation under this subsection shall take effect only with the approval of both the board of directors and the commissioner, and may be made only to a corporation, association, or organization which extends protection not substantially less favorable and effective than that provided by this Act.

Comment: The subcommittee recognizes current discussion at both the regulatory and industry levels concerning the possible creation of a non-federal interstate organization to perform various functions relating to the protection of policyholders and claimants from insurer insolvency. It is difficult at present to predict the type of interstate arrangement which may evolve. At the same time, the subcommittee would like to avoid the necessity of returning to each state legislature if a desirable non-federal interstate approach is developed. Consequently, this subsection, with appropriate standards and regulatory safeguard, provides a highly flexible transition device. The subsection operates on the theory of a revocable delegation of functions in the plan of operations if approved by the industry and the commissioner. The board of directors would continue in existence in each state which would, among other things, provide the commissioner with a contact for his regulatory control. In addition, membership would continue to be mandatory state by state as recognized under this bill and no new legislation would be necessary. This approach would permit the gradual development (e.g. a partial delegation of powers) of an interstate system as opposed to an all or nothing choice. Finally, it should be noted that the Association may not delegate its powers to assess or borrow money. Assessments would continue to be made on a state by state basis in accordance with the provisions of the individual state statutes.

Section 10. *Duties and Powers of the Commissioner.*

(1) The commissioner shall:

(a) Notify the Association of the existence of an insolvent insurer not later than 3 days after he receives notice of the determination of the insolvency.

(b) Upon request of the board of directors, provide the Association with a statement of the net direct written premiums of each member insurer.

(2) The commissioner may:

(a) Require that the Association notify the insureds of the insolvent insurer and any other interested parties of the determination of insolvency and of their rights under this Act. Such notification shall be by mail at their last known address, where available, but if sufficient information for notification by mail is not available, notice by publication in a newspaper of general circulation shall be sufficient.

(b) Suspend or revoke, after notice and hearing, the certificate of authority to transact insurance in this state of any member insurer which fails to pay an assessment when due or fails to comply with the plan of operation. As an alternative, the commissioner may levy a fine on any member insurer which fails to pay an assessment when due. Such fine shall not exceed 5% of the unpaid assessment per month, except that no fine shall be less than $100 per month.

(c) Revoke the designation of any servicing facility if he finds claims are being handled unsatisfactorily.

(3) Any final action or order of the commissioner under this Act shall be subject to judicial review in a court of competent jurisdiction.

Comment: This subsection may be omitted if the insurance statutes of a state provide for judicial review of all actions or orders of the commissioner.

Section 11. *Effect of Paid Claims.*

(1) Any person recovering under this Act shall be deemed to have assigned his rights under the policy to the Association to the extent of his recovery from the Association. Every insured or claimant seeking the protection of this Act shall cooperate with the Association to the same extent as such person would have been required to cooperate with the insolvent insurer. The Association shall have no cause of action against the insured of the insolvent insurer for any sums it has paid out except such causes of action as the insolvent insurer would have had if such sums had been paid by the insolvent insurer. In the case of an insolvent insurer operating on a plan with assessment liability, payments of claims of the Association shall not operate to reduce the liability of insured's to the receiver, liquidator, or statutory successor for unpaid assessments.

(2) The receiver, liquidator, or statutory successor of an insolvent insurer shall be bound by settlements of covered claims by the Association or a similar organization in another state. The court having jurisdiction shall grant such claims priority equal to that which the claimant would have been entitled in the absence of this Act against the assets of the insolvent insurer. The expenses of the Association or similar organization in handling claims shall be accorded the same priority as the liquidator's expenses.

Comment. The priority of claims against the assets of the insolvent insurer may be determined by the liquidation statutes. States which do not set such priorities by statute may wish to revise the language in this subsection. It seems probable that the courts would treat claims by the Association on the basis of the underlying claim, as this subsection requires, even in the absence of this provision.

(3) The Association shall periodically file with the receiver or liquidator of the insolvent insurer statements of the covered claims paid by the Association and estimates of anticipated claims on the Association which shall preserve the rights of the Association against the assets of the insolvent insurer.

Section 12. *Non-duplication of Recovery.*

(1) Any person having a claim against an insurer under any provision in an insurance policy other than a policy of an insolvent insurer which is also a covered claim, shall be required to exhaust first his right under such policy. Any amount payable on a covered claim under this Act shall be reduced by the amount of any recovery under such insurance policy.

(2) Any person having a claim which may be recovered under more than one insurance guaranty association or its equivalent shall seek recovery first from the association of the place of residence of the insured except that if it is a first party claim for damage to property with a permanent location, he shall seek recovery first from the association of the location of the property, and if it is a workmen's compensation claim, he shall seek recovery first from the association of the residence of the claimant. Any recovery under this Act shall be reduced by the amount of recovery from any other insurance guaranty association or its equivalent.

Comment: This subsection does not prohibit recovery from more than one association, but it does describe the association to be approached first and then requires that any previous recoveries from like associations must be set-off against recoveries from this association.

Section 13. *Prevention of Insolvencies.*

To aid in the detection and prevention of insurer insolvencies (1) It shall be the duty of the board of directors, upon majority vote, to notify the commissioner of any information indicating any member insurer may be insolvent or in a financial condition hazardous to the policyholders or the public.

(2) The board of directors may, upon majority vote, request that the commissioner order an examination of any member insurer which the board in good faith believes may be in a financial condition hazardous to the policyholders or the public. Within 30 days of the receipt of such request, the commissioner shall begin such examination. The examination may be conducted as a National Association of Insurance Commissioners examination or may be conducted by such persons as the commissioner designates. The cost of such examination shall be paid by the Association and the examination report shall be treated as are other examination reports. In no event shall such examination report be released to the board of directors prior to its release to the public, but this shall not preclude the commissioner from complying with subsection (3). The commissioner shall notify the board of directors when the examination is completed. The request for an examination shall be kept on file by the commissioner but it shall not be open to public inspection prior to the release of the examination report to the public.

Comment: The board of directors could be expected to request an examination when they have information suggesting the presence of activities which could lead to rehabilitation under the Wisconsin Rehabilitation and Liquidation Act which has been endorsed by the NAIC. These activities are outlined in section 645.31 of the Wisconsin Statutes.

(3) It shall be the duty of the commissioner to report to the board of directors when he has reasonable cause to believe that any member insurer examined or being examined at the request of the board of directors may be insolvent or in a financial condition hazardous to the policyholders or the public.

(4) The board of directors may, upon majority vote, make reports and recommendations to the commissioner upon any matter germane to the solvency, liquidation, rehabilitation or conservation of any member insurer. Such reports and recommendations shall not be considered public documents.

(5) The board of directors may, upon majority vote, make recommendations to the commissioner for the detection and prevention of insurer insolvencies.

(6) The board of directors shall, at the conclusion of any insurer insolvency in which the Association was obligated to pay covered claims, prepare a report on the history and causes of such insolvency, based on the information available to the Association, and submit such report to the commissioner.

Section 14. *Examination of the Association.*

The Association shall be subject to examination and regulation by the commissioner. The board of directors shall submit, not later than March 30 of each year, a financial report for the preceding calendar year in a form approved by the commissioner.

Section 15. *Tax Exemption.*

The Association shall be exempt from payment of all fees and all taxes levied by this state or any of its subdivisions except taxes levied on real or personal property.

Section 16. *Recognition of Assessments in Rates.*

The rates and premiums charged for insurance policies to which this Act applies shall include amounts sufficient to recoup a sum equal to the amounts paid to the Association by the member insurer less any amounts returned to the member insurer by the Association and such rates shall not be deemed excessive because they contain an amount reasonably calculated to recoup assessments paid by the member insurer.

Comment: Although generally rates are prospective in nature, this section would permit recoupment of amounts assessed in the past.

Section 17. *Immunity.*

There shall be no liability on the part of and no cause of action of any nature shall arise against any member insurer, the Association or its agents or employees, the board of directors, or the commissioner or his representatives for any action taken by them in the performance of their powers and duties under this Act.

Section 18. *Stay of Proceedings; Reopening of Default Judgments.*

All proceedings in which the insolvent insurer is a party or is obligated to defend a party in any court in this state shall be stayed for 60 days from the date the insolvency is determined to permit proper defense by the Association of all pending causes of action. As to any covered claims arising from a judgment under any decision, verdict or finding based on the default of the insolvent insurer or its failure to defend an insured, the Association either on its own behalf or on behalf of such insured may apply to have such judgment, order, decision, verdict or finding set aside by the same court or administrator that made such judgment, order, decision, verdict or finding and shall be permitted to defend against such claim on the merits.

General comments: Each state may wish to consider the following when preparing this bill:

1. The addition of an effective date section.
2. The addition of a section amending the state retaliatory law so that assessments by insurance guaranty associations or similar organizations are not considered in determining retaliatory taxation.
3. The addition of a section amending the state liquidation statute to permit or require the liquidator to make periodic partial payments to the Association. This will serve to reduce the size and frequency of assessments.
4. The addition of a section specifically permitting or prohibiting advertisements by member insurers which include a reference to the coverage of the insurance guaranty association.

Mr. WORTHINGTON. The bill requires that all insurers licensed to do business in the State be members of the guaranty fund association as a condition to receiving a license to do business. It then provides that there be selected from among the companies licensed to do business in the State a board of directors. This board of directors is selected by the industry themselves and then submitted to the insurance commissioner for his approval or disapproval.

So, the regulatory function remains with the commissioner or the supervisory official in the State. The selection of the directors is the only activity which would occur until such time as there would be reasonable belief that a company was operating in such a manner that might be hazardous to the policyholders or the public, and if this should occur, several things could happen.

Some mention was made this morning about the nonpreventive parts of State guaranty funds. I would say already the State examination procedures are geared primarily toward the prevention of insolvencies or the detection of insolvencies, and though there have been some problems with that in the past, this is the crux of State regulation, and there are thousands of insurance companies that have not gone insolvent.

Many insurance companies have been rehabilitated, many insurance companies which would have gone insolvent were it not for the regulatory process of the insurance commissioner. Recognizing this, we still recognize there are obvious problems, and you mentioned two just a minute ago. So, the board has as its duties under the provisions of our model bill the notification of the insurance department if they have reason to believe through the rumors in the business which are always prevalent that there may be a company which is in difficulty.

Then they also request the commissioner, if the commissioner doesn't act, to conduct an examination which may be either an NAIC examination, which would involve more than the commissioner of one State, or an examination force which would be delegated by the commissioner, such as outside accounting firms.

Upon request, the commissioner must within 30 days begin the examination. Now, after the examination has begun, when it reaches a point at which time he has reason to believe that there may be activities which would be hazardous to the policyholders and the public, he then

must notify the board that this is the case and that the association which has been created will in all probability be subjected to an assessment.

Assuming that it is carried out to its logical conclusions and the company is found to be insolvent, then immediately the assessment functions would take over and the companies would be assessed in proportion to their direct premiums in that State up to a maximum of 2 percent in any one year, and the maximum is put on in order to attempt to solve the problem of companies pledging their total assets and leaving them open to claims on the surplus of their company which they couldn't plan for.

When the assessments are made, the association then assumes all the liabilities and responsibilities that the insolvent company had to its insurers and begins immediately to settle claims without waiting for the courts to go through the process of liquidating them. So, the policyholders receive their moneys immediately as if the company had not in fact become insolvent.

The association then would have a right to share in the amounts of money or the assets that would be left upon liquidation in proportion to the moneys they had paid out on behalf of that association.

We have included in our model bill provision for paying back to the policyholders on a deductible basis all claims in excess of $100, including unearned premium as well as the claims they might have as an result of losses. We have placed a limitation of $300 on any claim in order to avoid having the association paying out large claims which would go to people who would not be hurt as significantly as the average person would, because the thrust of our bill is to protect the average person, to provide them with immediate payment as though the company was not insolvent and to provide a payment whereby the public can maintain its confidence in the insurance industry.

There were some statements made about postassessment guarantee funds; one, they don't prevent insolvency. We maintain in our bill we have the same thrust as you would have under S. 2236, only more effectively probably, because it would be conducted without the confusion of two agencies probably or possibly going in different directions, that it would be conducted with industry people involved not to the regulating point but to the point of counsel and advice.

The exposure of the unknown liability is not nonexistence. It is limited to 2 percent in 1 year. It does, we admit, place the burden of solvency on well-managed companies. We don't deny that. We feel it is the responsibility of the insurance industry to care for the insurance buying public and to provide a kind of protection, recognizing however that in their rating structure the costs which would be assessed them if they are significant to support this would be passed on to the policyholders and the consumer just as they would be the way I understand S. 2236.

The self-policing aspect of the industry is one which we think is sound. We feel that the industry ought to assume some responsibility for policing themselves and to assure the public that they are in fact what they represent themselves to be. We do not in any way, however, abrogate the responsibility of the commissioners to assume the burden for regulation, and the thrust of regulation is upon the commissioners, not upon the industry.

The model bill has a provision wherein the commissioner in any state can mesh the postassessment guarantee fund, as we propose it, into any other fund that has been adopted on a national or regional basis so there would not be conflict or confusion or the need to go back to the legislative process in order to make the change which might come through the establishment of what we call a nationwide non-Federal facility or reinsurance pool or voluntary association of insurers to guarantee their solvencies.

Senator HART. We will receive that draft bill for the record.

(The draft bill follows:)

NAIC STATE POSTASSESSMENT INSURANCE GUARANTY ASSOCIATION MODEL BILL

Section 1. Title

This Act shall be known and may be cited as the (state) Insurance Guaranty Association Act.

Section 2. Purpose

The purpose of this Act is to provide a mechanism for the payment of covered claims under certain insurance policies to avoid excessive delay in payment and to avoid financial loss to claimants or policyholders because of the insolvency of an insurer, to assist in the detection and prevention of insurer insolvencies, and to provide an association to assess the cost of such protection among insurers.

Section 3. Scope

This Act shall apply to all kinds of direct insurance, except life, title, surety, disability, credit, mortgage guaranty, and ocean marine insurance.

Comment. This bill focuses on property and liability kinds of insurance and therefore exempts those kinds of insurance deemed to present problems quite distinct from those of property and liability insurance. "Credit insurance" as used here is intended to mean insurance on accounts receivable.

Section 4. Construction

This Act shall be liberally construed to effect the purpose under s.2 which shall constitute an aid and guide to interpretation.

Section 5. Definitions

As used in this Act [Optional (1) "Account" means any one of the three accounts created by s.6.].

Comment. This definition should be used by those states wishing to create separate accounts for assessment purposes.

For a note on the use of separate accounts for assessments see the comment after section 6. If this definition is used, all subsequent subsections should be renumbered.

(1) "Association" means the (state) Insurance Guaranty Association created under s.6.

(2) "Commissioner" means the Commissioner of Insurance of this State.

(3) "Covered claim" means an unpaid claim, including one for unearned premiums, which arises out of and is within the coverage and not in excess of the applicable limits of an insurance policy to which this Act applies issued by an insurer, if such insurer becomes an insolvent insurer after the effective date of this Act and (a) the claimant or insured is a resident of this state at the time of the insured event; or (b) the property from which the claim arises is permanently located in this state. "Covered claim" shall not include any amount due any reinsurer, insurer, insurance pool, or underwriting association, as subrogation recoveries or otherwise.

Comment. The subcommittee feels that the claims covered by the Association should include all claims, including unearned premiums, arising from the policies of the insolvent insurer. A state may wish to exclude unearned premiums, in which case "excluding" should be substituted for "including" in the first line. However, recovery from this state's Association should be limited to persons having sufficient contacts with the state. The subcommittee does not feel that coverage should be extended to elements of the insurance

industry which know or reasonably can be expected to know the financial condition of various companies.

The meaning of the term "residence" should be determined by the law of each state. This is especially true in relation to corporations, for the subcommittee feels the "residence" of a corporation should not necessarily be equated with its domicile.

(4) "Insolvent Insurer" means (a) an insurer authorized to transact insurance in this state either at the time the policy was issued or when the insured event occurred and (b) determined to be insolvent by a court of competent jurisdiction.

(5) "Member insurer" means any person who (a) writes any kind of insurance to which this Act applies under s. 3, including the exchange of reciprocal or inter-insurance contracts, and (b) is licensed to transact insurance in this state [, except (at option of state)].

Comment. A state may wish to exempt from the act certain kinds of companies, such as farmer, county, township, or assessment mutuals, fraternals, or nonprofit service plans.

(6) "Net direct written premiums" means direct gross premiums written in this state on insurance policies to which this Act applies, less return premiums thereon and dividends paid or credited to policyholders on such direct business. "Net direct written premiums" does not include premiums on contracts between insurers or reinsurers.

(7) "Person" means any individual, corporation, partnership, association or voluntary organization.

Comment. In some states it may be necessary to add reciprocals and insurance exchanges to this definition.

Each state will wish to examine its own statutes to determine whether this definition and the others listed above should be deleted and to determine whether additional definitions are necessary.

Section 6. Creation of the Association

There is created a non-profit unincorporated legal entity to be known as the (state) Insurance Guaranty Association. All insurers defined as member insurers in s. 5(5) shall be and remain members of the Association as a condition of their authority to transact insurance in this state. The Association shall perform its functions under a plan of operation established and approved under s. 9 and shall exercise its powers through a board of directors established under s. 7.

[*Alternate Section 6. Creation of the Association*

There is created a non-profit unincorporated legal entity to be known as the (state) Insurance Guaranty Association. All insurers defined as member insurers in s. 5(6) shall be and remain members of the Association as a condition of their authority to transact insurance in this state. The Association shall perform its functions under a plan of operation established and approved under s. 9 and shall exercise its powers through a board of directors established under s. 7. For purposes of administration and assessment, the Association shall be divided into three separate accounts: (a) The workmen's compensation insurance account; (b) The automobile insurance account; and (c) The account for all other insurance to which this Act applies.]

Comment. Although the Association is created here as a "non-profit unincorporated legal entity," each state will wish to examine its law to determine whether some alteration in this terminology is desirable.

The alternate section 6 should be used if a state, after examining its insurance market, determines that separate accounts for various kinds of insurance are necessary and feasible. The major consideration is whether each account will have a base sufficiently large to cover possible insolvencies. Such separate accounts will permit assessments to be generally limited to insurers writing the same kind of insurance as the insolvent company. If this approach is adopted the alternate provisions for sections 8(1)(c) and 8(2)(f) and new provision 5(1) should also be used.

Section 7. Board of Directors

(1) The board of directors of the Association shall consist of not less than five (5) nor more than nine (9) persons serving terms as established in the plan of operation. The members of the board shall be selected by member insurers subject to the approval of the commissioner. Vacancies on the board shall be filled for the remaining period of the term in the same manner as initial appointments. If no members are selected within 60 days after the effective date of this Act, the commissioner may appoint the initial members of the board of directors.

(2) In approving selections to the board, the commissioner shall consider among other things whether all member insurers are fairly represented.

(3) Members of the board may be reimbursed from the assets of the Association for expenses incurred by them as members of the board of directors.

Comment. The number of members on the board of directors may be left open to some extent, as it is here, or it may be specified. The same holds true for the terms of office. A state may also wish to provide that a majority of the members of the board represent domestic insurers.

Section 8. Powers and Duties of the Association

(1) The Association shall:

(a) Be obligated to the extent of the covered claims existing prior to the determination of insolvency and arising within 30 days after the determination of insolvency, or before the policy expiration date if less than 30 days after the determination, or before the insured replaces the policy or causes its cancellation, if he does so within 30 days of the determination, but such obligation shall include only that amount of each covered claim which is in excess of $100 and is less than $300,000, except that the Association shall pay the full amount of any covered claim arising out of a workmen's compensation policy. In no event shall the Association be obligated to a policyholder or claimant in an amount in excess of the obligation of the insolvent insurer under the policy from which the claim arises.

Comment. The obligation of the Association is limited to covered claims unpaid prior to insolvency, and to claims arising within 30 days after the insolvency, or until the policy is canceled or replaced by the insured, or it expires, whichever is earlier. The basic principle is to permit policyholders to make an orderly transition to other companies. There appears to be no reason why the Association should become in effect an insurer in competition with member insurers by continuing existing policies, possibly for several years. It is also felt that the control of the policies is properly in the hands of the liquidator. Finally, one of the major objections of the public to rapid termination—loss of unearned premiums with no corresponding coverage—is ameliorated by this bill since unearned premiums are permissible claims against the Association.

The deductible amount ($100) and the maximum ($300,000) represent the subcommittee's concept of practical limitations.

(b) Be deemed the insurer to the extent of its obligation on the covered claims and to such extent shall have all rights, duties, and obligations of the insolvent insurer as if the insurer had not become insolvent.

(c) Assess insurers amounts necessary to pay the obligations of the Association under par. (a) subsequent to an insolvency, the expenses of handling covered claims subsequent to an insolvency, and the cost of examinations under s. 13 and other expenses authorized by this Act. The assessments of each member insurer shall be in the proportion that the net direct written premiums of the member insurer for the preceding calendar year bears to the net direct written premiums of all member insurers for the preceding calendar year. Each member insurer shall be notified of the assessment not later than 30 days before it is due. No member insurer may be assessed in any year an amount greater than 2% of that member insurer's net direct written premiums for the preceding calendar year. If the maximum assessment, together with the other assets of the Association, does not provide in any one year an amount sufficient to make all necessary payments, the funds available shall be pro-rated and the unpaid portion shall be paid as soon thereafter as funds become available. The Association may exempt or defer, in whole or in part, the assessment of any member insurer, if the assessment would cause the member insurer's financial statement to reflect amounts of capital or surplus less than the minimum amounts required for a certificate of authority by any jurisdiction in which the member insurer is authorized to transact insurance. Each member insurer may set off against any assessment, authorized payments made on covered claims and expenses incurred in the payment of such claims by the member insurer.

[Alternate (c) Allocate claims paid and expenses incurred among the three accounts separately, and assess member insurers separately for each account amounts necessary to pay the obligations of the Association under par. (a) subsequent to an insolvency, the expenses of handling covered claims subsequent to an insolvency, the cost of examinations under s. 13 and other expenses authorized by this Act. The assessments of each member insurer shall be in the proportion that the net direct written premiums of the member insurer for the preceding

calendar year on the kinds of insurance in the account bears to the net direct written premiums of all members insurers for the preceding calendar year on the kinds of insurance in the account. Each member insurer shall be notified of the assessment not later than 30 days before it is due. No member insurer may be assessed in any year on any account an amount greater than 2% of that member insurer's net direct written premiums for the preceding calendar year on the kinds of insurance in the account. If the maximum assessment, together with the other assets of the Association in any account, does not provide in any one year in any account an amount sufficient to make all necessary payments from that account, the funds available shall be pro-rated and the unpaid portion shall be paid as soon thereafter as funds become available. The Association may exempt or defer, in whole or in part, the assessment of any member insurer, if the assessment would cause the member insurer's financial statement to reflect amounts of capital or surplus less than the minimum amounts required for a certificate of authority by any jurisdiction in which the member insurer is authorized to transact insurance. Each member insurer may set off against any assessment, authorized payments made on covered claims and expenses incurred in the payment of such claims by the member insurer if they are chargeable to the account for which the assessment is made.]

Comment. The maximum assessment per year may be varied from state to state depending on the size of the base. The figure used should produce sufficient funds to handle any possible insolvency, keeping in mind that the total amount may not be needed in one year.

The 2% maximum used here would have produced in 1968 on a nation wide basis, from the kinds of insurance to which this Act applies, approximately $500,000,000. For a note on the use of alternate sections for separate accounts see the comment after section 6.

(d) Investigate claims brought against the Association and adjust, compromise, settle, and pay covered claims to the extent of the Association's obligation and deny all other claims and may review settlements, releases and judgments to which the insolvent insurer or its insureds were parties to determine the extent to which such settlements, releases and judgments may be properly contested.

(e) Notify such persons as the commissioner directs under s. 10(2)(a).

Comment. The liquidation statutes of the state may describe the persons to be notified by the liquidator, but since this association provides a distinctive service, the commissioner may wish to require a separate notification by it.

(f) Handle claims through its employees or through one or more insurers or other persons designated as servicing facilities. Designation of a servicing facility is subject to the approval of the commissioner, but such designation may be declined by a member insurer.

(g) Reimburse each servicing facility for obligations of the Association paid by the facility and for expenses incurred by the facility while handling claims on behalf of the Association and shall pay the other expenses of the Association authorized by this Act.

(2) The Association may:

(a) Employ or retain such persons as are necessary to handle claims and perform other duties of the Association.

(b) Borrow funds necessary to effect the purposes of this Act in accord with the plan of operation.

(c) Sue or be sued.

(d) Negotiate and become a party to such contracts as are necessary to carry out the purpose of this Act.

(e) Perform such other acts as are necessary or proper to effectuate the purpose of this Act.

(f) Refund to the member insurers in proportion to the contribution of each member insurer to the Association that amount by which the assets of the Association exceed the liabilities, if, at the end of any calendar year, the board of directors finds that the assets of the Association exceed the liabilities of the Association as estimated by the board of directors for the coming year.

[Alternate (f). Refund to the member insurers in proportion to the contribution of each member insurer to that account that amount by which the assets of the account exceed the liabilities, if, at the end of any calendar year, the board of directors finds that the assets of the Association in any account exceed the liabilities of that account as estimated by the board of directors for the coming year.

Comment. The subcommittee feels that the board of directors should determine the amount of the refunds to members when the assets of the Association exceed its liabilities. However, since this excess may be quite small, the board is given the option of retaining all or part of its to pay expenses and possibly remove the need for a relatively small assessment at a later time. For the notes concerning the use of the alternate section for separate accounts, see the comment after section 6.

Section 9. Plan of Operation

(1) (a) The Association shall submit to the commissioner a plan of operation and many amendments thereto necessary or suitable to assure the fair, reasonable, and equitable administration of the Association. The plan of operation and many amendments thereto shall become effective upon approval in writing by the commissioner.

(b) If the Association fails to submit a suitable plan of operation within 90 days following the effective date of this Act or if at any time thereafter the Association fails to submit suitable amendments to the plan, the commissioner shall, after notice and hearing, adopt and promulgate such reasonable rules as are necessary or advisable to effectuate the provisions of this Act. Such rules shall continue in force until modified by the commissioner or superseded by a plan submitted by the Association and approved by the commissioner.

(2) All members insurers shall comply with the plan of operation.

(3) The plan of operation shall:

(a) Establish the procedures whereby all the powers and duties of the Association under s. 8 will be performed.

(b) Establish procedures for handling assets of the Association.

(c) Establish the amount and method of reimbursing members of the board of directors under s. 7.

(d) Establish procedures by which claims may be filed with the Association and establish acceptable forms of proof of covered claims. Notice of claims to the receiver or liquidator of the insolvent insurer shall be deemed notice to the Association or its agent and a list of such claims shall be periodically submitted to the Association or similar organization in another state by the receiver or liquidator.

Comment. On the general subject of the relationship of the association to the liquidator, the subcommittee takes the position that since this is a model state bill, it will be able to bind only two parties—the association and the in-state liquidator. Nevertheless, the provisions should be clear enough to outline the requests being made to out-of-state liquidators and the requirements placed on in-state liquidators in relation to out-of-state associations.

(e) Establish regular places and times for meetings of the board of directors.

(f) Establish procedures for records to be kept of all financial transactions of the Association, its agents, and the board of directors.

(g) Provide that any member insurer aggrieved by any final action or decision of the Association may appeal to the commissioner within 30 days after the action or decision.

(h) Establish the procedures whereby selections for the board of directors will be submitted to the commissioner.

(i) Contain additional provisions necessary or proper for the execution of the power and duties of the Association.

(4) The plan of operation may provide that any or all powers and duties of the Association, except, those under ss. 8(1)(c) and 8(2)(b), are delegated to a corporation, association, or other organization which performs or will perform functions similar to those of this Association, or its equivalent, in two or more states. Such a corporation, association or organization shall be reimbursed as a servicing facility would be reimbursed and shall be paid for its performance of any other functions of the Association. A delegation under this subsection shall take effect only with approval of both the board of directors and the commissioner, and may be made only to a corporation, association, or organization which extends protection not substantially less favorable and effective than that provided by this Act.

Comment. The subcommittee recognizes current discussions at both the regulatory and industry levels concerning the possible creation of a nonfederal interstate organization to perform various functions relating to the protection of policyholders and claimants from insurer insolvency. It is difficult at present to predict the type of interstate arrangement which may

evolve. At the same time, the subcommittee would like to avoid the necessity of returning to each state legislature if a desirable non-federal interstate approach is developed. Consequently, this subsection, with appropriate standards and regulatory safeguard, provides a highly flexible transition device. The subsection operates on the theory of a revocable delegation of functions in the plan of operations if approved by the industry and the commissioner. The board of directors would continue in existence in each state which would, among other things, provide the commissioner with a contact for his regulatory control. In addition, membership would continue to be mandatory state by state as recognized under this bill and no new legislation would be necessary. This approach would permit the gradual development (e.g. a partial delegation of powers) of an interstate system as opposed to an all or nothing choice. Finally, it should be noted that the Association may not delegate its powers to assess or borrow money. Assessments would continue to be made on a state by state basis in accordance with the provisions of the individual state statutes.

Section 10. Duties and Powers of the Commisioner

(1) The commissioner shall:

(a) Notify the Association of the existence of an insolvent insurer not later than 3 days after he receives notice of the determination of the insolvency.

(b) Upon request of the board of directors, provide the Association with a statement of the net direct written premiums of each member insurer.

(2) The commissioner may:

(a) Require that the Association notify the insureds of the insolvent insurer and any other interested parties of the determination of insolvency and of their rights under this Act. Such notification shall be by mail at their last known address, where available, but if sufficient information for notification by mail is not available, notice by publication in a newspaper of general circulation shall be sufficient.

(b) Suspend or revoke, after notice and hearing, the certificate of authority to transact insurance in this state of any member insurer which fails to pay an assessment when due or fails to comply with the plan of operation. As an alternative, the commissioner may levy a fine on any member insurer which fails to pay an assessment when due. Such fine shall not exceed 5% of the unpaid assessment per month, except that no fine shall be less than $100 per month.

(c) Revoke the designation of any servicing facility if he finds claims are being handled unsatisfactorily.

(3) Any final action or order of the commissioner under this Act shall be subject to judicial review in a court of competent jurisdiction.

Comment. This subsection may be omitted if the insurance statutes of a state provide for judicial review of all actions or orders of the commissioner.

Section 11. Effect of Paid Claims

(1) Any person recovering under this Act shall be deemed to have assigned his rights under the policy to the Association to the extent of his recovery from the Association. Every insured or claimant seeking the protection of this Act shall cooperate with the Association to the same extent as such person would have been required to cooperate with the insolvent insurer. The Association shall have no cause of action against the insured of the insolvent insurer for any sums it has paid out except such causes of action as the insolvent insurer would have had if such sums had been paid by the insolvent insurer. In the case of an insolvent insurer operating on a plan with assessment liability, payments of claims of the Association shall not operate to reduce the liability of insured's to the receiver, liquidator, or statutory successor for unpaid assessments.

(2) The receiver, liquidator, or statutory successor of an insolvent insurer shall be bound by settlements of covered claims by the Association or a similar organization in another state. The court having jurisdiction shall grant such claims priority equal to that which the claimant would have been entitled in the absence of this Act against the assets of the insolvent insurer. The expenses of the Association or similar organization in handling claims shall be accorded the same priority as the liquidator's expenses.

Comment. The priority of claims against the assets of the insolvent insurer may be determined by the liquidation statutes. States which do not set such priorities by statute may wish to revise the language in this subsection. It seems probable that the courts would treat claims by the As-

sociation on the basis of the underlying claim, as this subsection requires, even in the absence of this provision.

(3) The Association shall periodically file with the receiver or liquidator of the insolvent insurer statements of the covered claims paid by the Association and estimates of anticipated claims on the Association which shall preserve the rights of the Association against the assets of the insolvent insurer.

Section 12. Non-duplication of Recovery

(1) Any person having a claim against an insurer under any provision in an insurance policy other than a policy of an insolvent insurer which is also a covered claim, shall be required to exhaust first his right under such policy. Any amount payable on a covered claim under this Act shall be reduced by the amount of any recovery under such insurance policy.

(2) Any person having a claim which may be recovered under more than one insurance guaranty association or its equivalent shall seek recovery first from the association of the place of residence of the insured except that if it is a first party claim for damage to property with a permanent location, he shall seek recovery first from the association of the location of the property, and if it is a workmen's compensation claim, he shall seek recovery first from the association of the residence of the claimant. Any recovery under this Act shall be reduced by the amount of recovery from any other insurance guaranty association or its equivalent.

Comment. This subsection does not prohibit recovery from more than one association, but it does describe the association to be approached first and then requires that any previous recoveries from like associations must be set-off against recoveries from this association.

Section 13. Prevention of Insolvencies

To aid in the detection and prevention of insurer insolvencies (1) It shall be the duty of the board of directors, upon majority vote, to notify the commissioner of any information indicating any member insurer may be insolvent or in a financial condition hazardous to the policyholders or the public.

(2) The board of directors may, upon majority vote, request that the commissioner order an examination of any member insurer which the board in good faith believes may be in a financial condition hazardous to the policyholders or the public. Within 30 days of the receipt of such request, the commissioner shall begin such examination. The examination may be conducted as a National Association of Insurance Commissioners examination or may be conducted by such persons as the commissioner designates. The cost of such examination shall be paid by the Association and the examination report shall be treated as are other examination reports. In no event shall such examination report be released to the board of directors prior to its release to the public, but this shall not preclude the commissioner from complying with subsection (3). The commissioner shall notify the board of directors when the examination is completed. The request for an examination shall be kept on file by the commissioner but it shall not be open to public inspection prior to the release of the examination report to the public.

Comment. The board of directors could be expected to request an examination when they have information suggesting the presence of activities which could lead to rehabilitation under the Wisconsin Rehabilitation and Liquidation Act which has been endorsed by the NAIC. These activities are outlined in section 645.31 of the Wisconsin Statutes.

(3) It shall be the duty of the commissioner to report to the board of directors when he has reasonable cause to believe that any member insurer examined or being examined at the request of the board of directors may be insolvent or in a financial condition hazardous to the policyholders or the public.

(4) The board of directors may, upon majority vote, make reports and recommendations to the commissioner upon any matter germane to the solvency, liquidation, rehabilitation or conservation of any member insurer. Such reports and recommendations shall not be considered public documents.

(5) The board of directors may, upon majority vote, make recommendations to the commissioner for the detection and prevention of insurer insolvencies.

(6) The board of directors shall, at the conclusion of any insurer insolvency in which the Association was obligated to pay covered claims, prepare a report on the history and causes of such insolvency, based on the information available to the Association, and submit such report to the commissioner.

Section 14. Examination of the Association

The Association shall be subject to examination and regulation by the commissioner. The board of directors shall submit, not later than March 30 of each year, a financial report for the preceding calendar year in a form approved by the commissioner.

Section 15. Tax Exemption

The Association shall be exempt from payment of all fees and all taxes levied by this state or any of its subdivisions except taxes levied on real or personal property.

NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS,

Milwaukee, Wis.

To All Members of The NAIC:

Re: The Need for a State Insolvency Fund Bill—The NAIC State Post Assessment Insurance Guaranty Association Model Bill.

GENTLEMEN: As you know, after several months of study and drafting, the NAIC adopted the model State Post Assessment Insurance Guaranty Association Bill at the recent December 1969 meeting in New Orleans. Because of the importance of and vigorous discussion concerning guaranty fund legislation, Commissioner Worthington, as Chairman of the Executive Committee and Commissioner Walton, as Chairman of the Guaranty Fund Subcommittee, requested this office to prepare a memorandum for the information of each commissioner to be used in whatever manner he deems appropriate. This memorandum will summarize the need for such legislation. In addition, there is attached a description of the principle themes underlying the model bill, some comments on various objections raised against the concept of a state guaranty fund and a copy of the model bill.

(1) *A Gap in Public Protection.* No one questions the essential role which property and liability insurance plays in today's economic and social environment in protecting an individual as a driver, passenger, property owner, etc. from the damaging consequences of a variety of accidents and/or fortuitous events. Protection is provided against losses resulting from deaths, injuries and illness; for damage to property; and for economic disaster resulting from legal liability. But the vital protective function performed by the insurance institution is seriously impaired when an insurance company becomes insolvent and cannot fully meet its obligations on a timely basis. Hence, there is a gap in the security provided by the existing insurance system.

In the automobile insurance area this gap has been primarily closed by the availability of the uninsured motorist (UM) coverage with the insolvency provision. But such coverage does not provide the complete answer.

Protection is still lost when an insured's own insurer becomes insolvent. He loses benefits due him under first party coverage (e.g. medical payments, uninsured motorist coverage). His own company is no longer interested in or able to provide him legal defense against third party claims whether they are valid or frivolous. If he is found liable, his insolvent company may be unable to provide financial redress for valid claims against him. When an insolvency results in the loss of the unearned premiums, the insured in seeking replacement coverage must pay a premium for the second time. Even if an insured eventually received the amount due him, delays attributable to the liquidation proceedings may pose severe hardship. Furthermore, uninsured motorist coverage is limited to automobile insurance and does nothing to afford protection against insolvencies in the other areas of property and liability insurance. Thus the UM provision has not completely closed the gap.

Different individuals or groups have presented varying figures or interpretations concerning losses to the public attributable to insurance company insolvencies. On the one hand advocates of a federal insurance guaranty fund assert that automobile insureds and claimants have lost $200 million or more over a ten year period. On the other hand, some segments of the industry assert that

the annual loss averages $1 million which is de minimis and does not warrant any kind of guaranty fund legislation at either the state or federal level. An NAIC study suggests that the annual loss to claimants for the period 1966–68 was less than $5.4 million or 49 cents per $1,000 of premium. Whatever set of figures or interpretations thereof is accepted, when the total amount of automobile insurance written (approximately $11 billion in 1969) is considered, the relatively small magnitude of policyholder and claimant losses due to insolvencies attests to the basic strength of the existing state insurance regulatory system rather than justifying calls for fundamental regulatory changes. Although the insolvency problem may not be great when viewed on a national basis or on the basis of percentages, the consequences may nevertheless cause quite severe hardship for the significant number of individuals involved. An individual who cannot recover justified recompense for injuries and loss is little consoled or helped by the fact that he is only one of a few hundred or even thousand persons who find themselves in an often tragic plight. Furthermore, and this is important, every insurance company failure undermines public confidence and hence the value of the insurance institution whose very existence is the result of the public's desire and need to be and feel secure from risk.

At its 1967 meeting, the NAIC stated that it: "Believes that every promise to every policyholder should be kept fully. No policyholder should ever have to accept anything less than full performance of his contract."

More recently at the NAIC June 1969 meeting in Philadelphia, a position statement said:

"While the statistics have been interpreted by some in such a manner as to greatly overstate the magnitude of the problem, let it clearly be understood that it is the position of the NAIC that no person should suffer as a result of the insolvency of an insurer and that we stand ready to supplement our past actions with present actions to assure this end."

Subsequently the NAIC drafted and at the December 1969 meeting in New Orleans, adopted model guaranty fund legislation for consideration by the individual states.

(2) *State versus Federal Regulation.* As you know, there is substantial congressional concern over the absence of guaranty fund protection. Consequently, Senator Magnuson, with strong support, has introduced S. 2236 which would create a Federal Insurance Guaranty Corporation (FIGC) somewhat analogous to the Federal Deposit Insurance Corporation (FDIC) in the banking area. Virtually all property and casualty insurers would be required to participate and hence be subject to the S. 2236 regulatory provisions. The new federal agency would have extensive examination powers over insurers applying for and having guaranty status as well as being able to compel the filing of extensive reports. Furthermore, before granting guaranty status—which virtually all insurers would have to obtain in order to continue doing business—the Corporation is authorized to examine the applying insurer as to its capability "of conducting its business in a sound and solvent manner." The bill provides that in making this determination, among other things, the Corporation should consider capital and surplus, reasonableness of operating expenses, premium writings as related to surplus, adequacy of loss and expense reserves, reinsurance, investment portfolio, and managerial qualifications. The guaranteed status can be withheld if the insurer doesn't meet Corporation imposed conditions. Also, the Corporation may terminate guaranty status—which, in effect, precludes a company from doing business—if it finds that (1) the insurers, its directors or officers have or are engaged in unsafe or unsound practices; (2) the insurer is in an unsafe or unsound condition; or (3) the insurer has violated the statute, a regulation thereunder or conditions imposed by the Corporation. In other words, the power to grant, withhold or terminate guaranty status is very much akin to a state's licensing power. Thus, S. 2236 vests broad and pervasive regulatory powers over the operation and conduct of the insurance business—regulatory power which essentially duplicates that of the states.

The authority to examine, compel reports and license to assure financial soundness constitutes the fundamental underpinnings to the entire system of state regulation of the insurance business. S. 2236 would superimpose a system of federal supervision upon the existing pattern of state regulation. If the federal government assumes responsibility for the financial soundness of insurers, to protect the fund, the FIGC will reach further and further to exercie its powers and perhaps seek even more of them. How long would it be before state to state differences in capital and surplus, investment laws, rate administration, examinations and the like would no longer be tolerated? In Short, S. 2236 poses a broad,

complex and fundamental issue—i.e. should the insurance business be regulated at the state or the federal level. If enacted S. 2236 would in practical effect go a long way toward resolving the issue.

(3) *Impact on State Revenue.* The Honorable Ned Price, in his presidential report to the NAIC at the recent December meeting, also pointed out S. 2236's potential impact on state revenue. At the present time state premium taxes generate approximately one billion dollars of revenue for the state. (A state by state breakdown is attached). If the federal government becomes more and more involved in the insurance regulatory function, few doubt that it would capitalize on its new position and seek to acquire the tax revenues that go with it. Will there be a federal premium tax, a federal system of fees, or an increase in the federal income tax? If and when the federal government acts, will the states be "asked" to reduce or abandon premium taxation or will a dual system of state and federal taxation be established? In the long run taxes are paid in large measure by the consumer. Sooner or later the consumer will be compelled to pay a heavy price if there is duplicative federal involvement.

(4) *The Need for Prompt Enactment of State Guaranty Fund Legislation.*— It is anticipated that S. 2236 will reach the Senate floor for a vote by early spring. The indication is strong that such a bill would pass in the absence of prompt and widespread enactment of the model (or comparable) state insolvency legislation at the forthcoming state legislative sessions. Thus the need for state regulation stems from (1) the merits of closing the gap in public protection; (2) precluding federal usurpation of the state insurance regulatory function; and (3) protecting state revenue.

The drafting of insolvency fund bills is not new. Ample precedents are available. New York has the Workmen's Compensation Security Fund enacted in 1935; the Public Motor Vehicle (taxicabs) Liability Security Fund (1939); the Life Insurance Guaranty Fund (1941); and the Motor Vehicle Security Liability Fund (1947) as extended in 1969. Both Maryland and New Jersey have had Motor Vehicle Security Funds for several years. California, Michigan, New Hampshire and Wisconsin, enacted post assessment legislation in 1969. In each case a vast amount of expertise and effort from both Government and Industry went into the writing of these laws. In addition, one major industry trade association developed a carefully drafted model bill of its own. Thus, in the development of the NAIC model bill, the Subcommittee, with technical assistance of industry representatives, has been able to draw upon a long history of security fund legislation providing well conceived legislative precedents. It did not have to start from scratch. This, coupled with several months of study and drafting, produced a NAIC model bill which is submitted for your consideration.

JON S. HANSON.

STATE INSURANCE DEPARTMENT STATISTICAL DATA, YEAR ENDING DECEMBER 31, 1967, COMPILED BY THE INSURANCE INDUSTRY COMMITTEE OF OHIO

States	Companies	Premium volume all companies—1967	Premium and franchise taxes certified—1967	Fees collected 1967	Total taxes and fees	Funds spent for operation of department	Personnel	
							Total (Including Examiners)	Examiners
Alabama	894	$702,620,133	$12,643,844	$657,014	$13,300,858	$489,544	53	9
Alaska	453	66,800,715	1,946,854	142,354	2,089,208	[1] 98,623	7	0
Arizona	1,115	389,963,382	7,159,370	338,712	7,498,082	[1] 323,441	52	16
Arkansas	993	319,747,725	6,731,216	322,666	7,053,882	[2] 322,544	47	7
California	895	5,562,616,000	118,889,128	3,455,154	122,344,282	3,871,728	299	66
Colorado	841	467,187,345	10,087,897	352,738	10,440,635	454,803	51	16
Delaware	691	137,197,331	3,627,054	94,779	3,721,833	[1] 77,575	10	0
District of Columbia	743	222,447,643	4,448,953	168,773	4,617,726	323,481	26	9
Florida	961	1,556,798,928	22,310,562	2,337,808	24,648,370	[2] 1,567,043	215	10
Georgia	911	1,096,802,166	17,354,230	359,492	17,713,722	[1] 775,000	69	0
Hawaii	415	164,742,415	5,265,253	109,957	5,375,210	105,754	12	1
Idaho	740	139,558,065	3,894,624	212,330	4,106,954	[1] 156,328	10	0
Illinois	1,323	3,491,746,518	42,013,160	4,190,745	46,203,905	1,923,820	203	60
Indiana	1,125	1,433,053,748	19,694,252	600,473	20,294,725	[3] 586,652	61	20
Iowa	1,033	755,305,339	12,361,150	251,458	12,612,608	618,776	54	25
Kansas	811	633,257,526	8,826,320	413,192	9,239,512	[1] 582,324	90	8
Kentucky	782	629,930,106	10,116,990	295,387	10,412,377	[1] 450,878	66	7
Louisiana	1,025	881,624,918	15,004,993	220,380	15,225,373	[3] 538,475	45	9
Maine	666	203,641,663	3,619,584	260,920	3,880,504	200,823	24	4
Maryland	789	938,862,413	16,063,376	556,354	16,619,730	814,087	94	26
Massachusetts	524	1,580,035,927	28,640,780	1,098,206	29,738,986	2,158,344	301	132
Michigan	916	1,932,356,782	37,109,695	2,812,272	39,921,967	1,389,000	113	32
Minnesota	1,003	863,799,160	16,453,895	713,633	17,167,528	448,697	51	18
Mississippi	990	402,632,014	9,675,884	434,818	10,110,702	[1] 102,852	24	0
Missouri	918	1,396,093,907	20,728,706	714,024	21,442,730	[1] 514,497	96	17
Montana	707	159,241,940	3,369,997	147,510	3,517,507	98,029	11	2
Nebraska	824	404,353,827	6,249,098	346,086	6,595,184	337,733	40	14
Nevada	836	197,333,379	2,217,723	220,713	2,438,436	[1] 162,956	16	0
New Hampshire	550	156,560,250	3,131,207	159,240	3,290,447	[1] 140,550	18	1
New Jersey	770	2,258,843,431	31,440,650	1,565,842	33,006,492	1,275,502	148	38
New Mexico	831	210,954,814	4,571,641	353,098	4,924,739	220,112	26	0
New York	724	7,222,568,765	86,680,736	7,183,908	93,864,644	6,968,116	79	401
North Carolina	693	1,018,571,840	23,945,686	149,331	24,095,017	[2] 598,048	62	14
North Dakota	636	150,147,646	2,682,408	218,231	2,900,639	119,237	17	2
Ohio	1,023	2,803,608,350	47,061,933	956,445	48,018,378	900,706	84	23
Oklahoma	1,084	580,412,010	16,990,212	----------	16,990,212	[1] 282,450	38	0
Oregon	802	551,584,091	8,479,347	449,968	8,929,315	376,325	34	5
Pennsylvania	1,130	3,302,549,049	45,972,417	1,697,349	47,669,766	1,540,280	178	41
Rhode Island	580	260,675,603	4,644,302	164,075	4,808,377	173,030	18	6
South Carolina	733	521,572,020	10,604,863	782,942	11,387,805	738,057	86	10

States	Companies	Premium volume all companies—1967	Premium and franchise taxes certified—1967	Fees collected 1967	Total taxes and fees	Funds spent for operation of department	Personnel	
							Total (Including Examiners)	Examiners
South Dakota	705	146,357,788	3,147,718	97,027	3,244,745	[1] 115,857	12	0
Tennessee	895	878,406,846	18,052,370	2,667,811	20,720,181	985,615	125	2
Texas	1,605	2,643,149,692	45,336,627	2,319,635	47,656,262	3,625,430	465	67
Utah	785	205,768,000	4,030,044	193,913	4,223,957	[1] 109,148	19	8
Vermont	513	99,578,749	1,767,604	95,173	1,862,777	[1] 71,636	8	0
Virginia	880	991,997,667	21,916,141	262,644	22,178,785	735,282	77	15
Washington	850	813,153,032	13,784,169	276,088	14,060,257	837,078	88	20
West Virginia	781	412,786,229	8,841,233	226,620	9,067,853	[1] 207,458	36	9
Wisconsin	933	1,177,479,303	15,809,173	789,420	16,598,593	793,083	80	25
Wyoming	701	71,755,805	1,568,040	203,052	1,771,092	155,932	11	3
Total			886,963,109	42,639,760	929,602,869	40,462,759		
Territories:								
Canal Zone	48	4,755,429	71,332	480	71,812			
Puerto Rico	225	134,264,215	2,386,248	116,258	2,502,506	299,172	66	16
Virgin Islands	93	5,701,045	50,616	11,299	61,915			
Canada and Provinces:								
Dominion of Canada	445	2,902,213,965		1,127,404		1,324,124	103	32
Alberta	345	200,006,834	3,602,907	224,272	3,827,179	164,087	20	1
New Brunswick	262	67,554,774	1,057,730	58,690	1,116,420	27,585	3	
Nova Scotia	237	791,122,961	1,491,552	29,203	1,520,755	15,777	3	
Ontario	187	1,323,029,181						
Quebec	737	1,045,205,560	20,172,220	494,202	20,666,422	508,991	43	14
Prince Edward Island	143	8,727,764	165,721	42,078	207,799	2,128	2	
Saskatchewan	300	98,161,393	2,073,274	180,285	2,253,559	128,666	5	2

[1] Does not include examiners' salaries and expenses.
[2] Includes examiners' salaries only.
[3] Includes revolving fund for examination costs.

Note: Information unavailable for Connecticut, Guam, British Columbia, Manitoba, Newfoundland.

Synopsis of the NAIC State Post Assessment Insurance Guaranty Association Model Bill

The NAIC model bill, as adopted by the NAIC on December 4, 1969, contemplates two primary functions: (1) to avoid financial loss to policyholders or claimants because of the insolvency of an insurer by paying claims against insolvent insurers from funds raised through assessment of other insurers; and (2) to assist in the detection and prevention of insurer insolvencies. Both functions will be carried out through an insurance guaranty association to which all companies authorized to write insurance in the state must belong. (The use of an industry association is very much akin to the approached used by many states in the FAIR Plan area). The association will operate through a board of directors according to a plan of operation, both of which must be approved by the insurance commissioner.

Alll valid claims against the insolvent insurer arising before or within 30 days after the insolvency will be paid with certain limits by the association, except that workmen's compensation claims will be paid in full. Life, title, surety, disability, credit, mortgage guaranty and ocean marine policies are exempt. The association may, on a post assessment basis, assess members up to 2% of their premiums for one year to provide funds to pay such claims. When paid, the claims will be presented to the liquidator of the insolvent insurer by the association for payment from the assets. Member insurers may recoup assessments paid (to the extent not recouped from the liquidator) through an appropriate loading in the premium rates.

The prevention function contemplates reports to the commissioner by the board of directors when it has knowledge that an insurer may be in hazardous financial condition. In addition the board may request and the commissioner must then conduct, at the expense of the association, an examination of any company believed to be in hazardous financial condition. The board must also report on the causes of each insolvency and may present to the commissioner proposals for their prevention.

Possible Objections to State Post Assessment Guaranty Funds and Responses Thereto

Some have raised objections to the enactment of state post assessment guaranty funds. These include the following with responses thereto:

1. The amount of loss suffered by policyholders is de minimis and does not warrant guaranty fund legislation.

Although there is dispute as to the magnitude of the problem on a nationwide basis, there is no doubt that a gap in public protection exists and that the problem can be quite severe for the individuals involved. Furthermore, by using the post assessment technique, the mechanism would not be triggered and assessments would not be levied until the need arises. To the extent that de minimis argument is valid, under the post assessment approach, little burden is imposed on the industry and, in fact what burden there is, is ultimately borne by the consumer.

2. Guaranty funds place unsound—poorly managed insurers on a financial parity with sound—well managed insurers.

Such funds do not create financial parity. The sounder companies would continue to have better resources and investment returns to better serve the market. Only when an insolvency occurs does a guaranty fund tend to equate insurers in the performance of their guaranty function.

Furthermore, this financial parity argument, which is a competitive argument, would seem to be outweighed by broader considerations. First, it has long been accepted that insurance is "affected with the public interest." The public is virtually compelled to obtain property and liability insurance either by economic necessity or by state laws such as the financial responsibility or compulsory insurance laws. In most instances, the states have given private enterprise the opportunity to serve a market (which has strong social overtones) without competition from a state agency. Legal obligations (e.g. under the financial responsibility laws) may be discharged by procuring coverage from the private enterprise system. Under these conditions all insurers—whether small, medium or large—have a responsibility to see to it that the private insurance system performs its function without failure so as to justify the virtual market monoply of which it is the beneficiary. Second, the obligation to protect all insureds becomes even greater as insurers, by careful risk selection standards, tend to force a sizeable number of risks into marginal high risk insurers which may

be more prone to insolvency. Third, all insurers would benefit from increased public confidence in the insurance institution as a whole.

3. Guaranty funds compel the sound-well managed insurers to assume the burdens of the unsound-poorly managed companies (i.e. strong companies pay for the sins of the weak).

Under the model bill, insurers simply advance funds in the form of assessment payments for the payment of claims against insolvent insurers. Subsequently the companies would recoup such amounts through appropriate premium loadings. The burden ultimately falls on the policyholders, not the companies, and hence is spread among those who enjoy the security against insolvent insurers.

4. Guaranty funds put a premium on poor management.

This is a highly questionable argument. The existence of a guaranty fund does not prevent the management of an insurer, nor its stockholders if a stock company, from suffering the financial and other embarrassing consequences of an insolvency. A guaranty fund does not impair the incentives for good management.

5. Guaranty funds tend to make insurance regulators more complacent in dealing with insolvencies.

This has not been the experience in states having such legislation. An insolvency would be no less embarrassing for the regulator whose primary function is to assure the financial soundness of insurance companies. Insolvencies can result in lessened availability of coverage, loss of jobs, loss of tax revenue, etc.

Without a guaranty fund backup, there is greater tendency to unduly prolong efforts to save a troubled insurer despite the serious risk of further deterioration. In contrast, the availability of a guaranty backup enables the commissioner to move more expeditiously in dealing with a weakened company, thereby reducing losses, costs and grief to the public.

Furthermore, the model bill provides a mechanism whereby industry could trigger preventive action by the commissioner as well as provide a source of information and expertise to aid in the prevention of insolvencies. And, incidentally, when companies are confronted with the prospect of assessments in the event of an insolvency, they would be more inclined to assist in a "rescue operation" (e.g. arranging a merger with or takeover by a sound company).

6. Guaranty funds do nothing to strengthen the regulatory process.

This is not true with respect to the model bill. To aid in the detection and prevention of insolvencies a duty is imposed on the board of directors of the guaranty association to notify the commissioner of information indicating that an insurer may be insolvent or in a hazardous financial condition. The board can trigger the examination of such an insurer. However, it is the regulator and not the industry who conducts such examinations. Also, the board may make reports and recommendations on matters germane to solvency and for the detection and prevention of insurer insolvencies. In short, the model bill provides a mechanism whereby the commissioner may tap industry's vast reservoir of information and expertise while at the same time retaining direct control over the insurance regulatory and policing function.

7. Guaranty funds expose insurers to unknown liabilities.

The model bill places a maximum limit on the amount an insurer may be assessed in any year. Furthermore the assessment of an insurer may be exempted or deferred in whole or in part if it would cause the financial statement to reflect capital or surplus less than the minimum amounts required by states in which the insurer does business.

8. The proliferation of guaranty funds in 50 states would be inefficient and contrary to sound public administration and that a single federal guaranty fund, e.g. the Magnuson Bill (S. 2236), would be preferable.

Efficiency can be measured by several standards. (a) *Cost.* The Magnuson Bill would create a Federal Insurance Guaranty Corporation akin to the FDIC. Thus it is relevant to note that since its inception the FDIC has collected over $4 billion while paying out $55 million in net losses. In other words for every dollar paid to the public because of bank insolvencies, it has collected $76. Also, the FDIC has cost over $5 in administrative expense to return each dollar in loss to the public. In 1968 alone, it paid less than $1.5 million in net losses but spent $29 million (almost 20 times greater) to administer the program. Many believe that the proposed Federal Insurance Guaranty Corporation would be even more costly to administer. In contrast, the cost of opertaing a state post assessment plan would be negligible since the plan would require little or no additional administrative personnel and it would not become active until after an insolvency occurs thereby avoiding administrative costs for a program that may be rarely used.

(b) *Public convenience.* Efficiency can also be judged in terms of public convenience. Under the state approach a person would have to deal with only one plan which is located in his state. This seems preferable to compelling individual members of the public to find their way through the labyrinth of local, state and regional agencies interposed between him and the federal corporation in Washington.

(c) *Dislocation.* If efficiency is to be judged by the degree of dislocation, state plans would be more efficient since they fit directly into the present state regulatory pattern. In sharp contrast the proposed federal corporation would completely disrupt the regulatory pattern for years to come and would alter its basic characteristics. Also, since competent insurance examiners require years of experience and are in short supply, the creation of a federal examination staff could be expected to drain many such persons away from state insurance departments thereby weakening state regulation.

(d) *Sound Regulation.* An efficient insolvency program should not impair incentives for sound financial regulation of insurers. Instead the federal fund would create a counter incentive since insolvency losses in a given state would be paid largely by funds collected from persons in other states. On the other hand, inherent in the post assessment approach on a state by state basis, is the incentive for insurers in the state to assist the commissioner in identifying marginal companies and to create pressure for prompt action in preventing insolvencies. In addition, the model bill includes a specific prevention section. (See 6. above).

Senator HART. Commissioner, you don't feel, do you, that this post-assessment plan which brings a body of expert opinion to assist you as a State regulator and provides for insolvency coverage weakens State legislation, do you?

Mr. WORTHINGTON. No, we don't.

Senator HART. Why do you argue that having a comparable Federal body of experts plus a fund to protect against insolvency would cause you to be any less aggressive or effective as a regulator?

Mr. WORTHINGTON. There is a basic difference in the role that industry would play in the model state post-assessment guarantee bill in that they would be an advisory one. They would not share in the burden of regulation. Under S. 2236 the Federal Insurance Guaranty Corporation would share as an equal, if not in fact a super-equal, partner in the process of regulation. I think there lies the basic difference and the one that we think causes the problem.

Senator HART. You visualize an advisory committee plus a program that will produce money in the event of insolvency?

Mr. WORTHINGTON. The advisory committee is the board which would run the program of collecting the assessments and paying the claims.

Senator HART. We have got an advisory committee in S. 2236.

Mr. WORTHINGTON. Our experience, Senator, with advisory committees in Federal bills such as the one under the riot reinsurance bill has not been very successful in that they don't particularly listen to the advisors. Since the advisory committee of the Department of Transportation made their statement on the recommendation, we have not been asked back yet for any further advice either, I might add.

Senator HART. Mr. Sutcliffe.

Mr. SUTCLIFFE. Under the Federal Insurance Guaranty Corporation proposal there may be a basic distinction to draw in that this corporation would not be within the existing framework of any Federal Governmental agency. I think that would be at least a distinction that should be drawn for the record.

Mr. WORTHINGTON. All right.

Senator HART. With respect to the business of a State solution or Federal solution, there is a Federal agency, and I frankly did not know about it, at the present time which in a sense, in a rather precise sense examines insurance companies for solvency.

The Interstate Commerce Act requires the Interstate Commerce Commission to obtain evidence of security from motor carriers subject to its licensing jurisdiction, and its insurance rules and regulations provide that the Commission determine the acceptability of insurance or surety companies desiring to file the security.

I would like to add to the record at this point a letter from the Interstate Commerce Commission that explains the operations of this examination for solvency. A very small staff has been able to foresee insolvency in many cases a year or two before they occurred, it is rather clear. For the record, I submit a list of companies whose ICC qualifications have been discontinued, and that list has an asterisk after certain of the named companies. The asterisk identifies the companies that were later declared insolvent.

There is a second list that I would add to the record of companies that were refused because they were unable to meet the minimum policyholders' surplus requirements. The asterisk in the case of this, is it shows companies which subsequently became insolvent.

The third list is of those companies presently qualified to do business with the ICC.

On the basis of this experience, I think you can say it represents a regulation for insurance company solvency at the Federal level that has been successful. Admittedly, it is limited to the operations of the Interstate Commerce Commission. You will note, as you read this letter from the Commission, they say "In most instances we"—they mean the Commission—"notify the appropriate State insurance department of our action as to the disqualification of the company.

"However, there is some variance dependent upon the State involved. Where previous notifications did not result in any action being taken, we discontinued notifying States. However, these are few in number."

So, even without any legislative direction, the Federal bureau in that case is cooperating with the State insurance regulators as much as I would think reasonably could be expected, and the Commission's letter adds that generally this cooperation has been fruitful.

(Charts and letters follow:)

October 24, 1969.

HON. VIRGINIA MAE BROWN,
Chairman, Interstate Commerce Commission,
Washington, D.C.

DEAR MADAM CHAIRMAN: The Senate Antitrust and Monopoly Subcommittee is continuing its automobile insurance investigation. One aspect of this investigation has been an inquiry into fire and casualty insurance company insolvencies. As a result of this investigation Senator Magnuson and I are cosponsoring legislation (S. 2236) to establish a Federal Insurance Guaranty Corporation. The Senate Commerce Committee plans to hold hearings on this bill in November.

It is my understanding that under Section 215 of the Interstate Commerce Act, the ICC is required to obtain evidence of security from motor carriers subject to its jurisdiction. I understand further, that under the applicable regulations the ICC determines the acceptability of any insurance companies desiring to file evidence of security.

It would be helpful to our investigation to obtain the following information:

1. Names and state of domicile of insurance companies which the ICC has disqualified since 1958, and date of disqualification.

2. Names and state of domicile of insurance companies disqualified by the ICC which to your knowledge subsequently went bankrupt.

3. Names and state of domicile of insurance companies which were refused qualification, or which were unable to meet ICC minimum standards, and date of such refusal or notification, and the names of any of these companies which to your knowledge subsequently went bankrupt.

4. Names and state of domicile of companies currently qualified to file evidence of security with the ICC.

5. Please outline your normal basis for qualifying or disqualifying an insurance company desiring approval from the ICC.

6. What is the normal procedure with respect to notifying state insurance departments upon disqualifying any insurance company?

We would appreciate having the requested information by November 11, 1969. Thank you for your cooperation in this matter.

Sincerely,

PHILIP A. HART,
Chairman, Antitrust and Monopoly Subcommittee.

INTERSTATE COMMERCE COMMISSION,
Washington, D.C., November 4, 1969.

Hon. PHILIP A. HART,
Chairman, Antitrust and Monopoly Subcommittee,
U.S. Senate, Washington, D.C.

DEAR CHAIRMAN HART: This is in reply to your letter of October 24, 1969, wherein you request certain information for the use of the Senate Antitrust and Monopoly Subcommittee.

Under Section 215 of the Interstate Commerce Act, this Commission is required to obtain evidence of security from motor carriers subject to its jurisdiction. Further, the Commission's insurance rules and regulations provide that we may determine the acceptability of insurance or surety companies desiring to file evidence of security. Enclosed is a copy of the insurance rules and I refer you specifically to Section 1043.9 thereof. This authority has been upheld by numerous courts, including the Supreme Court. See for example, *Service Mutual Liability Insurance Co.* v. *United States*, 18 Fed. Supp. 613, 615.

I am pleased to furnish you with the requested information and will follow the same order as set forth in your letter:

1 and 2. Enclosed is Exhibit A which lists alphabetically those insurance companies whose ICC qualification was discontinued on the date shown. I have combined your item 2 by indicating with an "*" those companies, which to our knowledge, subsequently became bankrupt and the date thereof.

While most of the companies were disqualified by the ICC, some requested voluntary discontinue for varying reasons.

3. Exhibit B lists those insurance companies which requested ICC qualification but were either refused or unable to meet our minimum policyholders' surplus requirement. The date of our action is indicated. We have indicated with an "*" those insurers which, to our knowledge, subsequently became bankrupt and the date thereof.

4. Exhibit C lists those insurance companies currently qualified to file evidence of security with the ICC. Several are on a limited basis and appropriate notations are included. It should not be assumed that the absence of any insurance company from this list indicates it cannot qualify, as many do not desire such qualification.

5. Under our insurance rules and regulations, the ICC has discretion as to the qualification of insurance companies. Basically, we must be satisfied it possesses financial stability, business acumen, a good reputation, and knowledge of our insurance rules. The prime source of financial information is the annual statement on the convention form, as filed with the various state insurance departments. We require the filing of quarterly financial data by approximately fifty companies, and in some instances monthly financial statements. I believe less than a handful of state insurance departments require quarterly statements.

When occasions require, conferences are arranged with insurance company officials and also state insurance department officials. Further, we review all state examination reports, major reinsurance treaties, all affiliations (corporate or otherwise), management contracts, if any, and any additional data deemed essential to determine the qualification of a particular insurance company.

6. In most instances we notify the appropriate state insurance department of our action as to the disqualification of a company. However, there is some variance dependent upon the state involved. Where previous notifications did not result in any action being taken, we discontinued notifying such states. However, these are very few in number.

The Commission's prime responsibility in the insurance field is the protection of the public for claims incurred by motor carriers subject to our jurisdiction. As such, we have no jurisdiction to regulate the insurance industry. However, we make every attempt to cooperate with the state departments while performing our function of qualifying insurance companies. Generally, this cooperation has been fruitful.

I trust the foregoing furnishes you with the information you desired.

Sincerely yours,

GEORGE M. STAFFORD,
Acting Chairman.

INTERSTATE COMMERCE COMMISSION

RULES AND REGULATIONS GOVERNING THE FILING OF SURETY BONDS, CERTIFICATES OF INSURANCE, QUALIFICATIONS AS A SELF-INSURER OR OTHER SECURITIES AND AGREEMENTS BY MOTOR CARRIERS AND BROKERS SUBJECT TO PART II OF THE INTERSTATE COMMERCE ACT

SECTIONS 211(c) AND 215 OF THE INTERSTATE COMMERCE ACT

SEC. 211(c). The Commission shall prescribe reasonable rules and regulations for the protection of travelers or shippers by motor vehicle, to be observed by any person holding a brokerage license, and no such license shall be issued or remain in force unless such person shall have furnished a bond or other security approved by the Commission, in such form and amount as will insure financial responsibility and the supplying of authorized transportation in accordance with contracts, agreements, or arrangements therefor.

SEC. 215. No certificate or permit shall be issued to a motor carrier or remain in force, unless such carrier complies with such reasonable rules and regulations as the Commission shall prescribe governing the filing and approval of surety bonds, policies of insurance, qualifications as a self-insurer or other securities or agreements, in such reasonable amount as the Commission may require, conditioned to pay, within the amount of such surety bonds, policies of insurance, qualifications as a self-insurer or other securities or agreements, any final judgment recovered against such motor carrier for bodily injuries to or the death of any person resulting from the negligent operation, maintenance, or use of motor vehicles under such certificate or permit, or for loss or damage to property of others. The Commission, may, in its discretion and under such rules and regulations as it shall prescribe, require any such common carrier to file a surety bond, policies of insurance, qualifications as a self-insurer, or other securities or agreements, in a sum to be determined by the Commission, to be conditioned upon such carrier making compensation to shippers and/or consignees for all property belonging to shippers and/or consignees, and coming into the possession of such carrier in connection with its transportation service. Any carrier which may be required by law to compensate a shipper and/or consignee for any loss, damage, or default for which a connecting motor common carrier is legally responsible

shall be subrogated to the rights of such shipper and/or consignee under any such bond, policies of insurance, or other securities or agreements, to the extent of the sum so paid. The Commission may prescribe, with respect to motor carriers operating within the United States in the course of engaging in transportation between places in a foreign country or between a place in one foreign country and a place in another foreign country, such reasonable regulations concerning security for the protection of the public as the Commission is authorized, by this section, to prescribe for other motor carriers.

TITLE 49—TRANSPORTATION

CHAPTER I—Interstate Commerce Commission

SUBCHAPTER A—GENERAL RULES AND REGULATIONS

Part 1043—Surety Bonds and Policies of Insurance

EX PARTE NO. MC 5

IN THE MATTER OF SECURITY FOR THE PROTECTION OF THE PUBLIC AS PROVIDED IN PART II OF THE INTERSTATE COMMERCE ACT, and of rules and regulations governing filing of surety bonds, certificates of insurance, qualifications as a self-insurer, or other securities and agreements by motor carriers and brokers subject to part II of the Interstate Commerce Act.

Sec.

1043.1 Surety bond, certificate of insurance or other securities.
(a) Property damage; public liability.
(b) Common carriers—cargo insurance; exempt commodities.
(c) Carriers partially exempt; leased rights.
(d) Continuing compliance required.
1043.2 Insurance, minimum amounts.
(a) Motor carriers; bodily injury liability, property damage liability.
(b) Motor common carriers; cargo liability.
1043.3 Combination vehicles.
1043.4 Brokers.
1043.5 Qualifications.
(a) As a self-insurer.
(b) Other securities or agreements.
1043.6 Bonds and certificates of insurance.
1043.7 Forms and procedure.
(a) Forms of endorsements, cancellation notices, etc.
(b) Filing of certificates of insurance and cancellation notices, etc.
(c) Name of insured.
(d) Cancellation notice.
(e) Termination by replacement.

Sec.

1043.8 Insurance and surety companies; authorized.
(a) State authority and designation of agent.
(b) Financial resources.
1043.9 Refusal to accept, or revocation by Commission of surety bond, etc.
1043.10 Fiduciaries.
(a) Insured and principal defined.
(b) Insurance coverage in behalf of fiduciaries to apply concurrently.
1043.11 Operations in foreign commerce.

(Authority: 49 Stat. 546 as amended, 49 U.S.C. 304—Interpret or apply 49 Stat. 554 as amended 557, 49 U.S.C. 311, 315)

§ 1043.1 Surety bond, certificate of insurance, or other securities.

(a) *Property damage; public liability.* Except as provided in paragraph (c) of this section, no common or contract carrier subject to part II of the Interstate Commerce Act shall engage in interstate or foreign commerce, and no certificate or permit shall be issued to such a carrier or remain in force unless and until there shall have been filed with and accepted by the Commission a surety bond, certificate of insurance, proof of qualifications as a self-insurer, or other securities or agreements, in the amounts prescribed in section 1043.2, conditioned to pay any final judgment recovered against such motor carrier for bodily injuries to or the death of any person resulting from the negligent operation, maintenance or use of motor vehicles in transportation subject to part II, Interstate Commerce Act, or for loss of or damage to property of others.

(b) *Common carriers—cargo insurance; exempt commodities.* Except as provided in paragraph (c) of this section, no common carrier by motor vehicle subject to part II of the Interstate Commerce Act shall engage in interstate or foreign commerce, nor shall any certificate be issued to such a carrier or remain in force unless and until there shall have been filed with and accepted by the Commission a surety bond, certificate of insurance, proof of qualifications as a self-insurer, or other securities or agreements in the amounts prescribed in section 1043.2, conditioned upon such carrier making compensation to shippers or consignees for all property belonging to shippers or consignees and coming into the possession of such carrier in connection with its transportation service; Provided, that the requirements of this paragraph shall not apply in connection with the transportation of the following commodities:

Ashes, wood or coal.
Bituminous concrete (also known as blacktop or amosite), including mixtures of asphalt paving.
Cement, dry, in containers or in bulk.
Cement building blocks.
Cinders, coal.
Coal.
Coke.
Commercial fertilizer.
Corn cobs.
Cottonseed hulls.
Fish scrap.
Forest products; viz: Logs, billets, or bolts, native wood, Canadian wood or Mexican pine; pulpwood, fuel wood, wood kindling; and wood sawdust or shavings (shingle tow) other than jewelers' or paraffined.
Garbage.
Gravel, other than bird gravel.
Ice.
Iron ore.
Lime and limestone.
Lumber.
Manure.
Meat scraps.
Ores in bulk, including ore concentrates.
Peat moss.
Poles and piling, other than totem poles.
Salt, in bulk or in bags.
Sand, other than asbestos, bird, iron, monazite, processed, or tobacco sand.
Scrap iron.
Scrap steel.
Shells, clam, mussel or oyster.
Slag, other than slag with commercial value for the further extraction of metals.
Slate, crushed or scrap.
Soil, earth or marl, other than infusorial, diatomaceous, tripoli, or inoculated soil or earth.
Stone, unglazed and unmanufactured, including ground agricultural limestone.
Sugar beet pulp.
Sugar beets.
Water, other than mineral or prepared water.

39-251 O—70——12

Wrecked or disabled motor vehicles.
Other materials or commodities, of low value, upon specific application to and approval by the Commission.

(c) *Carriers partially exempt; leased rights.* The requirements of paragraphs (a) and (b) of this section shall not apply to motor carrier operations partially exempt from regulation by sections 202(c) and 203(b) (49 U.S.C. 302 (c) and 303(b)), or to motor carriers which have, with the approval of the Commission, leased their entire operating rights to others, but only so long as the lessee of such rights, with the approval of the Commission, continues such operations. Lessors may not resume operations unless and until full compliance is effected.

(d) *Continuing compliance required.* Such security as is accepted by the Commission in accordance with the requirements of sections 211(c) and 215 of part II, Interstate Commerce Act, shall remain in effect at all times.

§ 1043.2 Insurance, minimum amounts.

The minimum amounts referred to in section 1043.1 are hereby prescribed as follows:

(a) *Motor carriers; bodily injury liability, property damage liability.*

(b) *Motor common carriers; cargo liability.* Security required to compensate shippers or consignees for loss of or damage to property belonging to shippers or consignees and coming into the possession of motor common carriers in connection with their transportation service, (1) for loss of or damage to property carried on any one motor vehicle—$1,000; (2) for loss of or damage to or aggregate of losses or damages of or to property occurring at any one time and place—$2,000.

(1) Kind of equipment	(2) Limit for bodily injuries to or death of one person	(3) Limit for bodily injuries to or death of all persons injured or killed in any one accident (subject to a maximum of $25,000 for bodily injuries to or death of one person)	(4) Limit for loss or damage in any one accident to property of others (excluding cargo)
Passenger equipment (seating capacity):			
7 passengers or less	$25,000	$100,000	$10,000
8 to 12 passengers, inclusive	25,000	150,000	10,000
13 to 20 passengers, inclusive	25,000	200,000	10,000
21 to 30 passengers, inclusive	25,000	250,000	10,000
31 passengers or more	25,000	300,000	10,000
Freight equipment: All motor vehicles used in the transportation of property	25,000	100,000	10,000

§ 1043.3 Combination vehicles.

The following combinations will be regarded as one motor vehicle for purposes of this part, (a) a tractor and trailer or semi-trailer when the tractor is engaged solely in drawing the trailer or semi-trailer, and (b) a truck and trailer when both together bear a single load.

§ 1043.4 Brokers.

No person, firm or corporation shall engage in the business of a broker as defined in part II, Interstate Commerce Act, and no brokerage license shall be issued to any such person, firm or corporation nor remain in force unless and until such person, firm or corporation shall have furnished a bond or other security approved by the Commission in an amount of not less than $5,000, and in such form as will insure the financial responsibility of such broker and the supplying of authorized transportation in accordance with the contracts, agreements, or arrangements therefor.

§ 1043.5 Qualifications.

(a) *As a self-insurer.* The Commission will give consideration to and will approve the application of a motor carrier to qualify as a self-insurer if such carrier furnishes a true and accurate statement of its financial condition and other evidence which will establish to the satisfaction of the Commission the ability of such motor carrier to satisfy its obligations for bodily injury liability, property damage liability, or cargo liability without affecting the stability or permanency of the business of such motor carrier.

(b) *Other securities or agreements.* The Commission will also consider applications for approval of other securities or agreements and will approve any such applications if satisfied that the security or agreement offered will afford the security for the protection of the public contemplated by sections 211(c) and 215 of part II, Interstate Commerce Act.

§ 1043.6 Bonds and certificates of insurance.

Each certificate of insurance or surety bond filed with the Commission must be for the full limits of liability required under these sections, *Provided*, that only corporations or companies approved by the Commission may qualify to act as surety.

§ 1043.7 Forms and procedure.

(a) *Forms of endorsements, cancellation notices, etc.* Endorsements for policies of insurance, and surety bonds, certificates of insurance, applications to qualify as a self-insurer, or for ap-

proval of other securities or agreements, and notices of cancellation must be in the form prescribed and approved by the Commission. Surety bonds and certificates of insurance shall specify that coverage thereunder will remain in effect continuously until terminated as herein provided, except that in special or unusual circumstances special permission may be obtained for filing certificates of insurance or surety bonds covering periods of less than twelve months duration.

(b) *Filing of certificates of insurance and cancellation notices, etc.* Certificates of insurance, surety bonds, and notices of cancellation must be filed with the Commission in triplicate.

(c) *Name of insured.* Certificates of insurance and surety bonds shall be issued in the full and correct name of the individual, partnership, corporation or other person to whom the certificate, permit, or license is, or is to be, issued. In the case of a partnership all partners shall be named.

(d) *Cancellation notice.* Except as provided in paragraph (e) of this section, surety bonds, certificates of insurance and other securities or agreements shall not be cancelled or withdrawn until after thirty (30) days' notice in writing by the insurance company, surety or sureties, motor carrier, broker or other party thereto, as the case may be, has first been given to the Commission at its office in Washington, D.C., which period of thirty (30) days shall commence to run from the date such notice is actually received at the office of the Commission.

(e) *Termination by replacement.* Certificates of insurance or surety bonds which have been accepted by the Commission under these rules may be replaced by other certificates of insurance, surety bonds or other security, and the liability of the retiring insurer or surety under such certificates of insurance or surety bonds shall be considered as having terminated as of the effective date of the replacement certificate of insurance, surety bond or other security, *Provided* the said replacement certificate, bond or other security meets all of the following conditions: (1) it must be acceptable to the Commission under the rules and regulations in this part: (2) it must be accompanied by a letter of authorization, in duplicate, signed by the motor carrier involved or an authorized employee of such motor carrier, authorizing such replacement and verifying the effective date thereof; and (3) its effective date must coincide with the effective date specified in the letter of authorization and the said date may not be more than thirty days prior to the date of receipt by the Commission of the letter of authorization and replacement certificate.

§ 1043.9 Insurance and surety companies; authorized.

(a) *State authority and designation of agent.* No certificate of insurance or surety bond will be accepted by the Commission under these sections unless written or issued by an insurance or surety company legally authorized to issue policies of the type indicated by such certificate or surety bond, as the case may be, in each State in which the motor carrier is authorized to operate under part II of the Interstate Commerce Act and such company fully complies with paragraph (b) of this section: *Provided*, however, That in lieu of the licensing requirement with respect to any State except that in which the motor carrier has its principal place of business or domicile, the company will file with the Commission an agreement stating that with respect to any State requested it will furnish the Commission a designation in writing of the names and address of a person upon whom process issued by or under the authority of any court having jurisdiction of the subject matter may be served in any proceeding at law or equity brought in such State against such company. Such agreement shall be effective so long as the company is authorized to file security with the Commission, and thereafter with respect to any claims arising during the effectiveness of any previously filed certificates or surety bonds.

(b) *Financial resources.* Each insurance and surety company must possess and maintain surplus funds (policyholders' surplus) of not less than $1 million, which minimum will be determined on the basis of the values of assets and liabilities as shown in its financial statements filed with and approved by the insurance department or other insurance regulatory authority of the State of domicile (home State) of such company, except in instances where, in the judgment of the Commission, additional evidence with respect to such values is considered necessary; Provided, however, That this paragraph shall be effective December 31, 1970, as respects insurance and surety companies which are, on December 31, 1967, authorized to file certificates of insurance and surety bonds with the Commission.

§ 1043.9 Refusal to accept, or revocation by Commission of surety bond, etc.

The Commission may, at any time refuse to accept or may revoke its acceptance of any surety bond, certificate of insurance, qualifications as a self-insurer, or other securities or agreements if, in its judgment such security does not comply with these sections or for any reason fails to provide satisfactory or adequate protection for the public. Revocation of acceptance of any certificate of insurance, surety bond, or other security shall not relieve the motor carrier from compliance with section 1043.1(d).

§ 1043.10 Fiduciaries.

(a) *Insured and principal defined.* The terms "insured" and "principal" as used in certificates of insurance, surety bonds and notices of cancellation filed by or in behalf of motor carriers under these sections shall be construed to include not only the motor carrier named in the certificate, surety bond or notice of cancellation, but also the fiduciary of such motor carrier as defined in section 1132.3 of this chapter—Transfers of Operating Rights. The coverage of fiduciaries herein provided for shall attach at the moment of succession of such fiduciaries.

(b) *Insurance coverage in behalf of fiduciaries to apply concurrently.* The coverage furnished under the provisions of this section on behalf of fiduciaries shall not apply subsequent to the effective date of other insurance, or other security, filed with and approved by the Commission in behalf of such fiduciaries. After the coverage provided in this section shall have been in effect thirty (30) days, it may be canceled or withdrawn within the succeeding period of thirty (30) days by the insurer, the insured, the surety, or the principal upon ten (10) days' notice in writing to the Commission at its office in Washington, D.C., which period of ten (10) days shall commence to run from the date such notice is actually received by the Commission. After such coverage has been in effect for a total of sixty (60) days, it may be canceled or withdrawn only in accordance with section 1043.7.

§ 1043.11 Operations in foreign commerce.

No motor carrier may operate in the United States in the course of transportation between places in a foreign country or between a place in one foreign country and a place in another foreign country unless and until there shall have been filed with and accepted by the Commission a certificate of insurance, surety bond, proof of qualifications as a self-insurer, or other securities or agreements in the amount prescribed in section 1043.2(a), conditioned to pay any final judgment recovered against such motor carrier for bodily injuries to or the death of any person resulting from the negligent operation, maintenance, or use of motor vehicles in transportation between places in a foreign country or between a place in one foreign country and a place in another foreign country, insofar as such transportation takes place in the United States, or for loss of or damage to property of others. The security for the protection of the public required by this section shall be maintained in effect at all times and shall be subject to the provisions

of sections 1043.5, 1043.6, 1043.7, 1043.8, 1043.9 and 1043.10; *Provided*, that the requirements of section 1043.8(a) shall be satisfied if the insurance or surety company, in addition to having been approved by this Commission, is legally authorized to issue policies or surety bonds in at least one of the States in the United States, or one of the Provinces in Canada, and has filed with this Commission the name and address of a person upon whom legal process may be served in each State in or through which the motor carrier operates. Such designation may from time to time be changed by like designation similarly filed, but shall be maintained during the effectiveness of any certificate of insurance or surety bond issued by the company, and thereafter with respect to any claims arising during the effectiveness of such certificate or bond; and Provided further, that the term "motor carrier" as used in this section shall not include private carriers or carriers operating under the partial exemptions from regulation in sections 202(c) or 203(b) of the Interstate Commerce Act (49 U.S.C. 302(c) and 303(b)).

Exhibit A

Companies whose ICC qualification was discontinued

*Atlantic National Insurance Co., April 1962, Voluntarily liquidated 7/31/63, Miami, Florida
Bankers Fire & Marine Insurance Co., April 1964, Birmingham, Alabama
*Bankers & Telephone Employees Insurance Co., March 1965, Receivership 3/30/67, Gettysburg, Pennsylvania
Capital Mutual Insurance Co., April 1963, Lincoln, Nebraska
Capitol Indemnity Insurance Co., April 1960, Indianapolis, Indiana
Casualty Insurance Co. of California, April 1962, Los Angeles, California
*Central Casualty Company, August 1960, Placed in liquidation 1962, Evanston, Illinois
*Central Mutual Casualty Co., April 1960, Placed in receivership 4/27/67, Kansas City, Missouri
Citizens Casualty Company of New York, May 1968, New York, New York
Cimarron Insurance Co., Inc., August 1958, Cimarron, Kansas
Consolidated Underwriters, March 1968, Kansas City, Missouri
Cornbelt Insurance Company, April 1962, Freeport, Illinois
*Cosmopolitan Insurance Company, April 1961, Placed in liquidation Nov. 1963, Chicago, Illinois
*Equity General Insurance Company, September 1960, Placed in receivership 9/23/60, Boulder, Colorado
*Exchange Casualty & Surety Company, March 1961, Placed in receivership 4/27/62, Grandview, Missouri
Farmers Casualty Company, March 1964, Des Moines, Iowa
Farmers Elevator Mutual Insurance Company, May 1967, Des Moines, Iowa
*Farmers Mutual Automobile Insurance Co., April 1957, Placed in receivership 6/19/58, Madison, Wisconsin
Fidelity General Insurance Company, March 1967, Chicago, Illinois
General Guaranty Insurance Company, April 1967, Winter Park, Florida
General Mutual Insurance Company, November 1964, Albany, New York
Georgia Casualty & Surety Co., March 1960, No further filings without prior approval, Atlanta, Georgia
*Highway Insurance Company, June 1958, Placed in receivership 7/6/67, Chicago, Illinois
Iowa Home Mutual Casualty Company, May 1960, Des Moines, Iowa
Inland Mutual Insurance Company, March 1963, Huntington, West Virginia
*Interstate Indemnity Company, May 1958, Became insolvent Nov. 1958, Los Angeles, California
Liberty Universal Insurance Company, August 1967, Fort Worth, Texas
Manufacturers & Wholesalers Indemnity Exchange, May 1963, Denver, Colorado
*Market Mens Mutual Insurance Company, Placed inactive March 1958. Requested it be reactivated 1961 but was refused. Placed in liquidation 5/9/62 Milwaukee, Wisconsin
*Marquette Casualty Company, July 1962, Placed in liquidation 8/16/65, New Orleans, Louisana.
Midland National Insurance Company, February 1964, Chicago, Illinois
*Michigan Surety Company, November 1959, Placed in receivership 2/19/62, Lansing, Michigan
*Mid-Union Indemnity Company, April 1959, No further filings. June 1959 cancel all outstanding filings immediately. August 1959 placed in receivership, Elgin, Illinois
Mohawk Insurance Company, April 1967, New York, New York
*National Fidelity Insurance Company, June 1961, Placed in receivership 8/7/62, Spartansburg, South Carolina
New York Fire & Marine Underwriters, Inc., May 1967, New York, New York
*Preferred Insurance Company, August 1962, Placed in conservatorship May 1963, Grand Rapids, Michigan
*Preferred Risk Insurance Company, April 1960, Believe bankrupt several years later, Fayetteville, Arkansas
Public National Insurance Company, June 1958, Miami, Florida
*Reliable Insurance Company, March 1966, Voluntary conservatorship May 1966, Chicago, Illinois
Republic Franklin Insurance Company, March 1967, Columbus, Ohio
Rockland Mutual Insurance Company, May 1963, Boston, Massachusetts

St. Louis Fire & Marine Insurance Co., May 1967, St. Louis, Missouri
Security Fire & Indemnity Company, May 1966, Winston-Salem, North Carolina
*Security General Insurance Company, June 1961, Placed in receivership April 3, 1964, Sioux Falls, South Dakota
Southern General Insurance Company, April 1964, Atlanta, Georgia
*Surety National Insurance Company, August 1959, Liquidation March 1962, Omaha, Nebraska
*United Benefit Fire Insurance Co., April 1961, Placed in liquidation November 24, 1965.
*United Public Insurance Company, November 1960, Placed in receivership January 1962, Indianapolis, Indiana
United States Liability Insurance Co., May 1968, Voluntarily withdrew
Wabash Fire and Casualty Insurance Co., May 1967, Indianapolis, Indiana
Western Fire & Indemnity Company, May 1958, Lubbock, Texas
Wilshire Insurance Company, April 1969, Los Angeles, California

EXHIBIT B

COMPANIES WHICH WERE REFUSED QUALIFICATION OR UNABLE TO MEET MINIMUM POLICYHOLDERS SURPLUS REQUIREMENT OF $1,000,000 AS OF DECEMBER 31, 1967, OR $500,000 PRIOR THERETO

12/66—Coal Operators Insurance Company, Rockwood, Pa.
6/69—Dealers National Insurance Company, Dallas, Texas.
9/66—First National Indemnity Company, Cisco, Texas.
4/62—Guaranty National Insurance Company, Denver, Colo.
9/67—Home Owners Insurance Company, Chicago, Illinois.
*8/62—International Automobile Insurance Exchange, Indianapolis, Indiana. Placed in liquidation 3/64.
3/67—Knickerbocker Insurance Company, New York, N.Y.
5/67—LaSalle National Insurance Company, Chicago, Ill.
8/68—Main Insurance Company, Chicago, Ill.
9/69—Members Insurance Company, San Francisco, Calif.
6/65—Nathan Hale Fire and Casualty Company, Springfield, Ill.
*6/67—Approx. (by phone) State Fire and Casualty Company, Miami, Fla. Placed in receivership 4/69.
12/68—Tower Insurance Company, Inc., Milwaukee, Wisc.
8/64—United National Insurance Company, Philadelphia, Pa.

EXHIBIT C

COMPANIES QUALIFIED WITH I.C.C. AS OF OCTOBER 1969

Abington Mutual Fire Insurance Company, Abington, Mass.
The Aetna Casualty & Surety Company, Hartford, Conn.
Aetna Fire Underwriters Insurance Company, Hartford, Conn.
Aetna Insurance Company, Hartford, Conn.
Affiliated F M Insurance Company, Providence, Rhode Island.
Agricultural Insurance Company, Watertown, New York.
Albany Insurance Company, New York, New York.
Allcity Insurance Company, New York, New York.
Alliance Assurance Company, New York, New York.
Allied Mutual Insurance Company, Des Moines, Iowa.
Allstate Insurance Company, Northbrook, Illinois.
American Automobile Insurance Company, San Francisco, Calif.
American Casualty Company of Reading, Pa., Chicago, Illinois.
American Empire Insurance Company of S. D. Watertown, New York.
American Employers Insurance Company, Boston, Mass.
American Fidelity Company, Manchester, New Hampshire.
American Fidelity Fire Insurance Company, Westbury, Long Island, New York.
American Fire and Casualty Company, Orlando, Florida.
American & Foreign Insurance Company, New York, New York.
American General Insurance Company, Houston, Texas.
American Guarantee and Liability Insurance Company, Chicago, Illinois.
American Hardware Mutual Insurance Company, Minneapolis, Minnesota.
American Home Assurance Company, New York, New York.
American Indemnity Company, Galveston, Texas.
American Insurance Company, San Francisco, Calif.

American Liberty Insurance Company, Birmingham, Alabama (Filings limited).
American Manufacturers Mutual Insurance Company, Chicago, Illinois.
American Motorists Insurance Company, Chicago, Illinois.
American Mutual Insurance Company (of Boston), Wakefield, Mass.
American Mutual Liability Insurance Company, Wakefield, Mass.
American National Fire Insurance Company, New York, New York.
American Policyholders' Insurance Company, Wakefield, Mass.
American Re-Insurance Company, New York, New York.
American Star Insurance Company, San Francisco, Calif.
American States Insurance Company, Indianapolis, Indiana.
American States Insurance Company *of Texas*, Dallas, Texas.
American Universal Insurance Company, Providence, Rhode Island.
Argonaut Insurance Company, Argonaut Northwest Insurance Company, Argonaut Southwest Insurance Company, Menlo Park, Calif.
Associated Indemnity Corporation, San Francisco, Calif.
Assurance Company of America, Baltimore, Maryland.
Atlantic Insurance Company, Dallas, Texas.
Atlantic Mutual Insurance Company, New York, New York.
Atlas Assurance Company, Ltd. (of London), Short Hills, New Jersey.
Austin-St. Paul Mutual Insurance Company, Minneapolis, Minn.
Auto Owners Insurance Company, Lansing, Michigan.
Badger Mutual Insurance Company, Milwaukee, Wisconsin.
Balboa Insurance Company, Los Angeles, Calif.
Bankers Multiple Lines Insurance Company, Chicago, Illinois.
Bankers & Shippers Insurance Company of New York, New York, New York.
Bay State Insurance Company, Andover, Mass.
The Beacon Mutual Indemnity Company, Columbus, Ohio.
Berkshire Mutual Insurance Company, Pittsfield, Mass.
Birmingham Fire Insurance Company (of Pa.), Pittsburgh, Pa.
Bituminous Casualty Corporation, Rock Island, Illinois.
Bituminous Fire & Marine Insurance Company, Rock Island, Illinois.
Boston Old Colony Insurance Company, Boston, Mass.
British & Foreign Marine Insurance Company, Ltd., New York, New York.
The Buckeye Union Insurance Company, Columbus, Ohio.
California Casualty Indemnity Exchange, San Francisco, Calif.
California Compensation & Fire Company, San Francisco, Calif.
California Union Insurance Company, Los Angeles, Calif.
Calvert Fire Insurance Company, Baltimore, Maryland.
Cambridge Mutual Fire Insurance Company, Andover, Mass.
The Camden Fire Insurance Association, Philadelphia, Pa.
Canadian Indemnity Company, Los Angeles, Calif.
Canal Insurance Company, Greenville, South Carolina.
Capitol Indemnity Corporation (Qualified to file broker surety bonds only), Madison, Wisconsin.
Carolina Casualty Insurance Company, Jacksonville, Florida.
Carriers Insurance Company, Des Moines, Iowa.
Casualty Reciprocal Exchange, Kansas City, Missouri.
Cavalier Insurance Corporation, Baltimore, Maryland.
The Celina Mutual Insurance Company (Filings Limited) Celina, Ohio.
Centennial Insurance Company, New York, New York.
The Central Mutual Insurance Company, Van Wert, Ohio.
Central National Insurance Company of Omaha, Omaha, Nebraska.
The Century Insurance Company Ltd., New York, New York.
The Charter Oak Fire Insurance Company, Hartford, Conn.
Cherokee Insurance Company, Nashville, Tenn.
Chicago Insurance Company, Chicago, Illinois.
The Cincinnati Insurance Company, Cincinnati, Ohio.
Citizens Insurance Company of N.J., Hartford, Conn.
Citizens Mutual Insurance Company, Howell, Michigan.
Coastal Casualty Company, St. Paul, Minn.
Colonial Insurance Company, Los Angeles, Calif.
Commercial Insurance Company of Newark, N.J., Newark, New Jersey.
Commercial Standard Fire & Marine Company, Fort Worth, Texas.
Commercial Standard Insurance Company, Fort Worth, Texas.
Commercial Union Insurance Company of America, Boston, Mass.
Companion Insurance Company (Filings limited), Indianapolis, Indiana.
The Connecticut Indemnity Company, Hartford, Conn.

Consolidated American Insurance Company, Columbia, South Carolina.
Consolidated Insurance Company, Indianapolis, Indiana.
Consolidated Mutual Insurance Company, Brooklyn, New York.
Consolidated Underwriters (No additional filings permitted), Kansas City, Missouri.
Continental Casualty Company, Chicago, Illinois.
The Continental Insurance Company, New York, New York.
Continental Western Insurance Company, Des Moines, Iowa.
Cosmopolitan Mutual Insurance Company, New York, New York.
Cotton States Mutual Insurance Company, Atlanta, Georgia.
Country Mutual Insurance Company, Bloomington, Illinois.
Countryside Casualty Company, Columbia, Missouri.
Country-Wide Insurance Company, New York, New York.
Countrywide Insurance Company, Los Angeles, Calif.
Dorchester Mutual Fire Insurance Company, Boston, Mass.
Eagle Star Insurance Company, Ltd., New York, New York.
Economy Fire & Casualty Company, Freeport, Illinois.
Eldorado Insurance Company, Palo Alto, Calif.
Electric Mutual Liability Insurance Company, Lynn, Mass.
Elite Insurance Company, Vancouver, British Columbia.
Empire Fire & Marine Insurance Company, Omaha, Nebraska.
Empire Mutual Insurance Company, New York, New York.
Employers Casualty Company, Dallas, Texas.
The Employers Fire Insurance Company, Boston, Mass.
The Employers Liability Assurance Corporation, Limited, Boston, Mass.
Employers Mutual Casualty Company, Des Moines, Iowa.
Employers Mutual Fire Insurance Company, Wausau, Wis.
Employers Mutual Liability Insurance Company of Wis., Wausau, Wis.
Employers National Insurance Company, Dallas, Texas.
Employers Surplus Lines Insurance Company, Boston, Mass.
Equitable Fire & Marine Insurance Company, Hartford, Conn.
Equity Mutual Insurance Company, Kansas City, Missouri.
Erie Insurance Exchange, Erie, Pa.
Eveready Insurance Company (Filings limited), Brooklyn, New York.
Excelsior Insurance Company, Syracuse, New York.
Exchange Mutual Insurance Company (Filings limited), Buffalo, New York.
Farm Bureau Mutual Insurance Company, Inc., Manhattan, Kansas.
Farm Family Mutual Insurance Company, Delmar, New York.
Farmers Alliance Mutual Insurance Company, McPherson, Kansas.
The Farmers Automobile Insurance Association, Pekin, Illinois.
Farmers & Merchants Insurance Company, Tulsa, Okla.
Federal Insurance Company, New York, New York.
Federal Mutual Insurance Company, Decatur, Illinois.
Federated Mutual Implement & Hardware Insurance Company, Owatonna, Minn.
The Fidelity & Casualty Company of New York, New York, New York.
Fidelity and Deposit Company, Baltimore, Maryland.
Fidelity and Guaranty Insurance Underwriters Inc., Baltimore, Maryland.
Fidelity-Phenix Insurance Company, New York, New York.
Fireman's Fund Insurance Company, San Francisco, Calif.
Firemen's Insurance Company of Newark, N.J., Newark, N.J.
First Insurance Company of Hawaii Ltd., Honolulu, Hawaii.
Fitchburg Mutual Fire Insurance Company, Fitchburg, Mass.
General Accident Fire & Life Assurance Corp., Ltd. (of Perth), Philadelphia, Pa.
General Casualty Company of Wisc., Madison, Wisc.
General Fire & Casualty Company, New York, New York.
General Insurance Company of America, Seattle, Washington.
Glen Falls Insurance Company, Glen Falls, N.Y.
Globe Indemnity Company, New York, N.Y.
Globe Security Insurance Company, Chicago, Illinois.
Grain Dealers Mutual Insurance Company, Indianapolis, Ind.
Grange Insurance Association, Seattle, Wash.
Grangers Mutual Insurance Company, Middletown, Maryland.
Granite State Insurance Company, Manchester, New Hampshire.
Graphic Arts Mutual Insurance Company, New York, N.Y.
Great American Insurance Company, New York, N.Y.
Great Central Insurance Company, Peoria, Illinois.
Great Northern Insurance Company, Minneapolis, Minn.

Great West Casualty Company, South Sioux City, Nebr.
Greater New York Mutual Insurance Company, New York, New York.
Guarantee Insurance Company (Name changed to Pacific Insurance Co.) San Francisco, Calif.
Guarantee Mutual Assurance Company of America, Worcester, Mass.
Gulf American Fire & Casualty Company, Montgomery, Alabama.
Gulf Insurance Company, Kansas City, Missouri.
Hanover Insurance Company, New York, New York.
Harbor Insurance Company, Los Angeles, Calif.
Hardware Dealers Mutual Fire Insurance Company, Stevens Point, Wisc.
Hardware Mutual Casualty Company, Stevens Point, Wisc.
Harleysville Mutual Insurance Company, Harleysville, Pa.
Hartford Accident & Indemnity Company, Hartford, Conn.
Hartford Fire Insurance Company, Hartford, Conn.
Hastings Mutual Insurance Company, Hastings, Michigan.
Hawkeye-Security Insurance Company, Des Moines, Iowa.
Highlands Insurance Company, Houston, Texas.
Holland America Insurance Company, Kansas City, Missouri.
Holyoke Mutual Fire Insurance Company, Concord, Mass.
Home Indemnity Company, New York, New York.
Home Insurance Company, New York, New York.
Home Mutual Insurance Company, Binghamton, New York.
Houston Fire & Casualty Insurance Company, Fort Worth, Texas.
Ideal Mutual Insurance Company, New York, New York.
Illinois Insurance Company, Chicago, Ill.
Illinois National Insurance Company, Springfield, Ill.
Indemnity Marine Assurance Company, Ltd., New York, New York.
Indiana Insurance Company, Indianapolis, Indiana.
Indiana Lumbermens Mutual Insurance Company, Indianapolis, Indiana.
Industrial Indemnity Company, San Francisco, Calif.
Industrial Underwriters Insurance Company, Dallas, Texas.
Insurance Company of North America, Philadelphia, Pa.
Insurance Company of the State of Pennsylvania, New York, New York.
Insurors Indemnity & Insurance Company, Fort Worth, Texas.
Interboro Mutual Indemnity Insurance Company, Mineola, New York.
Inter-Insurance Exchange of the Chicago Motor Club, Chicago, Ill.
International Insurance Company, New York, New York.
International Service Insurance Company, Fort Worth, Texas.
Interstate Fire & Casualty Company, Chicago, Ill.
Interstate Insurance Company, Cranford, New Jersey.
Iowa Mutual Insurance Company, DeWitt, Iowa.
Iowa National Mutual Insurance Company, Cedar Rapids, Iowa.
Jamestown Mutual Insurance Company, Jamestown, New York.
Jefferson Insurance Company of New York, New York, New York.
Jersey Insurance Company of New York, New York, New York.
KFB Insurance Company, Inc., Manhattan, Kansas.
Keystone Insurance Company, Philadelphia, Pa.
Kansas City Fire & Marine Insurance Company, Kansas City, Missouri.
Lawyers Surety Corp. (Filings limited to broker surety bonds only), Dallas, Texas.
Liberty Mutual Fire Insurance Company, Boston, Mass.
Liberty Mutual Insurance Company, Boston, Mass.
Liverpool & London & Globe Insurance Company, Ltd., New York, New York.
The London Assurance, Los Angeles, Calif.
London Guarantee and Accident Company, Ltd., New York, New York.
London & Lancashire Insurance Company, Ltd., New York, New York.
Lumbermens Mutual Casualty Company, Chicago, Ill.
Lumbermens Mutual Insurance Company, Mansfield, Ohio.
Lumber Mutual Fire Insurance Company of Boston, Cambridge, Mass.
Lynn Mutual Insurance Company, Concord, Mass.
M. F. A. Mutual Insurance Company, Columbia, Missouri.
Maine Bonding & Casualty Company, Portland, Maine.
Manhattan Fire & Marine Insurance Company (Filings to be canceled. Notified September 1969), Los Angeles, Calif.
Manufacturers & Merchants Mutual Insurance Company, Concord, New Hampshire.

Marine Insurance Company, Ltd., New York, New York.
Maritime Insurance Company, Ltd., New York, New York.
Maryland Casualty Company, Baltimore, Maryland.
Merchants Mutual Insurance Company, Buffalo, New York.
Meridian Mutual Insurance Company, Indianapolis, Indiana.
Merrimack Mutual Fire Insurance Company, Andover, Mass.
Michigan Millers Mutual Insurance Company, Lansing, Mich.
Michigan Mutual Liability Company, Detroit, Mich.
Mid-Century Insurance Company, Los Angeles, Calif.
Mid Continent Casualty Company, Tulsa, Okla.
Middlesex Mutual Insurance Company, Concord, Mass.
Midland Insurance Company, New York, New York.
Midwest Mutual Insurance Company, Des Moines, Iowa.
Midwestern Indemnity Company, Cincinnati, Ohio.
Midwestern Insurance Company, Tulsa, Okla.
Millers Mutual Fire Insurance Company *of Texas*, Fort Worth, Texas.
Millers Mutual Insurance Association *of Illinois*, Alton, Illinois.
Millers National Insurance Company, Chicago, Ill.
Milwaukee Mutual Insurance Company, Milwaukee, Wisc.
Minnesota Mutual Fire & Casualty Company, Minneapolis, Minn.
Monarch Insurance Company of Ohio, New York, New York.
Motor Vehicle Casualty Company, Elmhurst, Ill.
Motorists Mutual Insurance Company, Columbus, Ohio.
Mountain States Mutual Casualty Company, Albuquerque, New Mexico.
Mutual Creamery Insurance Company, Minneapolis, Minn.
Mutual Insurance Company of Hartford, Hartford, Conn.
Mutual Service Casualty Insurance Company, St. Paul, Minn.
National Automobile and Casualty Insurance Company, Los Angeles, Calif.
National Ben Franklin Insurance Company of Pittsburgh, Pa., Newark, New Jersey.
National Casualty Company, Detroit, Mich.
National Farmers Union Property and Casualty Company, Denver, Colo.
National Fire Insurance Company of Hartford, Chicago, Ill.
National Grange Mutual Insurance Company, Keene, New Hampshire.
National Indemnity Company, Omaha, Nebr.
National Mutual Insurance Company, Celina, Ohio.
National Surety Corp., San Francisco, Calif.
National Union Fire Insurance Company, Pittsburgh, Pa.
National Union Indemnity Company, Pittsburgh, Pa.
Nationwide Mutual Fire Insurance Company, Columbus, Ohio.
Nationwide Mutual Insurance Company, Columbus, Ohio.
Netherlands Insurance Company, Keene, New Hampshire.
Newark Insurance Company, New York, New York.
New Hampshire Insurance Company Manchester, New Hampshire.
New Hampshire Merchants Insurance Co., Inc., Buffalo, New York.
New Jersey Manufacturers Insurance Company, Trenton, New Jersey.
New York Underwriters Insurance Company, New York, New York.
New Zealand Insurance Company Ltd., San Francisco, Calif.
Niagara Fire Insurance Company, New York, New York.
Norfolk & Dedham Mutual Fire Insurance Company, Dedham, Mass.
North River Insurance Company, New York, New York.
Northern Assurance Company of America, Boston, Mass.
Northern Insurance Company of New York, Baltimore, Maryland.
Northland Insurance Company, St. Paul, Minn.
Northwestern Mutual Insurance Company, Seattle, Washington.
Northwestern National Casualty Company, Milwaukee, Wisc.
Northwestern National Insurance Company, Milwaukee, Wisc.
Occidental Fire & Casualty Company of N.C., Denver, Colo.
Ohio Casualty Insurance Company, Hamilton, Ohio.
Ohio Farmers Insurance Company, LeRoy, Ohio.
Old Republic Insurance Company, Greensburg, Pa.
Olympic Insurance Company, Los Angeles, Calif.
Oregon Automobile Insurance Company, Portland, Oregon.
Oregon Mutual Insurance Company, McMinnville, Oregon.
Pacific Automobile Insurance Company, Los Angeles, Calif.
Pacific Employers Insurance Company, Los Angeles, Calif.
Pacific Indemnity Company, Los Angeles, Calif.

Pacific Insurance Company of New York, New York, New York.
Pan American Fire & Casualty Company, Houston, Texas.
Pan American Insurance Company, Houston, Texas.
Pawtucket Mutual Insurance Company, Pawtucket, Rhode Island.
Peerless Insurance Company, Keene, New Hampshire.
Pekin Insurance Company, Pekin, Illinois.
Pennsylvania Insurance Company, Philadelphia, Pa.
Pennsylvania Lumbermens Mutual Insurance Company, Philadelphia, Pa.
Pennsylvania Manufacturers' Association Insurance Company, Philadelphia, Pa.
Pennsylvania Millers Mutual Insurance Company, Wilkes Barre, Pa.
Pennsylvania National Mutual Casualty Insurance Company, Harrisburg, Pa.
Phoenix Assurance Company of New York, New York, New York.
The Phoenix Insurance Company, Hartford, Conn.
Pilot Fire & Casualty Company, Greensboro, North Carolina.
Planet Insurance Company, Madison, Wisc.
Potomac Insurance Company, Philadelphia, Pa.
Preferred Mutual Insurance Company, New Berlin, New York.
Protective Insurance Company, Indianapolis, Indiana.
Providence Washington Insurance Company, Providence, Rhode Island.
Public Service Mutual Insurance Company, New York, New York.
Queen Insurance Company of America, New York, New York.
Ranger Insurance Company, Houston, Texas.
Reciprocal Exchange, Kansas City, Missouri.
Reliance Insurance Company, Philadelphia, Pa.
Reliance Marine Insurance Company Ltd., New York, New York.
Republic-Franklin Insurance Company (Filings limited), Columbus, Ohio.
Republic Indemnity Company of America, Las Angeles, Calif.
Republic Insurance Company, Dallas, Texas.
Reserve Insurance Company, Chicago, Ill.
Resolute Insurance Company, Providence, Rhode Island.
Royal Exchange Assurance of America Inc., New York, New York.
Royal Indemnity Company, New York, New York.
Royal Insurance Company, Ltd., New York, New York.
Safeguard Insurance Company, New York, New York.
St. Paul Fire & Marine Insurance Company, St. Paul, Minn.
St. Paul Mercury Insurance Company, St. Paul, Minn.
The Sea Insurance Company Ltd., New York, New York.
Seaboard Fire & Marine Insurance Company, New York, New York.
Seaboard Surety Company, New York, New York.
Security Insurance Company of Hartford, Hartford, Conn.
Security Mutual Casualty Company, Chicago, Ill.
Security Mutual Insurance Company of New York, Bronx, New York.
Security National Insurance Company, Dallas, Texas.
Select Insurance Company, Dallas, Texas.
Selected Risks Insurance Company, Branchville, New Jersey.
Selective Insurance Company, Cincinnati, Ohio.
Shelby Mutual Insurance Company, Shelby, Ohio.
Signal Insurance Company (Filings limited) Los Angeles, Calif.
South Carolina Insurance Company, Columbia, South Carolina.
Southern Farm Bureau Casualty Insurance Company, Jackson, Mississippi.
Southern Fire & Casualty Company, Greensboro, South Carolina.
Southwestern Insurance Company, Oklahoma City, Okla.
Standard Fire Insurance Company of Hartford, Hartford, Conn.
Standard Marine Insurance Company, Ltd., New York, New York.
State Automobile & Casualty Underwriters, Des Moines, Iowa.
State Automobile Insurance Association, Indianapolis, Indiana.
State Automobile Mutual Insurance Company, Columbus, Ohio.
State Farm Fire and Casualty Company Bloomington, Illinois.
State Farm Mutual Automobile Insurance Company, Bloomington, Illinois.
State Wide Insurance Company (Filings limited) Jamaica, New York.
Statesman Insurance Company, Indianapolis, Indiana.
The Stuyvesant Insurance Company, Allentown, Pa.
The Sun Insurance Company of New York, Short Hills, New Jersey.
Sun Insurance Office Ltd., Short Hills, New Jersey.
Superior Risk Insurance Company, LeRoy, Ohio.
Switzerland General Insurance Company, Ltd. of Zurich, New York, New York.
Texas Casualty Insurance Company, Austin, Texas.

Texas Farm Bureau Mutual Insurance Company, Waco, Texas.
Tico Insurance Company, Dallas, Texas.
Tokio Marine & Fire Insurance Company, Ltd., New York, New York.
Toledo National Insurance Company, Toledo, Ohio.
Traders & General Insurance Company, Dallas, Texas.
Traders & Mechanics Insurance Company (Filings limited), Lowell, Mass.
Transamerica Insurance Company, Los Angeles, Calif.
Transcontinental Insurance Company, Chicago, Illinois.
Transit Casualty Company, St. Louis, Missouri.
Transport Indemnity Company, Los Angeles, Calif.
Transport Insurance Company, Dallas, Texas.
Transportation Insurance Company, Chicago, Illinois.
Travelers Indemnity Company, Hartford, Conn.
Trinity Universal Insurance Company, Dallas, Texas.
Tri-State Insurance Company, Tulsa, Okla.
Truck Insurance Exchange, Los Angeles, Calif.
Twin City Fire Insurance Company, Minneapolis, Minn.
Underwriters Insurance Company, Chicago, Illinois.
Underwriters at Lloyd's London, New York, New York.
Union Automobile Indemnity Association, Bloomington, Illinois.
Union Insurance Company (Mutual), Lincoln, Nebraska.
Union Insurance Society of Canton, Ltd., New York, New York.
Union Marine & General Insurance Company Ltd., New York, New York.
Union Mutual Insurance Company of Providence, Providence, Rhode Island.
United Fire & Casualty Company, Cedar Rapids, Iowa.
United Pacific Insurance Company, Tacoma, Washington.
United Security Insurance Company, Des Moines, Iowa.
United States Fidelity & Guaranty Company, Baltimore, Maryland.
United States Fire Insurance Company, New York, New York.
Universal Insurance Company, New York, New York.
Universal Surety Company (Filings limited to broker surety bonds only), Lincoln, Nebraska.
Universal Underwriters Insurance Company, Kansas City, Missouri.
Utah Home Fire Insurance Company, Salt Lake City, Utah.
Utica Mutual Insurance Company, Utica, New York.
Valley Forge Insurance Company, Chicago, Illinois.
Vigilant Insurance Company, New York, New York.
Virginia Mutual Insurance Company, Richmond, Virginia.
Virginia Surety Company Inc., Denver, Colorado.
Warner Reciprocal Insurers, Chicago, Illinois.
Washington General Insurance Corporation, New York, New York.
West American Insurance Company, Hamilton, Ohio.
West Bend Mutual Insurance Company, West Bend, Wisconsin.
Westchester Fire Insurance Company, New York, New York.
The Western Casualty & Surety Company, Fort Scott, Kansas.
Western Fire Insurance Company, Fort Scott, Kansas.
Western Pacific Insurance Company, Seattle, Washington.
Western Surety Company, Sioux Falls, South Dakota.
Wilshire Insurance Company (No more filings acceptable as of April 1959), Los Angeles, Calif.
Wolverine Insurance Company, Battle Creek, Michigan.
Worcester Mutual Fire Insurance Company, Worcester, Mass.
Yosemite Insurance Company (Limited filings), San Francisco, Calif.
Zurich Insurance Company, Chicago, Illinois.

INTERSTATE COMMERCE COMMISSION,
Washington, D.C., December 19, 1969.

Hon. WARREN G. MAGNUSON,
Chairman, Committee on Commerce,
U.S. Senate, Washington, D.C.

DEAR CHAIRMAN MAGNUSON: Thank you for your letter of December 10, 1969 regarding S. 2236 and this Commissions' qualification of insurance and surety companies.

We have had no dealings with the Agriculture Department on the matters of insurance company insolvency and have no knowledge as to its method of operation in such matters.

No action by this Commission has led to the failure of any insurance company. Rather, we believe the opposite to be the case, i.e., our actions have, in several instances, kept an insurance company from becoming insolvent. Many insurance companies which desired to maintain or acquire ICC qualification agreed to correct situations we believed improper. Examples of this are reductions in premium volume, improvement in nature of investments, or making needed contributions to surplus.

If further information is desired, please be assured of our cooperation.

Sincerely,

VIRGINIA MAE BROWN, *Chairman.*

Senator HART. Doesn't this example suggest that a Federal agency with this kind of authority does not take over state regulation but through expansion, as the Federal Guaranty Corporation Act would conceivably do, could aid and not hinder the State commissions in attempting to protect the public?

Mr. WORTHINGTON. Senator, I have not had any experience with the ICC except as a manager of a truck company that was examined by them, but I have had experience with another Federal agency that does examine or have minimum requirements for insurance companies before they will allow them to do business, and that is the Agriculture Department.

For companies to be able to write the kind of bonds that are required for grain elevators, for example, to be able to store Government grain, they have to meet certain minimum standards of the Agriculture Department. We had an occasion which I think can be illustrative of the kinds of problems I anticipate. We had a company in our State which by virtue of the fact that they were hit quite seriously from Hurricane Betsy found themselves in a precarious financial position, not insolvent, found to be in a precarious position.

The insurance department immediately sent its examiners in, examined the company, and noted the extent of the problems, contacted those people that were involved in the company and received from them $3 million in cash to be contributed to the surplus of the company to bring them from their verge of insolvency to a solvent company. While this was happening, the Agriculture Department sent word, without notifying the insurance department, without examining the company physically, without determining what things were being done, sent word to grain elevators all over the Midwest that they can no longer insure with this company and by virtue of doing so almost precipitated an insolvency despite what we attempted to do to stop it.

This is the kind of thing we fear. It is my experience and it is one I have to call to your attention.

Senator HART. I don't dispute that that experience may be repeated in other areas, but it is because of that that we require in this Federal guarantee fund that that not occur.

Mr. WORTHINGTON. One provision in your bill, if I remember correctly, says that the Federal guarantee fund may send reports to the insurance commissioner. It doesn't say it "shall."

Senator HART. It was intended that it be an explicit direction. If it isn't "shall," it should be "shall."

Mr. WORTHINGTON. I may not have an up to date copy, but that was my impression.

Mr. SUTCLIFFE. You make reference to that point in your testimony, and let me see if I can find that provision in the bill. The other important point within the framework of the Federal Insurance Guar-

anty Corporation proposal is that any examination that takes place within the State must be filed with the State commissioner as well as sent to the Federal Insurance Guaranty Corporation. No Federal examination takes place without the cooperation or assistance of the State examining process.

So, in situations as described by you there would never be any lack of knowledge on the part of the State insurance commissioner as to the activities of the Federal examiner at a particular point within a State, and there is an opportunity for the State insurance commissioner to comment upon the examination conducted by the Federal examiner.

I think the language you are referring to as far as the permissiveness is the permissiveness of the State insurance director to comment upon that Federal examination. It is not required that he submit comments on that Federal examination, but is permitted.

Mr. WORTHINGTON. Obviously, one of the things in line with what you are saying that concerns us is who sets the standards, whose standards are paramount, can there be two sets of standards. If so, what if the State standards are higher than the Federal standards? In any examination, who's in charge of the examination? If there is a dispute about, for example, the valuation of the assets of the company, whose valuation should stand? What kinds of reports are required to be made? Will the reports be ones that are based upon the accounting practices that the NAIC requires the companies to follow, or will they be on ones that the FIGC would require them to follow?

It appears in creating this sort of thing, unless one assumes that the FIGC would be paramount in all things, we have caused ourselves serious regulatory problems by requiring people to meet two potentially different standards in subjecting two potentially different examinations by two different groups who hold control over whether you can do business.

There appears in your bill no adequate provision, unless it is assumed by virtue of the fact that it is on the Federal level it is paramount, to say which will take precedence and how your reports will be made and the other things which I make, which would cause us some problems. We have on the State level faced these problems, because we have 50 different States requiring in many areas 50 different kinds of things, and yet we have agreed among the States on the method of examination, the method of accounting, the way of evaluating the securities of the company, and the kinds of things that let them do business nationally without serious hinderment on the State basis.

With the creation of the FIGC, we think these old problems we have solved on a State-by-State basis will once again come up, because there are no clear cut answers in the bill as to how to solve those problems.

Mr. SUTCLIFFE. Do you feel that all those problems you have mentioned have been solved, the problems of adjusting and creating standards for State examinations.

Mr. WORTHINGTON. What I was saying is that the method of examination, evaluation of the securities, which is an integral part of the examination——

Mr. SUTCLIFFE. Is that satisfactorily being handled at the present time?

Mr. WORTHINGTON. We feel we are making steps toward having it satisfactorily conducted, but the significant thing is it is being done uniformly generally.

Mr. SUTCLIFFE. What about the uniform liquidation procedures that only 28 States have, and the initial one was passed in 1939 in New York.

Mr. WORTHINGTON. We have a new one which Wisconsin enacted and we are trying to get the other States to do the same—just enacted in Wisconsin.

Mr. SUTCLIFFE. You are still going through the process of trying to achieve uniformity?

Mr. WORTHINGTON. Yes. I see in your bill no machinery or no framework within which the cooperative endeavors of State and Federal Governments are outlined so it is not clear who has what at all.

Mr. SUTCLIFFE. Senator, with your leave, I would like to suggest what mechanism is available.

The thrust of your presentation with regard to the counter-incentive argument suggests that the State insurance departments will be concerned to preserve their longstanding operations of regulation of the insurance industry. In order to do that, the Federal Government will be cooperating and accepting the examinations of those departments that are doing an adequate job, and there are many.

It seems to me that the Federal Insurance Guaranty Corporation presents a much better vehicle for standardizing and strengthening the operations of the State insurance departments.

Let me use one example that has come to the attention of this committee.

In the developing of information or in the financial statements for the companies, State examinations do not always present or make a break-out of the attorney's fees that are paid by a company. We have one example where the State insurance commissioner did not have information in his financial examination as to the amount of attorney's fees that were being paid. Those attorney's fees amounted to $35,000 a month.

I am in no position to judge whether that was excessive or not, but if I were a State insurance commissioner, I would like to know that, and I would like to know it before the company became insolvent. It seems to me this is one example of the way in which a Federal Insurance Guaranty Corporation could assist the States and the National Association of Insurance Commissioners in attempting to standardize and strengthen their State regulation. I think S. 2236 attempts to preserve and save and strengthen State regulation rather than detract from it or displace it.

I think it is that vehicle and that mechanism that would assist your particular group in approving the adoption of standardized forms.

The Liquidation Act, I was not aware there was a new one, but the previous one was in 1939, the Uniform Liquidation Act was only passed by 28 States as of last March, I believe, when my figures were current. So, these are the kinds of things and kinds of problems that I feel the Federal Insurance Guaranty Corporation could go toward assisting State regulation.

Mr. WORTHINGTON. Mr. Sutcliffe, we don't doubt or question the motives or intent of the bill in any way. We have to go by experience, however. Prior to being insurance commissioner, one of my roles in State government was to regulate savings and loan associations, which, as you know, are insured under the FSLIC which provides for dual examinations by the Federal Home Loan Bank Board and the State

regulatory authorities for the State-chartered savings and loan association. My experience in that separate but equal kind of examining process was one of being the person who was required to follow around. The tone of the examination was set by the Federal Home Loan Bank Board examiners. The time of calling the examination was determined by the Federal Home Loan Bank Board examiners; the nature of the examination, the extent of the examination, the art of procedures. So my staff of men who were recognized to be capable and eminent people in the field, some of them had been previous Federal Home Loan Bank Board examiners themselves—we found ourselves to have no continuing effective voice in the examination of savings and loan associations in our State.

I see no basic difference in the proposal of S. 2236 in its force and effect than that of the FSLIC, in that I think the logical conclusion that would be reached, maybe not immediately but in a few years, would be the superseding of the State regulatory authorities by the Federal association. Like I say, I can only go by my experience.

Senator HART. This will go further than is intended by my comment, I know that, but I just can't resist it anyway. I have been looking through, as you will when you get copies, these exhibits that the ICC sent us, and I don't know how we do it within this concept of creative federalism that we are supposedly marching forward under, but with the ICC's judgment as to what would protect the public in the case of the insurance and the surety companies that they were reviewing, and I am told they do it with two men and two secretaries, the public was substantially better off as a result of the ICC suspensions and discontinuance than were those who were doing business with these same companies but not as carriers.

You look that over and see if you don't agree.

How can we feed that kind of intelligence, information, judgment, into the 50 States? I notice Michigan is included. Michigan Surety was discontinued by the ICC in 1959, and we got around to putting it into receivership in 1962.

Mr. WORTHINGTON. One thing you must consider, and I'm not trying to make speeches at all, but my experience with the Agriculture Department led me to this conclusion, and that is the putting of a company on a list, if they are not in fact insolvent, generally makes them so.

Senator HART. As I looked at that, I thought that it could have this effect.

Mr. WORTHINGTON. Obviously some of those companies on the list were insolvent no matter whether the ICC was going to say so or not.

Senator HART. You see before they put it on the list, they do go to the State departments and in any number of these cases there was, as you say, disagreement and there was rejection of disagreement. You can say that the State commissioner was right, if the ICC hadn't put it on the list, it wouldn't have become insolvent.

Mr. SUTCLIFFE. Are you prepared to discuss at this time the allegation that the $200 million statement of loss is an overstatement of the actual loss?

Mr. WORTHINGTON. The NAIC asked the Texas Insurance Department and their actuaries to prepare for us statistics based on information received from receivers and liquidators, and they are included in the report of the Special Committee on Automobile Insurance

Problems. I am familiar with the figures that are in there. I am not an actuary, and I am not aware of the assumptions which were made nor the extent of the work which was done creating those statistics.

We submit them to you for your information. If you have particular questions that you would like to address to the truthfulness or the accuracy of the statistics or the assumptions on which they were based, we can and will direct those questions to people conducting the studies and furnish the answers to you.[1]

Mr. SUTCLIFFE. For the record, if you will allow me to lay out certain of the questions and then explain the way in which the $200 million figure is justified on the part of those people who have published that figure, we may be in a better position to arrive at some kind of answer.

Mr. WORTHINGTON. Mr. Sutcliffe, for the record, let me repeat again, too, that the NAIC position, and that is regardless of what the figures are, we recognize there is a problem, and we don't intend to hide behind figures or to say that the problem is so small in terms of the total number of people, although we feel it is small in terms of percentages, that we stand ready to do nothing; we stand ready to do something in the attempt to solve the problem and recognize there is one.

Mr. SUTCLIFFE. I appreciate that statement, but in your testimony you did mention cost benefit figures, so I think it is important to run through this if we might. The assumptions of the NAIC report are contained within an attachment to the document you were referring to. It is an assumption that the claimant loss, whatever that is, equals 21 percent of premiums written.

Now, the figure for total claimant loss compiled by Senate Antitrust and Monopoly Subcommittee for 88 automobile insurance insolvencies amounts to $517 million. That is for a 10-year period. Applying the 21 percent factor to the $517 million of premium written, you come up with approximately $108 million loss. Spread over a 10-year period it produces a yearly average loss of $10.8 million compared to the NAIC statements of $6 million in one period of time and $5 million in another period of time.

The figures include only 88 of 109 insolvencies. The average premium written by the insolvent companies was over $5 million. This is the average. So to get the figures that we don't have for the other 22 companies, we have averaged the yearly loss and assumed that those companies had a yearly loss average of $5 million to come up with $1.05 million per year additional to the $10.8. This adds a total of $21 million to the previous total of $108 million.

In your staff report, you calculate, as nearly as possible—and this is the June 16 staff report on the entire automobile compensation problem—you calculate there is approximately $111.1 million of unearned premiums and you say this calculation presents a more balanced picture of the magnitude of the problem than the $517 million figure.

I don't know what is included within that calculation of $111.1 million, but even using that figure, you go on to say that of all the people that had claim forms mailed to them, 42 percent of those to whom the claim forms were mailed returned them. So there was about 58 percent that did not return their claim forms. This produces a total unearned premiums loss even assuming that the claimant loss figures that you presented in the NAIC study included unearned premiums of $66 million.

[1] See information on p. 208.

Because of the lack of reporting data and the assumptions upon which this was calculated, this has to add at least a minimum of $66 million of unearned premium loss to the total $108 million for the 88 companies and $21 million for the remaining 22 companies. This comes to a total calculation of direct loss of $195 million.

We are getting awfully close to the $200 million figure. This doesn't even begin to include the assessable loss. The most recent figures we have show a potential liability of $69 million for assessable loss and as of January 1969 $3 million paid already. Even if we assume only $5 million will be collected, this easily puts us, in our calculations, over the $200 million figure. And these are only direct costs. It doesn't include the fire and casualty company insolvencies or any other indirect losses associated with insurance company insolvencies.

I want to present that for the record and ask for you to give a comment and breakdown of where we are in error.

Mr. WORTHINGTON. We will be pleased to furnish you information for that.

Can you write those questions out for us?

Mr. SUTCLIFFE. Yes, they will be part of the record, and we will clarify them.

Senator HART. Mr. Sutcliffe did state, as I listened to him, fully the series of figures which now we would like you to react to, identifying those you think are properly assigned and properly estimated and so on.

Mr. WORTHINGTON. We will be glad to do so.[1]

Mr. SUTCLIFFE. I would like to ask some questions on the uninsured motorist coverage, if I may, which you discuss on page 3 of your testimony. Has the endorsement been available since 1956?

Mr. WORTHINGTON. The insolvency endorsement?

Mr. SUTCLIFFE. No, just the uninsured motorists endorsement.

Mr. DINEEN. It was available before that time.

Mr. SUTCLIFFE. In other words, the standardizing——

Mr. DINEEN. The idea was developed in the late 1940's and very early 1950's, and then evolved.

Mr. SUTCLIFFE. Was it prevalent in the 1960's?

Mr. DINEEN. Yes.

Mr. SUTCLIFFE. Was insolvency protection usually afforded the policyholder who had a UM endorsement in his policy, either expressly or by operation of law?

Mr. DINEEN. As Mr. Jones said, this is a development within the last 2 or 3 years. In other words, you started off first, it was an endorsement. Then they wove it into the policy, and then they extended the coverage.

It is something like you do in Congress, dealing with the Securities and Exchange Act, you keep dealing with it. You learn more and you keep——

Mr. SUTCLIFFE. That was not my question. The question I was getting at, "by operation of law," in other words, the court decisions. Was insolvency protection afforded under the uninsured motorist endorsement in 1960? It is my understanding it was.

Mr. DINEEN. My understanding is it was not, but I don't want to be positive.

---

[1] See information on p. 208.

Mr. SUTCLIFFE. In any event, we have had considerable loss in the 1960's, is this correct?

Mr. DINEEN. Of what?

Mr. SUTCLIFFE. We have gone from the uninsured motorist endorsement, and we have attempted to go to the uninsured motorist endorsement with insolvency protection.

My question is, there was considerable loss during the 1960's.

Mr. DINEEN. You heard Mr. Jones' answer. Mr. Jones, answer was this particular coverage was extended about 2½ or 3 years back. What he said to you was the number of claims that were covered by that were so small they didn't have to make an addition to the premium. You are applying this to countrywide figures, $10 billion, which would lead me to believe the problem can't be very heavy or they would have had more claims to follow.

Mr. SUTCLIFFE. The opposite conclusion is also possible, that the uninsured motorist protection is not picking up much of the loss from insolvency.

Mr. DINEEN. You can argue it both ways.

Mr. SUTCLIFFE. Does the uninsured motorist endorsement with insolvency protection cover property damage loss?

Mr. WORTHINGTON. In most instances, if not all instances, it does not.

Mr. SUTCLIFFE. Does it protect noncar owning pedestrians?

Mr. DINEEN. No.

Mr. SUTCLIFFE. Does it provide any protection for first party coverage of the policyholder of the insolvent company?

Mr. DINEEN. No.

Mr. WORTHINGTON. I will have to say, I think, if I may, that we have never said that uninsured motorist coverage was the answer. We said rather than the uninsured motorist coverage was a part of the evolutionary process to continually fill in the gaps, and it does fill in a gap.

Mr. SUTCLIFFE. What is the cost of filling that gap to the American consumer? Do you have any estimate of the cost of that gap?

Mr. WORTHINGTON. No. Only I know it is available in my State for $3.

Mr. SUTCLIFFE. Is that just on a $100 premium, $200 premium?

Mr. WORTHINGTON. The average policyholder, automobile policyholder, pays $3 for his uninsured motorist coverage.

Mr. SUTCLIFFE. This is compared to 12½ cents per $100 of premium for the Federal Insurance Guaranty Fund?

Mr. DINEEN. This covers much more than the insurance things.

Mr. SUTCLIFFE. Can you give us a breakdown of what the insurance cost is, versus the $3 figure in Iowa?

Mr. WORTHINGTON. The insurance companies have said there is no cost, really, in the insolvency protection because they didn't add it into the figures in arriving at their rates.

The uninsured motorist coverage figure has in many States been an unprofitable line.

Mr. SUTCLIFFE. Do you have figures to substantiate that for the record?

Mr. WORTHINGTON. I can get them for you. I'm not saying it is national.[1]

[1] See information on p. 208.

Mr. SUTCLIFFE. I would like to discuss the protection of the public interest under the State postinsolvency assessment plan. In whose hands is the liquidation placed during a postinsolvency assessment?

Mr. WORTHINGTON. The receiver.

Mr. SUTCLIFFE. Who is?

Mr. WORTHINGTON. The liquidator, the court.

Mr. SUTCLIFFE. What role does the industry play in that?

Mr. WORTHINGTON. They assume the liabilities and pay them.

Mr. SUTCLIFFE. They have absolutely nothing to do with marshalling the assets for settling the claims?

Mr. WORTHINGTON. They settle the claims and pay the claimants.

Mr. SUTCLIFFE. Are they operating somewhat in the capacity of receiver and liquidator?

Mr. WORTHINGTON. They go to them to try to get reimbursed from the assets of the company that are left from the payment they have made, recognizing they are not going to receive full payment.

Mr. SUTCLIFFE. If the payment is large, doesn't the insurance industry have an interest in minimizing as much as possible the claims against the defunct company who produced postassessment?

Mr. WORTHINGTON. You are talking about a selfish interest of trying to minimize their losses by——

Mr. SUTCLIFFE. Let me see if there is that selfish interest. Can insurance companies recoup any assessments levied against them in the ratemaking process?

Mr. WORTHINGTON. Yes; they can.

Mr. SUTCLIFFE. Postassessment?

Mr. WORTHINGTON. Yes. We recognize that the rates are such that you don't physically recoup for past losses, but a provision of the bill does say because provision is made in there for postassessments under the Guaranty Association, the rate should not be considered excessive for that reason, the rate requested, which allows them effectively to recoup from the policyholders for losses which they have had.

Mr. SUTCLIFFE. Do you have any estimate of the costs, then? This would vary as the insolvency varies, would it?

Mr. WORTHINGTON. Yes; it would vary.

Mr. SUTCLIFFE. Can you give us any rough idea of the kinds of payout would be paid in these situations if we had to compare this to the Federal Insurance Company Guaranty costs?

Mr. WORTHINGTON. I would assume, under the model State assessment guaranty bill it would be the same losses that the insurer would have paid had it not become insolvent.

Mr. SUTCLIFFE. With the exception for the deductible on unearned premium.

Mr. WORTHINGTON. On the $100 deductible.

Mr. SUTCLIFFE. Is that on all aspects?

Mr. WORTHINGTON. On all aspects. Let me read for you the purpose of this model bill, which may speak to one of the things that you ask.

> The purpose of the act is to provide a mechanism for the payment of covered claims under certain insurance policies, to avoid excessive delay in payment, and to avoid financial loss to policyholders because of the insolvency of the insurer, to assist in the detection and prevention of insurance insolvency, and to provide an association to assess the cost of such protection among insurers.

Mr. SUTCLIFFE. What provision have you made for marshalling assets and speeding up the liquidation process?

Mr. WORTHINGTON. It is relatively unimportant that the liquidation process be speeded up, because the only claimant against the liquidator is the association.

Mr. SUTCLIFFE. In other words, the company does not use existing assets of the defunct company to pay settlement claims. They have to pay them out of pocket, and then go to the liquidator.

Mr. WORTHINGTON. If the liquidator would make partial payments, which they do, these would be given to the association. They would use them to recoup them for payments they have made prior to that.

Mr. SUTCLIFFE. So there would be no delay to the policyholder?

Mr. WORTHINGTON. There should be no delay to the policyholder or the claimant.

Mr. SUTCLIFFE. You have mentioned that you disagreed with previous testimony about the preventive aspects of this postinsolvency assessment plan. Do you feel it is realistic for the industry to call in an examination upon its own?

Mr. WORTHINGTON. The industry role in the examination process is only one of activating the machinery and paying for the cost of the examination. In order to avoid what some might consider to be coercion or intimidation against a brother company by the association, the company to be examined bears none of the cost of the examination.

There is no public knowledge of the examination until it is completed, so that there is no stigma attached to the fact that it is being examined. It is an insurance department examination under the auspices of the NAIC.

So the industry role really is to trigger an examination which an insurance examiner may not have been aware of the need to have triggered.

Mr. SUTCLIFFE. Would any member of the industry participate in that examination?

Mr. WORTHINGTON. No. As a matter of fact, the results of the examination cannot be made available.

Mr. SUTCLIFFE. Does it vary from the proposal of the American Mutual Insurance Alliance in any significant way?

Mr. WORTHINGTON. It varies in several ways, not the least of which role the industry plays.

In our bill the industry does not get into the company and they do not have inside information. They merely trigger the action by the insurance commissioner, and then bear the cost for it. When we tried to draft our bill, we took the insurance commissioners from the State of California, which has a bill, Michigan, which has a bill, Wisconsin, which has a bill, New Hampshire, which has a bill, made them the nucleus of the committee, and then had two or three other insurance commissioners who were actively involved in this process—Bill Walton, who is vice chairman of the Special Committee on Automobile Insurance and myself, as chairman, were on that committee, and we attempted to draw the best from all the bills that had been enacted, and from the proposed bill of the American Mutual Insurance Alliance, and to put the best parts of those in our bill and add what we thought was necessary.

Mr. SUTCLIFFE. Was the threat of Federal legislation, specifically S. 2236, impetus for State activity?

Mr. WORTHINGTON. I can't speak for the other insurance commissioners, but I can speak for myself. That is, my philosophy of government, and my role as a regulator and a protector of the consumer was such that if the Federal Government were not involved in this area I would be involved anyway.

Mr. SUTCLIFFE. What happens if Congress fails to act at this particular time?

Mr. WORTHINGTON. There will be postassessment insurance guarantee associations bills passed in a majority of the States of the country.

Mr. SUTCLIFFE. What happens in the minority of States and their constituents?

Mr. WORTHINGTON. Well, maybe when I said majority, I should have said I think nearly all States will. If not in fact all States. I wouldn't want to say that all States won't. But if, when that time comes, and we learn that there is still a gap, and that is the business we are in, trying to close the gaps for the protection of the policyholder, then, I'm sure there will be action taken at some appropriate level to assure that the gap is closed.

NAIC is pledged to closing the gaps.

Mr. SUTCLIFFE. Is uninsured motorist coverage primary under your State postinsolvency assessment plan?

Mr. WORTHINGTON. Yes.

Mr. SUTCLIFFE. Any settlement that the policyholder agrees to forecloses it from going with further claims to the insolvency fund?

Mr. WORTHINGTON. No. It just reduces the total amount it can receive.

Mr. SUTCLIFFE. Is that below the $10,000 normal financial responsibility figure? Let me throw out an example. A $2,000 claim; the claimant is able to negotiate with his company to obtain $1,000. If he still feels he has a legitimate claim for the other $1,000, may he go to the post——

Mr. WORTHINGTON. He can claim to the postassessment insolvency fund, and undoubtedly they would deny it. And he would have to go to court against the insurance company.

I wouldn't say undoubtedly, but assuming the insurance company and the adjusting process of the fund of the association were similar I would.

Mr. SUTCLIFFE. If he has to sue his own company, can he make a claim against the insolvency fund for contingent fees to pay attorneys?

Mr. WORTHINGTON. Specifically, we are saying that he needs to make claim first against the uninsured motorist coverage of his own company. We are not saying that he then is estopped from going to the guarantee fund of the association. He can go to the guarantee fund for any other claim which he may have which is a legitimate claim. The guarantee association obviously is not going to automatically pay everyone that submits claims, but they will pay the claims which will be rightfully paid if the insurer had not become insolvent.

So he then would have action against the association.

Mr. SUTCLIFFE. Who is making the determination as to whether that claim will be paid.

Mr. WORTHINGTON. The association has the authority under the bill to contract with a service agency, which would be an insurance company, an adjusting bureau, some agency which is in the business of

settling claims. If they have some disatisfaction, they can appeal to the commissioner or to the courts.

Mr. SUTCLIFFE. What supervision of the claim settlement process would the commissioner engage in?

Mr. WORTHINGTON. In the same supervision we engage in in all claim settlements today.

Mr. SUTCLIFFE. Which is what?

Mr. WORTHINGTON. Assuring that the companies perform under the contracts as they promised to do.

Mr. SUTCLIFFE. You discuss the Interstate Guaranty Fund. What is the present status of the Interstate Guaranty Fund and the attempts of the NAIC to close the "residual" gap?

Mr. WORTHINGTON. The Interstate Non-Federal Guaranty Fund situation is one that we are studying. We put a list of priorities on what we were doing, and the first priority is the postassessment model bill that now has been completed, and while we were working on that bill, we put off work on the Interstate Association, we put off work on the prefunded model bill, and now we have got No. 1 off our priority list, and we will again resume.

We have discussed, and I discussed with you earlier, some of the ideas that we had in mind, and we are trying to find ways to put those ideas into some sort of practical application in a bill form, or interstate compact form for voluntary compliance by the industry.

There are several ways it could be done. We are trying to search out the best way.

Mr. SUTCLIFFE. Why did you even undertake the examination of an interstate guarantee fund? What are the public interest considerations that caused you to examine that alternative?

Mr. WORTHINGTON. I said earlier that the NAIC is interested in closing the gap.

Mr. SUTCLIFFE. What gaps specifically would the interstate guarantee fund close?

Mr. WORTHINGTON. In response to your earlier question, what would happen if all States did not adopt a postassessment guarantee association, then obviously one of our alternatives would have to be to come to some sort of combination of these.

Another alternative would be in areas of less dense population in the country than other areas, such as the part of the country I come from, it may be more practical to join together with several other States in the administration of the program we are planning, to pool our experience together, and we want the opportunity to do that if it shows it to be necessary. The model bill provides for that eventuality.

Mr. SUTCLIFFE. Do you have any estimates of the cost for any kind of interstate guarantee fund?

Mr. WORTHINGTON. I think in our statement that the fund such as you propose we estimate would cost $30 million.

Mr. SUTCLIFFE. Would you say that would have application to the interstate non-Federal guarantee fund?

Mr. WORTHINGTON. If it were set up on—either way it would not cost that much because we would utilize the examinations which are already being conducted by the State insurance departments and not superimpose another level of bureaucracy on top.

Mr. SUTCLIFFE. What do you do with the argument that the Federal Insurance Guaranty Corporation would also utilize existing reports?

Let me phrase it another way.

In your staff report you said, and I quote:

> A second important function of the Corporation would be to ascertain potential insolvencies in their incipiency, prevent incipient insolvencies from coming to fruition whenever possible, and mitigate the adverse impact of insolvencies which become inevitable. To do this, the Corporation must be able to maintain close scrutiny of marginal insurers which are in trouble. This would involve the powers of visitation and examination.

Now, you are willing to do this in the interstate non-Federal guaranty fund. Why are you unwilling to do this under the Federal Insurance Guaranty Corporation context?

Mr. WORTHINGTON. We are already attempting to do that on the State regulatory level through the process of its own examinations. We would envision that this would only be a continuation of that examination of it that we are now already involving ourselves in.

Mr. SUTCLIFFE. Are you satisfied with the present zone examination procedures?

Mr. WORTHINGTON. I think anybody that is satisfied with the status quo is probably living behind his times, and we would have to say we would hope that our examination procedures would be improved, just like we hope the efficiency of government on all levels would be improved.

Mr. SUTCLIFFE. What do you plan to do about the Office of Securities Valuation which has come under criticism by the industry itself of late and which played an inactive but perhaps causal role in the State Fire and Casualty situation?

Mr. WORTHINGTON. The Securities Valuation Office of the NAIC is one which has been under supervision of one of the committees of the NAIC, and that committee I think, testified before Senator Hart's Antitrust and Monopoly Subcommittee of the Judiciary that there had been some problems in the past. As a result of the problems, there had been other problems created, but that they recognize the problems and had begun a process, again to use the word we have been using today, to close the gaps so those problems would not occur again, and it is my understanding—I am not a member of that particular committee—that the staff of the Securities Valuation Office and the commissioners that chair those committees and subcommittees, that the commissioners on those committees have very diligently tried to create safeguards against what did occur in the State Fire and Casualty situation.

Mr. SUTCLIFFE. What is the basic distinction between your interstate non-Federal guarantee fund and the Federal Insurance Guaranty Corporation?

Mr. WORTHINGTON. There are several basic differences. I cannot say there is one basic difference, but the most obvious to me is it would be done within the structure of existing regulation, without creating a new structure which would have to be defined at some point.

Secondly——

Mr. SUTCLIFFE. It has visitation and examination power. There has to be a change. Also, in your discussion of it, at the staff level, at least, you suggested that it would not necessarily confine itself to the NAIC type of examination; that it may use other procedures for examining companies.

Mr. WORTHINGTON. There is already resident within the NAIC structure the provision that any insurance commissioner who has a company doing business in his State can examine any other insurance company and can seek any records or make the examination in any way that he sees fit. So, this would not be anything new.

Mr. SUTCLIFFE. For the record, would you provide this committee with the number of times which the State insurance commissioners have asked for that examination to be made by the NAIC in a specific case because of the suspicion of insolvency?

In other words, we would like to know how many times they have called upon the NAIC for expert help in an insolvency situation.

Mr. WORTHINGTON. Let me say historically the NAIC has not had a staff with the capability of providing staff assistance to the various commissioners.

Mr. SUTCLIFFE. Perhaps I did not understand you.

Mr. WORTHINGTON. Currently, we have staff people and we can have staff involvement. What I was talking about was individual States exercising this right to go and provide examination for companies in other States where they felt that that commissioner may not have been functioning as they would like to see him function. This is really what we are talking about on the interstate non-Federal guaranty corporation, would be that the commissioners already have that right and collectively we could exercise that right.

Mr. SUTCLIFFE. In other words, the examiners in the State of California and the State of New York would be displacing the State regulation of some other sister or brother State. Your argument with the Federal Insurance Guaranty Corporation was if it went in there and started making these examinations it would displace State regulation and you would have Federal regulation. Your description of the way in which a State can go in suggests to me you would have one State regulatory body displacing another State body. I do not see the distinction. Perhaps you could draw that distinction for me.

Mr. WORTHINGTON. I suppose maybe the best way to do it would be an illustration, recognizing that illustrations are inadequate. On the State-by-State basis, it is us doing it to us, and it is not as distasteful or objectionable because we set our standards as it is for someone else or you—by "you," I mean the Federal Government—I do consider the Federal Government to be an outside force—coming in and doing it and setting the standards without the requirement that you adhere to the particular conditions in the State or to the needs of the State or to the understandings of what that particular commissioner is doing.

The U.S. Senate operates, to my understanding, a great deal on the basis of tradition and respect for one another, and in my legislative experience, when we stand up to disagree with someone, we stand up and disagree with a gentleman from such-and-such a county, even though we may not even have thought he was a gentleman. This is the kind of thing I am saying.

The State insurance commissioners, being the oldest organized body of State officials, since 1871, have created, much the same as legislative bodies have to create, a sense of tradition and respect for one another, and we can operate within that framework and do things to one another and for one another that outsiders cannot do and cannot accomplish because that is just the way it has been established.

I think from your experience working here you can see that those kinds of traditions and respect have greater merit and work in many ways to the advantage of everyone involved.

Mr. SUTCLIFFE. I am curious how this fits with your statement about the protection of the status quo.

Mr. WORTHINGTON. Hopefully, all 50 commissioners are changing and we are not preserving the status quo except that we maintain respect for one another.

Mr. SUTCLIFFE. And that mutual respect, then, even if there is the assumption of one State examining in another State, would not have the kind of irritation or lack of respect that the Federal examination would have?

Mr. WORTHINGTON. I know of two instances currently, which because they are still under consideration cannot be said publicly, in which commissioners from other States have bolstered the commission from the domestic State and helped him perform duties which he may not be able to do otherwise.

Mr. SUTCLIFFE. You much prefer to see it remain within the "traditional" State insurance commissioner; even though it may be a displacement of that State regulation to some extent, at least it would be a displacement by another State?

Mr. WORTHINGTON. I would not say there would be a displacement. It would be a complementary effort.

Mr. SUTCLIFFE. If it were done by the Federal Government, it would be a displacement; if it were done by another State regulator, it would be a complementary effort?

Mr. WORTHINGTON. You are trying to get me into semantics.

Mr. SUTCLIFFE. I am just trying to understand differences and distinctions where seemingly they do not exist.

Mr. WORTHINGTON. Basically, I suppose I would have to say to have the Federal Government come in and impose minimum standards and rules and procedures and methods of reporting would be different than to have a legislative body of the NAIC, where each commissioner has the right to vote and to state his case, set the same kind of standards and have the minority abide by the majority rule. There is a great difference in that, and that is what I am really trying to say.

Mr. SUTCLIFFE. You object to the projected cost-benefit ratio of the FIGC; is that correct?

Mr. WORTHINGTON. Our cost-benefit ratio shows 5 to 1, $30 million in cost to $5 million in expense.

Mr. SUTCLIFFE. We have engaged in a conversation which will lead to a resolution of whether or not that is an accurate assessment of the cost-benefit ratio.

Leaving that aside, do you have any cost-benefit ratio figures for your alternative proposals?

Mr. WORTHINGTON. We think the alternative proposal would result in minimal costs, because the only time the machinery were ever involved would be where there was an insolvency.

Mr. SUTCLIFFE. Does not State regulation at the present time cost $40 million directly? Is that not an accurate figure?

Mr. WORTHINGTON. I do not know. That sounds not unreasonable.

Mr. SUTCLIFFE. And the total amount of taxes and fees collected by the State insurance departments amounts to close to a billion dollars a year; is that correct?

Mr. WORTHINGTON. That is right, sir.

Mr. SUTCLIFFE. And about 4 percent of that then is used for actual regulation of the industry from which those fees are collected?

Mr. WORTHINGTON. I do not know how it is in other States; but in Iowa none of that money is used for regulation. The tax on premiums is a direct tax, the same as a sales tax or income tax. It is not a tax for regulation purposes.

I think the analogy between total taxes collected and total expenditures on the insurance companies is inaccurate, though I like to use it as a way of getting more funds for my department. It is not an accurate one, because the premium taxes I think generally across the United States are not a regulatory tax. They are a tax to receive income for the coffers of the State.

Mr. SUTCLIFFE. You say you are always attempting to get more funds from your State government for regulation. Are you suggesting the $30 million you project the Federal Insurance Guaranty Corporation would add to the $40 million of existing money available for regulation really would benefit you? In other words, my question is this: You have just mentioned that you spend a lot of time or use that argument to get more funds, and if you do——

Mr. WORTHINGTON. Only with tongue in cheek I use the argument, because I do not believe in it.

Mr. SUTCLIFFE. But you are after more funds?

Mr. WORTHINGTON. Absolutely.

Mr. SUTCLIFFE. And S. 2236 would give funds for assisting your regulation.

Mr. WORTHINGTON. The reason I seek more funds—the examination process does not cost the department significantly. It costs the insurance companies.

Mr. SUTCLIFFE. Wait a minute. It costs the insurance companies who then put this in their rate-making figures and the American people pay for it; is that correct?

Mr. WORTHINGTON. Yes.

Mr. SUTCLIFFE. It does not make a lot of difference whether it is a direct tax by the Government or whether it comes out of the cost of the insurance. So, I do not see the distinction there.

Mr. WORTHINGTON. The reason I seek more funds for my Department—I think most commissioners do—is to provide better service to the consumer, to provide divisions in the department where they can come in and register complaints, seek answers to their questions, and learn about the policies that they purchase. This is the thing that insurance companies are getting involved more and more in today, particularly because of the new awareness on the part of the consumer of his rights.

We stand ready to serve them and help them to understand the insurance policies they buy and that they receive dollar for dollar paid.

Mr. SUTCLIFFE. It would be helpful for us in an examination of the cost-benefit ratio, which you urge us to make, if you could provide us with figures on the cost of uninsured motorist insolvency protection to the American people, the projected costs for a 50-State postinsolvency assessment fund—there must be some involvement of the State commissioner in that, there must be some pay-out that would be attendant with the situation—and also take into account the possibility of a postassessment program at the Federal level to counteract or to create a better cost-benefit ratio and also any kind of projections you might have about an interstate guaranty corporation which you may feel is the next step to close the so-called residual gap. We would appreciate that kind of information, because this would assist us in our legislative endeavor.

Mr. WORTHINGTON. We will try to gather that information for you, insofar as possible.

(The information referred to follows:)

INSURANCE DEPARTMENT OF IOWA,
STATE OFFICE BUILDING,
Des Moines, January 16, 1970.

Hon. WARREN G. MAGNUSON,
Chairman, U.S. Senate, Commerce Committee,
Washington, D.C.

DEAR SIR: On November 26, 1969, I had the pleasure of testifying on S. 2236 before your Commerce Committee on behalf of the National Association of Insurance Commissioners. During the course of the testimony, members of the Committee and of the staff requested the submission of certain supplemental information. This letter is in response to those requests.

I. STATISTICS ON LOSSES DUE TO INSOLVENCIES

At pages 326–330 of the transcript, Mr. Sutcliffe posed several questions in connection with statistics on losses attributable to insolvencies and invited written comment thereon. Before doing so, let me reiterate what I said then.

"Mr. Sutcliffe, for the record, let me repeat again, too, that the NAIC position, and that is regardless of what the figures are, we recognize there is a problem, and we don't intend to hide behind figures or to say that the problem is so small in terms of the total number of people, although we feel it is small in terms of percentages, that we stand ready to do nothing; we stand ready to do something in the attempt to solve the problem and recognize there is one."

As was indicated during the course of the hearing, the NAIC was then in the process of drafting model guaranty fund legislation recommended for enact-

ment by those states which do not have some type of comparable statute already on the books. At the December 1969 meeting, the model act was adopted by the Association as a whole and has been made available to the individual states for their consideration at the forthcoming legislative sessions. (A copy of the model bill is attached.) Thus, even though the NAIC believes that the extent of loss due to insolvencies has been overstated, it is nevertheless convinced that the situation warrants remedial action and consequently the NAIC has acted. However, since the Committee is still apparently interested in the "figure" debate we have pursued the question further.

At the beginning of my testimony, I submitted for the record the Report of the Special Committee on Automobile Insurance Problems (NAIC), July 16, 1969. As a part of that report, there was included detailed studies on insolvency losses conducted by the Texas Insurance Department following both the "Dodd" hearings and updated after the "Hart" hearings last summer. The conclusions of that study indicated that the average annual losses due to insolvencies were $5.4 million to $6.0 million depending upon the time period being looked at. More recently we retained the independent judgment of a third party actuary. While he approached the problem somewhat differently than did the Texas study, he concluded that the average annual loss was in the neighborhood of $5.5 million. The Texas figures did not include losses on unearned portions of the premium paid by the policyholders. Our actuary has included an additional estimate of $2.0 million due to the loss of unearned premium, bringing the total to a $7.5 million average loss per year. To put the problem in perspective it should be pointed out that the estimated premium for automobile insurance in 1969 is in excess of $11 billion. Thus the loss attributable to insolvencies represents 68 cents per $1,000 of premium or less than 7/100 of 1% of the total business written. Based upon an insured automobile population of 89 million cars, the cost would be less than 9 cents per car. A copy of his memorandum is attached including comments on the points made by Mr. Sutcliffe during the course of my testimony.

While we have tried to be responsive in commenting on the statistical debate, let me reiterate. The NAIC does not defend the status quo using low statistics as the rationale. We think there is a problem. As a result we have drafted a model guaranty fund act which was adopted by the NAIC as a whole. The problem is being solved at the state level. The debate over the figures seems to have little revelance when viewed in this context.

II. ESTIMATED COSTS OF THE PROPOSED FEDERAL BUDGET

During the course of the hearings a number of claims have been advanced as to the benefits to be rendered to the public by creating the proposed federal corporation. At the same time, relatively little attention has been focused on the cost of such benefits. In this connection it is significant to note that S. 2236 has been premised on the FDIC concept and structure. Thus, in attempting to appraise the proposed federal insurance guaranty corporation, it is relevant to consider this counterpart in the banking world.

Since its inception in 1933, the operations of the FDIC have been quite expensive. Its 1968 Annual Report (hereafter referenced to as the Annual Report) reveals that during this period the FDIC has collected nearly $4.2 billion while paying out $55 million in net losses. In other words, for every dollar the FDIC has paid to the public, it has collected $76. (Of course a sizable portion of this revenue is used to build reserves against future losses.) Over this same period of time, $307.1 million was used to pay administrative and operating expenses while only $55.2 million went toward the payment of net losses. That is, administrative and operation expenses were nearly 5.6 times greater than benefits paid. To be more recent, in 1968, of the total FDIC expenses of $30.4 million, $29.0 million went to administrative and operating expenses whereas only $1.4 million were in the form of benefits—i.e. cost-benefit ratio of approximately 20 to 1.

These figures are not cited to detract from the performance of the FDIC. While its own figures demonstrate that the cost has been quite high in terms of benefits paid, there is no doubt that it has contributed to stability in the banking business and to maintaining public confidence in the banking system. Back in 1933, the FDIC stepped into a vacuum in public protection. The situation today concerning the proposed federal insurance guaranty corporation is entirely different. There is no regulatory vacuum. The states have long regulated the insurance business. Several states have their own guaranty fund programs. As stated earlier, the NAIC has adopted a model guaranty fund bill which we believe will pass in most if not all states at their next legislative sessions. Against

this backdrop, it would be wasteful and inefficient to create a new large federal bureaucracy, particularly when patterned after one whose expenses far exceed the benefits paid thus far.

But, some argue, the expense of administering the proposed federal insurance guaranty program would not be as great as for the FDIC. Of course, it is difficult to estimate operating cost of an organization which has not come into being as yet and whose modus operandi is not established. Even with that caveat the probability seems quite high that the cost will exceed even that of the FDIC. This estimate can be developed as follows.

Presumably the biggest single item of administrative expenses relates to examiners.[1] It is estimated that in 1969 the states employed approximately 1400 examiners (including a few on the contract basis.) How many of these examiners can be said to be involved in examining property and liability companies? Using relative premium volume as a rough guide, we can say that 45% of the examiners are so involved, i.e., 630. However, this figure should be adjusted to reflect the fact that many property and liability insurers are affiliated with life companies which would also have to be examined for purposes of the guaranty fund. We will arbitrarily add 70 examiners needed to bring the total up to 700 examiners needed.

The argument is made that the new federal corporation would cooperate with the states so as to avoid duplication of the examination costs. But as we all know, whatever the initial intent, those persons charged with the responsibility of administering a law (particularly when safeguarding a federal fund) are most reluctant to rely on others (i.e., the states) over whom they do not exercise control. The FDIC is a perfect example of this. In its 1968 Annual Report (pp. 15–16) the FDIC noted its power to examine any insured bank. To avoid duplication of effort, the FDIC accepts reports of other *federal* supervisory agencies. However, insured banks which are not members of the federal reserve system are under no other federal regulatory body. Hence the FDIC examines such banks at least once every 12 months. In approximately half of the states it cooperates with the states to the extent of joint or concurrent examinations. In the others, the FDIC conducts bank examinations on its own. On this basis, we could perhaps reduce our estimated number of federal insurance examiners by 25% to 525 reflecting joint efforts in ½ of the states.[2]

Insurance companies are typically examined once every three to five years. For this computation, we shall assume an average of once every 4 years. (Of course marginal companies can be examined more often as the situation requires. Also comprehensive financial statements must be submitted annually or even more frequently by insurers when the situation warrants.) S. 2236 provides that virtually every insurance company may be examined. The bill contemplates annual scrutiny. If the banking area is any precedent, examinations on annual basis by the proposed corporation can be anticipated. Since the frequency of regular federal examinations may be four times as great, the number of federal examiners needed would increase to 2100 on an extrapolation basis.

The average salary level for FDIC bank examiners exceeds $11,600. If we add to this an additional 50% (which we believe is conservative) to reflect the cost of social security, fringe benefits and travel expense, the total expenses per year per examiner to the proposed corporation would be $17,400. When this amount is multiplied by the estimated number of federal insurance examiners that would be needed, the annual expense would be $36.5 million.

The examiners represent only one aspect of the personnel cost of the proposed corporation. Examination reports have to be reviewed and analyzed. Persons would be needed to investigate, adjust and compromise claims against insolvent insurers. This can be a difficult, expensive and time consuming function.[3] Attorneys will be needed to defend actions as well as for other staff work. The obligation to determine whether a participating insurer is engaging in "an unsafe or unsound practice" would involve the corporation in questions such as rate

[1] FDIC has 2,365 employees of which 1,401 were in the Division of Examination.

[2] If 700 examiners are needed in all of the states and if in one half of the states there is no cooperation, 350 examiners would continue to be needed. In the other half of the states where examinations are conducted concurrently or jointly, it is assumed that only one half would be required, i.e., 175 (350 x 50%). This results in a total of 525.

[3] For example, the 1968 ratios of loss adjustment expenses to net earned premiums of the 20 largest stock companies was 12.6% for auto bodily injury liability, 10.9% for auto property liability, 7.9% for auto collision, 5.6% for auto fire, theft and comprehensive, 3.7% for fire, 0.8% for extended coverage, 7% for homeowners, 22.5% for bodily injury liability other than auto, etc. See Loss and Expense Ratios (1968) published by the New York Insurance Department.

adequacy, classification, policy forms, underwriting practice, etc. These activities can absorb a vast amount of manpower, as would the clerical support needed by the corporation. Of the FDIC's total 2365 employees, almost 1200 are not examiners. The activities of the proposed insurance guaranty corporation would extend considerably beyond those of the FDIC. We would conservatively estimate the need for a minimum of 1500 employees other than examiners. Assuming that the average salary would be $10,000 plus 25% (or $2,500) for social security and fringe benefits, the personnel expense to the corporation would be nearly $18.8 million.

In addition to the cost of the examiners and other personnel, there would be the multitude of overhead expense such as office space (presumably in various parts of the country like the FDIC which has 14 district offices), supplies, utilities, etc. Let's arbitrarily add $4.8 million to reflect these items and round out the total estimated administrative and operating expense at $60.0 million (vis-a-vis the $29.0 million for the FDIC).

When administrative and operating costs of $60.0 million are compared to the benefits which accrue, the cost benefit ratio does not look very good. If the NAIC calculation of $5.4 million average annual loss attributable insolvencies is accepted, the ratio would be 11 to 1. That is, for every dollar of benefit paid, there would be $11 expense. If our third party actuary's figure of $7.5 million is accepted, the ratio would be 8 to 1. Even if Mr. Sutcliff's $20 million annual loss figure is accepted, the cost-benefit ratio would still be $3 of expense for every $1 of benefit paid. And, such expense is unnecessary when there is a variable, and inexpensive alternative at the state level such as the insolvency coverage under UM provisions, the state guaranty fund laws and the NAIC model bill.

Of course, as noted at the outset, cost estimates at this juncture at best are speculative. However, past experience suggests that when cost projections for federal agencies err, they tend to err on the side of being too low. This may very likely be true here as well.

III. UM COVERAGE

At pages 334–335 of the transcript, Mr. Sutcliffe inquired as to what portion of the premium for UM coverage is attributable to the addition of the insolvency protection. We are told that insurers belonging to the IRB have made no increase in UM premium rates due to the introduction of the insolvency coverage. A large independent writer of automobile insurance indicated that data has not been kept on insolvency claims since, at least up to this point, they have been considered as minor. In other words detailed information segregating out the insolvency aspect of UM coverage has not been compiled because of the nominal amount of the cost. These examples seem to be representative of the experience of the industry.

Incidentally, if there were any substantial number of insurer insolvencies, with the large number of individual members of the public affected, the number of claims under the insolvency provision of the UM coverage would reflect this fact. Consequently, provision would have to be made in the premium charge for the UM coverage. The low number of insolvency claims is potent evidence that at this juncture the problem, while significant, has not reached overwhelming dimensions.

In the course of my testimony, I stated that the uninsured motorist coverage has, in many states, been an unprofitable line. Mr. Sutcliffe asked us to produce figures to substantiate this. Due to the relatively low claim frequency characteristics of this coverage, both state and countrywide, the underwriting experience tends to be erratic. Here are State Farm's Figures from 1960 through three-quarters of 1969.

Year:	*Underwriting profit*
1960	—$2,420,322
1961	1,562,621
1962	216,263
1963	—708,380
1964	—565,485
1965	—156,072
1966	—564,457
1967	—768,181
1968	3,750,469
1969 ¾	3,086,730
Total	3,433,186

We do not have, readily available, comparable figures for other carriers. However, State Farm is a large writer, and we believe that the above figures are fairly representative. They show that the companies did go through a period of adverse underwriting results, but that the business is now stabilized and is showing a profit.

IRB figures, as of September 1, 1969, show a countrywide loss and adjustment expense ratio of .587% which means that for their stock company members, the business on an overall basis is now being written profitably. Two states, Kansas and New Hampshire, showed combined loss and expense ratios of 100%.

State Farm's average semi-annual rate for this coverage as of the year end 1969 was $2.36.

IV. COST OF STATE POST ASSESSMENT GUARANTY FUND

At page 356 in the transcript, Mr. Sutcliffe requested information as to (1) the cost of the insolvency portion of the uninsured motorist coverage to the American public, (2) the projected cost of state post-assessment insolvency funds including consideration of a federal post-assessment program and (3) the cost of an interstate guaranty corporation. In light of the preceding testimony relating to the estimated cost of operating the proposed federal guaranty corporation, we gather that what is being sought is a comparison between the cost of the state and federal approach. In attempting a comparison, we should remember that two functions are involved: (a) the guaranty function—i.e. paying valid claims against an insolvent insurer, and (b) the prevention function so as to avoid to the extent possible insurers becoming insolvent.

First, as to the guaranty function, S. 2236 would create a new permanent federal agency requiring staffing, office space, overhead, etc. The model NAIC post-assessment bill would require none of this. Unlike the S. 2236 situation, no permanent staff or office would be needed. If no insolvency occurs, the state post-assessment approach would generate no expense other than nominal expenses incurred by the board of directors meeting periodically.

If an insolvency does occur, costs can be broken down into two types, (1) the cost of the claims and (2) the administrative cost of adjusting, settling and litigating claims. Presumably the former—i.e. the cost of the claims—would be approximately the same under either the state or the S. 2236 approach. However, we submit that administrative cost under S. 2236 would be significantly greater than those under the NAIC model. Under the model bill, the facilities of the industry in the area where the insolvency occurs and its existing expertise would be utilized. Although an insurer designated to handle the claims would have increased overhead, the work would be a natural extension of its everyday activities. In contrast, the proposed federal agency would have to put together a new staff, establish local and regional offices around the country, acquire expertise over a period of many years, etc. Thus, we virtually see no prospect that a federal agency could perform the loss settlement function as economically as would occur under the NAIC model bill.

It is quite difficult to measure quantitively in advance the cost of the state post-assessment approach. The cost would vary depending upon the type of insurer which becomes insolvent, its volume and distribution of business, etc. However, since the claims would be handled through the facilities of the industry, the expenses might approximate those experienced by the industry as a whole. Attached is a table of loss adjustment expense to net earned premium drawn from statistics developed by the New York Insurance Department.

Second, as to the insolvency prevention function, S. 2236 would generate expenses vastly in excess of those under the model bill. A new federal agency to perform examination, reporting and licensing function would be created requiring substantial manpower to duplicate existing functions of the states. In sharp contrast, the model bill, while providing a mechanism to tap the informational resources of the industry, would create no new costly regulatory machinery.

Mr. Sutcliffe also asked about the cost of UM insolvency coverage. Because of the nominal amounts involved precise data has not been kept or compiled (see III above). However, what is important to note here is that under both approaches, the UM coverage has been made primary. Thus its impact on cost would be the same for both. Cost estimates as to a nonfederal interstate fund were also requested. In the absence of a more definite formulation as to the nature and modus operandi of such a fund, meaningful estimates are not possible at this time.

Very truly yours,

LORNE R. WORTHINGTON,
Chairman, NAIC Executive Committee.

MEMORANDUM

To: Honorable Ned Price, Chairman, National Association of Insurance Commissioners.
From: Willis A. McVey, Assistant Casualty Actuary, Casualty Division, Texas State Board of Insurance.
Subject: Automobile Insurance Company Insolvencies—Magnuson Committee.
Date: January 2, 1970.

The staff of the Texas Insurance Department has been requested to give background information on the so-called Texas figures which were developed and the source from which they were derived, relating to insurance company insolvencies which originally appeared in the "Dodd" report, and the subsequent "Hart" exhibit.

Also, we have been asked to comment on the testimony of Mr. Lynn Sutcliffe, Counsel for the Magnuson Committee, appearing on Pages 326–330 of the transcript of the Hearing.

PROCEDURE USED BY TEXAS INSURANCE DEPARTMENT IN SECURING STATISTICAL DATA RELATING TO AUTOMOBILE INSURANCE COMPANY INSOLVENCIES AND SOURCE OF DATA

1. When the "Dodd" report was published, the Texas Insurance Department, in 1966, prepared instructions and a questionnaire in order to secure the automobile premium writings of the high-risk automobile insurance companies which failed from 1960 through 1965, covering those 58 companies listed in the "Dodd" report (Exhibit I).

These instructions and questionnaires (Exhibit II) were forwarded by Wm. Hunter McLean, Chairman, Texas State Board of Insurance, directly to the various Insurance Commissioners where the insolvent companies were domiciled, in order to secure the information directly from those Insurance Departments or the Receivers of the insolvent companies.

Also, we directed another inquiry to an outside source, The National Bureau of Casualty Underwriters (presently the Insurance Rating Board), in an effort to secure the automobile premium writings of these same companies for the purpose of: (1) serving as a double-check on the information secured from the 20 state insurance departments where the insolvent companies were domiciled and (2) securing premiums on some of the 58 companies which might not be available in the state insurance departments, as all of the companies were in receivership.

From these two sources, we were able to secure the premium writing of 51 out of the 58 companies listed in the "Dodd" report.

The results of this study are summarized in a memorandum to Wm. Hunter McLean dated April 4, 1966 (Exhibit III) and resulted in the accumulation of automobile premium writings for the 51 companies in the amount of $178.8 million for the years 1960–1965.

Exhibit IV is a transmittal letter to the other 20 Insurance Departments who co-operated in the survey.

2. Early in 1967, a second questionnaire and instructions were prepared by the staff of the Texas Insurance Department in order to secure claimant loss information for those 24 insolvent companies listed in Exhibit 3, Table 3, of the "Dodd" report (Exhibit V).

These forms were forwarded to the Washington office of the National Association of Insurance Agents, who in turn distributed the forms to local agents residing in the cities where the records of the insolvent companies were located.

The claimant loss information was more difficult to secure than premium writings since this information had to come directly from the Liquidator-Receiver of the various companies at the local level.

When the forms were returned to the NAIA, they were forwarded to the Texas Insurance Department for tabulation.

From the surveys mentioned in 1 and 2 above we accumulated Automobile Premium Volume and Claimant Losses and we were able to compare the *claims* listed in the "Dodd" report, Exhibit 3, Table 3, with the estimated *Claimant Loss* developed by the Texas Survey for 20 out of the 24 companies listed therein (Exhibit VI). Also, we were able to compare the *Automobile Premiums* versus *Claimant Losses* which we secured for 17 out of the 20 companies listed in the Dodd Report, Exhibit 3, Table 3 (Exhibit VIA).

3. A third survey (Exhibit VII) was undertaken by the Texas Insurance Department in 1969 in order to secure an up-to-date claimant loss information for those insolvent companies listed in the later "Hart" Exhibit (Exhibit VIII) which became insolvent in 1966–1968. The claimant loss information was secured

by the Texas Insurance Department through direct questionnaire to the other State Insurance Departments or the Receivers of these companies. Out of a total of 14 companies covered by this period of time, claimant loss information and premium writing was secured for eight (Exhibit IX).

COMMENTS AND CONCLUSIONS OF "TEXAS" SURVEYS VS. "DODD" AND "HART" SURVEYS

1. Exhibit VI clearly shows how the *claims* were overstated by the "Dodd" staff—$106,836,636 for the Dodd Staff vs. $16,162,232 as developed by the Texas Survey.

2. Texas Exhibit VIA shows the relationships of the total *Automobile Premium* and *Claimant Loss* for the Dodd Exhibit 3, Table 3 companies, again demonstrating the fallacy of the "Dodd" staff inferences.

3. The "Hart Staff Exhibit"—Exhibit VIII attached indicates that the 88 companies listed therein wrote a Grand Total *Automobile Premium* of *$517,415,-614* for the years 1958–1968: We would suggest these figures should be re-checked since a number of these companies wrote lines of insurance *other than Automobile.*

Likewise, the eleven year period in the caption of this exhibit is incorrect since Premium Writings are shown for some of the companies for the years 1952, 1953, 1954, 1955, 1956 and 1957.

The $517 million dollar figure is meaningless since no effort was made by the "Hart" staff to display the *losses and loss adjustment expenses* which these 88 companies *paid* during the same period of time as their Premium Writings.

The Texas survey clearly reveals the "Dodd" staff overstated the *claims* for the insolvent companies and the later "Hart" staff prepared a later exhibit on *Automobile Premium Volume* which is equally erroneous and misleading.

4. Texas Exhibit IX again demonstrates the validity of *Premium* and *Claimant Losses* for those companies listed in the "Hart" Exhibit for the later years 1966–1968, as well as in the earlier Texas exhibit covering the years 1960–1965.

COMMENTS ON TESTIMONY OF MR. LYNN SUTCLIFFE BEFORE MAGNUSON COMMITTEE

Mr. SUTCLIFFE: "Are you prepared to discuss at this time the allegation that the $200 million statement of loss is an overstatement of the actual loss?"

Comment: Texas Exhibit VI attached clearly demonstrates the unreliability of the "Dodd" claims and how they are overstated. The Texas Department secured the *Automobile Claim Losses.* It is obvious that the Dodd claims include losses *other than* Automobile which the companies sustained.

We secured our figures directly from the other State Insurance Departments or the Liquidator—Receiver of the insolvent companies and we are amazed that, for this group of companies, the "Dodd" staff overstated these Automobile Claims by over $90 million to a Committee of the U.S. Senate.

Mr. SUTCLIFFE: "The assumptions of the NAIC report are contained within an attachment to the document you were referring to. It is an assumption that the claimant loss, whatever that is, equals 21 percent of premiums written."

Comment: No assumption is involved in the derivation of the basic 21 percent figure mentioned above by Mr. Sutcliffe. The staff of the Texas Insurance Department, through direct questionnaire to the Liquidation—Receiver or the particular State Insurance Department where the insolvent company was domiciled, secured reliable and factual information on the Total Automobile Premium from 1960–1965 as well as claimant loss for 17 companies out of those companies listed in Exhibit 3, Table 3, of the original "Dodd" Report. See Exhibit VIA attached.

The claimant loss of $15,534,744 divided by the Total Auto Premium of $72,942,375, equals 21 percent. This is a fact, *not an assumption* as stated by Mr. Sutcliffe.

In order to bring up-to-date and add the years 1966–1968, the Texas Department, in 1969, sent out additional questionnaires on those insolvent companies listed in the later "Hart" Exhibit which showed the Auto Premiums written for companies in 1966–1968. The claimant loss information was again secured by the Texas Department through direct questionnaire to the other state insurance departments or the Receivers of those companies. See Exhibit IX attached.

Out of a total of 14 companies covered by this period of time, we secured claimant loss information and premium writings for 8 of these companies. The total average annual premium for these 8 companies amounted to $16,084,212 and the average annual claimant loss for these 8 companies totaled $3,357,311. Therefore, $3,357,311 divided by $16,084,212 equals 20.87 percent or 21 percent rounded. This is a precise figure and *not* estimated or assumed as stated by Mr. Sutcliffe.

There were 6 companies listed in Exhibit IX for which the Claimant loss could not be supplied. We arrived at the claimant loss for these 6 companies by taking 21% of their average annual premium (which was available). This is clearly footnoted on Exhibit IX.

Mr. SUTCLIFFE: "Now the figure for total claimant loss compiled by Senate Antitrust and Monopoly Subcommittee for 88 Automobile insurance insolvencies amounts to $517 million. That is for a ten year period."

Comment: It is obvious that Mr. Sutcliffe does not understand insurance terminology or else he is deliberately attempting to mislead and misinform the Magnuson Committee by the above statement. The $517 million figure was arrived at by the staff of the Magnuson Committee—it is their figure and not one arrived at by the staff of the Texas State Board of Insurance.

The copy of the exhibit prepared by the Committee Staff is clearly titled "Automobile Insurance Premium Writings of Fire and Casualty Companies that Failed 1958–1968." The grand total of "Auto Premiums Written" for the 88 companies is shown to be $517,415,614. This is "Premiums Written" and *not* "Claimant Loss" as stated above by Mr. Sutcliffe. Exhibit VIII.

This error merely points up that the Committee Staff people cannot interpret and present their *own* figures and we can, therefore, understand why they cannot interpret some of our figures.

Mr. SUTCLIFFE: "Applying the 21 percent factor to the $517 million of premiums written, you come up with approximately $108 million loss. Spread over a ten year period it produces a yearly average loss of $10.8 million compared to the NAIC statements of $6 million in one period of time and $5 million in another period of time."

Comment: Mr. Sutcliffe has again failed to understand and accurately present the figures prepared by the committee staff (Exhibit VIII). The caption of this exhibit states that the exhibit covers the Automobile insurance premium writings of Fire and Casualty companies that failed 1958–1968. A close review of their exhibit reveals that the period of time covered for some companies listed therein includes the years 1952, 1953, 1954, 1955, 1956 and 1957. Therefore, Mr. Sutcliffe's yearly average loss of $10.8 million—over a 10 year period—is completely without foundation or fact. Another glaring example of deception.

Mr. SUTCLIFFE: "The figures include only 88 of 108 insolvencies. The average premium written by the insolvent companies was over $5 million. This is the average. So to get the figures that we don't have for the other 22 companies, we have averaged the yearly loss and assumed that these companies had a yearly loss average of $5 million to come up with $1.5 million per year additional to the 10.8. This adds a total of $21 million to the previous total of $102 million.

Comment: It appears evident from the above statement, as well as the preceding paragraph in Mr. Sutcliffe's testimony, that he is no actuary in that he is confused as to the meaning of "premiums" and "losses". He not only violates the principles of actuarial science, but his basic arithmetic is faulty. The "$1.5 million" quoted above should be "$1,050,000"—a mere $450,000 error.

Mr. SUTCLIFFE: "In your staff report, you calculate, as nearly as possible—and this is the June 16 staff report on the entire Automobile Compensation Problem—you calculate there is approximately $111.1 million of unearned premiums and you say this calculation presents a more balanced picture of the magnitude of the problem than the $517 million figure."

"I don't know what is included within that calculation of $111.1 million, but even using that figure, you go on to say that of all the people that had claim forms mailed to them, 42 percent of those to whom the claim forms were mailed

returned them. So there was about 58 percent that did not return their claim forms. This produces a total after unearned premiums lost even assuming that the claimant loss figures that you presented in the NAIC study included unearned premiums."

"Because of the lack of reporting data and the assumptions upon which this was calculated, this has to add at least a minimum of $66 million of unearned premium loss to the total $108 million for the 88 companies and 21 million for the remaining 22 companies. This comes to a total calculation of direct loss of $195 million."

"We are getting awfully close to the $200 million figure. This doesn't even begin to include the assessable loss. The most recent figures we have show a potential liability of $69 million for assessable loss and as of January 1969 $3 million paid already. Even if we assume only $5 million will be collected, this easily puts us in our calculations over the $200 million figure. And these are only direct costs. It doesn't include the Fire and Casualty Company insolvencies or any other indirect losses associated with insurance company insolvencies."

"I want to present that for the record and ask for you to give a comment and breakdown of where we are in error."

Comment: The reference by Mr. Sutcliffe to "unearned premiums", line 16, Page 328 of his testimony, again demonstrates his lack of understanding of insurance terminology. There is a great deal of difference between "written premium", "earned premium" and "unearned premium".

Mr. Sutcliffe, on line 22, Page 328, refers to "42 percent" of claim forms as having been returned and he infers that the 42 percent figure was developed by the staff of the NAIC. Based upon information we have, this 42 percent was developed through a survey made by the staff of the "Hart" Committee.

On line 5, Page 329 of Mr. Sutcliffe's testimony, he refers to "$66 million of unearned premium loss" and he proceeds to add this to $108 million of some unrelated figure and $21 million of something else and "backs into" a total "direct loss of $195 million". This would be nice if it were possible but you don't add apples and oranges (or insurance) on that basis.

Since Mr. Sutcliffe has asked for comments, lines 19–20, page 329, the following are offered:

1. The testimony is extremely false and misleading due to his lack of understanding and meaning of certain basic insurance terms.

2. Due to this lack of understanding, basic principles of actuarial science have been violated.

3. The results of the surveys contained in Exhibits 1–4, Tables 1–4, of the Hearings held by the Sub-committee on Antitrust and Monopoly—Committee on the Judiciary—United States Senate—89th Congress—1st Session, Part 12, 1966, High Risk Automobile Insurance, May 11 & May 12, 1965 was an effort on the part of the "Dodd" staff to show how much had been lost by policyholders and other claimants as a result of the insolvency of 58 insurers writing high risk Automobile business.

After reviewing these exhibits prepared by the Dodd staff, the Texas Insurance Department undertook a survey of its own since the Exhibits prepared by the Dodd staff were obviously colored and misleading.

We prepared survey forms in order to secure reliable data on premiums and claimant losses for those companies listed in the Dodd Report. We went directly to the Receivers of the insolvent companies or the State Insurance Departments in the states having records for those companies.

The first survey in 1966 secured the Premium Writings of 51 out of the 58 companies listed in the Dodd Report and aggregated $178,847,475 for the years 1960–1965.

In 1967, a second survey was sent out by the Texas Insurance Department to the other State Insurance Departments or Receivers in order to secure claimant loss information for those 24 insolvent companies listed in Exhibit 3, Table 3 of the Dodd Report.

The results of these surveys revealed that those companies listed in Exhibit 3, Table 3 for 1960–1965, wrote $72,942,375 in Automobile Premium and sustained claimant losses of $16,725,488.

The Dodd Report for these same companies indicated total claims of $106,836,-636—over $90,000,000 more than the Texas Survey.

It is evident that the Texas Survey proved up the fallacy of Exhibit 3, Table 3 prepared by the staff of the Dodd Committee.

A third survey was made by the Texas Department in 1969 in order to secure up-to-date claimant loss information for those insolvent companies listed in the later "Hart" Exhibit displaying Auto Premiums Written which were shown to have become insolvent in 1966–1968. Again, reliable statistical claim data was secured directly from the State Insurance Departments or the Receivers. Note the staff of the Hearing Committee switched from "losses" to "premiums". We kept our surveys on a consistent basis in order to make reliable comparisons with the previous Texas surveys.

The mere premiums written as tabulated by the Staff of the Hart Committee on the insolvent companies is meaningless since no effort on their part was made to display the losses or loss adjustment expenses which these companies paid during the period 1958–1968, plus the actual claimant losses resulting from the insolvency of these companies.

Examples of errors in the original Dodd Report as respects Illinois insolvencies:

1. American Bowlers—Dodd report estimates percent of dollar amount claimed which will be paid based on the dollar amount filed as 3.2%. Actually a dividend of 90% was paid on allowed claims. Estate closed February 10, 1966.

2. Bedford Mutual—Dodd report shows 135 claims filed against the company estate demanding $70,000 and that a dividend of 128% is estimated will be paid based on the dollar amount filed. Actually 62 claims were filed for a gross amount of $35,760.12. The Liquidator paid a dividend of 93% on all claims allowed. Estate closed June 9, 1966.

3. Whitehall Mutual Fire and Marine Insurance Company—Dodd report shows 250 claims filed against the company estate demanding a gross amount of $180,000 and that a dividend of 32% will be paid based on the dollar amount filed. Actually 37 claims were filed seeking a gross amount of $65,426.58. After evaluation a dividend of 100% was paid on all allowed claims.

4. Monroe Mutual—Dodd report shows 1463 claims filed against the company estate demanding a gross of $3,736,386.00.

Actually the figure listed reflect filings made in the Illinois ancillary proceeding involving the Crown Insurance Company of West Virginia. Monroe Mutual was merged with Crown Insurance Company prior to May 7, 1964, date of the West Virginia liquidation order. Liquidation proceedings were instituted against Monroe Mutual Insurance Company in Illinois on November 18, 1964 but solely for the purpose of revoking the company's charter and its dissolution. No claims were filed against the estate which was formally closed on November 29, 1965.

5. Banner Mutual Insurance Company—Dodd report shows 6,000 claims filed against company estate while actually 3,747 claims were filed with the Liquidator of the Banner Mutual Insurance Company.

(Part 12—1966 High-Risk Automobile Insurance; Hearing Days May 11 and May 12, 1965)

EXHIBIT 1

APPENDIX I. GENERAL MATERIAL

TABLE 1.—LIQUIDATIONS BY STATE OF DOMICILE AND NUMBER OF PERSONS INSURED FOR INSOLVENT INSURANCE COMPANIES WRITING HIGH-RISK AUTOMOBILE BUSINESS, 1960–65 [1]

State of domicile and name of company	Date of receivership	Number of States admitted	Operating on non-admitted basis	Number [2]
Illinois:				
Lake States Casualty	October 1965	1	([3])	30,000
Bell Casualty Insurance Co	September 1965	1	([3])	4,400
Bell Mutual Insurance Co	do	1	([3])	60,000
Banner Mutual Insurance Co	June 1965	2	No	7,000
Bedford Mutual Insurance Co	April 1965	1	No	1,600
Whitehall Mutual Insurance Co	January 1965	1	No	7,400
Monroe Mutual Insurance Co	November 1964	1	No	3,800
Multistate Interinsurance Exchange	September 1964	1	([3])	33,000
Oxford General Casualty Mutual Insurance Co	April 1964	1	([3])	300
Cosmopolitan Insurance Co	November 1963	10	Yes	130,000
Adams Mutual Insurance Co	October 1963	1	No	2,800
American Bowlers Mutual Casualty Co	do	1	No	56
General Union Mutual Insurance Co	June 1962	1	([3])	1,800
Central Casualty Co	March 1962	34	Yes	42,000
Pennsylvania:				
Lawn Mutual Insurance Co	April 1965	1	([3])	[4] 142
Delaware Valley Mutual Casualty Co	February 1965	1	([3])	3,000
Commonwealth Mutual Insurance Co	February 1964	1	([3])	[4] 0
Empire Mutual Insurance Co	January 1964	1	Yes	20,000
Graphic Arts Mutual Insurance Co	December 1962	1	([3])	10,000
Springfield Mutual Insurance Co	do	1	([3])	[4] 1,000
State Mercantile Mutual Insurance Co	November 1961	1	([3])	[4] 44
Missouri:				
Midwest Mutual Casualty Insurance Co	November 1965	([3])	([3])	60,000
Surety Insurance Exchange	June 1965	1	No	2,500
Allied Western Mutual Insurance Co	July 1964	2	Yes	24,000
American Midwest Mutual Insurance Co	November 1963	1	Yes	10,000
Guaranty Insurance Exchange	August 1962	4	Yes	100,000
Missouri Union Insurance Co	June 1960	1	No	1,000
Indiana:				
International Automobile Insurance Exchange	March 1964	18	No	20,000
Insurance Corporation of America	December 1962	1	Yes	[4] 1,700
Universal Automobile Insurance Co	October 1962	4	Yes	3,500
United Mutual Insurance Co	March 1962	1	No	2,300
United Public Insurance Co	June 1965 [5]	24	Yes	[4] 0
Michigan:				
Preferred Insurance Co	January 1964	35	No	[6]0
Exchange Casualty & Surety Co	April 1962	12	Yes	38,000
Michigan Surety Co	February 1962	43	No	18,800
Wisconsin:				
Market Mens Mutual Insurance Co	May 1962	12	No	64,000
Superior Mutual Insurance Co	May 1961	6	Yes	36,000
West Virginia:				
Crown Insurance Co	May 1964	3	Yes	[7] 65,000
National Automobile Insurance Co	September 1960	1	Yes	15,000
Texas:				
Career Insurance Co	July 1964	2	No	[8] 27,200
Government Services Insurance Underwriters	September 1963	1	Yes	29,500
Florida:				
National Home Insurance Co	April 1962	3	No	([3])
Equity General Insurance Co	June 1961	49	No	([3])
California:				
Cosmopolitan Insurance Exchange	December 1964	1	No	1,000
All Coverage Insurance Exchange	November 1962	1	No	36,000
Maryland:				
Chesapeake Insurance Co	November 1965	12	No	20,000
National Motors Insurance Co	March 1964	2	No	55,000
Maine:				
Washington Insurance Co	December 1965	([3])	([3])	([3])
Washington Mutual Insurance Co	do	([3])	([3])	([3])

TABLE 1.—LIQUIDATIONS BY STATE OF DOMICILE AND NUMBER OF PERSONS INSURED FOR INSOLVENT INSURANCE COMPANIES WRITING HIGH-RISK AUTOMOBILE BUSINESS, 1969–65 [1]—Continued

State of domicile and name of company	Date of receivership	Number of States admitted	Operating on non-admitted basis	Number
Tennessee: Monticello Insurance Co	July 1963	1	Yes	[4] 0
South Dakota: Security General Insurance Co	April 1964	6	No	[4] 0
South Carolina: First Citizens Fire & Casualty Co	August 1963	1	No	20,000
Minnesota: American Allied Insurance Co	August 1965	1	Yes	120,000
Massachusetts: Suffolk Insurance Co	November 1964	1	No	31,500
Delaware: National Automobile Insurance Co	September 1960	4	No	([3])
Colorado: Western Standard Indemnity Co	April 1961	1	No	[4] 0
Arkansas: United Automobile Insurance Co	April 1964	50	No	[4] 500
Nebraska: United Benefit Fire Insurance Co	November 1965	17	([3])	[9] 40,000

[1] The persons insured under an automobile liability policy includes the policyholder, the spouse and other residents of the household, permissive users, and persons or organizations legally responsible for use.

[2] These data are based on estimates of persons insured derived from the number of policyholders or policies in force furnished by the receiver. See p. 2 of Exhibit 15 which may be found on p. 6886. In table I, number of persons insured was estimated by multiplying policies in force by two.

[3] Data not available.

[4] All or a number of policies were canceled, allowed to expire, or assumed by another insurer prior to receivership.

[5] In rehabilitation since January, 1961.

[6] From May, 1963, date of conservatorship, to time of receivership, some 16,620 policies in force were canceled, allowed to expire, or assumed by another insurer.

[7] 50,000 of these persons insured were Missouri residents.

[8] Nearly all of these persons insured were Michigan residents.

[9] Estimated by company officials.

Source: Compiled from data furnished by State insurance departments, receivers, and attorneys for receivers. These data may be found in the files of the subcommittee.

TABLE 2.—ASSETS AND CLAIMS FILED, EVALUATED, APPROVED, AND PAID AS OF NOVEMBER 1965 FOR INSOLVENT INSURANCE COMPANIES WRITING HIGH-RISK AUTOMOBILE BUSINESS

State of domicile and name of company	Claims								Value of assets for purpose of liquidation	Estimated percent of dollar amount claimed which will be paid based on—		
	Filed		Evaluated by receiver		Approved by court		Paid			Amount filed (percent)	Amount evaluated (percent)	Amount paid (percent)
	Number	Amount	Number	Amount	Number	Amount	Number	Amount				
Illinois:												
Lake States Casualty	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)			
Bell Casualty Insurance Co	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	[2] $965,420			
Bell Mutual Insurance Co	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	[3] 182,118			
Banner Mutual Insurance Co	6,000	$11,000,000	(1)	(1)	0	0	0	0	[4] 500,321	4.5		
Bedford Mutual Insurance Co	135	70,000	(1)	(1)	0	0	0	0	[5] 89,785	128		
Whitehall Mutual Insurance Co	250	180,000	(1)	(1)	0	0	0	0	[6] 57,321	32		
Monroe Mutual Insurance Co	1,463	3,736,386	(1)	(1)	(1)	(1)	(1)	(1)	(1)			
Multi-State Inter-Insurance Exchange	2,086	17,541,044	(1)	(1)	0	0	0	0	[7] 498,212	2.7		
Oxford General Casualty Mutual Insurance Co	438	4,036,132	120	$46,170	0	0	0	0	[8] 89,400	2.3		
Cosmopolitan Insurance Co	21,945	68,654,699	(1)	(1)	0	0	0	0	[9] 3,638,483	5		
Adams Mutual Insurance Co	651	4,771,861	250	102,161	250	$102,161	0	0	[10] 142,000	3		
American Bowlers Mutual Casualty Co	8	33,459	(1)	(1)	0	0	0	0	[11] 10,780	3.2		
General Union Mutual Insurance Co	192	265,285	61	73,957	61	73,957	0	0	[12] 98,638	29		
Central Casualty Co	[13] 3,340	[13] 32,552,592	3,339	952,390	2,822	531,186	0	0	[14] 1,222,028	4	140	
Pennsylvania:												
Lawn Mutual Insurance Co	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	196,239			
Delaware Valley Mutual Casualty Co	1,158	2,859,184	1,158	1,140,000	0	0	0	0	40,238	1.6	3.5	
Commonwealth Mutual Insurance Co	1,668	3,742,246	1,668	1,500,000	0	0	0	0	1,107	.03	.07	
Empire Mutual Insurance Co	1,090	6,299,076	1,090	2,520,000	0	0	0	0	4,070	.06	.08	
Graphic Arts Mutual Insurance Co	50	61,852	50	30,000	0	0	0	0	7,665	1.2	25	
Springfield Mutual Insurance Co	60	29,219	60	28,000	0	0	0	0	2,085	6	7	
State Mercantile Mutual Insurance Co	(1)	(1)	22	9,500	22	9,500	0	0	719	0	0	0
Missouri:												
Midwest Mutual Casualty Insurance Co	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)			
Surety Insurance Exchange	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	100,055			
Allied Western Mutual Insurance Co	4,250	(1)	4,250	2,000,000	0	0	0	0	142,000		7	
American Midwest Mutual Insurance Co	10,000	(1)	(1)	(1)	0	0	0	0	145,000			
Guaranty Insurance Exchange	[15] 3,800	(1)	(1)	(1)	2,500	2,000,000	2,500	$83,000	[16] 94,000		4	4
Missouri Union Insurance Co	(1)	(1)	(1)	(1)	(1)	(1)	250	(1)	(1)			[17]

TABLE 2.—ASSETS AND CLAIMS FILED, EVALUATED, APPROVED, AND PAID AS OF NOVEMBER 1965 FOR INSOLVENT INSURANCE COMPANIES WRITING HIGH-RISK AUTOMOBILE BUSINESS

State of domicile and name of company	Claims								Value of assets for purpose of liquidation	Estimated percent of dollar amount claimed which will be paid based on—		
	Filed		Evaluated by receiver		Approved by court		Paid			Amount filed (percent)	Amount evaluated (percent)	Amount paid (percent)
	Number	Amount	Number	Amount	Number	Amount	Number	Amount				
Indiana:												
International Automobile Insurance Exchange	8,300	[18] $12,151,776	8,300	$6,265,731	0	0	0	0	$1,700,000	1.4	28	----
Insurance Corporation of America	1,254	5,000,000	(1)	(1)	2	$2,000	0	0	157,892	3	----	----
Universal Automobile Insurance Co	5,368	(1)	2,650	2,000,000	0	0	0	0	134,000	----	6	----
United Mutual Insurance Co	1,631	(1)	1,631	282,548	0	0	0	0	26,000	----	9	----
United Public Insurance Co	(1)	[19] 809,323	(1)	[20] 656,000	0	0	0	0	400,000	50	60	----
Michigan:												
Preferred Insurance Co	10,800	26,743,000	(1)	(1)	(1)	428,714	0	0	1,508,000	6	----	----
Exchange Casualty & Surety Co	17,900	25,914,000	12,350	(1)	12,400	3,022,131	0	0	398,633	1.6	----	----
Michigan Surety Co	8,500	(1)	4,649	(1)	5,068	3,857,619	0	0	1,878,337	----	----	----
Wisconsin:												
Market Mens Mutual Insurance Co	8,000	13,135,000	7,500	2,100,000	0	0	0	0	876,402	6.6	41	----
Superior Mutual Insurance Co	(1)	(1)	2,400	1,770,000	0	0	0	0	1,264,749	----	71	----
West Virginia:												
Crown Insurance Co	5,000	5,000,000	(1)	(1)	0	0	0	0	352,000	7	----	----
National Automobile Insurance Co	1,906	991,331	1,876	227,334	0	0	0	0	290,000	3	128	----
Texas:												
Career Insurance Co	(1)	(1)	650	2,760,000	0	0	0	0	300,000	----	11	----
Government Services Insurance Underwriters	3,539	(1)	[21] 3,539	712,337	539	442,337	539	$442,337	[22] 565,313	80	117	117
Florida:												
National Home Insurance Co	2,500	[23] 7,202,410	2,500	630,000	0	0	0	0	157,624	2.3	25	----
Equity General Insurance Co	7,456	8,545,887	7,456	1,116,605	0	0	0	0	800,000	9.9	71	----

California:												
Cosmopolitan Insurance Exchange	(1)	(1)	(1)	300,000	0	0	0	0	325,000	----	108	----
All Coverage Insurance Exchange	(1)	(1)	(1)	1,200,000	1,700	938,977	0	0	940,000	78	100	----
Maryland:												
Chesapeake Insurance Co	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	----		
National Motors Insurance Co	(1)	(1)	[24] 1,748	338,178	0	0	0	0	1,000,000	----		
Maine:												
Washington Insurance Co	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	----		
Washington Mutual Insurance Co	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	----		
Tennessee, Monticello Insurance Co	386	275,661	(1)	(1)	(1)	(1)	(1)	(1)	(1)	----		
South Dakota, Security General Insurance Co	600	1,257,000	(1)	(1)	(1)	(1)	0	0	350,000	30	----	
South Carolina, First Citizens Fire & Casualty Co	6,032	443,577	(1)	(1)	(1)	(1)	0	0	350,000	78	----	
Minnesota, American Allied Insurance Co	13,000	9,000,000	(1)	(1)	0	0	0	0	500,000	5.6	----	
Massachusetts, Suffolk Insurance Co	4,711	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	----	[35]	----
Delaware, National Automobile Insurance Co	2,635	10,700,000	(1)	1,230,000	(1)	(1)	0	0	713,000	6.6	57	----
Colorado, Western Standard Indemity Co	(1)	74,038	(1)	(1)	(1)	(1)	[26]	[26]	(1)	----	----	[26]
Arkansas, United Automobile Insurance Co	435	1,848,893	411	316,652	411	316,652	0	0	104,000	6	33	----
Nebraska, United Benefit Fire Insurance Co	2,500	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	----		

[1] Data not available.
[2] Includes agents balances, $575,980, estimated reinsurance recoverable, $65,000, cash on hand, $14,439, and time certificates of deposits $310,000.
[3] Includes agents balances, $85,368, estimated reinsurance recoverable, $71,748, and time certificates of deposit, $25,000.
[4] Includes agents balances, $24,832, estimated reinsurance recoverable, $106,503, cash on hand, $18,984, and time certificates of deposit, $350,000.
[5] Includes agents balances, $1,640, estimated reinsurance recoverable, $63,700, and cash on hand, $25,444.
[6] Includes agents balances, $9,257, estimated reinsurance recoverable, $681, and cash on hand, $48,382.
[7] Includes agents balances, $448,212, estimated reinsurance recoverable, $40,000, and cash on hand, $10,000.
[8] Includes agents balances (or uncollected premiums), $53,500, estimated reinsurance recoverable, $35,000, and cash on hand, $900.
[9] Includes agents balances (or uncollected premiums), $1,560,000, estimated reinsurance recoverable, $600,000, cash on hand, $227,000, and time certificates of deposit, $1,251,483.
[10] Includes agents balances (or uncollected premiums), $113,000, and cash on hand $29,000.
[11] Includes agents balances (or uncollected premiums), $5,700, and cash on hand, $5,080.
[12] Includes agents balances, $87,172, and cash on hand, $11,465.
[13] 244 claims in the amount of $28,060,000 were filed by United Cab Association (petition for bankruptcy pending) on behalf of individual members; no action has been taken, on these claims as they have not been liquidated.
[14] Included agents balances, $275,394, estimated reinsurance recoverable, $385,908, cash on hand $76,859, and time certificates of deposit, $483,865.
[15] Receiver mailed 10,000 proof of claim forms.
[16] Includes $11,000 for administrative costs.
[17] Claimants were paid 40 cents on the dollar when estate was closed in January 1965.
[18] Receiver reduced all claims by some $5,400,000 to bring them within policy limits.
[19] Includes general trade creditors' claims of $44,176.
[20] Includes general trade creditors' claims of $31,000.
[21] Includes 3,000 policyholders' unearned premium claims evaluated for $270,000.
[22] Includes $45,000 for administrative costs.
[23] Does not include $5,000,000 reinsurance claim filed by receiver of Exchange Casualty & Surety Co. of Michigan.
[24] Receiver reports that there are many other claims pending.
[25] Receiver estimates claimants will receive 10 cents on the dollar.
[26] All claims have been paid and receivership is currently in the process of winding up its affairs according to the Colorado insurance department.

Source: Complied from data furnished by State insurance departments, receivers, and attorneys for receivers. These data may be found in the files of the subcommittee.

TABLE 3.—ANALYSIS OF CLAIMS, BY TYPE, SUBMITTED TO RECEIVERS OF INSOLVENT INSURERS WRITING HIGH-RISK AUTOMOBILE BUSINESS,[1] 1960–65

State of domicile and name of company	Amount of personal injury and property damage claims					Policyholders' claims[3]				
	Filed	Evaluated	Approved	Paid	Unpaid[3]	Filed	Evaluated	Approved	Paid	Unpaid
Pennsylvania:										
Delaware Valley Mutual Casualty Co	$2,859,184	$1,140,000	0	0	$1,140,000					
Commonwealth Mutual Insurance Co	3,742,246	1,500,000	0	0	1,500,000					
Empire Mutual Insurance Co	6,299,076	2,520,000	0	0	2,520,000					
Graphic Arts Mutual Insurance Co	61,852	30,000	0	0	30,000					
Springfield Mutual Insurance Co	29,219	28,000	0	0	28,000					
State Mercantile Mutual Insurance Co		9,500	$9,500	0	9,500					
Missouri:										
Allied Western Mutual Insurance Co		2,000,000	0	0	2,000,000					
Guaranty Insurance Exchange			2,000,000	$83,000	1,917,000		[4] $200,000	0	0	$200,000
Indiana:										
International Auto Insurance Exchange	12,151,776	6,167,842	0	0	6,167,842	$97,907				
United Public Insurance Co	671,140	625,000	0	0	625,000	94,007				
Michigan:										
Preferred Insurance Co	[5] 25,793,000	135,714		0	135,714	[6] 950,000	293,000	$293,000	0	293,000
Exchange Casualty & Surety Co	[7] 25,914,000		2,532,131	0	2,532,131	[8] 764,000		490,000	0	490,000
Michigan Surety Co	(9)		3,816,919	0	3,816,919	[10] 45,500		40,700	0	40,700
Wisconsin:										
Market Mens Mutual Insurance Co	[11] 13,035,000	[11] 2,000,000		0	2,000,000		[12] 100,000		0	100,000
Superior Mutual Insurance Co		[13] 1,770,000		0	1,770,000		[14] 170,000		0	170,000
West Virginia, National Automobile Insurance Co	777,618	(15)			(15)	188,810	(15)			(12)

Texas:										
Career Insurance Co		[16] 870,000			870,000		1,890,000		0	1,890,000
Government Services Insurance Underwriters		442,337	442,337	[17] 442,337			[18] 270,000		0	270,000
Florida, National Home Insurance Co	[19] 7,092,410	[19] 520,000		0	520,000		[20] 110,000		0	110,000
California, All Coverage Insurance Exchange			[21] 908,977					[22] 30,000		
Maryland, National Motors Insurance Co		[23] 258,382	0	0	258,382		[24] 61,899	0	0	61,899
South Dakota, Security General Insurance Co	334,000			0		423,000			0	
South Carolina, First Citizens Fire & Casualty Co	[25] 288,200			0		[26] 155,377			0	
Arkansas, United Automobile Insurance Co	1,657,476	241,988	[27] 241,988		241,988	[28] 140,239	32,154	[29] 32,154		32,154

[1] Insurers have been omitted where data showing type of claim is not available.
[2] Evaluated or approved claims less paid claims to November 1965.
[3] Namely, claims for return premiums, property damage, and out-of-pocket expenses for which reimbursement is sought.
[4] Not included under "Claims—Evaluated by Receiver" in exhibit 2, table II, herein.
[5] Represents 7,000 claims.
[6] 3,800 return premium claims were filed, 3,020 were allowed, and 780 remain open.
[7] 9,900 claims were filed, 5,872 were allowed (3,151 disallowed), and 877 remain open.
[8] 8,000 return premium claims were filed, 6,500 were allowed (1,500 disallowed), and none are cognized as open by the receiver.
[9] 6,700 claims were filed and 4,868 were allowed.
[10] 1,800 return premium claims were filed, and 1,200 were allowed (600 disallowed).
[11] Represents 4,500 claims.
[12] Represents 2,500 return premium claims and 500 trade creditor claims.
[13] Represents 1,950 claims.
[14] Represents 450 return premium claims, and property damage claims.
[15] As of July 1965, 1,876 loss, return premium and miscellaneous claims filed in gross amount of $637,517 were adjusted to $227,334, and recommended to the court for approval.
[16] Represents 650 claims.
[17] Represents 539 claims.
[18] Represents 3,000 claims.
[19] Represents 800 claims.
[20] Represents 1,700 return premium claims.
[21] Represents 1,200 claims.
[22] Represents 500 return premium claims.
[23] Represents 270 claims.
[24] Represents 1,469 return premium claims.
[25] Represents 232 claims.
[26] Represents 5,800 return premium claims, and other policyholder claims.
[27] Does not include $42,510 of approved administrative expenses ($51,178 claimed).
[28] Includes return premium claims of $9,867 and property damage and other policyholders' claims of $130,372.
[29] Includes return premium claims of $3,497 and property damage and other policyholders' claims of $28,657.

Source: Compiled from data furnished by State insurance departments, receivers, and attorney for receivers. These data may be found in the files of the subcommittee.

TABLE 4.—*Summary analysis of aggregate experience of insolvent insurers writing high-risk automobile business, 1960–65*

Number of insolvent insurers	58
Number of States of domicile	21

Number of persons insured at time of receivership related to number of companies involved

Number of persons insured	1,200,842
Number of companies	53

NUMBER OF CLAIMS RELATED TO NUMBER OF COMPANIES INVOLVED

	Number of claims	Number of companies
Filed	171,037	40
Evaluated	69,728	25
Approved	25,775	[1] 11
Paid	3,289	[2] 4

AMOUNT OF CLAIMS RELATED TO NUMBER OF COMPANIES INVOLVED

	Amount of claims	Number of companies
Filed	$284,224,931	33
Evaluated	30,307,563	27
Approved	11,725,234	[1] 12
Paid	525,337	[2] 3

AMOUNT OF PERSONAL INJURY AND PROPERTY DAMAGE CLAIMS RELATED TO NUMBER OF COMPANIES INVOLVED

Filed	$100,706,197	15
Evaluated	20,258,763	17
Approved	9,951,852	[1] 7
Paid	525,337	[2] 3
Unpaid [3]	28,082,476	19

AMOUNT OF POLICYHOLDERS' CLAIMS RELATED TO NUMBER OF COMPANIES INVOLVED

Filed	$2,858,840	9
Evaluated	3,127,053	9
Approved	885,854	[1] 6
Paid	0	[2] 1
Unpaid [3]	3,657,753	11

APPROXIMATE PERCENTAGE OF CLAIMS PAID TO CLAIMS FILED, EVALUATED, AND APPROVED

Number of companies involved	Percent of filed claims	Percent of evaluated claims	Percent of approved claims
34	5		
24		35	
3			26

[1] Includes only those companies for which claims were submitted for court action as of Oct. 31, 1965.
[2] Includes only those companies for which distribution was authorized as of Oct. 31, 1965.
[3] Evaluated or approved claims less paid claims to November 1965.

EXHIBIT II

STATE BOARD OF INSURANCE,
Austin, Tex., March 8, 1966.

As you know, the recent release of the printed volume of the Senate Antitrust and Monopoly Subcommittee, on hearings chaired by Senator Dodd, indicated that 58 "high-risk automobile insurance carriers" had failed from 1960 through 1965.

In an effort to secure some information in connection with the carriers which this report listed as being domiciled in your state, it will be greatly appreciated if you will have someone in your office fill out the total automobile premiums as called for on the attached listing.

If at all possible, we should like for this information to be returned to us by March 21, 1966.

Sincerely yours,

WM. HUNTER MCLEAN, *Chairman.*

Enclosure.

Name of company_____

TOTAL AUTOMOBILE PREMIUMS WRITTEN IN ALL STATES

Year	Bodily iniury	Property damage	Physical damage	Total, automobile
1960	$	$	$	$
1961				
1962				
1963				
1964				
1965				

EXHIBIT III

MEMORANDUM

To: Wm. Hunter McLean, Chairman, Texas State Board of Insurance.
From: Willis A. McVey, Assistant Casualty Actuary.
Subject: Subcommittee on Antitrust and Monopoly—High-Risk Automobile Insurance.
Date: April 4, 1966.

In accordance with your instructions, we mailed a questionnaire to the twenty State Insurance Departments listed in the "Dodd" Report in an effort to secure the automobile premium writings of the "High-Risk Automobile Companies" which failed in those states from 1960 through 1965. The information on the two Texas Companies was readily available in this Department. A total of 58 insolvent companies was involved.

Also, in accordance with your request, we directed another inpuiry to an outside source, the National Bureau of Casualty Underwriters, in an effort to secure the automobile premium writings of these same companies for the purpose of: (1) serving as a double-check on the information secured from the other 20 states and (2) perhaps securing premiums on some of the 58 companies which might not be available in the State Insurance Departments since all these companies are now in receivership.

Overall, the response from the other state departments was extremely good.

From the limited number of states which were unable to provide us with the information requested, we were able, in most instances, to fill in with the information which we secured from the National Bureau of Casualty Underwriters.

The data we received from the other states was on a direct *written* basis, whereas, the premiums we secured from the National Bureau of Casualty Underwriters was on a direct *earned* basis. However, our analysis reveals that this was of no real consequence in collating the statistical data.

The statistical data approximates 100% of the writings.

The consolidated recapitulation of this data was prepared as follows:

Exhibit I contains the premium data, separately, for Automobile Bodily Injury, Automobile Property Damage and Automobile Physical Damage, covering the years 1960–1965 including the data as *actually reported* by the other states and the National Bureau of Casualty Underwriters. In most instances, no premium was reported for the year a particular company became insolvent, since no Annual Statement was filed.

EXHIBIT I[1]

Year	Bodily injury	Property damage	Physical damage	Total automobile
1960	$23,099,615	$12,850,430	$12,429,336	$48,379,381
1961	25,922,996	13,473,140	11,158,049	50,554,185
1962	23,109,004	11,992,911	9,461,325	44,563,240
1963	9,886,162	6,555,028	4,133,719	20,574,909
1964	5,691,593	2,711,582	2,129,837	10,533,012
1965	2,456,862	875,354	910,532	4,242,748
Total	90,166,232	48,458,445	40,222,798	178,847,475

[1] Contains the statistical data as actually reported by the various State insurance departments and the NBCU.

Set out below is a comparison of the total B.I., P.D. and Physical Damage automobile premiums written for the 51 insolvent companies listed above compared with the total automobile premiums written for all companies on a countrywide basis (Fifty States and the Dist. of Columbia), for the years 1960 through 1965:

EXHIBIT II

Year	Total premiums, 51 insolvent companies	Total premiums, countrywide	Ratio col. 2 divided by col. 3 (percent)
(1)	(2)	(3)	(4)
1960	48,379,381	6,168,780,702	0.78
1961	50,554,185	6,342,142,178	.80
1962	44,563,240	6,967,464,065	.64
1963	20,574,909	7,020,076,217	.29
1964	10,533,012	7,582,032,235	.14
1965	4,242,748	[1] 8,000,000,000	.05
Total	178,847,475	42,080,495,399	.43

[1] Estimate based on previous year's experience.

CONCLUSION

The total Automobile premium written by the insolvent companies for 1964 and 1965 is only 1 to 1,055—or for each $1.00 of premium written by the insolvent companies, $1,055.00 in premium was written by all companies.

The ratio of Automobile premium written by the insolvent companies compared with the total Automobile premium written by all companies, on a countrywide basis, ($42,080,495,397 ÷ $178,847,475) is 1 to 235—which means for each $1.00 of premium written by the insolvent companies, $235.00 in premium was written by all companies.

The total Automobile premium written by the insolvent companies compared with the total Automobile premium written by all companies on a countrywide basis, ($178,847,475 ÷ $42,080,495,397) represents only 43 hundreths of 1% of the Nationwide Automobile premium written for the years 1960–1965.

Of the seven companies for which no experience was reported, two of those companies wrote no Automobile insurance; three of them went into receivership in 1960 and one of them went into receivership in 1961; and the remaining company was reinsured. Therefore, the actual reporting of Automobile premium for the insolvent companies approximates 100%.

APPENDIX I

List of insolvent companies whose experience is included in Exhibits I & II and the source from which such experience was obtained:

STATE OF DOMICILE, NAME OF COMPANY

Illinois:[1]

1. Lake States Casualty
2. Bell Mutual Insurance Company
3. Banner Mutual Insurance Company
4. Bedford Mutual Insurance Company
5. Whitehall Mutual Insurance Company

6. Multistate Interinsurance Exchange
7. Oxford General Casualty Mutual Ins. Co.
8. Cosmopolitan Insurance Company
9. Adams Mutual Insurance Company
10. General Union Mutual Insurance Company
11. Central Casualty Company

Pennsylvania: [2]

12. Lawn Mutual Insurance Company
13. Delaware Valley Mutual Casualty Company
14. Commonwealth Mutual Insurance Co.
15. Empire Mutual Insurance Company
16. Graphic Arts Mutual Insurance Company
17. Springfield Mutual Insurance Company

Missouri: [1]

18. Midwest Mutual Casualty Insurance Company
19. Surety Insurance Exchange
20. Allied Western Mutual Insurance Company
21. American Midwest Mutual Insurance Company
22. Guaranty Insurance Exchange

Indiana: [1]

23. International Automobile Insurance Exchange
24. Insurance Corporation of America
25. Universal Automobile Insurance Company
26. United Mutual Insurance Company
27. United Public Insurance Company

Michigan: [1]

28. Preferred Insurance Company
29. Exchange Casualty and Surety Company
30. Michigan Surety Company

Wisconsin: [2]

31. Market Mens Mutual Insurance Company
32. Superior Mutual Insurance Company

West Virginia: [1]
33. Crown Insurance Company
Texas: [1]
34. Career Insurance Company
35. Government Services Insurance Underwriters
Florida: [1]
36. National Home Insurance Company
37. Equity General Insurance Company
California: [2]
38. Cosmopolitan Insurance Exchange
39. All Coverage Insurance Exchange
Maryland: [1]
40. Chesapeake Insurance Company
41. National Motors Insurance Company
Maine: [1]
42. Washington Insurance Company
43. Washington Mutual Insurance Company
Tennessee: [2] 44. Monticello Insurance Company
South Dakota: [1] 45. Security General Insurance Company
South Carolina: [1] 46. First Citizens Fire and Casualty Company
Minnesota: [1] 47. American Allied Insurance Company
Massachusetts: [1] 48. Suffolk Insurance Company
Colorado: [2] 49. Western Standard Indemnity Company
Arkansas: [1] 50. United Automobile Insurance Company
Nebraska: [1] 51. United Benefit Fire Insurance Company

---

[1] Experience for the insolvent companies listed for these states was obtained directly from the records available in those State Departments or the Receiver.
[2] Experience for the insolvent companies listed for these states was obtained from the National Bureau of Casualty Underwriters.

APPENDIX II

List of insolvent companies whose experience was not available, either from the state of domicile, or from the National Bureau of Casualty Underwriters:

STATE OF DOMICILE, NAME OF COMPANY

Illinois:
1. Bell Casualty Insurance Company (no Automobile business written)
2. Monroe Mutual Insurance Company
3. American Bowlers Mutual Casualty Co. (Wrote Workmen's Compensation only)

Pennsylvania: 4. State Mercantile Mutual Insurance Company
Missouri: 5. Missouri Union Insurance Company
West Virginia: 6. National Automobile Insurance Company
Delaware: 7. National Automobile Insurance Company

EXHIBIT IV

STATE BOARD OF INSURANCE, *Austin, Tex., May 2, 1966.*

To the insurance departments listed below:

Arkansas	Michigan
California	Minnesota
Colorado	Missouri
Delaware	Nebraska
Florida	Pennsylvania
Illinois	South Carolina
Indiana	South Dakota
Maine	Tennessee
Maryland	West Virginia
Massachusetts	Wisconsin

Enclosed is a copy of a memorandum that summarizes some statistics on "high-risk automobile companies," the subject of our request of your Department a few weeks ago.

Although the data is from 51 companies, out of 58 companies involved, Page 3 of the memorandum shows that figures from the seven remaining companies would have been of little consequence.

Failures of such companies in the calendar years of 1964 and 1965 have been the subject of comparison with bank failures in the same years. The 31 insurance companies failing had premium income of $14,775,000 in that two year period, an average of less than $7,500,000 annually. By comparison, total countrywide automobile premiums for the two years were $15,582,000,000, an average of $7,791,000,000 annually.

It has been pointed out that the premiums of the insolvent companies in the years 1964 and 1965 do not include the premiums of sick companies which might fail in subsequent years. However, the premium volume of insolvent companies in the six year period averaged about $30 million annually, an amount that would hardly justify a federal agency requiring annual salaries of that amount or more and, in addition, guaranty insurance deposits plus substantial administrative expenses of the companies involved at the expense of policyholders.

We also emphasize that the exhibit of premiums of insolvent insurers does not include all of the premiums *in the year of insolvency* of the particular companies. These figures were not readily available. An attempt was made to develop such premiums by interpolation but the results were wholly unreliable because many of the companies had rapidly declining premium income, some even developed minus figures, due to wholesale cancellations of policies by insureds and agents in the last months of the companies' existence.

This data is not supplied for the purpose of publication or other use where the results might be quoted without proper qualification.

We appreciate your cooperation which made possible this study.

Yours truly,

WM. HUNTER MCLEAN, *Chairman.*

EXHIBIT V

Attached you will find form(s) bearing the name(s) of insurance companies domiciled in your State which became insolvent in 1960–1965. These are the companies which the "Dodd Report" indicated were "high-risk automobile insurance carriers."

We are desirous of securing the information called for on these forms from the Receiver at your earliest convenience. If possible, a personal visit with the Receiver would be helpful in securing this information.

In order to aid you and the Receiver, the following explanation of the information requested in the forms may be helpful:

Line 1 of the form asks for the Receiver's estimate of the *total* Automobile (Bodily Injury, Property Damage and Physical Damage) incurred claims liability of the Receivership estate. This information should be given as of the *present* date (if the receivership has not been closed) or as of the date of closure of the Receivership.

Line 2. Receiver's estimates of amounts *paid* and *to be paid* on total Automobile Bodily Injury, Property Damage and Physical Damage claims. We realize actual amounts called for under Line 2(b) may be difficult to obtain. Projected or estimated amounts will be satisfactory if the actual amounts are not available.

Line 3. Loss to Claimants. This is merely Line 1 minus Line 2.

Line 4. Amount of estimated Automobile Bodily Injury claim liability *under* $100. This would require a total of all Automobile Bodily Injury claims *under* $100. For instance, if a claim for Bodily Injury amounted to $75 then $75 would be tabulated. If a Bodily Injury claim amounted to $500, then only $100 would be tabulated. In other words, each Bodily Injury claim amounting to $100 or less would be included for the full amount of each claim, whereas, each Bodily Injury claim amounting to over $100 would be included at $100.

Line 5. Amount of estimated Automobile Property Damage and Physical Damage claim *under* $300. We are seeking here the same information as outlined under Line 4, except the breaking point is $300. Each Property Damage or Physical Damage claim under $300 would be included at its assessed value and those exceeding $300 would be included at $300.

In order that you may understand the reason for requesting the information under Lines 4 and 5, there is quoted below Sec. 205, Federal Motor Vehicle Insurance Guaranty Act.

PAYMENT OF GUARANTY

"Sec. 205. In the event an insurer or other entity the motor vehicle insurance policies of which are guaranteed under this title is determined by a court of competent jurisdiction to be insolvent, the Corporation shall assume the obligation of the insurer or other entity under any policy guaranteed by it, if a claim based on such policy is then pending against the insurer or other entity, or is thereafter made against the insurer or other entity while it is in liquidation or receivership. Upon the assumption of the obligation of any insurer or other entity with respect to any claim, the Corporation is authorized to investigate, adjust, compromise, or settle such claim up to the limit of liability provided in the applicable policy: *Provided*, That no injured party claim in the amount of $100 or less and no policy holder claim in the amount of $300 or less shall be paid by the Corporation. With respect to any injured party claim, the Corporation shall pay only that portion of the claim which is in excess of $100, and the Corporation shall pay only that portion of any policy holders claim which is in excess of $300. Upon the payment of any claim, the Corporation shall succeed to the rights of the policyholder or assured, to the extent of such payment, for purposes of asserting any rights of such policyholder or assured against an insurer or other entity."

It is extremely important that this information be secured as soon as possible. Please return the completed forms directly to me.

Very truly yours,

MAURICE G. HERNDON,
Federal Liaison.

Enclosure

Date_____

Name of Company_____
State of Domicile_____
Date or Receivership_____

AUTOMOBILE LOSS CLAIMS—AT PRESENT OR AT TIME OF CLOSURE OF RECEIVERSHIP

(Do not include unearned premium claims nor other types of claims)

1. Receiver's estimate of total Auto. incurred claims liability of Receivership estate ..... $.....
2. Receiver's estimate of:
   (a) Amounts *paid* on total Auto. claims $.....
   (b) Amounts *to be paid* on total Auto claims $..... $.....
3. Loss to Claimants as result of Insolvency (Line 1–Line 2) ..... $.....
4. Amount of estimated Automobile Bodily Injury claims liability *under* $100 ..... $.....
5. Amount of estimated Auto. Property Damage and Physical Damage claim liability under $300 ..... $.....

Above information *supplied* by: Above information compiled by:

Name Name

Title Title

Address Address

When completed, please return this form to: Maurice G. Herndon, Federal Liaison, National Association of Insurance Agents, Suite 801, Warner Building, 13th & E, N.W., Washington 4, D.C.

EXHIBIT VI

COMPARATIVE SURVEY BODILY INJURY AND PROPERTY DAMAGE CLAIMS—EXHIBIT 3, TABLE 3, SENATE HEARING (DODD) REPORT PT. 12, JANUARY 1966 VERSUS RECEIVER SURVEY, SPRING 1967

State of domicile	Name of company	Claims from Senate report[2]	Estimated claimant loss, 1967 survey[3]
Pennsylvania	Delaware Valley Mutual Casualty Co	$2,859,184	$1,140,000
	Commonwealth Mutual Insurance Co	3,742,246	750,000
	Empire Mutual Insurance Co	6,299,076	500,000
	Graphic Arts Mutual Insurance Co	61,852	160,008
	Springfield Mutual Insurance Co	29,219	25,200
	State Mercantile Mutual Insurance Co	9,500	9,620
Missouri	Allied Western Mutual Insurance Co	[4]	[4]
	Guaranty Insurance Exchange	[4]	[4]
Indiana	International Auto Insurance Exchange	12,151,776	834,000
	United Public Insurance Co	671,140	733,500
Michigan	Preferred Insurance Co	25,793,000	2,200,000
	Exchange Casualty & Surety Co	25,914,000	3,200,000
	Michigan Surety Co	3,816,919	3,127,002
Wisconsin	Market Mens Mutual Insurance Co	13,035,000	1,073,000
	Superior Mutual Insurance Co	1,770,000	528,000
West Virginia	National Automobile Insurance Co	777,618	0
Texas	Career Insurance Co	870,000	156,609
	Government Services Insurance Underwriters	442,337	0
Florida	National Home Insurance Co	7,092,410	617,868
California	All Coverage Insurance Exchange	908,977	0
Maryland	National Motors Insurance Co	258,382	900,000
South Dakota	Security General Insurance Co	334,000	187,427
South Carolina		[5]	[5]
Arkansas		[5]	[5]
Total		106,836,636	16,162,232

[1] Survey forms distributed to receivers by State headquarters of National Association of Insurance Agents and collected by its national headquarters. Amounts assembled for this comparison by Texas Insurance Department.

[2] Amounts are "filed claims" or "evaluated claims" or "approved claims," in that order of availability, from exhibit 3, table 3, of Senate hearing report.

[3] Amounts are totals of claims, less (1) receivership payments to date and (2) conservative receiver estimates of future payments. Where receivers declined to estimate future payments, gross amount of claims has been included. These amounts are regarded as extremely conservative.

[4] Missouri receivers replied that a classification of claims as between automobile and others had not been maintained and could not be obtained at this time without some burden of expense.

[5] Survey forms not completed.

Note: (a) The details relating to some of the individual companies have been supplied on a confidential basis and this confidence should be honored. Release of the company detail could adversely affect the receivership estates. (b) The totals in this report are not confidential nor privileged and such totals may be used.

Comment: The $106,836,636 of claims is from a total of $112,782,312 calculated from exhibit 3, table 3, of the Senate report on the basis used in this comparison, a representative 95 percent of the report total. The conservatively estimated $16,162,232 of ultimate loss to claimants represents 15 percent of unpaid claims as contained in the Senate report.

EXHIBIT VI A

TOTAL AUTO PREMIUM AND CLAIMANT LOSS, FROM 17 COMPANIES OUT OF "DODD" REPORT, (EXHIBIT 3, TABLE 3)

State of domicile	Name of company	Total auto premium (1960–65)	Claimant loss
Pennsylvania	Delaware Valley Mutual Casualty Co	$2,442,771	$1,140,000
	Commonwealth Mutual Insurance Co	2,636,865	750,000
	Empire Mutual Insurance Co	1,700,969	500,000
	Graphic Arts Mutual Insurance Co	2,157,094	160,008
	Springfield Mutual Insurance Co	72,378	25,200
Indiana	International Auto Insurance Exchange	14,091,893	834,000
	United Public Insurance Co	2,101,095	733,500
Michigan	Preferred Insurance Co	17,870,696	2,200,000
	Exchange Casualty & Surety Co	7,554,479	3,220,000
	Michigan Surety Co	−(38,134)	3,127,000
Wisconsin	Market Mens Mutual Insurance Co	8,712,351	1,073,000
	Superior Mutual Insurance Co	2,587,450	528,000
Texas	Career Insurance Co	139,980	156,609
	Government Services Insurance Underwriters	2,703,294	0
California	All Coverage Insurance Exchange	4,176,613	0
Maryland	National Motors Insurance Co	1,809,949	900,000
South Dakota	Security General Insurance	2,226,632	187,427
Total		72,942,375	15,534,744

EXHIBIT VII

STATE BOARD OF INSURANCE,
Austin, Tex.

You will recall in 1967 that a "Loss To Claimants" survey was made for the fifty-eight insolvent automobile-writing companies listed in the "Dodd Report" as high-risk automobile insurance carriers, covering the years 1960–1965.

The more recent "Hart Committee" has expanded the original fifty-eight company listing to eighty-eight companies, covering insolvencies between 1958–1968. They have lumped eleven years of premium writings of these companies to inflate the total in an attempt to document their proposal for a Federal Guaranty Fund, as reflected in an exhibit furnished to us by Robert E. Dineen, Consultant to N.A.I.C.

We urgently need your cooperation in helping us to secure the "Loss To Claimants" for those additional companies in your State in order that the Hart Committee may be provided with actual loss information rather than the misleading premium writings of these companies for eleven years.

Attached you will find form(s) bearing the name(s) of these additional companies domiciled in your State which became insolvent.

We are desirous of having these forms returned to us no later than May 15, 1969, either from you, your staff or the Receiver in your State.

In order to aid you and the Receiver, the following explanation of the information requested in the form may be helpful:

Line 1 of the form asks for the Receiver's estimate of the *total* Automobile (Bodily Injury, Property Damage and Physical Damage) incurred claims liability of the Receivership estate. This information should be given as of the *present* date (if the Receivership has not been closed) or as of the date of closure of the Receivership.

Line 2 Receiver's estimates of amounts *paid* and *to be paid* on total Automobile Bodily Injury, Property Damage and Physical Damage claims. We realize actual amounts called for under Line 2(b) may be difficult to obtain. Projected or estimated amounts will be satisfactory if the actual amounts are not available.

Line 3 Loss to Claimants. This is merely Line 1 minus Line 2.

Yours, very truly,

NED PRICE, *President, N.A.I.C.*

Date_____

Name of Company_____
State of Domicile_____
Date of Receivership_____

AUTOMOBILE LOSS CLAIMS— AT PRESENT OR AT TIME OF CLOSURE OF RECEIVERSHIP

(Include total auto liability and physical damage—do not include unearned premium claims nor other types of claims)

1. Receiver's estimate of total Auto. incurred claims liability of Receivership estate _____ $_____
2. Receiver's estimate of:
   (a) Amounts *paid* on total Auto. claims $_____
   (b) Amounts *to be paid* on total Auto claims $_____ $_____
3. Loss to Claimants as result of Insolvency (Line 1–Line 2) ____ $_____

Above information compiled by:

_____
Name

_____
Title

_____
Address

Note: Please return this form, by May 15, 1969 to: Ned Price, President, N.A.I.C., State Board of Insurance, 1110 San Jacinto, Austin, Tex. 78701.

EXHIBIT VII

AUTOMOBILE INSURANCE PREMIUM WRITINGS OF FIRE AND CASUALTY COMPANIES THAT FAILED, 1958–68

[Hart staff exhibit]

Home State [1] and companies	Years	Auto premiums written [2]
Pennsylvania:		
Home Mutual Casualty	1961–67	$2,658,000
Bankers & Telephone	1961–66	8,207,068
Sylvania Mutual	1964	200,000
Bankers Allied Mutual	1961–67	27,915,000
National Commercial		[3]
Municipal Mutual		[3]
Scandia Mutual		[3]
Palmyra General	1962–65	3,121,000
Tri-State Mutual	1962–65	592,000
Wissahickon Mutual	1963–65	1,049,000
Wilton Mutual		[3]
Reliable Mutual	1962–65	604,000
Lawn Mutual	1960–64	16,509,400
Delaware Valley Mutual	1960–64	2,442,771
Commonwealth Mutual	1957–63	5,616,865
Empire Mutual	1959–63	4,228,212
Graphic Arts Mutual	1959–62	2,717,111
Springfield Mutual	1960–62	72,378
State Mercantile Mutual		[3]
Total (14 companies)		75,932,805
Illinois:		
Progressive General	1961–67	12,990,000
Trans-World Mutual		[3]
Highway	1960–66	11,415,730
St. Lawrence	1960–66	14,154,395
Mercury Mutual	1960–65	1,316,990
Lincoln Casualty	1959–65	8,947,685
Lake States Exchange	1961–65	4,354,370
Bell Mutual	1961–65	2,976,349
Bell Casualty		[3]
Banner Mutual	1959–65	20,630,918
Bedford Mutual	1963–65	75,425
Whitehall Mutual	1961–64	503,873
Monroe Mutual		[3]
Multi-State Interinsurance Exchange	1958–64	7,299,099
Oxford General Casualty Mutual	1961–64	2,090,042
Cosmopolitan	1958–63	18,361,777
Adams Mutual	1959–63	2,010,627
General Union Mutual	1959–62	179,242
Central Casualty	1956–61	3,871,860
Mid-Union Indemnity	1956–59	6,362,916
Total (17 companies)		117,541,298
Missouri:		
Central Mutual	1960–66	8,772,000
Midwest Mutual	1961–65	3,004,252
Surety Insurance Exchange	1960–65	904,379
Allied Western Mutual	1959–65	5,844,512
American Midwest Mutual	1962–64	1,835,836
Guaranty InsuranceExchange	1961–63	2,322,282
Missouri Union	1955–59	2,502,000
Independence		[3]
Eagle Exchange	1954–56	741,000
Total (8 companies)		25,926,261
Arkansas:		
Independent Casualty		[3]
North American Guaranty	1963–67	14,525,316
Republic Casualty	1963–67	2,643,721
Mid-South	1961–65	2,117,434
Homestead Fire & Casualty		[3]
People's Indemnity		[3]
Royal Standard	1959–65	1,590,814
United Auto	1960–63	1,359,133
National Auto	1958–60	46,679
Total (6 companies)		22,283,097
Texas:		
American Insurors		[3]
Great American County Mutual		[3]
Career	1960–65	139,980
Government Service Exchange	1958–64	4,368,045
Lumbermans Insurance		[3]
Franklin American	1956–58	1,480,000
Highway Exchange	1952–57	8,445,000
Total (4 companies)		14,433,025
Indiana:		
United Public	[4] 1957–62	11,452,576
International Auto Exchange	1958–64	17,611,893
Insurance Corp. of America	1956–62	656,323
Universal Auto	1959–63	7,004,197
United Mutual	1957–63	2,188,123
Old Line Auto	1955–61	2,499,833
Total (6 companies)		41,412,945

AUTOMOBILE INSURANCE PREMIUM WRITINGS OF FIRE AND CASUALTY COMPANIES THAT FAILED, 1958–68—Continued

Home State [1] and companies	Years	Auto premiums written [2]
Maryland:		
National Guild	1963–65	2,691,000
Olympic		[3]
Chesapeake	1961–66	7,672,284
National Motors	1963	1,805,949
Total (3 companies)		12,169,233
California:		
Consumers & Distributors Insurance Exchange	1958–64	2,231,000
Tower Indemnity Co		[3]
All Coverage Exchange	1959–63	4,324,897
Interstate Indemnity	1952–58	13,019,000
Total (3 companies)		19,574,897
Michigan:		
Preferred	1957–63	32,027,696
Exchange Casualty	1957–63	15,132,813
Michigan Surety	1956–59	6,362,916
Total (3 companies)		53,523,425
Wisconsin:		
Market Mens Mutual	1956–62	25,008,351
Shawano Mutual		[3]
Superior Mutual	1955–61	10,379,450
Total (2 companies)		35,387,801
West Virginia:		
North Central	1964	1,125,000
Crown	1958–64	2,677,825
National Auto	1959	95,726
Total (3 companies)		3,898,551
Florida:		
Florida Insurance Exchange	1963–66	4,257,000
National Home	1960–63	2,228,847
Equity General	1958–61	3,274,333
Total (3 companies)		9,760,180
Minnesota:		
United States Mutual		[3]
American Allied	1963–66	3,408,910
Total (1 company)		3,408,910
Delaware:		
American Military International [5]	1959–62	7,147,047
National Auto	1956–60	4,648,740
Total (2 companies)		11,795,787
Nebraska:		
United Benefit	1960–66	11,143,167
Surety National	1956–60	2,622,000
Total (2 companies)		13,665,167
Tennessee:		
National Service	1964–68	24,840,613
Monticello	1958–63	1,297,372
Total (2 companies)		26,137,985
Colorado:		
Western Standard	1955–61	941,938
Mountain Standard	[6] 1954–59	914,000
Total (2 companies)		1,855,938
Louisiana:		
Marquette	1958–64	7,830,090
Delta Fire & Casualty	1953–59	2,429,000
Total (2 companies)		10,259,090
New York: Manhattan Casualty		[7]
Nevada: Great Basin	1961–67	7,766,100
Massachusetts: Suffolk	1962–64	1,506,169
Maine: Washington	1962–66	915,436
New Hampshire: Sutton Mutual		[3]
South Carolina: First Citizens	1960–64	3,830,882
South Dakota: Security General	1958–64	4,420,632
Grand total (88 companies)		517,415,624

[1] Not all premiums written in home State necessarily.
[2] Direct gross. Earned, instead of written, premiums are used in some instances.
[3] Not available.
[4] Placed in conservatorship in 1962, and in liquidation in 1965.
[5] Wrote mainly American servicemen in Europe.
[6] Not available for 1957.
[7] New York has an insolvency fund which pays automobile bodily injury and property damage claimants. Company wrote no auto physical damage coverages.

Sources: State insurance departments; annual statements; Bests reports.

EXHIBIT IX

1969 TEXAS SURVEY—AVERAGE ANNUAL PREMIUMS AND LOSSES COVERING COMPANY INSOLVENCIES 1966, 1967, AND 1968

Home State and companies	Years	Average annual premium	Average annual claimant loss
Pennsylvania:			
Home Mutual Casualty	1961–67	$379,714	[1] $79,740
Bankers & Telephone	1961–66	1,367,845	[1] 287,247
Bankers Allied Mutual	1961–67	3,987,857	[1] 837,450
Illinois:			
Progressive General	1961–67	1,855,714	0
Highway	1960–66	1,630,819	1,066,667
St. Lawrence	1960–66	2,022,056	600,000
Missouri: Central Mutual	1960–67	1,253,143	[1] 263,160
Arkansas:			
North American Guaranty	1963–67	2,905,063	483,333
Republic Casualty Co	1963–67	528,744	638,333
Florida: Florida Insurance Exchange	1963–66	1,064,250	500,000
Nebraska: United Benefit	1960–66	1,591,881	[1] 334,295
Tennessee: National Service	1964–68	4,968,123	0
Nevada: Great Basin	1961–67	1,109,443	68,978
Minnesota: American Allied	1963–66	852,228	[1] 178,968

[1] These claimant losses arrived at by applying factor of 21 percent to average annual premiums for these companies. (The companies for which both premiums and losses were secured produced a ratio of 21 percent.)

1968 ratio of loss adjustment expense to net earned premiums (based on 20 largest stock companies)

	(Percent)
Fire	3.7
Extended coverage	6.8
Homeowners multiple peril	7.0
Commercial multiple peril	5.7
Ocean marine	5.9
Inland marine	5.3
Workmen's compensation	7.5
Bodily injury liability other than auto	22.5
Auto bodily injury liability	12.6
Auto property damage liability	10.9
Auto collision	7.9
Auto fire, theft, comprehensive	5.6
Property damage liability other than auto	14.9
Fidelity	9.1
Surety	5.5
Glass	8.4
Burglary and theft	9.9
Boiler and machinery (10 cos.)	1.3

Source: 1968 Loss and Expense Ratios (N.Y. Insurance Department).

JANUARY 13, 1970.

To: Lorne R. Worthington, Chairman NAIC Executive Committee.
From: John E. Bailey, F.S.A.
Subject: Claimant Losses from Automobile Insurance Company Insolvencies.

After examining the material which you made available to me and the methods used for determining average annual claimant losses from auto insurance company insolvencies, I find that $6 million is a reasonable estimate of this figure. Since I used only the data contained in the reports which you provided, this estimate necessarily depends upon the accuracy and completeness of that data. For example, it is not clear whether or not unearned premiums and assessable losses are included in the data. If not, these items must be added to the $6 million figure. This figure is a rough estimate of the annual claimant loss over the entire period 1960–1968 and I found no particular evidence that the annual loss was either increasing or decreasing over the period. This is largely due to the fact that the data was not broken down by year of failure and that only totals for longer periods were available.

The above estimate will be supported by considering the calculations made by the Texas State Board of Insurance and the testimony of Mr. Lin Sutcliffe, Counsel for the Magnuson Committee.

TEXAS BOARD OF INSURANCE FIGURES

The Texas Board of Insurance made estimates of claimant losses for two different periods as explained in the June 10, 1969 file memorandum of Mr. Willis A. McVey. The basic data for these estimates are contained in the exhibits labelled VI A and IX. Exhibit VI A relates to the earlier Dodd marterial and applies to failures in the period 1960 through 1965, while exhibit IX is strictly Texas material covering failures over the period 1966 through 1968. *Apparently* the same methods are used in these two exhibits, but closer examination shows that not to be the case. The general procedure is to divide the total in the "claimant loss" column by the total in the premium column to obtain a loss-to-premium ratio which is then applied to the appropriate premium data to obtain a total loss figure. This calculation is not strictly comparable for the two exhibits because periods of different length are involved, and one exhibit uses totals while the other uses averages.

The 1966–1968 exhibit is the more accurate of the two. It uses *average* annual claimant losses over the period under study—1966 to 1968. This means that in each case the total losses experienced were divided by the length of the study period—three years. The premiums are also averages, using the period for which they were available on a company-by-company basis. Theoretically, it would be preferable to use the same number of years prior to failure for each of the companies, but this is a minor criticism. The loss-to-premium ratio which results (21.0%) represents the average annual claimant loss over the period 1966–1968 as a percentage of average annual premium. It is easy to see that the nation-wide annual claimant loss can be estimated by multiplying this ratio by the total average annual premium of all companies which failed in 1966–1968. Texas determined this total annual premium to be $25,516,880 and 21.0% of that amount is $5,338,171, their estimate of the average annual claimant loss. I concur in this calculation. Of course, there can always be a bias introduced by estimating the losses for so large a percentage of the companies, but this factor cannot be controlled. The rate of 49 cents per $1,000 of automobile premiums is also correct.

Exhibit VI A is not as theoretically correct, however. It relates the total claimant losses over the period 1960–1965 to the total premiums over the same period. Obviously, such a ratio is dependent upon the length of the period chosen. The longer the period is, the larger the premium total will be and the lower the ratio will be. This factor is largely offset by multiplying the resulting loss-to-premium ratio by the premiums over the entire period to estimate total losses. Note, however, that some failures occur early in the study period and have premiums for only one or two years in the total, while other failures occur later in the period and contribute for a number of years to the total premium figure. The longer the period, the more relative effect these late failures have. It may be concluded that the estimate of average annual claimant losses is affected both by the length of the period selected and by the distribution of failures throughout the period (early or late).

In Appendix A I have attempted to offset these factors by redoing Exhibit VI A using average annual premium and average annual claimant losses. The average annual premiums were taken from the exhibit of premiums for 88 companies which failed in 1958–1968 prepared for the Senate Committee. Average annual losses were determined by dividing the total losses in exhibit VI A by 6. The result is an average annual claimant loss of $2,589,158, and average annual premiums of $23,961,630. This produces a loss-to-premium ratio of 10.8 percent.

Appendix B shows the total average annual premium for 49 of the 51 companies used in the 1967 Texas report to be $49,948,597. Assuming the other two (Cosmopolitan Insurance Exchange of California and Washington Mutual Insurance Company of Maine) to be proportional, the total average annual premium for these 51 companies was $51,987,315 applying the 10.8% ratio determined above, an average annual loss of $5,614,630 is obtained. This is relatively close to the $6,348,250 calculated by Texas for the same period. Both estimates exclude the seven companies for which no data was available.

A few additional comments about the Texas data are in order. While they illustrate a decrease in annual claimant loss from $6,348,250 in 1960–1965 to $5,338,171 in 1966–1968, my analysis shows a more level pattern—$5,614,630 in 1960–1965 and $5,338,171 in 1966–1968. Considering the increasing volume of total auto premiums, however, the loss per $1,000 of total premium appears to be trending down. The methods of collecting statistics by the Texas Department appear to be very good.

Under this heading, two major items will be considered. First is the exhibit showing automobile premiums for companies which failed in 1958–1968. Then the testimony by Mr. Lin Sutcliffe, Counsel for the Magnuson Committee will be analyzed.

Automobile Insurance Premium Writings of Fire and Casualty Companies That Failed 1958–1968

The exhibit with this title is attributed to the Senate Antitrust and Monopoly Subcommittee by Mr. Sutcliffe. Since the details of the methods used in obtaining the figures are not presently available, no assessment of their reliability can be made. However, it is clear that their manner of use is misleading. A varying number of years' results are included for the various companies (seven years worth of premiums are included for Company A, three years for Company B and so on). This might be excused if the premiums included started with the common year, but they don't. Under these circumstances, the individual entries retain their meaning, but the total has no meaning. What does the total represent? The heading of the table indicates that these were companies which failed in the period 1958–1968, but says nothing about the period over which the premiums are accumulated. This is a good heading (although a little misleading if not read carefully) because there *is* no such period. Mr. Sutcliffe, in his testimony, implies that these are premiums for the period 1958–1968, but that is obviously incorrect as may be seen from the very first entry (years 1961–1967).

Attached is Appendix C showing the average annual premium for each of these companies. These averages were necessarily calculated over the period for which the data was given for each company. The total of these averages is $90,595,982 and this may be called the composite average annual auto insurance premium for 88 companies which failed in the period 1958–1968. This average is determined over periods of varying length, but each component *is* an average annual premium.

It is possible to estimate the average annual claimant loss over the period 1958–1968 by using the 10.8% loss-to-premium ratio developed above for 17 of these companies. Since the ratio is based on failures over a six-year period, the $90,595,982 must be multiplied by 6/11 to obtain a comparable premium figure. The resulting premiums are $49,416,600. Application of the 10.8% ratio to this amount results in an average annual claimant loss of $5,336,928, very close to the figure determined above using the Texas data.

Sutcliffe Comments

I do not understand the manner in which Mr. Sutcliffe uses his data and the inferences he draws to support an average annual loss figure of $20 million. Since he requested the NAIC to react to his remarks, I will conclude by commenting on them.

Page 327. Lines 19–20 "Mr. Sutcliffe: it is an assumption that the claimant loss, whatever that is, equals 21% of premiums written." *Comment*: strictly speaking, the 21% figure *is* an assumption as it applies to the companies for which loss figures were not available. But it is based upon the overall loss-to-premium ratio of those companies for which both premium loss information was available and thus was the best (and only practical) method of estimating the losses for those companies for which this information was not directly available. Unquestionably, if properly used, such a procedure provides results accurate enough for the present purposes in the absence of any knowledge that the loss-to-premium ratio of any of the remaining companies will differ markedly from that of the companies for which data is available.

Page 327, Lines 21–24 "Mr. Sutcliffe: Now the figure for total claimant loss compiled by the Senate Antitrust and Monopoly Subcommittee for 88 automobile insurance insolvencies amounts to $517 million. That is for a ten-year period." *Comment:* the $517 million is a *premium* figure, not a loss figure. The auto premiums included in that total are for a variety of different periods, some of which do not even fall between the years 1958–1968 inclusive (which incidentally is an 11 rather than a 10 year period). Thus any figures derived from this $517 million amount are meaningless and need not be considered further. My analysis in the preceding section illustrates the appropriate use of this data. In my opinion Mr. Sutcliffe's development of $10.8 million figure has no foundation.

Page 328, Line 5 "Mr. Sutcliffe: The figures include only 88 of 109 insolvencies." *Comment*: this is a valid point. Assuming the companies to be of the same average size, a matter of conjecture, the earlier figures could be increased 24% to account for these other companies.

Further Comment Mr. Sutcliffe referred to a $111.1 million as being in the NAIC staff study which was submitted to the Commerce Committee as a part of the Report of the Special Committee on Automobile Insurance problems. The $111.1 million does not appear in that study. Upon checking, however, I ascertained that this was not an unearned premium figure as Mr. Sutcliffe had thought, but rather it was a rough preliminary premium figure developed in an early working draft of the staff study. I am told that it represented an effort to convert the $517 million premium figure into an average annual premium. The figure was not used after the more comprehensive and detailed Texas figures became available. Thus Mr. Sutcliffe's point as to this item no longer seems relevant since the figure was never intended to represent an unearned premium figure.

I believe that the 6 million dollar figure developed in the NAIC study does not include unearned premiums. In order to estimate the magnitude of losses attributable to this factor, we can use the figure of $90,595,932 derived from the Senate data as the average annual premium of companies failing within the 11 year period 1958–1968. Obviously, the average premium figure for companies failing in one average year would be 1/11 of this or $8,235,998. For successful companies unearned premiums represent roughly ⅓ to ½ of annual premium writings. Using the higher figure, the estimate of average annual losses, due to unearned premium forfeiture, would be $4,118,000. This is a conservative estimate. Unearned premiums vary from company to company depending upon such facts as whether the business is written on an annual, semiannual, or monthly basis, on whether premiums are financed or paid in installments, etc. Furthermore, when a company is "on the skids" the picture is still different. Many agents do not renew policies or they withhold the premium from the company. Many policyholders cancel and some do not pay their premium. Thus in practical effect the average annual unearned premium used above in estimating unearned premium losses would very likely be substantially reduced. It might be more accurate to say that the estimate of losses due to unearned premiums would be closer to an average of $2 million per year.

I have no figures with respect to amount lost to policyholders resulting from the collection of assessments on assessible policies. However, most mutual companies are no longer on the assessible basis. Furthermore, the amount that a liquidator recoups through this mechanism is quite nominal.

CONCLUSION

Based upon the discussion above it seems that the total average annual losses (including unearned premium) is in the neighborhood of $7.5 million per year. To put this figure into perspective, it is worth noting that the estimated premium for automobile insurance in 1969 is in excess of $11 billion. In other words the losses due to insolvencies represents 68 cents per $1,000 of premium or less than 7/1000 of 1% of the total business written. Based upon an insured automobile population of 89 millions cars, the cost would be less than 9 cents per car.

APPENDIX A

AVERAGE ANNUAL PREMIUM AND CLAIMANT LOSS—17 COMPANIES OUT OF DODD REPORT

Home State and company	Average annual premium	Average annual claimant loss, 1960–65
Pennsylvania:		
Delaware Valley Mutual Casualty Co	$448,554	$190,000
Commonwealth Mutual	802,409	125,000
Empire Mutual	845,642	83,335
Graphic Arts Mutual Insurance Co	679,279	26,670
Springfield Mutual Insurance Co	24,126	4,200
Indiana:		
International Auto Insurance Exchange	2,515,985	139,000
United Public Insurance Co	1,272,508	122,250
Michigan:		
Preferred Insurance Co	4,575,385	366,674
Exchange Casualty and Surety Co	2,161,830	536,677
Michigan Surety Co	1,590,729	521,177
Wisconsin:		
Market Mens Mutual Insurance Co	3,572,622	178,837
Superior Mutual Insurance Co	1,482,779	88,000
Texas:		
Career Insurance Co	23,330	26,100
Government Services Insurance Underwriters	624,006	0
California: All Coverage Insurance Exchange	864,979	0
Maryland: National Motors Insurance Co	1,805,949	150,000
South Dakota: Security General Insurance Co	631,519	31,238
Total	23,961,630	2,589,158

Note: Ratio of losses to premiums 10.8 percent.

APPENDIX B

AVERAGE ANNUAL AUTOMOBILE INSURANCE PREMIUMS, 51 COMPANIES OF 1967 TEXAS SURVEY

State	Companies	Average annual premium
Pennsylvania	6	$6,141,889
Illinois	11	10,282,309
Missouri	5	2,972,549
Arkansas	1	339,783
Texas	2	647,336
Indiana	5	5,595,681
Maryland	2	3,084,663
California	1	864,979
Michigan	3	8,327,944
Wisconsin	2	5,055,401
West Virginia	1	382,546
Florida	2	1,375,795
Minnesota	1	852,228
Nebraska	1	1,591,881
Tennessee	1	216,212
Colorado	1	134,563
Massachusetts	1	502,056
Maine	1	183,087
South Carolina	1	766,176
South Dakota	1	631,519
Total	49	49,948,597

APPENDIX C

AVERAGE AUTOMOBILE INSURANCE PREMIUMS, 88 FIRE AND CASUALTY COMPANIES WHICH FAILED 1958–68

Company	Number of years	Total premium	Average premium
Pennsylvania:			
Home Mutual Casualty	7	$2,658,000	$379,714
Bankers & Telephone	6	8,207,068	1,367,845
Sylvania Mutual	1	200,000	200,000
Bankers Allied Mutual	7	27,915,000	3,987,857
Palmyra General	4	3,121,000	780,050
Tri-State Mutual	4	592,000	148,000
Wissahickon Mutual	3	1,049,000	349,667
Reliable Mutual	4	604,000	151,000
Lawn Mutual [1]	5	16,509,400	3,301,880
Delaware Valley Mutual [1]	5	2,442,771	488,554
Commonwealth Mutual [1]	7	5,616,865	802,409
Empire Mutual [1]	5	4,228,212	845,642
Graphic Arts Mutua [1]	4	2,717,111	679,278
Springfield Mutual [1]	3	72,378	24,126
State total			13,506,222
Illinois:			
Progressive General	7	12,990,000	1,855,714
Highway	7	11,415,730	1,630,819
St. Laurence	7	14,154,395	2,022,056
Mercury Mutual	6	1,316,990	219,498
Lincoln Casualty	7	8,947,685	1,278,241
Lake States Exchange [1]	5	4,354,370	870,874
Bell Mutual [1]	5	2,976,349	595,270
Banner Mutual [1]	7	20,630,918	2,947,274
Bedford Mutual [1]	3	75,425	25,142
Whitehall Mutual [1]	4	503,873	125,968
Multi-State Interinsurance Exchange [1]	7	7,299,099	1,042,728
Oxford General Casualty Exchange [1]	4	2,090,042	522,511
Cosmopolitan [1]	6	18,361,777	3,060,296
Adams Mutual [1]	5	2,010,627	402,125
General Union Mutual [1]	4	179,242	44,811
Central Casualty [1]	6	3,871,860	645,310
Mid-Union Indemnity	4	6,362,916	1,590,729
State total			18,879,366
Missouri:			
Central Mutual	7	8,772,000	1,253,143
Midwest Mutual [1]	5	3,004,252	600,850
Surety Insurance Exchange [1]	6	904,379	150,730
Allied Western Mutual [1]	7	5,844,512	834,930
American Midwest Mutual [1]	3	1,835,836	611,945
Guaranty Insurance Exchange [1]	3	2,322,282	774,094
Missouri Union	5	2,502,000	500,400
Eagle Exchange	3	741,000	247,000
State total			4,973,092
Arkansas:			
North American Guaranty	5	14,525,316	2,905,063
Republic Casualty	5	2,643,721	528,744
Mid-South	5	2,117,434	423,487
Royal Standard	7	1,590,814	227,259
United Auto [1]	4	1,359,133	339,783
National Auto	3	46,679	15,560
State total			4,439,896
Texas:			
Career [1]	6	139,980	23,330
Government Service Exchange [1]	7	4,368,045	624,006
Franklin American	3	1,480,000	493,333
Highway Exchange	6	8,445,000	1,407,500
State total			2,548,169
Indiana:			
United Public [1]	9	11,452,576	1,272,508
International Auto Exchange [1]	[1] 7	17,611,893	2,515,985
Insurance Corp. of America [1]	7	656,323	93,760
Universal Auto [1]	5	7,004,197	1,400,839
United Mutual [1]	7	2,188,123	312,589
Old Line Auto	7	2,499,833	357,119
State total			5,952,800

APPENDIX C—Continued

AVERAGE AUTOMOBLE INSURANCE PREMIUMS, 88 FIRE AND CASUALTY COMPANIES WHICH FILED 1958–68—Continued

Company	Number of years	Total premium	Average premium
Maryland:			
National Guild	3	2,691,000	897,000
Chesapeake [1]	6	7,672,284	1,278,714
National Motors [1]	1	1,805,949	1,805,949
State total			3,981,663
California:			
Consumers and Distributors Insurance Exchange	7	2,231,000	318,714
All Cover Exchange [1]	5	4,324,897	864,979
Interstate Indemnity	7	13,019,000	1,859,857
State total			3,043,550
Michigan:			
Preferred [1]	7	32,027,696	4,575,385
Exchange Casualty [1]	7	15,132,813	2,161,830
Michigan Surety [1]	4	6,362,916	1,590,729
State total			8,327,944
Wisconsin:			
Market Mens Mutual [1]	7	25,008,351	3,572,622
Superior Mutual [1]	7	10,379,450	1,482,779
State total			5,055,401
West Virginia:			
North Central	1	1,125,000	1,125,000
Crown [1]	7	2,677,825	382,546
National Auto	1	95,726	95,726
State total			1,603,272
Florida:			
Florida Insurance Exchange	4	4,257,000	1,064,250
National Home [1]	4	2,228,847	557,212
Equity General [1]	4	3,274,333	818,583
State total			2,440,045
Minnesota: American Allied [1]	4	3,408,910	852,228
Delaware:			
American Military International	4	7,147,047	1,786,762
National Auto	5	4,648,740	929,748
State total			2,716,510
Nebraska:			
United Benefit [1]	7	11,143,167	1,591,881
Surety National	5	2,622,000	524,400
State total			2,116,281
Tennessee:			
National Service	5	24,840,613	4,968,123
Monticello [1]	6	1,297,372	216,212
State total			5,184,335
Colorado:			
Western Standard [1]	7	941,938	134,563
Mountain Standard	5	914,000	182,800
State total			317,363
Louisiana:			
Marquette	7	7,830,090	1,118,584
Delta Fire and Casualty	7	2,429,000	347,000
State total			1,465,584
Nevada: Great Basin	7	7,766,100	1,109,423
Massachusetts: Suffolk [1]	3	1,506,169	502,056
Maine: Washington [1]	5	915,436	183,087
South Carolina: First Citizens [1]	5	3,830,882	766,176
South Dakota: Security General [1]	7	4,420,632	631,519
Grand total		517,405,614	90,595,982

[1] Indicates companies included in Appendix B.

Senator HART. Gentlemen, would any of you care to make any comment or reaction before you leave?

Mr. WORTHINGTON. I think not, Senator. We appreciate the opportunity to speak to you and to have our views heard.

Senator HART. Thank you very much, gentlemen.

Normally, we would take a recess for lunch, but there is another committee meeting this afternoon and, if at all possible, I hope that we could continue.

Mr. Stringfellow, are you game to go right on now?

Mr. STRINGFELLOW. Yes, sir.

Senator HART. Our concluding testimony will be the reaction of the National Association of Mutual Insurance Agents.

The chairman of their Federal Legislative Steering Committee had anticipated being present; but we are delighted that the general manager, Mr. William A. Stringfellow, is here; and I am sure will present their position for the record.

STATEMENT OF WILLIAM A. STRINGFELLOW, GENERAL MANAGER, NATIONAL ASSOCIATION OF MUTUAL INSURANCE AGENTS; ACCOMPANIED BY ROBERT E. MORIN, MANAGER, FEDERAL RELATIONS, NATIONAL ASSOCIATION OF MUTUAL INSURANCE AGENTS

Mr. STRINGFELLOW. Thank you, Senator.

May I also introduce my associate, Mr. Robert Morin, who is a member of our legislative staff force?

Mr. Chairman and gentlemen of the committee, I appear here on behalf of our association and in accordance with instructions of our board of directors, whose position on this bill was determined at its most recent meeting on October 19, 1969, here in Washington, D.C.

So that our interest in this matter will be understood, let me relate that our membership is composed of more than 18,000 independent mutual agents serving their many clients primarily in the field of property and casualty insurance, including of course automobile, which is one of the principal concerns of this proposed legislation.

Our association is in its 39th year. Our headquarters are here in Washington. We serve our members through 36 affiliated State and regional associations operating in all but five of the United States. It is our function to look to the welfare of our members, to assist them in a greater emphasis on professionalism and service to their clients and to the public in general, and to act as a good corporate citizen of these United States. In short, we live and work at the grassroots level. We are an active and vital part of our communities, and we are generally concerned with the well-being of the insurance buying public.

Traditionally and currently, we strongly favor State regulation of the insurance business. We believe it to be a sound, equitable and publicly oriented concept for proper regulation of a business which, though national in scope, is closely identified with the immediate needs of the local public it serves.

We would be the first to confess that in this exploding population and economy, in this rapidly changing society in which we live, that an industry as large as ours—writing approximately $10 billion in business and covering the greater number of the 100 million automobile

operaters in this country—has found it a taxing and sometimes difficult and frustrating undertaking to meet the almost daily changing needs of the public. However, the insurance industry has been working in concert with State regulators in an attempt to overcome these difficulties. And I think with measurable success.

Directing my remarks specifically to the bill under consideration, let me state emphatically that our association is strongly in favor of the concept of complete protection of the insuring public, including the possible insolvency of insurance companies. For this, it seems to us, is the minimum protection deserved by our clients and other parties who may be involved in claims.

The delay which the States and the industry have exhibited in meeting this responsibility is to be regreted, but it is fair to say that the need has become apparent only in recent years. For an industry which is well along in its second century, the insolvencies which have occurred in the past 6 or 7 years are a relatively minor indictment of its performance. This is not to say that we consider any insolvency as unimportant or any loss to a member of the public as unimportant.

Certainly the industry and the States have moved with some speed toward rectifying this situation. We freely confess that we wish sound post-insolvency assessment laws had been enacted more expeditiously by all States, but it should be noted that some States have insolvency laws under consideration and several others already have such laws.

Repeating previous testimony, there were passed in 1969 insolvency laws in New Hampshire, California, Michigan, and Wisconsin. Already there are laws in New York, New Jersey, and Maryland.

Therefore, let us say first that we are in favor of appropriate legislation to guarantee the solvency of insurance companies. At the same time, let us emphasize that we do not believe it necessary for the Federal Government to provide this security. We are opposed to that for several reasons.

We believe that State regulation of the insurance business is best for the business as well as the public it serves—and that applies to insolvencies equally as to other aspects of regulation. We believe that such regulation at the State level can more quickly meet the needs of the public and the industry as they arise; that it can be more flexible.

Let me say parenthetically that the testimony of the NAIC which you have just heard on this subject, and which is much more "complete" than ours, seems to me well to the point.

We have said that we are heartily in favor of a guarantee against insolvency, and so it is incumbent upon us to give more than a negative reply to the highly motivated efforts of this committee and the sponsors of this bill. While we are of the opinion that this responsibility can be efficiently and fairly undertaken by State legislatures and State insurance departments, we are equally of the opinion that the overall solution should have some national character. This does not mean Federal regulation, but it does mean a national concept of standards to which each State can look for guidance.

To this end—and may I say this statement was prepared before we heard the testimony that have just been concluded—we submit that the National Association of Insurance Commissioners has been working on this problem. It is our understanding that a model bill will be proposed for enactment in all States.

We are hopeful that the model bill will be as strong as the New Hampshire law, a copy of which we would like to have permission to submit later in the record.[1]

Senator HART. It will be received.

Mr. STRINGFELLOW. I would like to point out that it was the Independent Mutual Agents Association of New England which actively supported the efforts of Commissioner John Durkin to secure passage of the New Hampshire law. It deals directly and specifically with the problem of insolvencies in the automobile insurance field.

We heartily recommend it to the NAIC, except that we would urge its model bill incorporate two other important provisions to benefit the policyholder:

(1) It should include all lines of insurance—the New Hampshire bill includes only automobile—and

(2) It should provide for a full return of unearned premium to the policyholder without the penalty of a deductible.

The NAIC historically has provided an avenue for important insurance legislation and, through previous efforts and preparation of other model bills, has secured passage of vital legislation in all our States. We believe they can—indeed, will—provide the sound basis for solution of the insolvency problem. We further believe that with the leadership and guidance of these influential regulators in individual states that these individual states will enact appropriate legislation.

We pledge our support, both of our national association and its affiliated State and regional associations, to work for enactment of significant legislation to protect the public from insurance company insolvencies, to provide for return of unearned premiums to the insured, and for passage and legislation that will encompass all lines of insurance in the fire and casualty fields.

Further we would state that because we know that one of the areas of concern of this committee lies in the fact that there has been delay in enactment of insolvency legislation, we would support a provision that sets a reasonable time limit for its enactment—with the understanding that a Federal program such as is being considered by this committee would automatically apply in those States that did not meet the deadline.

We would earnestly suggest to this committee that the basic objectives of Senate bill S. 2236 and your efforts toward solving this problem can be achieved better through this approach than any other.

Mr. Chairman, I am grateful for this opportunity to speak to the committee on behalf of our association. We applaud the efforts you make toward solution of this problem. We offer our services as we have stated—toward the same goal you seek, but simply by a different path.

I would hope to answer such questions as you might have, sir.

Senator HART. Thank you very much.

I understand that you speak from the point of view of the man who deals with the policyholder in very direct fashion. So, it is understandable that you, for example, would emphasize the desirability of providing for the return of the unearned premium. I suppose it is correct to assume that some of your member agents lose clients when a company becomes insolvent; is that not true?

[1] See copy of bill on p. 142.

Mr. STRINGFELLOW. I am sure they do. In any event, they are greatly distressed and discomforted when there is an insolvency.

Senator HART. Now, this bill we are considering, S. 2236, provides for a return up to one-half of the unearned premium. Do you think we should go beyond that?

Mr. STRINGFELLOW. Senator, I must confess we had not heard the argument in favor of the deductible when our committee discussed this matter.

I think we should hear the other argument.

At that time we felt if a person sustained a loss through no fault of his own, we could not see the logic of the deductible.

Senator HART. From discussions with member agents, how often do you hear complaints about the way the uninsured motorist with insolvency protection works? Is this discussed very often?

Mr. STRINGFELLOW. Senator, I have not had a complaint in this direction. I was somewhat surprised to hear the question and answer this morning. I would not say that there have not been any. It may be they have not come to our office. I had not heard of them as a problem. I am afraid sometimes we get in the ivory tower, too. The problem has not been reported to us.

Senator HART. You do not have any figures on how successful the UM is in picking up insolvency losses?

Mr. STRINGFELLOW. Actually, my best information is what I have heard here this morning, and it does not surprise me too much.

I think we understandably are slow in accumulating these types of figures. I think what you have heard this morning is my reflection of what I would have expected to hear.

Statistically, we are a bit slow and cumbersome, and I am afraid it is unavoidable.

Senator HART. After hearing the discussion this morning on post-insolvency non-Federal assessment programs, what is your feeling, your thinking in terms now of your agents' policyholders' interest? The policyholder would be likely to obtain a lesser settlement from an industry-operated fund, would he not; a fund where the assessment charges vary directly with the amount of payout it is making to the claimants?

Would this not tend to affect adversely your policyholders' interest?

Mr. STRINGFELLOW. Certainly the logic of your statement is pretty hard to dispute. I would not try to.

It seems to me if that danger is there, as would seem to be the case, that any such law should carefully provide that the industry be the one not to decide the payment of the claim, or at least it decide it under such regulations that would be effective. Certainly the right to adjust your own claims is the right to minimize them.

Senator HART. We can do better, I am sure you will agree, in terms of our existing liquidation procedures, where some author in the field says, "The duration of the liquidation proceedings of the companies studied"—I do not know whether he studied all the insolvencies at any given time or selected ones—"ran on the average of 11.5 years, suggesting much of the loss imposed upon the credit and the claimants may be the cost of the liquidation proceedings itself."

A policyholder is not amply protected when he has to wait 11 years to be reimbursed.

Mr. STRINGFELLOW. Certainly I would have to agree with you, but it seems to me that the matter of taking care of insolvencies and the problems of insolvencies of the industry was a somewhat short or rather an unexpected phenomenon as a result really of many other problems, and I think we would be the first to confess as regulatory people—we are not regulatory—anyway, as industry and regulatory we did not do as good a job as we would like to have.

On the other hand, as someone said here this morning, these are evolving things.

Senator HART. Insolvencies have been with us for a great many generations.

Mr. STRINGFELLOW. I am thinking of the ones that occurred 4 or 5 years ago, the flurry 4 or 5 years ago.

We had these insolvencies, which it seemed to me arose largely from these substandard companies arising overnight, to me a somewhat unprecedented situation.

I think the testimony here today would indicate that we did not do a good job. Obviously the people most charged with this responsibility, the commissioners, are properly concerned about overcoming what they have thought is a problem, and certainly this bill addresses itself to that.

Certainly, liquidation on the part of the policyholder should be prompt. I would go on reocrd in favor of that.

Mr. SUTCLIFFE. As a followup to that point, in a discussion we had with Mr. Worthington, he informed us that the proposed NAIC post-insolvency assessment plan would provide for immediate payment to the policyholder without delay because of liquidation proceedings. The question was not put to Mr. Worthington which I wish to put to you at the present time, because you are within the industry and perhaps can tell me.

Would the insurance company have to wait 11.5 years or whatever the duration of the liquidation period is, to determine what assessments can be recouped and to then record that with the State insurance commissioner to justify the fact that the rates are not unreasonable?

Do you understand the question at all? Do you have a reaction?

Mr. STRINGFELLOW. I think it is an irrelevant question. First, we are assuming that we are going to have a continuous flock of insolvencies, and the history of the last few years indicates we are not. The decline in insolvencies is distinctly notable, and I would suggest that the efforts of this committee deserve credit for this.

We are suggesting there is going to be a pox of insolvencies in many States, and this isn't going to happen. These gentlemen are getting on the ball. They are becoming more concerned about the capital requirements of the company. States are enacting laws. Examining committees are much more aggressive. So, your question to me is theoretical.

Mr. SUTCLIFFE. Let me see if I can place it in a more realistic context, because I didn't mean to be theoretical. We were told that the new model liquidation statute has been passed in one State and apparently not in many other States. Too, we still have the problem of marshaling assets and collecting moneys to disburse. It goes to the point that Senator Hart was making about the incentive of an insurance company to settle claims at a low rate. If they can't recoup their funds in terms of policyholder premium rates until the final liquidation takes place, which is a period of 5, 6, or 7 years, then under the

plan of immediate payment it is still a very strong incentive to settle for as small an amount as you can because if you lose the use of that amount of money over a period of 5 years you have lost a considerable amount of money.

Mr. STRINGFELLOW. I don't think so.

Mr. SUTCLIFFE. My question concerns the assumption—and it really goes to ratemaking activities.

Mr. STRINGFELLOW. I think it is irrelevant. You are talking about an $11 billion industry meeting a $4 or $5 million insolvency. The pennies involved would be insignificant. I don't question the theoretical knowledge.

Mr. SUTCLIFFE. That is very interesting in light of the claims by certain members of the industry on the very, very tight profit squeeze. That was perhaps an incorrect assumption.

Mr. STRINGFELLOW. I think the contracts would not be significant to their profit squeeze. Mathematically it would be insignificant.

Mr. SUTCLIFFE. That is where we went off on a different tangent.

You mentioned that the need was only apparent in recent years in your testimony, and that the States and the industry have exhibited——

Mr. STRINGFELLOW. If I said that, I should not have. I said that there was a flurry of very regrettable insolvencies I guess 4 or 5 years ago—perhaps longer than that—but it undoubtedly dramatizes the situation. Certainly there have been insolvencies in the past. I think, as it should have, it should have drawn it to the attention of the legislatures, both Federal and State.

Mr. SUTCLIFFE. You indicated that your organization supported the New Hampshire postinsolvency assessment bill, did you not?

Mr. STRINGFELLOW. Our affiliate association Independent Mutual Agents of New England.

Mr. SUTCLIFFE. Did any other segments of the industry assist you in the passage of that legislation?

Mr. STRINGFELLOW. I cannot answer that. I am under the impression that we were the forerunners.

Mr. SUTCLIFFE. That New Hampshire activity was prior to the introduction of S. 2236? The introduction of that bill was May 23, 1969.

Mr. STRINGFELLOW. My best information is this was passed in May of 1969.

Mr. SUTCLIFFE. In your testimony you stated you were in favor of some national standards to guide State insurance regulation. Is that correct?

Mr. STRINGFELLOW. Yes.

Mr. SUTCLIFFE. Are you suggesting, and I will let you answer this, are you suggesting that the NAIC is not now providing these standards?

Mr. STRINGFELLOW. Traditionally, it has provided standards. It seems to us because of the urgency, for one thing of this bill, of this concern, that there ought to be some uniformity in insolvency legislation. For one thing we hope it could be enacted more quickly. There are other problems that plague the industry with which you gentlemen are familiar, including recognizing rates.

Our president recently suggested that some uniformity here would be helpful. We feel that uniformity will bring about more relief.

Mr. SUTCLIFFE. Do you believe that the model legislation approach is a satisfactory approach to meeting the urgent situation we face?

Mr. STRINGFELLOW. We think it is a good idea. I don't think it is the only way to do it. For example, New York has a good situation, and we wouldn't want to change that. The bills that are in effect I assume are good bills by and large. I wouldn't say we studied them carefully. It seemed to us that model legislation could be most quickly effected, and if you notice in our statement we are asking the States to do this job in 2 years.

The regulatory process being what it is, that is a pretty tough order.

Mr. SUTCLIFFE. You are suggesting that your proposal for reasonable time is 2 years?

Mr. STRINGFELLOW. Yes.

Mr. SUTCLIFFE. And after that your organization would be prepared to support a Federal Insurance Guaranty Corporation bill?

Mr. STRINGFELLOW. Yes. We realize the democratic process is slow, and we are usually glad that it is. We would not want it to be too fast. On the other hand, this is a real problem, it is a problem that will affect our members as well as their clients, and we think we should not be glib and negative about this bill. We are willing to do all we can. We do not question the need.

Mr. SUTCLIFFE. What is your attitude toward the policyholders who are left exposed during this period of reasonable time? Is this just a cost?

Mr. STRINGFELLOW. We live in a very imperfect world, Mr. Sutcliffe, and unfortunately people get hurt along the way in this kind of business, but we get hurt a lot worse if we act too speedily and without proper precaution. The democratic process in both State and Federal is slow, sometimes much too slow in my judgment, but on the other hand, I would rather live with this than a system that deals too promptly with matters. I think 2 years, given the fact that this isn't the only thing to try to bring about relief in insolvencies—I think every commissioner there today is just as sensitive as he is to the possibility of insolvent companies, and this wasn't true several years ago.

We are not being insensitive to the fellow who is going to get hurt.

Mr. SUTCLIFFE. Let me ask you how you explain the initial activity in the insolvency area after the introduction of Senator Dodd's insolvency bill, and then a failure of anything to take place significantly when no action was taken? There were no new postassessment insolvency bills passed in the legislative sessions from 1966 through 1969, there were no efforts. Upon the introduction of S. 2236, four—actually, coincidental to S. 2236 was the New Hampshire plan, so that may be one area of activity—three other States then passed postinsolvency assessment plans after May 23, 1969. You are suggesting to us to give the States time to allow the democratic process to work out.

In that regard, I remind you that this particular committee and the Senate of the United States has to very much follow along the lines of democratic principles. We cannot avoid that in any way, shape or form and have no desire to, but how do you explain this sort of peaks and valleys of activity depending upon what the Federal Government is doing, and then how do you then come in and tell us that we should wait 2 years?

Mr. STRINGFELLOW. Your first question I suspect I have no particular expertise in. I would give you a theoretical observation. This is the way of life in the democratic government and free private enterprise. I could cite analogies that would occupy the time of the committee without profit. I think the activities of this committee have been extremely helpful.

If by our persuasion we are able to persuade you folks to give the industry another couple of years, this would be our thought of extending that concept, realizing all along the way that somebody is going to get hurt. Somebody is going to get hurt anyway. This is the nature of democracy and free private enterprise.

I am happy that people do not move so rapidly rather than to change the process.

Senator HART. Thank you very much.

Do you have anything you would like to add? Thanks again. Thank you for being patient with us.

Mr. STRINGFELLOW. Thank you, we appreciate the opportunity.

Senator HART. We adjourn to resume tomorrow morning at 10 o'clock in this same hearing room.

(Whereupon, at 1:30 p.m. the committee was adjourned, to reconvene at 10 a.m., Thursday, Nov. 20, 1969.)

FEDERAL INSURANCE GUARANTY CORPORATION

THURSDAY, NOVEMBER 20, 1969

U.S. SENATE,
COMMITTEE ON COMMERCE,
Washington, D.C.

The committee met, pursuant to recess, at 10 a.m. in room 5110, New Senate Office Building, Hon. Frank E. Moss, presiding.

Present: Senator Moss.

Senator Moss. The subcommittee will come to order.

Today we continue hearings on S. 2236, a bill to establish a Federal Insurance Guaranty Corporation. This corporation is designed to provide "insurance" protection for policyholders whose own companies become insolvent.

In previous hearings we have received valuable testimony arguing for and against S. 2236. For example, one large segment of the insurance industry has endorsed the bill, while the insurance commissioners of the States have squarely opposed it. I imagine testimony today will be as diverse.

A quick glance at the witness list suggests to me that this hearing will focus primarily on the consumer's interest in S. 2236. We welcome this testimony from the various consumer witnesses. We also welcome the remarks of the National Association of Mutual Insurance Companies.

Of those who are on the list today, I am going to call first on Mr. Richard Bloom, president of the National Association of Mutual Insurance Companies. I understand he will be accompanied by Mr. Wallace M. Smith, Washington counsel, and Mr. Dick Smock, from Indiana.

We are pleased to have you before the committee, and you may proceed in whatever manner you care to.

STATEMENT OF RICHARD C. BLOOM, PRESIDENT, NATIONAL ASSOCIATION OF MUTUAL INSURANCE COMPANIES; ACCOMPANIED BY WALLACE SMITH, WASHINGTON COUNSEL, AND RICHARD SMOCK, VICE PRESIDENT, LEGISLATIVE SERVICES

Mr. BLOOM. Mr. Chairman, my name is Richard C. Bloom. I am president of the National Association of Mutual Insurance Companies. Our association has a voluntary membership of over 1,000 mutual property and casualty insurance companies writing insurance in all 50 States and the District of Columbia.

Accompanying me is Wallace Smith, our Washington counsel on my left, and Richard Smock, vice president—legislative services on my right.

The insurance industry, in general, recognizes the serious nature of the insurance insolvency problem which confronts the Nation today. Our association recognizes the problem exists and is vitally interested in seeking a solution to it. We feel that a solution within the framework of State regulation would be more beneficial to the public and the insurance industry than a solution by Federal regulation. Therefore, Mr. Chairman, our association is opposed to S. 2236 as drafted.

Some controversy exists regarding the scope and effect of the problem. Such disagreement is evidenced by the disparity between the National Association of Insurance Commissioners and the Senate Antitrust and Monopoly Subcommittee studies on insurer insolvencies. I might observe, Mr. Chairman, that reportedly members of the Federal Government have expressed feelings that if only one person is adversely affected by an insurer insolvency it is one too many, and thus becomes a problem.

Regardless of the differences and opinions as to the size of the problem, our association believes it to be of such a degree that a concerted effort on the part of the insurance industry should and indeed must find a responsible solution.

Mr. Chairman, several proposals have been put forth as possible answers to the insolvency problem. Some of these are:

1. Uninsured motorists coverage, including insolvency protection.
2. Preassessment insolvency funds.
3. Post-assessment insolvency plans.
4. Custodial reserve plans.
5. National voluntary insolvency fund.
6. Federal Insurance Guaranty Corporation (S. 2236.).

Our association currently is studying all of these proposals. I say to you in all honesty and sincerity that we have not reached any conclusion as to which proposal has the greatest merit. Our desire is to find a solution which will prove most beneficial and protective to the public and to the insurance industry.

In line with this effort we would recommend strongly that a reasonable period of time be allowed for the States and the insurance industry to achieve a proper solution to the problem. In this manner the burden would be placed upon the responsible parties and an opportunity provided to prove in a clear and concise manner to the Congress that a proper solution could be achieved without the need of Federal Government intervention.

This, in all fairness on the part of Congress, would be notice to the States and the insurance industry, that a proper solution must be forthcoming to protect the public against insurer insolvencies.

Meanwhile, in such action, the Congress would be continuing its responsible interests to protect the public.

The National Association of Mutual Insurance Companies reaffirms its strong support of State regulation. We are firmly convinced that the problem of insurer insolvency can best be solved within the framework of State regulation.

Regardless of the disparity in the figures of Senator Hart's Antitrust and Monopoly Subcommittee and the National Association of Insurance Commissioners studies on insurer insolvency, both studies indicate a peak of insolvencies in the mid 1960's.

Since that time, these studies also indicate a decline in insurer insolvencies, showing, we feel, that the problem is not as severe as it was just 4 years ago. This improvement reveals a progressive decrease in insurance company insolvencies indicating responsive action on the part of State insurance regulators and the insurance industry.

We believe this record of improvement justifies our recommendation for the granting of a reasonable period of time to solve the insolvency problem by the States and the insurance industry. Therefore, we would recommend that the committee give serious consideration to adopting a resolution providing the States and the insurance industry a reasonable period of time to implement programs which would solve the insurance insolvency problem.

Our association pledges its full support in working with Government and industry to reach the most responsible solution at the earliest time to eliminate the insurance insolvency problem we are faced with today.

Senator Moss. Thank you very much, Mr. Bloom, for your testimony and your statement of position of the National Association of Mutual Insurance Companies.

In your statement, you state that you think that the States should be given time to correct the insolvency problem. Why do you think this should be done by the States?

Mr. BLOOM. We believe this is the place for regulatory authority, at the State level. Our association has been consistent in this position, and I believe that this is the most valid position we can take.

Senator Moss. Haven't many of the problems arisen by reason of disparity and type of regulations various States have had? Some have very excellent regulatory functions, and others not really so rigid?

Mr. BLOOM. Yes, sir; this is true, I'm sure. And I believe that there is indication here that this is one of the serious considerations.

Senator Moss. You also ask for time for the States to do it. How long is a reasonable time? How long should we wait to see if the States do resolve the problem?

Mr. BLOOM. We believe, sir, that a period of 2 years should be adequate time for action at the State level.

Senator Moss. How long did you say?

Mr. BLOOM. We feel a period of 2 years, or perhaps the end of the year 1971 should be adequate time.

Senator Moss. You indicated there had been some efforts made to close the "solvency gap." Was this effort undertaken before or after the introduction of S. 2236?

Mr. BLOOM. I might have to refer to either of my associates. I believe that probably much of it came directly after the introduction of this bill. I am not familiar with the dates of State adoption, sir.

Mr. SMITH. Mr. Chairman, we would agree, and I think other witnesses have also stated the fact, that S. 2236, and even prior to the introduction of that bill by the members of this committee and others, that Mr. Dodd's bill did instigate great action on the part of the States, and also on the part of the insurance industry to take action here and to move to improve the situation in the insolvency area.

Senator Moss. Mr. Dodd's bill was not adopted, and I wonder what happened when that went by the board, as it were?

Mr. SMITH. This is what we are talking about, sir, that action has been taken. We believe simply the introduction and discussion concerning or relative to Senator Dodd's bill, and even more so now on S. 2236, that insolvency funds have been established since the introduction of the Dodd bill, and discussion here under this bill.

And more States will also improve coverage; namely, the uninsured motorist coverage has taken effect, and we believe that this is a step in the right direction.

We certainly think that this comes as a result of these bills being introduced, and we think that even more progress will be made here in the immediate future.

In the 2-year period in which our president, Mr. Bloom, has mentioned to the committee here, we think this is a reasonable time, Mr. Chairman, simply because it would be most difficult for the Senate to act any more quickly than this 2-year period—probably so—but the difference would only be a matter of a few months. We would say then that if we cannot do the job, as our statement reveals, by the Senate placing this burden in the areas of State responsibility and the industry, then we don't believe anyone would have any question about whether the Federal Government should be able to take or should come in and take proper action or not.

Senator MOSS. Basically, the idea behind this is similar to the Federal Deposit Insurance Corporation, and what it did for banks. I don't think that ever could have been worked out on the State level. We had a National Guaranty Corporation, in effect, for the depositors in our banks, and it was mandatory for national banks to begin with. But the States all came in—State banks—very readily and quickly, and so far as I know, almost every bank today has deposit insurance.

In fact, it has spread to the savings and loans and other savings institutions, too. Is there any reason why we shouldn't do this on a national level for insurance guarantee, rather than just leaving it to the States?

What, really, is the objection to the national approach?

Mr. SMITH. Previous witnesses, Mr. Chairman, have testified as to the effectiveness of the banking insurance programs and plans. The only criticism that we have heard concerning those is the cost of it, and that there has been some excessive cost.

We look at those programs, though, as a similar situation to the insurance insolvency problem, and that is the focal problem—the protection of the public, and not what the cost is.

I think everyone would desire that the cost be minimized, at least that everyone gets the value of these programs in dollar costs. We would hope this, too. We would hope for this.

I believe yesterday in testimony before the committee here that the NAIC gave numerous reasons as to the effectiveness of State regulation. Again, I would repeat that this committee has instigated the action, the interest to be taken by the State regulators and the insurance industry.

It is our position, again, that we believe time should be given now, that this interest has been aroused, and let's see if we can't do the job. If we can't we would have no argument for any other action being taken.

Senator Moss. I appreciate your position. I don't think there is any intent in this bill to displace State regulation in any way. It is really to support and enhance the powers of the State to regulate. We appreciate your offer to seek the best possible solution to the problem recognizing the problem and your agreement to cooperate in every way you can in finding a solution. That is what we are trying to do here in our hearings, and in consideration of this bill.

So, I thank all three of you gentlemen for appearing and for the testimony that you have given here before the committee.

Our next witness will be John Yolton, who is administrative assistant to Olga Madar of the International Union of United Auto Workers.

Mr. Yolton, we are very glad to have you, sir.

Senator Hart indicated he would like to have been here, especially today, but he is out of town and not able to attend. I want to announce that because he had indicated he would especially like to hear this testimony.

You may go ahead.

STATEMENT OF JOHN YOLTON, ADMINISTRATIVE ASSISTANT, UNITED AUTOMOBILE, AEROSPACE, AND AGRICULTURAL IMPLEMENT WORKERS OF AMERICA; ACCOMPANIED BY PAUL A. WAGNER, OF THE WASHINGTON LEGISLATIVE OFFICE

Mr. YOLTON. Mr. Chairman, the UAW, a union with more than 1,600,000 members throughout the United States, is pleased to have this opportunity to share its views on S. 2236. This is a bill which would create a Federal Insurance Guaranty Corporation to prevent insurance company insolvencies. It is a bill designed to indemnify the victims of such insolvencies if they should occur.

The UAW has a record going back a number of years, which indicates our strong drive to seek meaningful reforms in a number of areas of American life. The president of our international union, Walter P. Reuther, has pressed on innumerable occasions for those measures which would achieve a better social and economic climate for all Americans. We are proud of the fact that our interest is not limited to those matters which can be handled at the bargaining table. The matter before us today can only be handled in the public forum. So, in keeping with a longstanding concern, we strongly support the enactment of S. 2236.

Our members have felt the sting of insurance company insolvencies. We have been powerless as individuals or as an organization to cope with the problems that have arisen.

S. 2236 appears then to be the most effective solution to the devastating problem of property and casualty insurance company insolvencies. We use the term "devastating" advisedly because as we will explain later, some of our members have been dealt sledgehammer blows when their particular auto insurance company went into bankruptcy.

I understand that motor vehicle registrations are now over 100 million. The tremendous number of cars, plus the unexcelled national mobility of the automobile compel us to the view that auto insurance policyholders must have the assurance that auto accident and injury claims must be honored. We are concerned, too, for those people who

are innocent victims of auto accidents and injury. We see this being accomplished through the establishment of the Federal Insurance Guaranty Corporation. This legislation should provide for the sure, certain and swift settlement of claims.

We have learned of the problems that our members have had when through bad luck they have unwittingly become policyholders in a company that soon goes bankrupt.

In many States, the lack of auto insurance means immediate cancellation of the privileges of driving. Some members we know about in Illinois were doubly-damned, perhaps triply-damned. They held auto policies in a bankrupt company. They lost their premiums. They held policies in mutual insurance companies, where, upon court ruling, made them subject to the debts of the company. In their economic anguish, they found their wages garnished and in some cases, workers lost jobs on that account.

Much of the rancor in the cities stems from this sort of white collar crime. We believe that the principle of an auto insurance guarantee corporation is imperative. We believe that the administrative and financial arrangements of the bill are proper. However, we do think that S. 2236 should be more positive in its relief. The time delay should be reduced to the shortest possible time in providing relief for whatever situation derives from the scope and operation of the auto insurance policy.

We ask that special attention be directed to section 9(a) (1), (2), and (3). Too much time will be lost if the guarantee corporation will only move into action after a court of competent jurisdiction has found an insurance company to be insolvent.

We think that as a matter of administration, the State referee in bankruptcy or the State insurance commissioner could make an initial finding within 10 days as to the probable financial condition of an insurance company in trouble.

Upon such preliminary investigation and certification to the Federal agency, such adequate notice would then have the effect of providing for action by the guarantee corporation to carry out its avowed purposes.

We want a law that will work. We are fearful of delay that can only continue to undermine the confidence the citizen has in the credibility of still another Government program.

Let me illustrate the delay that will be met by the experience in our neighboring State of Maryland. Here the State has moved to establish a motor vehicle liability insurance fund. The purpose of this fund is to pay claims against insolvent insurers. Even though the fund was begun on June 1, 1965, we checked with the office of the State of Maryland Commissioner of Insurance, Newton Steers, last week, to find that no payment has yet been made. Four years have elapsed and the fund is untouched.

According to Commissioner Steers' report of 1968, we find an explanation of the problem of applying the fund to accomplish its avowed purpose and why no payments have been made.

The insurance report states:

> This fund is financed by a tax of one quarter of 1 percent on premiums for automobile liability insurance written in Maryland. It was begun June 1, 1965, and receipts in calendar year 1967 have averaged approximately $26,000 per month. As of December 31, 1967, the fund amounted to approximately $722,000.

The law requires that the tax on the insurance companies be continued until the net value of the fund reaches the sum of $2,500,000. At that point, further contributions are suspended. Whenever thereafter the amount of the fund is reduced below that level by reason of payments from the fund, then contributions to the fund are to be resumed.

To date, no payments have been made from the Fund because of a court ruling that such payments may not legally be made until after completion of delinquency proceedings against an insolvent insurance company. At that time, the courts may allow payment of claims from the Fund to injured parties and policyholders who have been unable to receive satisfaction otherwise.

Access to the Fund is available only when the insurance company has made payment to the Fund as provided in the law. This includes the Chesapeake Insurance Company, and the National Guild Insurance Company, but not National Motors Insurance Company. Claims payments may not exceed the limit of liability provided in the insurance policy in question.

Since the problems of Maryland were centered in Baltimore and affected many inner-city residents, you can see how wide the repercussions are to delay in the prompt settlement of insurance claims.

We direct the attention of the committee to section 15 dealing with the moneys and investment of the corporation. We suggest that accrued funds be invested in obligations of the Government National Mortgage Association or mortgages guaranteed by the Veterans' Administration.

It seems sensible to us that as we try to work out one problem related to auto insurance coverage that we take the money generated through the assessment against premiums and place that money directly for significant social programs. There is, of course, no question about those mortgages being sound financial investments capable of returning the amount of interest required by the legislation.

In conclusion, we should like to recommend that in section 4, the advisory committee number among its membership a person who has a true consumer constituency. We suggest that such consumer groups as the Consumer Federation of America. Consumers Union, or the National Consumers League be among the groups considered when seeking representation from consumer-oriented organizations. We appear here not because there has been an overwhelming crisis in auto insurance company insolvencies. While we are concerned about the failure of more than 100 companies in widely separated parts of the country over the last 8 years, we believe that first and foremost, there is a challenge to be met. Enactment of this legislation will aid the image of meaningful government action.

Mr. Chairman, I have placed at the back of my statement, several attachments regarding the situation in Illinois that I referred to earlier.

Senator Moss. Those attachments will appear in the record at the conclusion of your testimony.

(Attachments follow:)

ILLINOIS INSOLVENCIES

Since 1959 the policy holders of seven insurance companies in Illinois have been assessed to raise money to pay claims that were filed against mutual companies that went into liquidation or rehabilitation. There were a total of 193,058 policy holders who had assessments against them in Illinois between 1958 and the present time. The assessments were made in Illinois against policy holders in mutual insurance companies under a law that provided that when such companies went into liquidation or insolvency that each policy holder might be assessed double the amount of his premium. (Source: Al Verb, Special Deputy in charge of liquidation in the Department of Insurance.)

COMPANIES ORDERED IN LIQUIDATION OR REHABILITATION SINCE NOVEMBER 1956, STATE OF ILLINOIS

Company name	Order	Claims filed
Adams Mutual Insurance Co	Oct. 16, 1963	651
Banner Mutual Insurance Co	June 1, 1965	3,410
Bell Casualty Co	Sept. 9, 1965	304
Bell Mutual Casualty Co	do	1,591
Blackhawk Mutual Insurance Co	Feb. 27, 1957	4,951
Cosmopolitan Insurance Co	May 1, 1963[1]	25,025
Crown Insurance Co	May 7, 1964	3,649
General Union Mutual Insurance Co	June 27, 1962	192
Central Casualty Co	Mar. 1, 1962	3,286
Commerce Insurance Co	July 1, 1964	32
Highway Insurance Co	July 6, 1967	4,730
Illinois Automobile Insurance Co	Nov. 15, 1956	4,362
Lake State Casualty (a reciprocal)	Oct. 8, 1965	1,350
Mercury Mutual Insurance Co	Feb. 11, 1966	420
Mid-Central Mutual Casualty Co	May 21, 1968[2]	----------
Mid-Union Indemnity Co	Aug. 31, 1959	4,437
Multi-State Inter-Insurance Exchange	Sept. 11, 1964	2,207
Oxford General Casualty Mutual Insurance Co	Apr. 21, 5964	447
Progressive General Insurance Co	Mar. 20, 1968	4,695
St. Lawrence Insurance Co	Jan. 13, 1967	4,432
Trans-World Mutual Casualty Co	Nov. 2, 1967	705
Whitehall Mutual Fire & Marine Insurance Co	Jan. 14, 1965	37
Bedford Mutual Insurance Co	Apr. 13, 1965	62
Great Northern Casualty Mutual Co	Dec. 6, 1966	341

[1] Rehabilitation.
[2] Rehabilitation May 5, 1969; liquidation: final date for filing claims in liquidation Apr. 20 1970.

Senator Moss. I do appreciate your statement, Mr. Yolton. Your organization has been noted over the years for speaking out in favor of programs beneficial not only to members of the union, but the public at large, and I think you have done so again today. I congratulate you on this.

And I appreciate the suggestions that you have made to improve the bill. I particularly commend your suggestion that there be a consumer representative on the advisory committee. I think that is an excellent idea, and one that I applaud.

You state in your text that this legislation "should provide for the sure, certain, and swift settlement of claims." You seem to say that S. 2236 provides for sure and certain settlement, but not swift settlement.

Could you elaborate a little bit on that?

Mr. YOLTON. Yes; I think an earlier witness this morning talked in terms the States would be able to do this on their own, and we used as an example—and I would like to refer to that in response to your question—the Maryland situation as one case where they did in the State, by legislation, enact a fund similar to what we are trying to do nationally, but no claims are being paid out of it because of the whole delay that occurs when you have to go through court and find that company definitely insolvent.

All during that period of time, nothing happens. This is where we feel that S. 2236 could possibly not provide the swift help that is needed in these cases when companies go under, because of the legal delays involved.

Senator Moss. It might take a matter of a year or 2 years, or even longer in an insolvency proceeding, if it goes through the courts.

Mr. YOLTON. Yes, and that is our feeling of misgiving about that section.

Senator Moss. If you have specific language that you would suggest to make sure that these claims are promptly paid from the fund, when a company is unable for any reason to pay them, I think at least we

would like to study it, because I agree with you very much. The thing we are trying to remedy is the harm that comes to the policyholder who depends on that policy for payment of his automobile accident, or whatever it is that the policy covers, and suddenly finds that he can't collect. To delay him for a year is almost equal to depriving him of his insurance altogether.

So, we haven't achieved much unless we get prompt response.

So, if you would suggest specific language, you can submit it to us, and we would like to consider that and see if we can make sure our legislation will do that in the event the bill becomes law.

Mr. YOLTON. We will be happy to make that attempt.

Senator MOSS. Mr. Sutcliffe of the staff indicates that perhaps the feature of the bill that provides for a loan to be made to the company might be a way. If the company later then becomes insolvent, that would simply be an insolvency claim, but that perhaps would meet this immediate payout requirement to those who had a proper claim to the policy.

Mr. YOLTON. If it was found later that the company was able to get over their financial hurdle, it could reimburse the fund in some way.

Senator MOSS. That is right, repay the loan back into the fund.

Mr. YOLTON. Right.

Senator MOSS. That is a good practical problem to consider and one that we want to make sure that we have dealt with.

As you pointed out in talking about that Illinois situation, in some cases individuals even lose their jobs. In that sense, this is a loss to society generally. It is an expense not only to that individual, but it puts a burden on the Government services that must then be called in to meet the situation where you have an unemployed person.

Mr. YOLTON. That is true, and it is very difficult for the victim to find another job, too, because other employers are reluctant to hire someone that has a problem of garnishment. In this case, the man is perfectly innocent. He had nothing to do with it. He just unwittingly signed up with the wrong company.

Senator MOSS. Thank you very much for your testimony.

Mr. WAGNER. I am Paul Wagner in the Legislative Office here. I would like to perhaps respond to what had happened earlier this morning.

We, too, see some analogy between what is being attempted in this legislation and the Federal Deposit Insurance Corporation, and I hope we don't get into the same kind of arguments that existed back in the 1930's, when this idea of bank deposit guarantees was attacked.

I have before me a quotation that seems to be somewhat humorous at this time, but it might bring some light to bear. This is a quotation from Gov. Alf Landon made in September of 1933. At that time Governor Landon said:

> There is no question in my mind but that the guarantee of bank deposits is a greater blow to the ultimate welfare of the American people than the wildest inflation of the currency could possibly be. In my judgment the guarantee of bank deposits if carried out in this country to its logical conclusion, will completely destroy the entire banking system of the nation. The present situation cannot be corrected by freak legislation or false and unsound assurance to the people such as a gesture toward a guarantee of deposits. The guarantee of bank deposits is the start of a vicious circle that is ruinous to depositors and stockholders alike.

Well, it seems to me that what we wanted to do is to strengthen the State banking—rather the insurance departments of the various States, and I see this as one of those excellent opportunities through Federal State partnership, to do this very thing.

Senator Moss. Thank you for that contribution, Mr. Wagner.

It is interesting to look back and see the objections that were raised to the Federal Deposit Insurance idea for banks and compare whether or not similar objections or fears are voiced about this legislation.

The FDIC has a fund and it is supported by a contribution of a fixed amount. So there is a considerable analogy here.

I wonder what your opinion is as to the cost—the Maryland system, it was a quarter of 1 percent until the fund reached a certain level. Do you have any projected figures of what the costs might run on this system that we are talking about in this bill?

Mr. WAGNER. Mr. Chairman, we have had not too great an opportunity to study it, but using the same analogy, and using the same type of ratio that is used in the Federal Deposit Insurance Corporation and the Federal inspectors as compared to the State bank examiners, it seems to me that same ratio could very well be maintained in the number of examiners that would be needed in this Federal Insurance Guarantee Corporation as compared now to the number of State commissioners of insurance, and the examiners in the various State departments of insurance.

So, using that and projecting some figures there, I think that it would be a cost of some 10 to 12 million dollars a year. That is what we would really be talking about in the setting up, staffing and carrying out the purposes of this present legislation.

Senator Moss. Thank you very much Mr. Wagner, and Mr. Yolton.

We appreciate your testimony. This has been very helpful.

Mr. YOLTON. Thank you, Mr. Chairman.

Mr. WAGNER. Thank you.

Senator Moss. Our next witness will be Mrs. Erma Angevine, who is the executive director of the Consumer Federation of America, here in Washington.

Is Mr. Berlin going to accompany you?

Mrs. ANGEVINE. I'm afraid not.

STATEMENT OF MRS. ERMA ANGEVINE, EXECUTIVE DIRECTOR, CONSUMER FEDERATION OF AMERICA, WASHINGTON, D.C.

Senator Moss. We are glad to have you before this committee again. We know that you will give us a fine, well-thought-out statement, as you always do.

So you may proceed.

Mrs. ANGEVINE. I regret that Mr. Berlin is not with me, because he always makes a great contribution, I think, to the legislative proposals that are before the committee.

Senator Moss. He does, indeed, but you do also, and we are happy to have you.

Mrs. ANGEVINE. I would like to say that United Auto Workers is one of the members of the Consumer Federation of America, and we are very proud also to support the statement which they just made.

We appreciate this opportunity to testify on S. 2236, a bill to create a Federal Insurance Guaranty Corporation to protect the American public against certain insurance company insolvencies.

The Consumer Federation of America is an organization of 140 consumer groups located in 38 States and the District of Columbia. Our member organizations have members themselves in all 50 States, and these people number in the millions.

Our purpose is to promote the cause of the American consumer and to encourage developments in all areas of the American economy that will operate to the consumer's benefit.

It is in keeping with this commitment that we appear here today, for the American consumer has a vital stake in the industry affected by this bill. Last year, according to the October 1969 edition of "Best's Review," American consumers spent more than $22.9 billion to purchase the property, casualty, and surety coverages affected by this legislation. This amount included more than $5.4 billion to protect our homes, businesses, and personal property from fire, theft, and other hazards; and more than $9 billion in the various kinds of automobile insurance coverages.

For almost all American consumers, insurance of one sort or another is a vital part of everyday life. As the report of the President's National Advisory Panel on Insurance in Riot-Affected Areas put it last year:

> Insurance is a basic necessity for a property owner * * * The opportunity for every responsible individual to obtain security for his savings and investments is vital in a free society * * *.
>
> * * * Without insurance, the savings of millions of individual citizens are exposed to the risk of loss from natural and man-made hazards they cannot control.

The Panel's report dealt with the problem of availability of insurance in certain of our inner cities, and it spurred the enactment of legislation creating the FAIR plans, which assure the access of consumers to essential property insurance.

S. 2236 addresses itself to the more serious problem of the reliability of insurance. Mr. Chairman, it seems to me this is serious not only to consumers which we are obviously most vitally involved with. I think it is also of importance to the insurance institutions themselves, because when insolvency or any other problem involves the whole insurance group, it undermines the faith of the consumer in the insurance industry, and therefore reacts adversely to the industry that the consumer is depending upon, as well as to the consumer.

I want to make it clear that we are not anti-insurance industry. We are concerned with the lack of security when insolvencies occur and make the consumer start thinking, "Well, can we trust any insurance company, then?"

And the upsetting element reflects on the whole industry, not just on the one insurance company that is insolvent.

Too often consumers who have purchased insurance protection—often at great cost and personal financial sacrifice—discover when they need the protection that the company they paid has become insolvent.

The financial and social costs to consumers of insurance company insolvencies can be truly staggering. On a direct basis, the Senate Antitrust and Monopoly Subcommittee estimated losses to policyhold-

ers and claimants from property and casualty insolvencies since 1934 at $600 million. This figure includes the consumer's loss of unearned premium, the nonpayment of his first party damage and liability claims, and the economic impact of the insurance company's failure to provide him with promised legal defense. It also includes the cost to the consumer of uninsured judgments against him in suits by third parties, judgments which in many cases he cannot hope to satisfy during his lifetime.

Indirectly, the consumer loses confidence in the private insurance mechanism and the ability of his Government to prevent future insurance company insolvencies. He also loses the benefit of tax dollars that must be used to support litigation stemming from the insolvency and in paying the cost of lengthy liquidation proceedings.

A graphic illustration of the consequences of insurance company insolvencies can be found in data prepared by the Senate Antitrust and Monopoly Subcommittee and inserted in the record of its February 1969, hearings.

The subcommittee's figures show that 88 of 109 property and casualty companies becoming insolvent during the period 1958 through 1968 wrote at least $517,415,614 in automobile insurance premiums (exclusive of other coverages) before they became insolvent. When the 88 companies failed, data on 80 of them shows that as of September 1968, 239,897 consumers were left with automobile policyholder and third-party claims against the companies totaling more than $525 million.

Oscar R. Goodman, professor of finance at Roosevelt University in Chicago estimated in testimony before the Senate Antitrust and Monopoly Subcommittee last February 25 that "at least $200 million was lost by the public as a result of these insurer insolvencies, as a very basic minimum."

It is evident from the 80 insolvencies studied by the Senate Antitrust Subcommittee that insurer failures impose heavy losses on the American economy and consumers generally. But the possible consequences for the individual consumer are even worse. I would like to trace some of these consequences to illustrate the need for the protection that S. 2236 will provide.

Let us assume that an individual consumer holds an automobile insurance policy written by an insurer which has become insolvent.

If he has a first-party claim against the insolvent insurer, say for $2,500 under the comprehensive coverage in his policy resulting from the theft of his car, he could conceivably recover absolutely nothing. Senate Antitrust Subcommittee figures show that seven mutual automobile insurance companies that became insolvent in Pennsylvania had total actual assets at the time of liquidation of only $21,000. Assets of four of these companies were as follows: $0, $13, $28, and $74. Recoveries from the 80 companies previously referred to ranged downward to 4 cents on the dollar.

If the consumer is in an accident and the circumstances indicate he is at fault, he has no protection under the liability portion of his policy. If he is sued, the defunct insurer will be unable to provide the legal protection it promised him. In many cases, he will be sued by the other party merely to establish his liability so that the other party can collect from his own insurer under the insolvency clause of his uninsured motorists coverage. The other party's insurer may then sue the con-

sumer in an effort to recover what it has paid out to its policyholder. If the accident was a bad one, and the consumer is found to be at fault, a judgment may be entered against him for a sum he cannot hope to pay during his lifetime. Worse, the court may order his home and other possessions attached and sold to satisfy the judgment. If these assets are insufficient, he will still be liable for the balance.

If the consumer is a claimant against the policyholder of an insolvent insurer and that policyholder is found to be at fault, it may be that the policyholder has no assets from which to satisfy a judgment against him. The consumer must hire an attorney and proceed against his own insurance company under the insolvency clause of his uninsured motorist coverage. His chances of any recovery are limited and in any event subject to the limits of the uninsured motorist coverage, which in most States is $10,000 to $20,000.

Returning to the policyholding consumer, and assuming he has no claim against his defunct insurer and no liability to other parties, we still find that he must suffer loss. First, he is notified that his policy is void because of the insurer's insolvency. If he attempts to recover the unearned premium, his demand is likely to be flatly rejected by the liquidator, who is concerned with conserving the company's assets for the payment of other claims. The consumer must then seek other coverage, ending up paying twice for the same protection.

If the consumer is unfortunate enough to be a policyholder of a mutual insurer whose members are subject to assessment for the company's losses, the consequences of an insolvency can be catastrophic. Let us assume that the consumer has no claims or liabilities. He purchases new coverage and dismisses the insolvency of his previous carrier from his thoughts. Years later, he receives a form letter from the liquidator of the defunct insurer demanding payment of an assessment based on premiums paid while he was insured by the company. The assessment may amount to several hundred dollars and the consumer has no recourse against its imposition. We submit for the record several letters from consumers describing the effects of these assessments.

Senator Moss. They will be received and printed, following your testimony.

(The material referred to follows:)

CHICAGO, ILL., *February 3, 1969.*

Re MULTI-STATE INTER INSURANCE EXCHANGE

DEAR MR. DRAEGER: With further reference to our conversation—In 1962 my son, Conrad A. Hecker, purchased a new car from Milo Brooks Ford Agency. Milo Brooks supplied liability insurance through Paramount Insurance Company, 30 North LaSalle Street, Chicago, Illinois 60602. Since Conrad was under age my name appears on the car and insurance.

My son is now in the army—the 724th Transportation Company activated last May, 1968. We have discussed this transaction in letter and by phone and neither of us recollect doing business with Multi-State Inter Insurance Exchange.

A summons was issued and served. I am to appear in court February 6, 1969, and have been assessed two hundred seventy six dollars and forty cents.

The plaintiff is listed as Leonard M. Groupe, 30 West Washington Street, Chicago, Illinois.

On contacting Mr. Groupe (on receipt of a form letter with a copy of the summons) he sent me a copy of the policy from Multi-State inter-insurance exchange. This policy or form is not signed by Paramount or me. The summons and the letter are Xerox copies, neither signed, dated, notarized or personalized.

Nowhere does he mention how and by whom the assessment was made. Nowhere does he list the amount of debt incurred by Multi State Inter Insurance Exchange. Who is Leonard Groupe. How was he appointed?

If you can shed any light on any of the above I'd appreciate it. Thanks ever so much.

SYLVIA HECKER.

P.S.—Copies of all forms sent me attached.[1]

CHICAGO, ILL., *June 5, 1968.*

BEELINE: Please help me. About three years ago, my son obtained auto insurance with Paramount Insurance Company. We were not aware that this was an agency that got insurance through Bell Mutual Insurance Company.

Since my son was a minor at that time, I was responsible for him. Last week, a man from the Sheriff's Office gave my daughter "some papers about a defunct insurance company" to give to me. I live upstairs of my daughter. These "papers" turned out to be a summons.

When I called the number on the summons. I was informed that in addition to the two hundred dollars I was being sued for, I must also pay fifteen dollars for having the summons issued.

I was never notified of the bankruptcy of Bell Insurance. The only way I was informed was after cancelling the insurance and waiting almost two months for a refund of the premium paid in advance, I called them and was told they were in the process of filing bankruptcy and I would be notified. I never was.

All this time, I was under the impression that the courts were settling this matter, and completely unaware that this was a mutual company making me liable for one year's premium for up to twenty years. Is this legal? Is this the only payment they can demand or can they issue another summons when more money is needed at a later date?

The court date is July 3, 1968, so, please, I need an answer now. I am enclosing a self-addressed stamped envelope.

Thank you,

Mrs. JOSEPHINE HUENING.

CHICAGO, ILL., *January 31, 1969.*

DEAR SIR: I am writing, hoping that you can give us some help with this problem.

My husband and I have been assessed by the *Multi-State Insurance Exchange* of which I am enclosing papers so you may know full details.

My problem is that we are unable to pay this at this time, and unable to obtain an attorney. My husband does construction work and hasn't been able to put in full time due to weather. And we are already behind in our current bills, and just trying to hang on until spring. We are behind now because of two fires we had in the house, January of 1968 and February of 1968 due to the furnace. We have really had a struggle to repair and replace things that the insurance on the house did not cover. And haven't finished yet, just able to live in it. I took ill with all the worry and have just been able to work part time, then two weeks ago I had another attack and the doctor has had me in bed under medication since. He says that if I don't stay quiet and stay in bed I will have to be hospitalized. So I can't go into court. And my husband's boss said that he must come as they are short of men and have to pour concrete today, they have to work as weather permits. I am now with All-State Insurance so I called my agent Mr. Kosic, to see if they could offer me some advise. He referred me to the Bee-line.

He thought the amount could be cut so we could handle it or postponed until my husband is working full time and able to pay it. We cannot borrow the money as we have two loans now. We would like to keep our credit good and not lose our house.

If you can help us in any way at all we would deeply appreciate it. As it would be a lot of worry and strain off of my mind and nerves which has caused my condition.

Sincerely,

EDWARD DORSEY,
JOSPHINE DORSEY.

---

[1] Some of the forms have been placed in committee files.

STATE OF ILLINOIS DEPARTMENT OF INSURANCE,
BUREAU OF LIQUIDATIONS,
Chicago, Ill., December 16, 1968.

EDWARD JOSEP DORSEY,
Chicago, Ill.

DEAR SIR OR MADAM: Several months ago, a Notice of Assement was sent by the Department of Insurance to you as a former policyholder of the Multi-State Inter-Insurance Exchange, now in liquidation. This assessment resulted from automobile insurance issued in your name in 1962 or 1963. Although Multi-State became insolvent and went out of business, its policyholders remained legally liable for an assessment in an amount equal to the original premium.

The Circuit Court of Cook County has ordered each policyholder during the period between November 30, 1962 and November 29, 1963 assessed regardless of when the policy expired or was cancelled. According to the records of the Department of Insurance, payment of this assessment by you has not yet been made.

The law requires the Director of Insurance of the State of Illinois to take such steps as may be necessary to collect this assessment. (*Section 819 (2), Chapter 73, Illinois Revised Statutes*). Your file has been referred to the undersigned, attorney and agent for John F. Bolton, Jr., Director of Insurance of the State of Illinois for the purpose of enforcing collection of this assessment.

I am now preparing to institute legal action against you to compel you to pay this assessment. I will furnish any information or cooperation you may need to pay this legal obligation without your being taken to court. Unless I hear from you within the next three days regarding arrangements to pay, a summons for you to appear in court will be issued.

No further notices will be sent—govern yourself accordingly.

Very truly yours,

LEONARD M. GROUPE.

Returnable in Room No. 602, Chicago Civic Center, 9:30 a.m. Sharp

IN THE NAME OF THE PEOPLE OF THE STATE OF ILLINOIS

In the Circuit Court of Cook County, Illinois
Municipal Department, First District

Name All Parties:

People of the State of Illinois ex rel John F. Bolton, Jr., Director of Insurance, State of Illinois, as liquidator of Multi-State Inter-Insurance Exchange, an inter-insurance exchange, plaintiff *v.* Edward & Joseph Dorsey, 9009 S. Dauphin, Chicago, Ill., defendant.

No. 68M1 170842.

Amount claimed, $326.58.

SUMMONS

To each defendant:

You are summoned and required either:

1. To appear in person in Room 602, Chicago Civic Center, Chicago, Illinois, at 9:30 A.M. on January 31, 1969, or

2. To file your written appearance by yourself or attorney in Room 602 at or before 9:30 a.m on that date, or

3. To file your answer to the complaint in Room 602 at or before 9:30 A.M. on that date.

If you fail to do so, a judgment by default may be taken against you for the relief asked in the complaint.

To the officer:

This summons must be returned by the officer or other person to whom it was given for service, with indorsement of service and fees, if any, immediately after service, and not less than 3 days before the day for appearance. If service cannot be made, this summons shall be returned so indorsed.

This summons may not be served later than 3 days before the day of appearance.

Name: Leonard M. Groupe
Attorney for: Plaintiff.
Address: 30 W. Washington St.
City: Chicago, Illinois 60602.
Telephone: [redacted].

Witness _____, 19____,
_____
Clerk of court
Date of service: _____, 19_____

[To be inserted by officer on copy left with defendant or other person]

NOTICE TO PLAINTIFF

*Not less than 28 or more than 40 days after issuance of summons if amount claimed is $500 or less; not less than 21 or more than 40 days after issuance of summons if amount claimed is in excess of $500.

NOTICE TO DEFENDANT

1. This case will not be heard on the day for appearance specified above. If you have filed your written appearance or answer, you need not appear in person on that day.
2. If the complaint is notarized, your answer must be notarized.
3. On the day for appearance specified above, the following will occur:
   (*a*) If you have not obeyed this summons, a judgment or an order of default will be entered against you. Judgment is entered only if the amount claimed is liquidated, the complaint is notarized, and a military affidavit is filed. Otherwise proof will be taken in Room 1307 and judgment may be entered.
   (*b*) If you are sued in forcible detainer, you need not file an answer. Your case will be heard on the 7th day after the day for appearance specified above, at 9:30 A.M. in a courtroom designated by the Presiding Judge.
   (*c*) If you are sued for $500 or less and no jury is demanded, you need not file an answer. Your case will be assigned for trial on the 14th day after the day for appearance specified above, at 9:30 A.M. in a courtroom designated by the Presiding Judge.
   (*d*) In all other cases, if you have filed your appearance on time, you must file your answer not later than 10 days after the day for appearance specified above. On the day for appearance your case will be postponed 21 days to the Default-for-Want-of-Answer Call at 11:00 A.M. in Room 1307. On the Default-for-Want-of-Answer Call, if you have not filed your answer, a judgment or an order of default will be entered against you. But, if you have filed your answer, your case will be postponed for trial on a date in a courtroom designated by the Presiding Judge.
4. Late filing of an appearance or answer will not relieve you from a judgment or default order except by court order.

MATTHEW J. DANAHER,
Clerk of The Circuit Court of Cook County.

Complaint Verified

THE MUNICIPAL COURT OF CHICAGO

First Municipal District of the Circuit Court of Cook County, Illinois

People of the State of Illinois ex rel John F. Bolton, Jr., Director of Insurance, State of Illinois, as Liquidator of Multi-State Inter-Insurance Exchange, an Inter-Insurance Exchange, plaintiff, *v.* Edward & Joseph Dorsey, 9009 S. Dauphin, Chicago, Illinois, defendant.

No. 68M1 170842.

Amount claimed $326.58.

Return date January 31, 1969.

COMPLAINT

The plaintiff claims as follows:

1. That by order of the Circuit Court of Cook County, Illinois, in case entitled "People of the State of Illinois vs. Multi-State Inter-Insurance Exchange," case No. 64 CH 5262, the Director of Insurance, State of Illinois, as Liquidator, was authorized, directed and empowered to levy an assessment against the members or policyholders of the said Multi-State Inter-Insurance Exchange who were policyholders at any time during the twelve months ending November 29, 1963 regardless of when said policy of insurance began or expired, in an amount equal to the total premium stated in the policy.

2. That pursuant to the above mentioned order, the Director of Insurance of the State of Illinois, as Liquidator, made the levy of assessment in the manner and form as provided in said order, and the levy of assessment was approved by order of court in the above entitled cause on the 31st day of August, 1966.

3. That the defendant became a member or policyholder in said Multi-State Inter-Insurance Exchange on 10/16/62–6/13/63 upon issuance of policy number 32181–53200 which was in effect at some time during the twelve month period in which all policyholders were ordered assessed.

4. That the defendant is legally liable for such assessment in the sum of $326.58 and although the Plaintiff had made demand for payment, the defendant has failed and refused to pay.

5. That Section 819 (2) of the Illinois Insurance Code, Chapter 73 of the *Revised Statutes of Illinois* requires that "The Director shall take such steps as may be necessary to enforce collection thereof."

Wherefore, plaintiff prays for judgment in the sum of $326.58 and costs of this suit.

I, Leonard M. Groupe, on oath state that I am the attorney and agent of plaintiff in the above entitled action. The allegations in this complaint are true.

Signed and sworn to before me December 19, 1968.

_____,
Notary public.

Name: Leonard M. Groupe.
Attorney for: Plaintiff.
Address: 30 W. Washington St.
City: Chicago, Illinois 60602
Telephone: [redacted].

MATTHEW J. DANAHER,
Clerk of the Circuit Court of Cook County.

Mrs. ANGEVINE. These individual experiences unfortunately are not isolated. They have befallen hundreds of innocent American consumers as the result of insurance company insolvencies. We do not seek to fix the blame for these failures; our purpose is only to advocate means of preventing the misery and hardship they bring to consumers.

S. 2236 applies the basic insurance principle—spreading risk over a large number of units—to create a national guarantee fund to indemnify the victims of property and casualty insurance company insolvencies.

Equally important, it provides for machinery to prevent such insolvencies. It authorizes the establishment of uniform standards and criteria for the admission of insurance companies to guaranteed status, and assures adherence to these standards through provisions for effective enforcement.

The best-intentioned State insurance commissioner is powerless to enforce his will beyond the borders of his home State. Similarly, the commissioners' organization, the National Association of Insurance Commissioners, lacks the essential tool to achieve uniformity of quality in State insurance regulation—the power to enforce its will on its constituent commissioners.

We believe the nationwide enforcement powers provided in S. 2236 will be of invaluable assistance to the NAIC in its efforts to upgrade State insurance regulation.

We do not believe that a State-by-State treatment of the insolvency problem is effective. The fundamental weaknesses of existing regulation cannot be corrected on a State-by-State basis. Without a central enforcement agency and communications center, disasters like the Inland Empire and State Fire and Casualty insolvencies cannot be prevented.

These two insolvencies, studied in detail by the Senate Antitrust and Monopoly Subcommittee, illustrate dramatically the inability of State regulators to—

(1) Prevent the interstate shuffling of securities from company to company to avoid the scrutiny of examiners;

(2) Compel other States to turn over the assets of a defunct company in liquidation proceedings;

(3) Promulgate and enforce uniform standards and procedures for the hiring of examiners and the conduct of examinations;

(4) Force other States to communicate information affecting policyholders in their own States.

States obviously do not support the so-called Uniform Insurers Liquidation Act, first proposed in 1939, since only 28 States have adopted it, up to this time.

We feel strongly that any State plan consisting of the uninsured motorist endorsement with insolvency protection and a postassessment insolvency fund is inadequate for the protection of American consumers from insurance company failures.

We believe S. 2236 will provide the protection consumers need against insolvencies at a price all consumers can afford. Accordingly, the Consumer Federation of America endorses S. 2236 and urges its prompt enactment by the Congress.

Thank you, sir.

Senator Moss. Thank you, Mrs. Angevine, for this very fine statement.

Of course, all of us agree that consumers have a very vital stake in the problem of insolvency, and therefore need protection that is sought, at least, in this bill that is before us.

It seems to me that your testimony says that we can't wait any longer to attack this problem, and therefore the argument that we should wait and see if the States won't do it on their own is not valid. Is that what you are saying?

Mrs. Angevine. We feel keenly that they have not been doing it adequately, and that if a central agency is needed, the Federal Government, can, through this means, develop the kind of an agency we need, which works also with the States. So the States are not being left out of this. It is a State-Federal relationship which we highly endorse.

Senator Moss. You mention that the tax dollars are lost because of increased litigation stemming from insolvency. Are you referring to the litigation connected with the uninsured motorist endorsement or other claims too?

Mrs. Angevine. I was thinking in terms of the uninsured motorist, yes; although I think when we think in terms of the tax dollar on litigation, you can make it a great, broad one. Because, of course, whenever there is litigation that goes on and on, we have the courts tied up in this, too, eating up tax dollars. You can build this up to be quite a case when you're talking about lengthy litigation of any sort.

Senator Moss. In cases such as we were discussing with the previous witness, where there actually is a loss of jobs sometimes by a policyholder because of his inability to collect his insurance and meet his obligations, and maybe have his wages garnished, it heaps an indirect cost on the taxpayer, doesn't it?

Mrs. Angevine. Yes, sir. And one of the most interesting letters of the ones I submitted for the record is from a woman whose husband paid one of these insolvency claims of a mutual company that had become insolvent, just in order to protect his job. They could not afford to pay this $300, but they did pay it so that he wouldn't lose his job.

She said in her letter that she was a native of England, and had always had high respect for the law, that you obey the law at all times. She felt in this case that the law was wrong. If it had been up to her, she would have gone to jail rather than pay.

Senator Moss. Well, I certainly appreciate your testimony, Mrs. Angevine. It has been very helpful. Thank you for coming.

Mrs. ANGEVINE. Thank you, sir.

Senator Moss. Our next witness is Mr. James E. Bailey, attorney, representing the American Society of Insurance Management. Mr. Bailey is an old friend of this committee, and we are glad to have you here before us today, Mr. Bailey.

STATEMENT OF JAMES E. BAILEY, ATTORNEY, REPRESENTING THE AMERICAN SOCIETY OF INSURANCE MANAGEMENT, WASHINGTON, D.C.

Mr. BAILEY. Thank you, Mr. Chairman.

I have a rather short statement today. Our legislative chairman had planned to be here today, and I would have appeared with him as counsel. However, I will be appearing today alone.

My name is James E. Bailey; I am a member of the District of Columbia Bar with offices at 1030 15th Street NW., Washington, D.C. I make this statement as the retained legislative counsel representing the American Society of Insurance Management, Inc., 8 West 40th Street, New York, N.Y.

The American Society of Insurance Management—known as ASIM—is the largest nationally organized group of insurance consumers in the United States. ASIM's current membership consists of 1,800 corporate consumers, with more than 2,650 risk management personnel, who are divided among 39 chapters in the United States and four in Canada. We also have members in Mexico, Germany, France, and England.

In total aggregate premium dollars, for all types of insurance, including workmen's compensation, our members spend an estimated $8½ billion annually.

Our national legislative committee has studied the insolvency problem and has authorized this statement on behalf of the ASIM.

The American Society of Insurance Management, Inc., is concerned about the problem of insolvent insurers. While our members are learned in insurance matters, on occasion, some one or more of our members have suffered a loss due to insolvency.

ASIM is opposed to the legislation under consideration today. We do not believe that S. 2236, a bill to create a Federal Insurance Guaranty Corporation is necessary, and we do not favor its enactment. It is our position that no Federal legislation should be enacted in this area until the States have had an adequate opportunity to develop and consider legislation on the problem of insolvencies. During the recent legislative year, a number of States have enacted laws designed to provide protection to policyholders, and to strengthen the insurance laws of the State. We believe that the States are doing an effective job of regulating insurance and that workable and enforceable State statutes can be developed and enacted to solve the insolvency problem.

Enactment of Federal guaranty fund legislation is viewed by our members as an unwarranted incursion into the regulatory role of the

States. The State regulatory officials and the National Association of Insurance Commissioners have, over the years, met every challenge, problem, and new situation with adequate measures to solve or control them. There is no reason to believe that these capable State officials will not perform their regulatory duties in creditable fashion now.

It is our considered opinion that the Federal Government does not have any advantages to offer to the insurance industry or the States in exchange for an extension of Federal jurisdiction into the business of insurance via the insolvency fund route.

The powers under the present bill are extensive. Many of our members do not believe that Federal regulation would be confined to the area suggested in this legislation, but rather, that Federal jurisdiction would extend to many other facets and areas presently being adequately regulated by the States. These areas include examinations, qualifications for doing business, financial requirements, and many other areas.

Members of the society are concerned about the high cost of money, the increasing costs of insurance protection and the tightening of the insurance market. Our buyers must constantly review their coverages and their entire insurance program to see that they are getting the best possible insurance for the dollars they spend. We believe that the ultimate costs of the Federal Guaranty Corporation will be passed on to the consumer through increased premiums. While the legislation purports to protect the consumer, we do not believe that it offers great protection. We believe that it will cost more to establish the fund and to implement it than current losses caused by insolvencies.

It is our considered opinion that State insurance commissioners and State legislatures are responsive to the consumer's needs in insurance. Further, we encourage the commissioners, through the National Association of Insurance Commissioners, to continue improving their statutes by providing better insurance protection.

It is the position of the American Society of Insurance Management that postassessment funds provide the best answer for financing protection. Postassessment funds deal with a known loss and do not get into speculative or undetermined losses. The administration costs are accordingly less and the ultimate cost to the individual policyholder would be less.

Our society does not believe the problem as great as some proponents of this legislation would lead the public to believe. We would suggest to the committee that it consider and adopt a moratorium on processing this legislation. Such a moratorium for a period of several years even, would give an adequate time for the State legislatures to act. I earnestly suggest that the committee take no action on legislation such as S. 2236. The public has faith in the present insurance system and I believe that system is attuned to the needs of the public. It can quickly respond when required to do so. Our faith is in the individual State insurance commissioner and his department. Through the National Association of Insurance Commissioners they receive considerable information bearing on interstate operations and they have these sources of information readily available. We have not noticed any instances where commissioners have been unwilling to act, or have taken an undue amount of time to respond to a situation when corrective action is necessary.

Accordingly, for the reasons stated above, the American Society of Insurance Management does not favor enactment of S. 2236.

Senator Moss. Thank you for your statement, Mr. Bailey, given on behalf of the American Society of Insurance Management.

Your organization represents corporate consumers, is that correct?

Mr. BAILEY. Yes, corporate consumers, including American business, public bodies such as cities, departments of cities, counties. We have many universities, we have many church bodies. We have archdioceses scattered throughout the United States that belong. We have some small business enterprises that have large insurance needs. We may have one company that would have only four employees, but spends several millions of dollars for insurance. We have large aircraft companies, steel companies. You name the industry, we have the companies, represented in our organization.

Of the 500 top corporations in the United States, more than 85 percent belong to ASIM.

Senator Moss. In your statement you said we ought to wait and give the States an adequate opportunity to develop legislation on this problem of insolvency, and indicated that the National Association of Insurance Commissioners has always responded to a situation when corrective action is necessary.

The National Association of Insurance Commissioners has been organized since 1871. How much longer do we have to wait for them to take adequate action on this?

Mr. BAILEY. Over the years, they have encouraged their State departments to act in certain smaller areas, and in recent years, since 1961, more States have become interested in insolvency provisions related to small areas of insurance, not quite as broadly as the bill under consideration, that is true. But even in the last year, many States have studied this type of legislation and some have enacted it.

The departments are aware of the need for action in this area, and I am sure they will act. That is why we suggest a moratorium. We would suggest a moratorium which would expire at the end of the next Congress. Not the Congress that we are in, which is the 91st Congress, but at the end of the 92d Congress, which would effectively give slightly more than 3 years for consideration of this legislation on a State level.

The reason we would suggest 3 years is that next year only 27 States will have their legislatures in session, many of which will be confined to strictly fiscal matters, and they will not be getting into areas such as we have under consideration here today, unless they would do it by way of a special session.

Senator Moss. Suppose we waited until 3 or 5 years, whatever time it was determined that we should wait to see if the States act, and we find that three-fourths of them do, or 80 percent of the States do and the others don't, then what is our position to be?

Mr. BAILEY. The problem is not acute in every single State. I am sure when the NAIC reports out its model bill which they expect to do in December at their meeting in New Orleans, it won't take very long before many of the States will begin to crank up their legislative activities and get busy in this area.

Senator Moss. But I am still talking about areas where the States do not act. There is no way we can compel them to act.

Mr. BAILEY. That is true, but with a strong lead of many of the important insurance States, many of the others will fall in line and I am sure you will see great improvements in this type of legislation on the State level.

Senator MOSS. As a matter of fact, several of the States acted after this bill was introduced and proposed, isn't that right, three or four of them?

Mr. BAILEY. That is true, and some of them acted before it, too.

Senator MOSS. I think it was Mrs. Angevine who made reference to the fact that we have had this uniform Liquidation Act for the States since 1939 and only 28 so far have adopted that.

Isn't that a marker of what might happen in this field?

Mr. BAILEY. Well, I don't consider that to be a serious indictment of all the rest of the States that haven't.

For one reason or another the conditions in the States may be different so that it is not needed.

Senator MOSS. What about the problem in Maryland, as was discussed earlier?

Mr. BAILEY. We like to think of our buyers as being sophisticated buyers. Our risk managers are engaged on a full-time basis. They know where to go for information on insurance companies. This information is available at the departments. Great public relations work has been done by Mr. Steers in Maryland to get people to call his department in case of doubt. They can find out what companies are solid.

With a little bit of investigation, I think much of this could have been avoided. You are not forced, nor compelled by anyone, to place your insurance with a company which is shaky. If you want to look into it a little bit further before you spend your dollars, you could have saved in many instances, the money that these people spent.

Senator MOSS. I would concede your point, that your clients are sophisticated, much more sophisticated about buying insurance than would be the average consumer, but the average man, without knowledge of where he can go and get background information—as a matter of fact, he is likely to buy his policy because some salesman comes to him and tells him it is a good policy and convinces him that he ought to do it, and he doesn't have the sophistication nor the means of checking that company out. So he buys it, and then it becomes insolvent. What is going to happen to him?

Mr. BAILEY. I didn't get the last of your question.

Senator MOSS. I say, he buys the insurance, and pays his premium and then an insolvency comes along and he has no recourse.

Mr. BAILEY. Well, he would have to wait for the settlement of his claim, for the liquidation of that company, that is true.

Senator MOSS. That is what the witness before was explaining. Even though Maryland had taken the step of setting up the fund, it hasn't paid out any of the money.

Mr. BAILEY. Some of these liquidations take a great deal of time. They are intricate. From a legal standpoint, it sometimes takes many years to move.

Senator MOSS. Some of them take 10 or 11 years.

Mr. BAILEY. The time interval has been shrinking, because you have been getting better people in the departments who have been handling them and the procedure has been speeded up in many instances.

Senator Moss. I harken back to the Federal Deposit Insurance again. I had some money in a bank that went broke in the big depression, and that was liquidated over more than 10 years' time. I got a little dab—I never did get more than about 20 percent of it back—I would get a little dab every 3 or 4 years.

Mr. BAILEY. I think today you are finding that the FDIC is still active in paying off claims over a period of years on some of the insolvencies, some of the difficulties that these banks have gotten into, and in just recent months, there have been quite a number of bank closings.

Senator Moss. It is true, we have a small country bank which became insolvent because of speculations made by the manager. The FDIC was there immediately and it wasn't more than 2 weeks until that bank had been turned around and assigned elsewhere, and all those deposits were guaranteed 100 percent.

I couldn't help but think back to the times when they were going broke and we just couldn't get our money and what a difference it is now under that system.

That is what appeals to me so strongly about the basic thrust of this bill, to try to follow that same general pattern with, of course, adjustments between insurance and banking. There are some differences, but the basic idea is much the same.

Mr. BAILEY. Yes; the basic idea may be much the same; however, in a situation involving the banking business, or the insurance business, no one is going to tell you when he is going to steal.

So unless you have adequate regulations in your State department of insurance, or in the Federal program, if it became enacted, for that matter, you would never know for sure when these are going to occur.

So the States have adopted protection in the form of regulations. They expect to extend it and statutes are being drawn. The American Mutual Insurance Alliance has a model bill which has been received very well by the States this past year.

I think great improvement will be made. I implore the committee to give the industry further opportunity—and I am not connected with the industry; don't misunderstand that I am. We belong to no trade association, we belong to no other groups, we are not involved with the companies in any way. I speak strictly for our own members.

Senator Moss. Thank you very much for coming to testify, Mr. Bailey, and giving the position of the organizations you represent. We are glad to have this for our record to consider.

Mr. BAILEY. Mr. Chairman, I thank you very much.

Senator Moss. Thank you.

We had one more witness, but he has been unable to come.

Mr. Ralph Nader was scheduled, and he has indicated he is not able to be here this morning, and has asked for permission to submit a written statement for the record.

That permission will be granted, or if there are further hearings, when we hear witnesses orally, he will be given an opportunity to testify then.

Senator Moss. That concludes the witnesses that we have for this morning.

The committee will be in recess.

(Whereupon, at 11:17, the committee was recessed, subject to the call of the Chair.)

FEDERAL INSURANCE GUARANTY CORPORATION

TUESDAY, FEBRUARY 10, 1970

U.S. SENATE,
COMMITTEE ON COMMERCE,
Washington, D.C.

The committee met at 11 a.m. in room 5110, New Senate Office Building, Hon. Frank E. Moss, presiding.

Present: Senators Cotton, Hart, Moss, and Pearson.

Senator Moss. The committee will come to order.

I apologize for being a few moments late. Like everyone around here, I sometimes have to spread myself a little thin. I've just come from chairing another hearing.

We are glad to welcome you here to this final hearing on S. 2236, a bill to establish a Federal Insurance Guaranty Corporation.

We are pleased to have visiting with us—I invited her to sit at the bench with us—Senator Maurine Neuberger who was formerly a member of this committee. We welcome her back whenever she can come. We are glad she is sitting in with us to listen to the testimony today.

Today the Senate Commerce Committee begins the final hearing on S. 2236, the Federal Insurance Corporation Act. I personally welcome the opportunity to chair the final hearing on this important consumer bill which would protect the American public against the tragic consequences of property and casualty insurance company insolvencies.

Previous hearings solicited the views of the insurance industry, the State insurance commissioners, and consumer groups. For the past several months the committee has been analyzing the testimony of the various witnesses whose views on S. 2236 differ markedly.

Despite the hesitancy of some opponents to come forward with constructive suggestions for further protecting the American public from insurance company insolvencies, the hearings have helped the committee in its search for complete solutions to the insolvency problem. It is hoped that the testimony from the administration today will further add to the committee's record and chart the appropriate direction for Federal legislation which is needed in this area.

Before asking the administration witnesses to come forward, I would like to introduce copies of correspondence which have come to the attention of the committee. These letters may explain why in recent weeks the Congress has been flooded with mail opposing S. 2236. The following letters from an insurance company and a trade association ask for this negative correspondence and indicate the source of much of the "public outcry" against S. 2236:

1. Letter from Kemper Insurance Co. to "our staff" asking for their help in defeating S. 2236 which the company says "would

39-251—70——18

set up a Federal czar with regulatory power over virtually every aspect of the insurance business."

2. A letter from the American Mutual Insurance Alliance to "Mutual Companies and Associations" which says that S. 2236 "could put many small companies out of business."

(The letters referred to follow:)

KEMPER INSURANCE CO.,
January 26, 1970.

To Our Staff: Your help is needed to defeat a federal bill which we believe is unnecessary, harmful to the insurance business, and not in the interest of the insuring public generally. Senate Bill 2236 is now pending before the Senate Commerce Committee. This bill would establish a Federal Insurance Guaranty Corporation from moneys collected from insurance companies to guarantee the payment of obligations of insolvent insurance companies.

While we favor the objective of protecting people against losses arising out of insurance company insolvencies, we are convinced that the establishment of a federal guaranty fund proposed by this bill is completely unnecessary, and, moreover, will bring about a direct, immediate and comprehensive system of federal regulation of the business of insurance.

The bill, as introduced, would set up a federal Czar with regulatory power over virtually every aspect of the insurance business. It would create a fund of up to $500 million through payments received from insurance companies which, of course, should inevitably wind up as a cost to policyholders. The bill contemplates such extensive federal regulation that it will inevitably replace state regulation, or even worse it could mean dual regulation with double expense. No insurance company could transact business in the various states unless and until it subscribed to the Federal Corporation. No insurance company could continue to do business unless it satisfied the new federal bureaucracy that it was solvent, that its expenses were "reasonable", that its ratio of surplus to premiums was correct, and that its loss and expense reserves were adequate. In addition, the federal people would have to be content that the insurance companies' reinsurance arrangements were satisfactory, that its investments were sound, and even that its management personnel were qualified.

It is actuarially estimated that the cost of administering the federal fund will amount to six times the amount of insolvency claims; that is, it will cost $6 to pay out $1 in losses. In our opinion, this is a costly, wasteful and unnecessary expenditure.

The major reason we think this bill is unnecessary lies in the fact that its proponents have grossly exaggerated the economic impact of insolvencies of insurance companies and, moreover, the insurance industry itself, together with the individual states, are fully capable of handling the problem on the state level. As you know, the Uninsured Motorists coverage now contains insolvency protection and this step alone has eliminated almost all of the problem.

The state insurance commissioners are moving to put into operation in each state an efficient and effective method of closing the small gap which remains. The National Association of Insurance Commissioners has adopted a positive program calling for the enactment of state post insolvency assessment laws. New York, New Jersey and Maryland have had for some time motor vehicle insolvency funds, and New York has recently expanded their fund to cover fire and other casualty lines. Recently California, Michigan, Wisconsin and New Hampshire have adopted their own laws, and it is almost certain that many of the states will have this as a first order of business at their next legislative session.

In our opinion, Senate Bill 2236 is a classic example of an unwarranted attempt by proponents of big federal government to intrude into an area of regulation properly the business of the individual states. This is particularly objectionable where the states have demonstrated their willingness and capability to act.

It is urgent that steps be taken right now to defeat this bill. The Senate Commerce Committee, under the Chairmanship of Senator Magnuson, will hold a one day hearing on this bill on February 10, and a committee vote will be taken at that time or within a few days. We urge you to contact both of your senators by letter, wire, or by personal conversation to express opposition to Senate Bill 2236 and to urge them to vote against it. It would be helpful if you would ask your senators to express opposition to the members of the Senate Commerce Committee and to prepare to vote against the bill if and when it comes to a vote on the Senate floor.

The action of the Senate Commerce Committee will be very important, so we urge that those of you who have a senator on the committee to immediately contact him so that he may have the benefit of your expression of opposition during the Committee's deliberations.

If it is convenient for you to do so, it would be helpful for us to know what reaction you get from your senators.

Sincerely,

JAMES S. KEMPER, Jr.

AMERICAN MUTUAL INSURANCE ALLIANCE,
January 20, 1976.

INSOLVENCY LEGISLATION—SPECIAL REPORT TO MUTUALS

To Mutual Companies and Associations: When we discontinued our Mutual Memo several months ago, we promised to correspond with you from time to time on matters of special interest to mutual companies.

This first report deals with the imminent threat to your interests contained in Senate Bill 2236. As detailed in the attached Fact Sheet, this bill would create a Federal Insurance Guaranty Corporation with sweeping powers to examine, regulate and collect a special "tax" from property and casualty insurers.

If this bill is enacted, it appears that most if not all, farm, county and township mutuals will become subject to its requirements along with other companies. The jurisdictional test is whether an insurer is "engaged in the business of issuing or reinsuring property, casualty or surety insurance policies in interstate commerce or engaged in the business of issuing property, casualty or surety policies which are reinsured (in whole or in part) in interstate commerce."

Thus, any company purchasing reinsurance from multistate carrier presumably would have to meet the requirements of the proposed federal law. It is possible that the issuance of an automobile insurance policy or a property insurance policy with off-premises coverage also would be construed as "issuing a policy in interstate commerce," since losses under these policies can occur in states other than the policyholder's state of residence. The definition of "interstate commerce" has been so expanded in recent years that almost any activity can be held to fall within its boundaries.

The implications of S. 2236 are especially onerous for assessable mutuals:

1. They would be required to pay a new federal "premium tax" of ⅛ of 1%, even though there is some question whether their own policyholders would ever receive any benefits from the federal insolvency fund to be created under the bill. At the very least, the policyholders would bear the major portion of any loss under the premium assessment provisions applicable to farm, county and township mutuals in most states. The federal insolvency fund would come into play only after all available policy assessments had been made and after recovery by claimants and policyholders from a state insolvency fund where such a fund exists.

2. Assessable mutuals also would become subject to far more onerous and time consuming regulatory requirements, including federal examinations. Moreover, future rules promulgated by the proposed federal corporation with regard to surplus, reserves, expense ratios, reinsuance, managerial qualifications and assessability of policies could put many small companies out of business.

For all of these reasons and others discussed in the Fact Sheet, we urge you to take action now to make known your opposition to S. 2236 by contacting your United States Senators.

The next few weeks are critical. Congress reconvened on January 19, and final hearings on S. 2236 are scheduled to begin in the Senate Commerce Committee on February 10. With 6 of the 18 members of that committee listed as co-sponsors of the bill, there is a strong possibility that it will be reported out of committee. Thus, it is important to express your view now to your Senators, whether they are on the Senate Commerce Committee or not.

Sincerely,

PAUL S. WISE, *President.*

Senator Moss. In my opinion, citizens should be encouraged to communicate their views to their representatives in Washington, D.C. But those representatives should know that companies or corporations have directed their employees to undertake letterwriting campaigns based on the companies' views "of the facts."

And now will Secretary Cherington and Secretary Passer please come forward to present testimony on S. 2236? We welcome the administration's views on this important bill.

Senator COTTON. May I make a brief statement?

Senator MOSS. Yes, indeed.

Before the witnesses speak I would like to ask Senator Cotton, the ranking minority member on the full Commerce Committee, for any statements that he has.

Senator COTTON. Mr. Chairman, first I want to join in the welcoming of our former highly esteemed colleague, Mrs. Neuberger, and join the chairman in his welcome.

Second, I want to compliment the chairman on his devotion and leadership in this measure that is before the committee and compliment him on most of his opening statement. I don't want, however, to let the statement pass without indicating on the record that I am a little puzzled by his comments on the activities of trade associations and of insurance companies in encouraging opposition to this bill.

The purpose of a trade association, as I understand it, is to alert their membership to what they in their opinion believe to be the facts or the fact of legislation upon them and I am sure that no Senator is so naive as not to understand that every kind of organization from the American League on to labor unions, the Farm Bureaus, chambers of commerce, and elsewhere and other fields, frequently encourage their membership to let the Members of Congress know their attitude. I think it is perfectly legitimate.

I note the inclusion of the special reference to the Kemper Insurance Co. and the inclusion of a letter signed by James S. Kemper, Jr., to the staff of his company, I gather. I don't know just why this particular communication was selected.

My acquaintance with Jim Kemper is rather slight. I have known his father, the senior Kemper, for many, many years. I know the only really vicious and wicked thing that he has ever done to my knowledge is that he was for many years the treasurer of the Republican National Committee. [Laughter.]

Whether that has any bearing on this, I don't know.

Senator MOSS. That is news to me, Senator. I didn't know that. [Laughter.]

Senator COTTON. Then I absolve you from that affecting your legislation. I am not criticizing the chairman. I am simply saying through the years that I served here I have anticipated that business concerns as well as other organizations would make their wishes known to the Congress and the very identity of the people who communicate with us rather indicates what business they are in and indicates prehaps the possible reasons for their attitude.

I cannot see any hidden menace in this procedure. That is all I wish to say.

I say it not in any criticism of the chairman, who is always most fair.

Senator MOSS. Thank you very much, Senator. It is very proper that you should point this out. I am glad you did.

Of course we expect to get letters from various trade associations and people of various sorts. I referred to this because of the number of letters being received. One writer sent the committee this Kemper

Insurance letter with a note saying "Thought you might be interested in what the insurance companies are requesting of their employees."

So it was sent by an employee and I thought that I would refer to that to indicate why letters have been coming in in considerable number and negative but—I certainly didn't want to imply that it was improper or reprehensible, in any sense. I just wanted to indicate the direction that things have been flowing since we had our earlier hearings. I hope we have my opening statement in perspective.

TELEGRAM FROM THE AMERICAN MUTUAL INSURANCE ALLIANCE IN RESPONSE TO SENATOR MOSS' OPENING STATEMENT

FEBRUARY 10, 1970.

Hon. FRANK E. MOSS,
U.S. Senate,
Room 5110, New Senate Office Building, Washington, D.C.

In your opening statement at today's hearing on S. 2236, you imply that there is something inappropriate in the fact that we sent an information bulletin on the provisions of S. 226 to mutual segment of the insurance industry. Providing such information is one of the purposes for which our association was created. We believe that we have not only the right but the obligation to inform our constituency and the insuring public about this legislation. How else would the public know of detrimental effect which this bill would have on their interests?

Certainly not from proponents of S. 2236, who have continued to deny that the issue of Federal regulation is involved even after Senator Vance Hartke called this bill the "ultimate assumption of Federal regulation." In the past, power frequently has been assumed by the Federal Government because the public was uninformed.

We feel that the issue of Federal versus State regulation raises profound questions affecting the personal interests of every member of the public. This issue should be debated and decided in the open, and not brought in by back-door methods, wearing the disguise of consumer legislation. There is intense concern among mutual companies over whether they can continue to serve their policy holders efficiently under the kind of Federal regulation contemplated in S. 2236. Some small mutual companies question whether they can even survive for very long under such a system. The alliance believes strongly that the insuring public is best served by State regulation, which is flexible and sensitive to local needs. The letters you have been receiving from chief executives of insurance companies are a reflection of those concerns for policyholders and for the ability of their institutions to continue serving public needs. The alliance agrees with you and other proponents of S. 2236 that the public must be protected against insurance company insolvencies. We and many other groups are taking vigorous action to accomplish that objective at the State level. We are working vigorously for enactment of State legislation to close the last small gaps in existing forms on insolvency protection. Our methods differ but our objectives are the same as yours. We believe these objectives can be accomplished without Federal legislation.

We respectfully request that this telegram be inserted in the record following your opening remarks.

PAUL S. WISE,
President, American Mutual Insurance Alliance,
Chicago, Ill.

Now we are going to have the Honorable Paul Cherington, Assistant Secretary for Policy and International Affairs, Department of Transportation; and Dr. Harold Passer, Assistant Secretary for Economic Affairs, who will be accompanied by Walter Hamilton, Deputy Assistant Secretary for Domestic Business Policy of the Department of Commerce.

Who is it that accompanied you, Mr. Cherington?

JOINT STATEMENT OF PAUL CHERINGTON, ASSISTANT SECRETARY FOR POLICY AND INTERNATIONAL AFFAIRS, DEPARTMENT OF TRANSPORTATION, ACCOMPANIED BY RICHARD WALSH, DIRECTOR OF OPERATIONS, AUTOMOBILE INSURANCE STUDY, DEPARTMENT OF TRANSPORTATION; AND DR. HAROLD PASSER, ASSISTANT SECRETARY FOR ECONOMIC AFFAIRS, ACCOMPANIED BY WALTER A. HAMILTON, DEPUTY ASSISTANT SECRETARY FOR DOMESTIC BUSINESS POLICY, DEPARTMENT OF COMMERCE

Mr. CHERINGTON. I am accompanied by Richard Walsh, head of our automobile insurance study in the Department of Transportation.

Senator MOSS. Very good. We are pleased to have Mr. Walsh here too.

We look forward to having the administration's point of view now from Transportation and Commerce on the bill that we have before us and on which we have had some previous hearings.

So I will call you first, Secretary Cherington.

Mr. CHERINGTON. Well, sir, we have a joint statement, and Dr. Passer will present that on behalf of the administration and both of the Departments, if that pleases the committee.

Senator MOSS. That is perfectly acceptable. We will have Dr. Passer then; proceed if you would.

Dr. PASSER. Mr. Chairman, members of the committee, we are pleased to appear before this committee today to present the views of the administration on S. 2236, a bill to create a Federal Insurance Guaranty Corporation.

This administration is strongly in support of Federal legislation to guarantee that every citizen, every policyholder, and every claimant is properly and fully compensated for his insured losses. We will present an administration proposal for your consideration next month. The insurance customer as well as those injured or those whose property is damaged by others who are insured have a right to expect that their losses will be compensated. The record of the American insurance industry and the State system of insurance regulation fully demonstrates that the vast majority of these consumer rights are properly protected today.

With more than $25 billion of premiums written annually, something less than $25 million of insured property and casualty losses are going unmet each year as a result of insurer insolvencies. The bulk of these involve auto insurance, but the implications and at times the impact reach out not only to other lines of insurance but to the public image of both business and Government regulatory processes as well. The Department of Transportation is concerned about the auto insurer insolvency problem and has learned much about it in the course of the auto insurance and compensation study which it is conducting. The Department of Commerce is concerned about the broader aspects of the problem, including the possible effect of insolvencies on the confidence of our citizens in the business community and the proper treatment of the consumer by business. Together, we speak for the administration when we say that although the problem area is modest in comparison with the insurance in force nationwide, the adverse impact of insurer insolvencies, especially on individuals and smaller insureds, warrants Federal legislation.

It is impossible not to be impressed by the remarkable consensus regarding the importance of the problem shared among those whose views as to its solution are divergent.

The Advisory Committee on Economic Regulation to the Auto Insurance Study, which included the Honorable Richard E. Steward, superintendent of insurance of New York, Honorable Lorne R. Worthington, commissioner of insurance of Iowa, Dean Spencer L. Kimball of the University of Wisconsin Law School, Prof. Richard S. L. Roddis, formerly commissioner of insurance of California, Prof. Samuel Loescher and Prof. Herbert S. Denenberg, identified the problem in the following language:

> We believe that there clearly is a need to guarantee that the insured public throughout the United States be protected from financial loss as a result of the insolvency of insurers.
>
> That need and the national interest in meeting it does not rest upon precise analysis of the frequency and severity of the numerous insurer insolvencies in recent years. Many innocent people, generally those already under stress from injury or loss and often those in our population least able to bear loss, have been the victims. The fact that these numbers have been small in relation to total premium volume or total number of persons insured is irrelevant, for the demonstrated reality of such losses, and the inescapable likelihood of further such losses in the future, undermines confidence in the insurance institution generally.

The auto insurance study's analysis of recent adverse developments in auto insurance underwriting results coupled with the generally unfavorable changes in the market values of securities held by insurers suggest that despite the best efforts of insurers and State supervisory authorities over recent years, an insolvency problem of some dimension remains. Many members of the industry and many State regulators have testified to this. There are still companies in a hazardous financial condition and in danger of insolvency.

We believe that action is needed now. Even though some States have enacted insolvency plans and a number of others are considering doing so, the continuing lack of adequate protection for many consumers from the financial consequences of insolvencies is incompatible with the interests of either the public or the insurance industry. Several remedies are available. The remedy selected must meet the needs of the insurance consuming public effectively and soon.

We also agree that if the insuring public is to be provided the protection it deserves in a timely fashion, action at the Federal level is needed. We are prepared to cooperate in taking that action.

In studying the insolvency problem and reviewing S. 2236 we, like you, have sought advice from many interested parties. All of the major insurance industry associations have been consulted, as has the National Association of Insurance Commissioners. We have conferred with knowledgeable and responsible leaders in industry and in government. All of the 55 members of the four advisory committees to the auto insurance study—representing consumers, State regulators, the industry, and academic specialists—were asked to give us their considered views on these matters; most of them did so and their replies were both thoughtful and thought provoking. One of these groups, the Economic Regulation Advisory Committee, convened a special meeting on the subject and developed its own statement of views on the insolvency problem.

It was the view of this advisory committee that although the objective of S. 2236 was sound, implementation in its present form

would result in the creation of several disincentives to good regulation by the States. The administration agrees. Recognizing that some Federal action would be necessary if the problem were to be met completely, this group proposed a heavy punitive tax on the insurance business of any State which did not move to set up a satisfactory mechanism to protect the public against insolvency-related losses. With this proposed remedy the administration does not agree.

The fact is that reasonable minds do differ as to what regulatory standards should be. Long and arduous debate would stand in the way of the enactment and implementation of a measure which established Federal regulatory standards. Moreover, the very establishment of such standards might very well itself constitute Federal regulation, leaving State regulation a meaningless shell.

The administration believes that consumers should be protected from the financial consequences of insolvencies of insurance companies in the property, surety, and casualty fields. Such protection can be afforded through a guarantee mechanism. This mechanism should be designed to: (1) avoid the unnecessary and undesirable intrusion of the Federal Government into the manner and conduct of State regulation of insurers; (2) avoid the intrusion of Federal influence into the approaches to the insolvency problem which have been or may be adopted by individual States; (3) preclude any unnecessary immobilization of insurance capital; (4) minimize Federal and other administrative burdens; and (5) assure that consumers are fully and completely protected from the financial consequences of insolvencies.

The administration does not favor the enactment of S. 2236 in its present form. We will submit a proposal next month which will apply the following principles:

(1) The activities of the Federal agency should be those only of an administrator of the guarantee mechanism and not a regulator of the insurance industry. The basic supervisory function should remain the province of State supervisory authorities. The Federal agency should work through the State supervisory authorities whenever any question arises as to the solvency of a specific company.

(2) There should be an assessment mechanism to meet reasonable and validated claimant and policyholder losses created by insolvencies through a postinsolvency assessment technique. Such assessment mechanism should be compatible with programs which have been or may be adopted by any of the several States to meet the insolvency problems on a State basis and at the same time avoid the immobilization of insurance capital which is needed to supply the economy's growing demands for insurance and also for the constructive employment of capital generally.

The administration believes that a measure can be developed and enacted which can effectively accommodate the needs and interests of the consumer public, the insurance industry, State supervisory authorities and State governments generally.

The Federal agency contemplated by the administration's proposal would operate on a significantly reduced scale both in size and scope compared with that proposed in S. 2236. The administration proposal would limit the role of the Federal agency to that of a vehicle for compensating the insolvency losses of claimants and policyholders while leaving full responsibility for insurance regulation in the hands of State authorities.

The States would continue to have sole authority for examination of insurers for solvency and would retain full and exclusive regulatory powers.

Upon his finding of insolvency or impairment, a State regulator would, in addition to his other statutory duties, notify the Federal agency of his determination. Individual policyholders and claimants would continue to deal with the State regulator and, upon a final adjudication of insolvency, the State would so advise the Federal agency and would submit to it a certified list of unpaid but valid claims against the insolvent insurer.

At this point, the Federal agency would assess other licensed insurers in the State of domicile of the insolvent company, collect the assessments, and pay the proceeds to the State liquidator for payment of claims. The Federal agency would thus serve as the financial conduit, channeling funds from the assessed companies to the liquidator.

With this limited function, the agency's annual operating budget would be small. It would also be subject to normal congressional and executive branch review. Loss assessments would not be part of its own budget. Such assessments would only be made as losses were incurred and funds advanced to State liquidators to meet claims of the insurance public. Assessments would be made payable on demand with interest charged if companies were delinquent in their payments.

Since this proposal contemplates continued reliance on State regulation for solvency, assessments for the payment of these claims up to a predetermined annual limit would be made on the basis of insurer participation in the insurance market in the State of domicile of the failing company. This would create an incentive to effective State regulation which would not exist if all losses were spread evenly across the entire national premium base. Insurance companies in the State where the insolvency occurs would thus bear the losses resulting from inadequate regulation by their own State's insurance department.

To the extent that these are reflected in future premium costs, they will alert the policyholders as well to the need for improved regulation by their own State's department. Competitive forces in the marketplace will undoubtedly prevent the full cost of assessed losses from being passed on to policyholders, however. Existing or prospective State guarantee funds could continue to be free to operate, with the Federal fund being secondary in such situations, providing a high degree of backup protection.

Mr. Chairman, I have summarized in broad outline our views on what would constitute desirable legislation in this field. While we do not have specific alternative legislative language in hand today, we are sufficiently advanced in our drafting of a measure along the lines I have marked out so that we will have an administration proposal available next month.

In concluding, we should note that the administration in this presentation does not address itself to the auto insurance and compensation study now being performed by the Department of Transportation at the request of the Congress. That study is not yet complete. Its results and recommendations will be forthcoming later this year.

Mr. Chairman, this concludes our prepared remarks. We will attempt to answer any questions which the committee may have.

Senator Moss. Thank you very much, Secretary Passer, for your statement. I am sure the committee is pleased with your statement that the administration "is strongly in support of Federal legislation to guarantee that every citizen, every policy holder and every claimant is properly and fully compensated for his insured losses."

You state that the "adverse impact of insurer insolvencies, especially on individuals and smaller insureds warrants Federal legislation." I agree. And I am sure this committee agrees, "we need action now." I am happy to note that you indicate that you are drafting language to achieve the general purposes that you set forth in your statement.

I want to urge you to get that to us as early as possible. We held hearings and this committee is anxious to move because we believe that we ought to complete our legislative work this year and get some sort of statute on the books to accomplish these worthy objectives. So if you can accelerate it and get it up maybe a little earlier than next month, like maybe the 24th of this month or something, we would appreciate it.

We have had this bill before us quite a little while, and we solicited information as early as last November when we had some hearings, so we are anxious to work it out as soon as we can. And we are glad that you offer to cooperate with us as we mark up the bill so that it can accomplish what all of us have in mind even though we may have different ideas on how we ought to go about it.

I have a few questions that I wanted to ask. The other Senators undoubtedly will have some—maybe members of the staff. In your testimony you state that, "The remedy selected must meet the needs of the insurance consuming public effectively and soon."

Do I gather from that statement that you believe the protection of the consumer should be the touchstone, the primary focus, of any Federal bill?

Dr. Passer. Yes, Senator. We certainly agree that the consumer needs to be fully and completely protected in this area. As you noted, we are in complete agreement that Federal legislation is needed to insure that this protection does in fact exist.

Senator Moss. I take it that the needs of the consuming public would be specifically a need to pay every policy holder and claimant the amount he would be entitled to recover if it hadn't been for the insolvency.

Dr. Passer. Yes, sir. That is exactly what we have in mind.

Senator Moss. And to pay it promptly because delay would be as disastrous, in some instances, as no payment at all. Is there a need to protect the consumer from possible abuses that he would not have been exposed to had there been no insolvency?

Dr. Passer. We have addressed ourselves here to the losses that consumers would undergo due to insolvency and not to the specific problem of such other aspects that might need some kind of attention.

Senator Moss. Your general outline of your belief that there ought to be an assessment made against those companies operating in the State where the insolvency occurred—you give the reason for this as the need to stimulate better State regulation. In the first place, doesn't this pose some problems of mobility of policyholders across State lines? Where an insurance company is domiciled might not be the place where it has a lot of policyholders, isn't that so?

Dr. Passer. Yes. Of course. While the attention here is given to the State of domicile, the claimants could be anywhere and would be on

this list of validated claims that would be paid wherever they are resident.

Senator Moss. Well, of course, we will wait to see the language, but it seems to me we need some clarification or definition of that in order to make up the claims of the insolvent company. We are going to get funds from other insurers who are not insolvent and I hope without unduly loading it on some companies resulting in their requirement to increase premiums to the consumer. That is what bothers me.

Dr. PASSER. Yes, sir; Senator. I would say that this approach puts the burden for the regulation on the States. By and large they have done a good job of regulation. I think the record shows that there is really no good reason that they shouldn't do a completely good job and the better a job they do, the fewer insolvencies that will occur in the first place.

Therefore, any incentive that can be put forward to encourage the States where it is needed to do an even better job, I think will help reduce the scope of the problem and make it easier to handle.

Senator Moss. Of course, I have agree with you as an abstract proposition. I am just a little troubled with the application. I am not familiar enough with this type of insurance to know whether it tends to concentrate in certain States. I think this is so. There are some areas where there are just a lot of insurance companies and they fan out and sell their coverage all over the United States.

I don't know whether your idea is to count up the number of policies of insurance that are held within the State in making the assessment or whether you just go back to the domiciled insurance company.

Dr. PASSER. As I understand it, your question is whether using the State as the basis for this assessment would be sufficient in the case of a nationwide company that happened to be domiciled in that State?

Senator Moss. Yes.

Dr. PASSER. Do we have any further information on that?

Mr. HAMILTON. It is our intention, Mr. Chairman, that the losses, whether they are sustained by residents of the State of domicile of the insurer or residents of any other State, would all be picked up in the operation of the liquidator as they are in most cases now, and be resolved. We would therefore be assessing against the companies doing business in the State of domicile of the insolvent company notwithstanding the residence of the policyholders.

We do have companies that are domiciled in one State and do the principal portions of their business elsewhere. We would expect that these would be picked up.

Senator Moss. Well, I think I understand your answer, and we undoubtedly want to discuss the desirability of that as against an overall small premium requirement or payment similar to what we do on deposits in order to make sure that all bank deposits are insured.

I agree heartily that anything we can do to stimulate better regulations by the State insurance agencies in the first instance ought to be done. That is the part that will be hard to work out, I think. Are you, in working out this bill and the language, working with Mrs. Knauer's office and consulting with her?

Dr. PASSER. Yes, Senator. We are indeed. She is aware of this and has assigned personnel to this problem.

Senator Moss. This is basically a consumer bill. I would think it would be most important that her office be involved in it.

Mr. HAMILTON. Our present thinking is that the advisory committee concept contained in S. 2236 would be retained and we would expect the consumer representation to include Mrs. Knauer or a spokesman from her office.

Dr. PASSER. In other words, the consumer interest would be taken care of not just in drawing up the proposed legislation but also in the continuing administration through this Federal agency.

Senator Moss. Well, I commend that. I think that is a fine idea.

Senator Cotton, you may have some questions.

Senator COTTON. Thank you, Mr. Chairman. Dr. Passer, my first question has been pretty well answered in your statement—the question I intended to ask you—and that was regarding the effect, if any, that the administration's proposal could have upon State insolvency laws in the insurance field which either may be enacted at some future date and which already have been enacted.

I gather from your statement that the proposals that you will submit will be of such nature that whether a State has acted already or whether it acts in the future, the Federal legislation, if your version should be adopted, would not conflict with it and would only reinforce and bolster it up.

Dr. PASSER. Yes, sir, Senator. That is very clearly part of this. In terms of the sources of funds to meet the claims of the policyholders or other claimants, of course, the first source is any resources of the insolvent corporation. This may be nothing.

The second source is any State fund, if there has been one established. The third source would be the funds obtained by the post-insolvency assessment by this Federal agency. But this would be completely coordinated with the State.

Senator COTTON. How would this compare with the probable impact upon such State laws by the present bill, Senate 2236 now before the committee? That is, have you analyzed the effect of the present bill, were it adopted, on State agencies and on State laws that either have heretofore or may hereafter be enacted?

Mr. HAMILTON. Senator Cotton, we have not completed what I would regard as a thorough analysis of S. 2236, but what we have done so far strongly suggests that S. 2236 would, if not directly and intentionally, soon or later intrude on State law. The right to go in and conduct separate examinations, the right to step into the shoes of the insurer and go into insolvency, and the right to step in with regard to rehabilitation, these matters put the Federal Government into the State process or supersede the State process.

Mr. CHERINGTON. If I may just add something to that, I think that under S. 2236 those States that have preinsolvency assessment and funds would perhaps find that the Federal fund would be redundant for their purposes.

Senator COTTON. I thank you.

I am particularly interested—I have a certain personal interest because the Governor of my State, the State of New Hampshire, called my attention since this bill has been under consideration to the fact that we signed into law, I believe June 30 of this past year, 1969, a bill which provides protection to those suffering as a result of insolvency within the State of New Hampshire.

I find in the news release, to which he called my attention, and which in fairness I should state was a release by the insurance commissioner

of the State, and we already know something about the feelings of the National Association of Insurance Commissioners, but I find that it is apparently in accord with the theory of the proposals that you are preparing insofar as we can identify those proposals.

It provides that no funds will be collected in advance. No elaborate administrative machinery will be required to operate the new association. The release to which the Governor called my attention says the New Hampshire insolvency law is in direct contrast to a proposed Federal insurance solvency fund now under consideration in Congress which according to estimates released by the National Association of Insurance Commissioners would cost property and casualty insurance policyholders in the United States at least $36 million a year in addition to premiums.

It goes on to assert that there is nothing in the Federal proposal which can't be done more effectively and more economically by other means and by State regulation. This type of State law enacted by, I understand, about 20 States that have under consideration State laws, and this particular law in my own State, which became a law last July, apparently, although drawn in advance of the administration's proposals, coincides with the basic theory that you have advanced this morning; is that correct?

Dr. PASSER. It sounds to me like that is correct, yes, Senator.

Senator COTTON. Now, as I said before, the National Association of Insurance Commissioners has registered opposition to S. 2236 in its present form. Have you received any reaction as to the position of the National Insurance Association Commissioners with respect to the administration's proposal?

Dr. PASSER. Senator, our proposal is still so much in the formative stage that I think at this time we can't answer that we have any reactions from anybody. It just is not pinned down yet. When we get the specific legislative language, then I think we will be able to find out the reaction of different people.

Senator COTTON. Mr. Chairman, I have no more specific questions to ask, but I would ask consent that at this point, after my questions, that the release I referred to, which goes into some detail regarding the law in my own State, be inserted in the record.

Senator MOSS. Without objection that will be done.

(The press release follows:)

PRESS RELEASE OF JOHN A. DURKIN, COMMISSIONER OF INSURANCE, STATE OF NEW HAMPSHIRE, JUNE 30, 1969

CONCORD, N.H., June 30—The State Insurance Department's bill to protect New Hampshire motorists against auto insurance company financial failures was signed into law today by Governor Walter R. Peterson.

The new state law creates an association to be known as the New Hampshire Automobile Assessment Association, to which all auto insurance companies doing business in New Hampshire must belong. After today, if an auto insurer should go broke and could not pay its claims, State Insurance Commissioner John A. Durkin will have the power to assess each association member to provide the funds necessary to pay the claims of the insolvent insurer.

Durkin said New Hampshire is the first state in the nation to adopt a law providing insolvency protection as comprehensive as this.

No funds will be collected in advance and no elaborate administrative machinery will be required to operate the new association.

The association will be run by a six-member insurance industry committee which will have the power to examine annual statements and reports of any licensed auto insurer in the state, submit reports and make recommendations

regarding the financial condition of any licensed auto insurer, and to investigate and examine any claim presented to the receiver of any insolvent insurer and submit recommendations to the receiver.

The new law applies to auto bodily injury and property damage liability claims, medical payment claims, uninsured motorist claims, auto physical damage claims and claims for unearned premiums, payable under the terms of a valid auto policy issued to New Hampshire residents by an insolvent insurer prior to being declared insolvent by a court of competent jurisdiction.

The New Hampshire insolvency law is in direct contrast to a proposed federal insurance insolvency fund now under consideration in Congress which, according to estimates released by the National Association of Insurance Commissioners, would cost property and casualty insurance policyholders in the U.S. at least $36 million a year in additional premiums. According to the NAIC, which is made up of the insurance commissioners, superintendents and directors of the 50 states, this $36 million tab represents a premium tax that American insurance policyholders in New Hampshire and other states would have to pay to defray the costs of administering the proposed government fund designed to guarantee payment of claims against insolvent property-casualty insurance companies.

The NAIC, which has been reviewing the problems facing the auto insurance industry and actively devising recommendations for reform, also said that "there is nothing in the federal proposal which cannot be done more effectively and more economically by other means, and by state regulation. Although the number of insolvencies is small and their consequences minimal when compared to the total insurance premium writings, the association recognizes that its goal should be to eliminate entirely the impact of insolvencies on the individual claimant.'

Ultimately, the federal bill, if enacted would also have some impact on insurance premium taxes—a vital source of present state revenue.

According to the NAIC, the already widespread availability of uninsured motorist coverage with insolvency protection has significantly limited the scope of the insolvency problem. New Hampshire and 33 other states have laws requiring that this coverage be offered to motorists. It is available in other states through voluntary action of most auto insurance companies. Under this coverage an auto acicdent victim from his own insurer if he can't collect from a negligent motorist whose insurance company went broke.

"The combination of the new insolvency law togethed with the availability of uninsured motorist coverage with insolvency protection will effectively handle any auto insurance insolvency problem which may occur in the state of New Hampshire," Commissioner Durkin said.

Senator COTTON. May I say for the benefit of the reporter, this need not be included in my remarks, as I studied this release I underlined certain parts of it. Those underlined should be disregarded. The emphasis is mine. [Laughter.]

Senator MOSS. Senator Hart.

Senator HART. Thank you.

Gentlemen, I appologize for being late, but I have had a chance to read the statement. I am delighted there is contained in—I take it it is the joint position of the Departments—the stress on the need for Federal regulation—that circumstances warrant Federal legislation. "The administration is strongly in support of Federal legislation," and so on. "Some Federal action is needed." That is all to the good.

I am sure, given that attitude—I would hope given that attitude—together, the committee here and its staff and you and your staff, we should be able to provide, before this session of Congress concludes, legislation that will protect the consumer against the failures created. Increasingly people acknowledge a need for Federal action.

The reservations I would have, I think, would come as no surprise to anybody. That doesn't necessarily mean my reservations are right, but I would hope in the drafting effort we could try and react to the kinds of reservations that others of us and I would suggest.

You need action now. But I wonder if the mechanism which you are suggesting, and admittedly in rather sketchy and understandably preliminary form, is a mechanism that is as effective as we might conceive—I wonder if, in fact, the step which you propose we take, which I think all of us could acknowledge is an improvement, is a shorter step than is within our power to take.

It seems to me—of course we would all agree the best way to protect consumers is by insuring that there is no insolvency. That is really what we should be busy with. Whether that goal is achieved by Federal intrusion of greater or lesser degree doesn't bother the consumer one iota. If more Federal intrusion than you would suggest in your present consideration will be made in order to insure fewer insolvencies, then I am sure you would join us in making that additional step. Would you?

Dr. PASSER. I think that a very important question is, as you say, how to reduce the insolvencies. Our general view is that there can really be no guarantee that there will be no insolvencies under any regulatory system so what in fact you do is get the best regulatory system possible and then have a backstop protection to make sure no consumer ever loses a dollar because of an insolvency.

Senator HART. Our real objective, though, is to insure that there are no insolvencies. That is the goal, is it not?

Dr. PASSER. I agree that is the goal.

Senator HART. If that is the case, our inquiry repeatedly should be addressed to the basic question: Which method, which device, most likely will provide the achievement of that goal of no insolvencies? It may be that Federal intrusion in the matter of examinations and standards is more likely to achieve that goal than continuing to rely on existing examinations and standards which have failed to insure against insolvency.

I suggest as we work this bill over we continue to see if we can't build in a role for the Federal Government that is not sort of a clearinghouse system of picking up the pieces but a prevention bureau as well. That would be the theme that I would hope together we would try and develop here.

I suppose I speak a little obscurely. It isn't that I am afraid to suggest that Federal standards and the right of Federal examination make good sense to me. They do. But those things seem to create such jangled nerves that I am afraid to raise them lest we fog up the effort to get to a happy middle ground here.

Mr. CHERINGTON. May I add a point here? I think the objective of preventing insolvencies is clearly a worthy one, but a major part of the problem that we are dealing with here I think can be traced to companies that engage in the high-risk automobile market. Therefore, in part, the solution would appear to be to either eliminate or cut down on the size of that market. Thus, the question of whether there is Federal regulation or State regulation may be somewhat less important to the long-range solution of the insolvency problem than how well we meet the problems of the high-risk insurance market.

Senator HART. High-risk insurance is not the only problem that has given rise to the concerns about losses, is it?

Mr. CHERINGTON. It is not the only problem, but it seems to loom fairly large as a dominant characteristic of the companies which have gone into insolvency. Under the aegis of the automobile insurance

study, for example, Prof. Douglas Olson, of the Wharton School, has just completed a study of the experience of Pennsylvania in this matter, and we will be glad to let the staff of the committee have a copy of his report. I think he confirms our impression that the high-risk auto insurance writers are a major factor in this matter.

Senator Moss. We would welcome having a copy of that report for our file.

Senator Hart. Let me ask this question: If we had no Federal insurance of bank deposits and you were now coming up here to suggest how we respond to what once was a very acute problem of losses because of bank failures, would you recommend structuring the bank deposit insurance system the way you are recommending structuring the insurance guarantee fund? If you could do it over again, would you put in the form you are urging us to put the insurance fund in?

Dr. Passer. That is certainly a very probing question. I think one difference that would distinguish the banking system from the casualty, property, and surety insurance business, is that the banks are suppliers of and participators in the money supply system in the United States, and this is part of the lifeblood of commerce and not just a business meeting a special need. Therefore, I think there is some basis for looking at it as a kind of a special situation.

I think it is interesting, though, that even with this extensive regulation of banks, not only by FDIC but also by other agencies, that there do continue to be bank failures. In other words, there are insolvencies and therefore if the goal, as you mentioned it, would be to cut it to zero, even with a good Federal system, a multidimensioned Federal system, it has not been reduced to zero.

Senator Hart. I am suggesting that is the goal both with respect to insurance failures and bank failures. I had the feeling that the lesson of the intervening years is that we have reduced bank failures to the extent that we have because we did indeed use the joint system. You suggest a distinction. I am not sure that you—maybe I shouldn't push you—answered the question I asked. Would you or wouldn't you recommend handling banks the same way you are now suggesting you will recommend insurance? You say there is a distinction because banks somehow affect the money flow. Insurance management would be surprised to be told that they don't have a role in that too.

Dr. Passer. Yes. Well, let me try to be responsive directly to your question. I would favor the present system on the banks.

Senator Hart. You would distinguish that from this on the ground that it has a role in the financing of capital enterprises in this country?

Dr. Passer. No. I would distinguish it on the grounds of confidence as a factor in the money system and as related to the demand and time deposits which are by far the bulk—nearly 90 percent of the money supply. The use of these depends upon the confidence of each depositor in each specific institution with which he deals. This is a daily kind of operation. In other words, this is a money that has been created and the confidence that you need in a system which creates money is, I think, a different order of magnitude from a system for any other kind of ordinary business service.

Senator Hart. You think we owe a higher duty to reassure that kind of capital interest against losses than we do with what is contained in this other——

Dr. PASSER. Not that it is a higher duty or different kind of obligation. It is just that there is this confidence factor in the banking institutions.

Senator HART. Then you are saying that we could generate greater confidence—that there will be fewer failures—by the joint system of the bank method rather than the separate one that you are suggesting?

Dr. PASSER. Yes, but I am saying that this is not——

Senator HART. Why don't we go to the more confident method that has been proven?

Dr. PASSER. I would say that this confidence factor is not critical in this sense. We are not talking about the means of payment; that is, the money supply of the country. We are talking about a service. There are many, many services and they all are important and this is one service among many, whereas the money supply is unique and has a very special characteristic.

Senator HART. Well, I would hope, Mr. Chairman, that given the meeting of the minds on the need for Federal legislation that we can together attempt to come up with something that is responsive and will prove of value.

Senator COTTON. Could I ask a few more questions?

Senator MOSS. Certainly.

Senator COTTON. First, I would like to join the chairman in the hope that you people get the actual proposal up here as soon as possible, because this bill has been before the committee for some time, and the sooner you get it up here, the more opportunity the committee will have to give it its honest and earnest consideration.

Now, from your statement about what your proposal is likely to be, I want to make it clear in my mind and on the record, if possible, under your proposal, first, in the case of any State that has no provision for protecting losses occasioned by insolvency, the Federal system would act; is that right?

Dr. PASSER. Yes, sir.

Senator COTTON. And would insure.

Dr. PASSER. It would insure, absolutely.

Senator COTTON. Insure no losses would take place?

Dr. PASSER. Yes, sir; it would do that.

Senator COTTON. And in the case of any State that has a provision but the provision, the first time it proves inadequate to protect all losses, your Federal system would again automatically act; is that correct?

Dr. PASSER. Yes, sir; that is correct.

Senator COTTON. So that essentially you give the States every opportunity to deal with the situation. You make sure they are dealing with it. And automatically the Federal action is triggered off when they fail to deal—I'm referring not to stopping insolvencies, but to reimbursing losses—is that correct?

Dr. PASSER. Yes, sir, Senator, that is correct.

Senator COTTON. And the one difference, or perhaps one of the differences, is that I notice that this reimbursement takes place—the fund is raised or the fund is levied and produced after the loss, rather than building up a pool in advance?

Dr. PASSER. That is correct.

Senator COTTON. That is one fundamental difference between what your proposal will be and the bill as it now stands?

Dr. PASSER. That is correct. It is a postinsolvency system.

Senator COTTON. Thank you, Mr. Chairman.

Senator MOSS. Thank you, Senator. Mr. Sutcliffe, on the staff, has done an analysis of the previous testimony we had in other hearings, and I think he has several pertinent questions that might help us in flushing out the record, even though your position is still preliminary.

I am going to call on him to pose those questions so we have them before us to examine.

Mr. Sutcliffe?

Mr. SUTCLIFFE. Thank you. I have several questions designed to see if we can understand some of the different thinking as to your proposal and your understanding and ideas about S. 2236.

So if I may begin by asking you: Is it your view that the implementation of S. 2236 in its present form would result in the creation of several disincentives to good regulation by States?

Dr. PASSER. We are concerned that this would be a possibility.

Mr. SUTCLIFFE. What are those disincentives as you see them?

Dr. PASSER. Principally that there would be a Federal authority or Federal agency which would also be directly involved in the regulation process, with the right to examine and the right to do the things that the State regulatory authorities currently do.

Mr. SUTCLIFFE. You feel that would be a disincentive to State regulation? Could you elaborate upon that a little bit? Perhaps Dr. Cherington could explain—I understand you begin with the Economic Regulatory Advisory Committee's notions of disincentive, and perhaps we could understand what those notions are, to understand the kind of disincentive mechanism you are talking about, within the existing piece of legislation.

Mr. CHERINGTON. Well, the Economic Regulation Advisory Committee recommended essentially a punitive tax in those States that didn't have adequate protection for their citizens against insurer insolvency; we didn't think that solution was particularly desirable. But the disincentives, as we see them in S. 2236, as it is presently drafted, stem, in part, from the fact that there would be a large pool of money collected from all the States by the Federal Government. There certainly would be a lessening of incentives for the States to take action, either to build up a preinsolvency fund or to provide for a postinsolvency fund.

There is, as Dr. Passer mentioned, a considerable body of examination authority and semiregulatory provisions in S. 2236 which may make the States feel that it is less important for them to regulate well and lead them to abdicate this responsibility to the Federal Government.

Mr. SUTCLIFFE. Is your theory, then, that the ability at the Federal level to move would cause the States not to move?

Mr. CHERINGTON. It is conceivable.

Mr. SUTCLIFFE. Is the opposite of that possible also, that the threat of possible Federal intervention, in the absence of the State regulatory action, is likely to cause an incentive for the State regulatory authority to perform its job as best it can? Is that an incentive in S. 2236 that may have been overlooked both by the Economic Regulatory Advisory Committee and perhaps in your initial discussions of the proposal?

Mr. CHERINGTON. We think that, by levying a postinsolvency assess-

ment on the companies doing business in the State of domicile of the failing company, there would be a very substantial incentive for them to press for not only sound insurance law in that State, but also reasonably good administration of that law.

Mr. SUTCLIFFE. From where does that incentive come?

Mr. CHERINGTON. Because the fewer the insolvencies in that State—the State that bears primary responsibility for financial supervision of its domiciled companies—the lower their assessment would be.

Mr. SUTCLIFFE. So you are suggesting that the regulated industry itself would press the regulator to do a better job of regulation to protect the funds of the insurance companies? So you have the regulated industry urging better regulation upon itself?

Mr. CHERINGTON. Yes, sir.

Mr. SUTCLIFFE. What happens when the regulated industry is able to pass those costs on to the policyholders?

Mr. CHERINGTON. Well, I think they may, in some instances, be able to pass them on to policyholders, but I still think there will be a substantial incentive on them to press for closer regulation.

Mr. SUTCLIFFE. So the incentive in your proposal for better State regulation—see if this is fair—would come from the regulated industry, whereas any possible incentives for better State regulation in S. 2236 would come from the threat of Federal Government; and one you prefer to the other. Is that a fair statement at all? Either gentleman can respond to that question.

Mr. WALSH. I think the incentives in the administration's concept would tend to work naturally and without the direct interference of a government entity.

Mr. SUTCLIFFE. Do they work naturally because of the present affinity between the regulated and the regulator in the State insurance departments?

Mr. WALSH. I am not willing to discount the effect of public pressure. To the extent that those costs are, in fact, passed on to the public, I would expect the public—to the extent that any public is able to bring pressure in such a sophisticated field as the regulation of insurance—to bring pressure for better regulation.

Mr. SUTCLIFFE. Let's examine the notion of the public bringing pressure to bear upon the State regulator if the regulated industry passes the costs of the insolvency on to the public. What do you think the raise in rates or assessment would be from a normal insolvency as reflected in each policy? An order of magniture of 50 cents, $1, $10?

Mr. WALSH. Very small.

Mr. SUTCLIFFE. Very small. How would the policyholder even be aware then, that any increase in cost was the result of the assessment? How would they, even if they were very organized, be aware that their State insurance regulatory body maybe didn't do quite the job it could have done, and therefore there has been an assessment which the company had to pick up and pass on to the policyholder?

Now you are suggesting that the incentive of the good State regulations would come back in through the policyholders' voice.

Mr. WALSH. I think insurance companies have always been very ready to tell their insureds the reasons why rates are going up. I don't think they would miss the opportunity to say they were being assessed by the regulator to indemnify the insureds of insolvent companies.

Mr. SUTCLIFFE. For a 10-cent price increase?

Mr. WALSH. Yes. But I guess that we will have to wait and see. That is my opinion.

Mr. SUTCLIFFE. OK. In that connection, for the record, and simply in the discussion here, let me read into the record what is said in the NAIC, National Association of Insurance Commissioners, Automobile Insurance Study Background Memorandum, which is found in the Report of the Special Committee on Automobile Insurance Problems, June 16, 1969, at page 184:

They said—the commissioners, or the staff preparing the memorandum for the commissioners—said:

> A new objection to guaranty funds is that their existence would tend to make insurance departments more complacent in dealing with insolvencies and those responsible for creating them. This line of thought is highly questionable. An insolvency would be no less embarrassing for the regulator. Department complacency resulting from the adoption of guaranty funds has not been the experience in states with such plans.

Do you have any comment or reaction to that statement from the NAIC?

Dr. PASSER. I would think this would support our position, Mr. Sutcliffe. You are talking about a State system. It is working well. We are assuming that this is feasible in most States, and what we really need is a Federal backup in those few cases where it isn't.

Mr. SUTCLIFFE. Very good. I think that, then, will cause us, in later questions, to examine the way in which present funds are operating in the States to provide what is the primary focus of both your proposal and the committee's proposal; namely, protection of the consumer interest.

I appreciate that comment and I think that is something we would be very happy to develop later in questioning here.

You note that there is a—you actually end up in your testimony rejecting the need for standards; is that correct?

Dr. PASSER. Are you referring to Federal standards?

Mr. SUTCLIFFE. For regulatory Federal standards? You are rejecting the need for Federal regulatory standards?

Dr. PASSER. Yes. The States have the responsibility, which they are now carrying out in most cases, to set the standards and to set the rates and determine the solvency standards, and so on.

Mr. SUTCLIFFE. I see. So you would then urge the continued practice of the NAIC asking for standards for regulation through the adoption of model legislation.

Dr. PASSER. Oh, yes, indeed. Indeed. In fact, in an ideal world, if this could be done tomorrow in all 50 States, this would be a different problem, but it won't be done tomorrow. It will take years to be done.

There is a very clear role here for a Federal backup until it has been definitely proven and demonstrated that the States in every case—not just in most cases but in every case—have provided every dollar that every consumer has coming to him.

I think this is the problem as you see it and as we see it.

Mr. SUTCLIFFE. It is your contention that Federal standards in this situation would really constitute Federal regulation; is that not correct?

Dr. PASSER. We feel that this was covered by the McCurran-Ferguson Act and this would be, it seems to us, a problem that has to be very carefully investigated as to possible overlap.

Senator HART. Is your objection to Federal standards because the McCurran Act would bar it or because you do not like the idea?

Dr. PASSER. We just note in passing that the McCurran-Ferguson Act seems to bar it. Our objection is more fundamental, sir.

Senator HART. Whether or not the Federal Government was prevented by law, you would still not want the Federal Government.

Dr. PASSER. Yes, Senator Hart, that is right.

Senator HART. But you are not troubled by the fact that we do it with banks.

Dr. PASSER. Well——

Senator HART. I am repetitious. But, you see, I have a hangup on this.

Dr. PASSER. Yes; I understand. You have to understand that my professional background is as an economist and I look at this situation in a special way—but it seems to me that money supply is a very special aspect of the total national economy. Almost all of it—not quite all of it—is demand and time deposits which are liabilities of financial institutions—namely, banks. There has to be 100-percent confidence in these banks not just every week or every month but every minute of every day in order for this system to work.

This is not true of all business services and all business products. I think it is a very special case and I think on that basis of that case, it is possible to say that a nationwide Federal standard for the banks is very well justified.

Senator HART. Lest my questions imply my interpretation of McCurran-Ferguson to restrain the Federal Government from attempting to do anything about the quality of State regulations, I do not read it that way. But I was really just trying to get your thinking as to whether it was wrong per se or whether it was wrong because the law would bar it.

Mr. SUTCLIFFE. Are there any other examples of administration proposals for regulation that involve Federal standards for the States to abide by?

For example, does the President's welfare program involve Federal standards or does the urban mass transportation bill provide Federal standards or a bill before the Consumer Subcommittee that sets up standards for private testing labs in the product-testing area which does provide for Federal standards; are these displacements of State regulation or are they instigating or implementing Federal regulation?

Mr. HAMILTON. Could I speak to one of those you had mentioned? That is, the proposals with regard to standards for the testing of consumer products.

There, we are not talking about setting standards in the sense you have been talking it here with regard to insurance. We are talking about it in a very different way. We are talking there about setting Federal standards with regard to what constitutes a proper test if a test is to be represented as having been made; not with regard to something that is going to be enforced for any lab that does any testing.

This has to do with representations as they are policed by an existing Federal enforcement agency. Each have their own special characteristics.

Mr. SUTCLIFFE. The President's message on the environment has just been released. One of the proposals is for State-Federal water quality standards to be "amended to impose precise fluid requirements in all industrial and mineral resources." Very strong involvement of the Federal Government in the setting of standards. Does that amount to, in effect, Federal regulation?

Mr. HAMILTON. We do not believe it necessarily will.

Mr. SUTCLIFFE. I think this might be helpful, then, as we go along to see if we could fashion a legislative solution along the lines of S. 2236, and with some of your proposals, that you did not think violated or led automatically to Federal regulation.

There is another point I think we might bring up here. The Economic Regulatory Advisory Committee had asked for the adoption of Federal standards. In that body, there were two present members of the National Association of Insurance Commissioners and one past member. I do not really believe that they would call down upon their own organization Federal regulation, and yet they were anxious to have Federal standards in the area of State regulation for insurance. And they were willing to do this through the imposition of a Federal premium tax if those standards were not adopted.

I would welcome any comments you might have on that.

Mr. WALSH. I think we should recognize that the standards to which the committee members were referring were standards for a satisfactory postinsolvency mechanism.

Mr. SUTCLIFFE. In your proposal, I do not notice any standards for that kind of criteria.

Mr. WALSH. No. I think our present inclination is to be neutral with respect to State action in this field. If a State chooses to develop an insolvency mechanism which treats only a portion of the property, casualty surety field and wishes its mechanism to be primary, then the Federal guaranty would become secondary for that portion, and primary for the rest.

Mr. SUTCLIFFE. As long as you are in the primary-secondary category, you started the discussion out by saying that the consumer interest in both our attempts at legislative action at the Federal level was the primary focus.

If the State program does not protect the consumer to the extent that you and the committee might feel necessary, then would you be willing to suggest that the Federal Government should have some opportunity for setting standards in order to protect the American consumer?

Mr. WALSH. I think we are, in effect, setting a standard here—and it is a very high standard—of protection for the consumer if the Federal Government stands ready to reparate all of his potential losses from the result of an insolvency. Our present disposition, as I think you understand, is not to tamper with the existing regulatory mechanism.

Mr. SUTCLIFFE. I think that at this point, then, it might be useful to trace through how the administration's proposal, as outlined in the testimony, would work. If you will bear with me so that we can understand and have a discussion about this, let me give you a hypothetical situation and let you tell the committee how your proposal would work.

Let us take a simple accident case. A and B are involved in an auto accident. Let us say B is cited by an officer at the scene for failure to

yield the right of way. Now A seeks compensation from B for injuries to property and person sustained in the accident.

Now B's insurance company stalls A and his company in any kind of payment of any claim. The State Insurance Department is told by several sources that B's company is not paying its claims at all. The Commissioner decides to conduct a special examination and that examination discloses that B's insurance company has liabilities which exceed assets.

Let us take this general framework, which is not a terribly unusual situation in the insolvency area, and have you sort of trace with us the steps that occur. Since I had the advantage of formulating this hypothetical and thinking it through after looking at your testimony, I will be glad to suggest or ask questions to develop this.

Now with that hypothetical, it is my understanding that the first thing the insurance commissioner would do at this point is to notify the Federal agency; is that correct or incorrect?

Mr. HAMILTON. If he has determined that the company is insolvent, or he now proposes to take an action in insolvency, he would so notify.

If he is contemplating it or believes the company is in ultrahazardous condition and is considering what he wishes to do, he is still working against the resources available to him within his jurisdiction, and the Federal Government has no involvement.

Mr. SUTCLIFFE. Let us say he finally determines that he thinks the company is insolvent. Then I guess the next step would be an adjudication for insolvency, is that correct?

Mr. HAMILTON. He would seek to place the company in insolvency. When he has done so, that notification would have to be given.

Mr. SUTCLIFFE. The notification is given at the point of filing adjudication for insolvency.

Mr. HAMILTON. Yes, as a notice.

Mr. SUTCLIFFE. Then what happens?

Mr. HAMILTON. Insolvency proceedings go forward.

Mr. SUTCLIFFE. OK. Then the insolvency proceedings go forward. Then what happens? There is an adjudication——there is a final determination of insolvency, is that correct?

Mr. HAMILTON. Yes.

Mr. SUTCLIFFE. Then what happens?

Mr. HAMILTON. At some point, the available assets are matched against the policyholder and claimant losses.

Mr. SUTCLIFFE. Are you suggesting, then, that the company goes through a process of liquidation? Would the company's assets be liquidated?

Mr. HAMILTON. You would not have to wait until all the process had been completed if it were clear to the liquidator that there was a deficiency that could not be met from other sources.

Mr. SUTCLIFFE. At some point in time the liquidator has to compile a list to give the Federal agency, is that correct?

Mr. HAMILTON. Yes.

Mr. SUTCLIFFE. How could he do that until all assets were accumulated and marshaled and all liabilities were ascertained?

Mr. HAMILTON. He would have to resort to those tools which are presently available to him.

Mr. SUTCLIFFE. OK. So that is an important point. He would have to use the present liquidation tools available to him, is that correct?

Mr. HAMILTON. Yes; except the climate within which he would be working would be radically different than it is today. In the climate in which he works in most States today, he is faced with the fact that there will not be the means with which to meet the losses that he is validating.

Mr. SUTCLIFFE. Then, after this Federal agency is presented with a list of claims, assuming that this takes place, then what happens? The Federal agency is presented with this list of claims. Then what happens?

Mr. HAMILTON. It then makes the pro rata assessment against the company.

Mr. SUTCLIFFE. It makes the pro rata assessment against the company. Then what happens?

Mr. HAMILTON. It gives that money that it collects to the liquidator for payment of claims.

Mr. SUTCLIFFE. He gives the money to the State liquidator to pay the claims.

Mr. HAMILTON. Yes; or whatever official is properly entitled to receive it.

Mr. SUTCLIFFE. Then what does the State liquidator do with the money?

Mr. HAMILTON. He follows the law applicable in his State.

Mr. SUTCLIFFE. Follows the law applicable in his State. When does the consumer get paid? Do you have any notion of the time reference we are talking about in this proceeding? No. 1, adjudication of insolvency; No. 2, some kind of liquidation of assets; No. 3, compilation of a list to present to the Federal agency; No. 4, presentation of the assessment and—collection of the assets by the Federal agency; No. 5, payment by the Federal agency to the State liquidator; No. 6, payment of the State liquidator to the insolvent insured.

We have forgotten, of course, several things. We forgot:

1. That we didn't have a State plan that interposed a second layer on here. We forgot, of course, to mention the fact he would have to first go to his own company, in this case, under the hypothetical given, and ask for payment under his uninsured motorist endorsement which could add time and another layer of required action by the consumer before he could get paid.

Do you have any notion of the kind of time we are talking about under the existing conditions in the States?

Mr. HAMILTON. Some payments might flow in a very short period of time. Some might flow only after many years. I would say that the situation would be vastly improved over the one today in which the final dollars sometimes never flow.

Mr. SUTCLIFFE. All right. So your point is that it may take many years before the consumer gets paid, but under your proposal he finally would get paid?

Mr. HAMILTON. That is correct. And he would be paid as expeditiously as the existing applicable laws permit.

Mr. SUTCLIFFE. As to the existing applicable laws, I think it might be interesting to note that Richard Heins, a professor at the Uni-

versity of Wisconsin, in an article entitled "The Causes of Insurance Company Insolvencies," on page 25, says:

> One of the more difficult problems is to conduct the liquidation procedures over a reasonable period of time and conserve the company's assets. The duration of the liquidation proceedings of the companies studied ran an average of 11.5 years.

That is just for liquidation. That doesn't even include adjudication for insolvency.

On the test of protecting the insuring public, do you feel any time span approaching 10 years before payment is sufficient?

Mr. HAMILTON. I would hope that that would no longer be the typical average, but I certainly would not think that anything we are talking about would give any incentive to a policyholder to seek a policy with a firm which might go into an ultrahazardous condition and ultimately insolvency.

This is not an attempt to make the poorest companies the competitive equals of the best. Only to provide consumers with absolute protection.

Mr. SUTCLIFFE. In other words, we are really not trying to put the consumer in the position that he would have been but for the insurance company insolvency. There is some need to penalize him for having poor judgment?—I guess I misunderstood.

Mr. HAMILTON. No one seeks to penalize him in any way. We can't relieve him——

Mr. SUTCLIFFE. Of his poor choice?

Mr. HAMILTON. Of those procedures, without having the Federal Government move in and take over.

Mr. WALSH. We must also recognize the fact that delay in the settlement of the claims that you are talking about is due very largely to the normal workings of the tort system, and the slowness with which major personal injury auto accident cases proceed through the settlement process.

Mr. SUTCLIFFE. I am not sure I followed you on that, Mr. Walsh. You are suggesting that——

Mr. WALSH. That delays are inherent in the system, whether it is a solvent company or an insolvent company. The delays occur largely in the settlement process.

Mr. SUTCLIFFE. You are talking about the determination of fault?

Mr. WALSH. That is right——

Mr. SUTCLIFFE. But even after fault is determined, and that would have to be determined by the liquidator, I guess, in suggesting whether the claim——

Mr. WALSH. And you are also talking about determining the value of the claim, which often cannot be done except after some time.

Mr. SUTCLIFFE. Also about the value of the claim. Now, if the Federal Government were to allow funds to flow to the consumer prior to adjudication of insolvency—Do you have any notion how long the adjudication of the insolvency has been running?

Mr. WALSH. No, but I am certain you can tell me.

Mr. SUTCLIFFE. Well, I don't mean to be leading you down the path at all. This was given to us in testimony on November 20, and it related to the adjudication for insolvency situations in Maryland, where adjudications for insolvency take a long time—more than 3 years. Incidentally, Maryland is a State with its own plan for protecting the consumer. It was created in 1965. To date, no funds have been paid out to policyholders or claimants of insolvent companies.

This is because they are awaiting the adjudication of insolvency in order to make a claim against the fund that already exists.

So the point that the testimony in November revealed was that a lot of people who were inner city inhabitants and who didn't have a reserve of their own weren't timely paid—And I think the thing we are trying to find here is a way of creating a Federal mechanism to assist the States—a mechanism that will insure the consumer gets the money at least as soon as he would under the present system—which you suggest may be too long in and of itself. But that is, I guess, another hearing at another time.

Do you have any comment about this adjudication for insolvency and your proposal for some kind of liquidation, your proposal for waiting until some kind of assessment has been completed?

Even the most effective State department probably couldn't accomplish this within 5 years. If that is incorrect, I think we would like to know about it.

Mr. HAMILTON. I would like to know what difference Mr. Sutcliffe sees in terms of the speed for processing and payment of claims between S. 2236 and what we described today?

Mr. SUTCLIFFE. That question was also asked on November 20 of us and we pointed to a section in the bill which allows the Federal Insurance Guaranty Corp. to come in with a loan of funds to assist a company that looks like it is in trouble and not paying its claims. It could come in and take over and assist that company in paying claims that are valid in a supervisory way, working with the State insurance department.

If that company recovers, the corporation could be repaid. We would have prevented an insolvency. There would have been no disruption in the consumer's ability to be paid.

If that company fails, the claims can simply be treated as paid claims of the insolvent company.

Now this is the procedure that is available in the bill at the present time but I think members of the committee, after the November 20 hearing, were of the opinion that this procedure should be defined a little more carefully than it is in the present bill because it certainly is a problem, and our primary focus is on protection of the consumer and giving him the money he has coming to him as soon as is humanly possible.

Mr. HAMILTON. I think the problem of the determination of what he has coming to him is still there in either case.

Mr. SUTCLIFFE. You are saying that determination as to whether or not he has it coming to him. You have to make a determination of some kind of settlement. But I don't think you have to wait through an adjudication of insolvency and liquidation before you start making the determination as to whether or not he has something coming to him. That is the only question we wish to pose.

Mr. HAMILTON. We do not envisage the Federal post-assessment mechanism working only at the completion of the entire process; we would assume that the liquidator would be able to come in for partial assessment advances.

Mr. SUTCLIFFE. But you cannot pay any money under your proposal for a long time. And perhaps this is why we are talking, and I think maybe what you are suggesting is that your proposal might have to be modified to some extent to provide funds to the consumer a

little more quickly. Is my understanding of your statement correct, or have I simply misread your proposal?

Mr. HAMILTON. I think that you perhaps drew more specificity in the language of the proposal than intended. We hope to have the details when we submit our proposal to you.

Mr. SUTCLIFFE. All right then. We have specificity in one place and that is in the existing State plans, postinsolvency assessment plans.

Your proposal, and Senator Cotton made it very clear, does nothing to change existing or future State plans. Some of the State plans being proposed and adopted operate exactly the way we have discussed. Both the Maryland prefunded plan and certain postinsolvency assessment plans may mean a delay of between 5 and 10 years for payment to the consumer. I think this is another area of your proposal that we might want to discuss.

Mr. HAMILTON. We will not be seeking to try and relieve the States of their obligations to consumers. They have obligations and we expect that they should discharge them. Citizens in those States have obligations to bring necessary pressures for resolution of those which lie within the powers of the States to accommodate.

Mr. SUTCLIFFE. That raises some problems to say that one single jurisdiction is responsible when it has been your contention that the reason for Federal legislation is to provide the consumer throughout the United States with protection.

Mr. HAMILTON. With the assurance that he will receive that to which he is due just as promptly as the law allows.

Mr. SUTCLIFFE. Which law? This is the purpose of our legislative endeavor.

Mr. HAMILTON. The citizen lives under two laws: That applicable in the State where he resides and that under the Federal law.

Mr. SUTCLIFFE. Just a couple other questions, if I may. Do you believe a postinsolvency assessment mechanism is preferable to a prefunded mechanism because it precludes any unnecessary immobilization of insurance capital?

Dr. PASSER. Yes, that is right, Mr. Sutcliffe.

Mr. SUTCLIFFE. Why are you permitting States under your proposal to create a prefunded mechanism or continue with their own prefunding mechanism?

Dr. PASSER. We are not either permitting or not permitting. This is the States decision. We just feel there is no need for a fund at the Federal level of this kind. This can be handled by a postassessment.

Mr. SUTCLIFFE. So your argument rests on something more than the tying up of capital.

Dr. PASSER. I am not making an argument for the States; that is their business to argue either pro or con.

Mr. SUTCLIFFE. If we turn to the States, then, to consider their views on immobilization of capital, we will have some better ideas to evaluate our own discussions following this hearing.

On page 184 of the National Association of Insurance Commissioners report, they say this about the immobilization of capital argument:

> There was another objection; namely, that the backup moneys in any prefunded guarantee plan were "sterile" like "surplus surplus" and hence were not being gainfully used. In the sense that these were not "go-go" moneys that complaint is true, but to give American insurers solidity, a major portion of their assets have long been invested in prime debt securities. These supply capital for every

conceivable range of business and governmental activity in the United States and in some cases abroad.

Subject to somewhat more stringent liquid needs, the proceeds of guarantee funds could be similarly invested to the benefit of the economy. The sterility argument does not seem to stand close scrutiny.

Again simply for the record, I want to point out another viewpoint in this discussion of the way we can best protect the American consumer from the problems associated with insurance company insolvencies.

Dr. PASSER. I would think that any kind of fund like this would have to be held in highly liquid form. This would be almost a requirement. It could not serve its purpose if it is not highly liquid. That is the point. How much money do you want to tie up in highly liquid form as compared to another form?

Mr. WALSH. Going beyond that, I also think the question here is one of the availability of that capital to the insurance function; not simply the availability of that capital to the economy in general. We are concerned about the availability of capital for the insurance industry to underwrite the volume of insurance that the economy will need in the years ahead. To the extent that you immobilize any portion of that unnecessarily, you hurt the ability of the industry to serve its market.

Mr. SUTCLIFFE. Under present State requirements is a certain portion of that immobilized already through reserve requirements?

Mr. WALSH. No question about it.

Mr. SUTCLIFFE. And you are suggesting that the small additional assessment above those reserve requirements would pose a problem or possibly pose a problem.

Mr. WALSH. Yes.

Mr. SUTCLIFFE. I think there is one other area to examine. That is your notion that the fund you propose provides a high degree of backup protection. Those are your words, I believe. Is that correct? How does the fund you propose offer backup protection? Say you have a State fund and the State fund is primary.

Dr. PASSER. I think your question is the fund I proposed as backup. However, I am not proposing a fund.

Mr. SUTCLIFFE. Excuse me. Your mechanism, guarantee mechanism, provides backup protection.

Dr. PASSER. Right. This is what provides it because it meets the validity of claims through the postassessment levy which provides the funds which are then paid off to the claimants.

Mr. SUTCLIFFE. Let us say you are in a State now that has a post-insolvency assessment plan and, for some reason, there has been a fairly large number of insolvencies within a very short period of time and the State mechanism does not function. Now where is the backup protection from your point?

Dr. PASSER. Then the Federal agency steps in and does its job.

Mr. SUTCLIFFE. Let us say the State mechanism does not function because, if they assessed within the State at the level necessary to compensate the policyholders, they would put every other company doing business in that State out of business or a large number of other companies into insolvency as well.

Dr. PASSER. I think it is pretty clear that the kind of remedy that is proposed for any problem has to depend on the dimensions of the

problem. This problem is pretty well documented in terms of what these losses are relative to the premiums written. It is a small fraction of a percent. Say one-tenth of a percent or less. Therefore, this mechanism that we are proposing in view of the past experience, which could get better by the way, there is no reason it should not work.

Mr. SUTCLIFFE. I guess the only point I think should be made is that if the State mechanism fails for whatever reason, it is very difficult to conceive of how the Federal mechanism would not also fail because the Federal mechanism also requires an assessment upon the companies doing business in the State. There is no broader premium base provided for and no loan authority is given.

Mr. HAMILTON. We expect the proposal when it comes forward will contain a limited borrowing authority from the Treasury to meet the kind of situation you are talking about.

Mr. SUTCLIFFE. I see.

Mr. HAMILTON. With Treasury borrowing interest passed on and snowplowed into the assessment.

Mr. SUTCLIFFE. Very good. So you do recognize the need for some kind of borrowing authority.

Mr. HAMILTON. We doubt that the situation we envisage is likely but we believe a limited borrowing authority is probably appropriate.

Senator Moss. Under this hypothetical case Mr. Sutcliffe is proposing, suppose there was a major disaster of some kind in the State which is the thing that caused one company to go under. It might have also put a large number of other companies just on the ragged edge because of this widespread disaster. Then if they had as assessment of postbankruptcy assessment on them, it might have been the thing that also turned them into insolvent companies.

Mr. HAMILTON. One of the reasons we don't have language with us now is because we are also concerned as to how we mesh what we do propose with the catastrophe problem. We welcome working with you and the committee members and the staff beca use we don't think we are setting out here to try and solve the typical catastrophe problem with which the Congress and the country have been concerned and unable to come to grips for some time. We do have to have something that says this is not the answer in that area. That answer is still to be forthcoming. The 747 kind of problem, we don't expect to resolve.

Mr. SUTCLIFFE. It has been pointed out, and for the record it should be clarified, that any discussions about the way in which the "committee" is operating should not be held to include all members of the committee and their attitudes and approaches to any changes in S. 2236. The committee, of course, has taken no action on S. 2236 and any time in the hearing or discussion here when the word the "committee" has been used it simply reflects the thinking on the kinds of issues that were raised in previous hearings and the kinds of directions that are being examined to solve those kinds of problems. I simply want to clarify that for the record.

In your testimony you argued that your proposed plan would provide an incentive for effective State regulation. I think the first question is, Is it necessary in Federal legislation to provide an incentive for effective State regulation?

Dr. PASSER. Well, I think that we all agree that, No. 1, the consumer has to be protected, and, No. 2, there is a need for some kind of Federal action. We believe that one direction that can take is to, in a sense, build upon the State mechanism which is already functioning and to try to set up a system which, in the few cases where it isn't, to bring about a situation where it is. I think that is a very legitimate aspect of a Federal program or a Federal involvement.

Mr. SUTCLIFFE. Is to provide better incentive for State regulation?

Dr. PASSER. Right.

Mr. SUTCLIFFE. Now, perhaps you could rephrase for me again where, under your proposal, the incentives to good State regulation would come.

Mr. PASSER. Well, I think the key point about it is that the assessment, the postinsolvency assessment, takes place on a statewide, not a nationwide, basis. The companies doing business in that State are assessed in proportion to their business in that State and they have good reason to be in favor of the kind of regulation to which 99.9 percent are conforming anyway. They have good reason to support the Commissioner and others in the attempt to bring the last black sheep into the fold. In other words, it is an industry that is predominantly successful, predominantly solvent. Only in isolated cases is this not so. This helps to put pressure on the Commissioner from the industry as well as from the general public and the policyholders to go that last little step in regulation in order to eliminate this problem.

Mr. SUTCLIFFE. Are there any other ways to accomplish an incentive to good regulation that you have considered?

Mr. HAMILTON. We have looked very hard at what we call the pocketbook incentive and we think we have one. We think when the people who have to pay the bill have to face up to that they may well exert their influence in a manner different than when they were simply trying to stave off having to foot the bill.

Mr. SUTCLIFFE. Which people are you referring to?

Mr. HAMILTON. Both the people in the State as a whole, the policyholders, and most especially the industry.

Mr. SUTCLIFFE. And that I guess gets us back to our discussions about the 10-cent increase in premium and I think it might be useful——

Mr. HAMILTON. We have seen very effective actions in the area of consumer protection by advocates of consumer protection, the ability to focus attention in these areas and pinpoint what it is that is causing the discrepancies, the difficulties. It has been very effective.

Mr. SUTCLIFFE. I would agree with you 100 percent and perhaps this is why—well, let's raise a question. If that is where incentive comes from, from publicity and focus, from embarrassment as the NAIC itself suggests, why do you need the incentive of assessment in the State if in fact you find out—and this is purely conjecture—if in fact you find out that it is more efficient and more economical to have a nationwide premium base for providing protection to policyholders of insolvent companies?

Mr. HAMILTON. If we had no States that adopted any plans, if there were no forward motion in evidence despite the pressure, one might argue for a national plan or at least a different remedy than we would propose. But that is not the case. You have a number of

States which have acted to have a high level of interest in prompt action——

Mr. SUTCLIFFE. How many States have acted at the present time?

Mr. HAMILTON. Eight States now have plans of one kind or another. Twenty-six State legislatures have the model State statute recommended by NAIC before them now. Twenty-odd of those are thought likely to act this year.

Senator Moss. Thank you, Mr. Sutcliffe, for posing those questions and stimulating the discussion here and the reaction.

We do appreciate what you gentlemen have told us. It has helped bring into focus some of the points with which we must come to grips when the administration proposal comes up.

I don't know if any of you have any further comments you want to make right now as a result of the colloquy. If you do I would welcome them. We do look forward to a continuing dialog as soon as we have the administration proposal before us to lay down beside S. 2236 because we are anxious to get into the marking-up phase as soon as we can get our thinking clarified and make sure of the direction we want to go. And we are going to need your continuing counsel as we do all this.

I want you to know we appreciate your coming this morning. Sorry to have held you right through the lunch hour, but since you all work for the Federal Government I guess you are used to that.

It has been very helpful to us. It has sharpened up some different points of view that many of us hold, and staff holds, and that you hold. And yet we are all, I think, seeking the same result and we want to get there with the best possible device we can.

Yes?

Dr. PASSER. I wanted to make one final comment. We do intend to be responsive to your request for expeditious action. We are assigning the maximum personnel resources to this that we can. We are not 100 percent sure that we can meet your 24th of February date, but we are going to try very hard to do so. We are hopeful that we will be able to submit our proposal by then or very shortly thereafter. We recognize the urgency and will put maximum effort into this.

Senator Moss. Thank you. We appreciate that very much, Dr. Passer. Any way we can cooperate in helping to get this moved, we want to do it. So thank you, Dr. Passer and Dr. Cherington and Mr. Hamilton and Mr. Walsh, all of you, for appearing here.

(Whereupon, at 1:15 p.m. the committee was adjourned.)

ADDITIONAL STATEMENTS AND LETTERS

NATIONAL ASSOCIATION OF INSURANCE AGENTS, INC.
Washington, D.C., February 10, 1970.

Senator WARREN G. MAGNUSON,
Chairman, Committee on Commerce,
U.S. Senate,
Washington, D.C.

DEAR CHAIRMAN MAGNUSON: The purpose of this letter is to express to you and your committee the views of this national association in connection with the bill, S. 2236. We respectfully request that this communication be included as part of the official record of your hearings on your proposal to establish a Federal Insurance Guaranty Corporation.

This statement is presented in behalf of the 50 state associations of insurance agents which, as a Federation, make up the National Association of Insurance Agents, Inc. Our membership consists of 36,000 member agencies and of 150,000 individual agents with a half million employees.

The National Association of Insurance Agents would be the first to concede that there were recognizable weaknesses in state regulation which left room for insolvencies of insurance carriers to occur. In retrospect, we see the unhappy results of noninsurance people deliberately collecting premiums and diverting monies to their own use; loose, if not dishonest, management; and simply, ineptness.

As opposed to the Senator Dodd allegations of 1967, the laboriously determined facts gleaned from insurance department records and court proceedings disclosed that for the period under study the actual loss through insolvency was less than one per cent of premium volume.

It has been clearly established by National Association of Insurance Commissioners' analysis that the Magnuson Bill (S. 2236) would result in costing six dollars for each net dollar available to the fund. Manifestly, any scheme which results in 83 per cent of the funding being spent for administration and supervision of the industry is a proposition that would be unworthy of application at any level of government.

The whole approach is as unsound as the use of an elephant gun to kill a gnat.

Three per cent of the insurance premium dollar is already being paid by the public in taxes and fees. Of the millions of dollars taken by the states, only a small portion has heretofore been allotted to the insurance departments for regulation of the business. A general, substantial increase in insurance department budgets has become the order of the day, enabling regulatory officials to greatly improve and expand company examination practices. As a consequence, any weakening of an insurance carrier's financial strength is being detected well in advance of possible failure.

We therefore cannot accept the proposition that the public be further burdened by an added tax for the creation of unnecessary preventive measures.

We do not advocate the preservation of state regulation for its own sake. We contend that the experienced, knowledgeable, career personnel of the state insurance departments are completely adequate to the task; that the creation of a federal apparatus superimposed upon the now satisfactory state regulatory machinery would represent an unnecessary burden to be financed by the public.

Consider now the steps taken by the states to prevent the recurrence of such happenings, viz:

1. Substantial increase in financial requirements for new carriers.
2. Investigation of the character of the persons involved.
3. Mandatory, frequent auditing by insurance department examiners.
4. Regulating the transfer of company assets.
5. Establishment of more adequate state regulatory budgets, enabling the departments to hire and retain fully qualified personnel.
6. The establishment of compulsory uninsured motorist coverage, expanded to include protection for the driver whose carrier is insolvent, thus eliminating

all but a tiny portion of financial hardship on the public, that tiny portion being the pedestrian.

7. In several instances, the creation of a state insolvency fund.

No one will deny that with the power to regulate goes the power to tax, and that, once machinery such as the proposed Federal insurance guaranty proposition is set in motion, there will be no end in sight. Therefore, the National Association of Insurance Agents advocates complete abandonment of the concept as expressed in S2236, Senator Magnuson's bill to establish a Federal Insurance Guaranty Corporation.

This Association, at the same time, dedicates itself to the strengthening of preventive measures in the states through the continuation of our close, personal rapport with our insurance departments and our state legislators. We are confident of our ability to, in the public interest, achieve the desired results.

Sincerely,

LYLE HUGGINS, *President.*

Re Federal Insolvency Fund for Property & Casualty Insurance Cos.

FEBRUARY 11, 1970.

Hon. WARREN G. MAGNUSON,
U.S. Senate,
Washington, D.C.

DEAR CHAIRMAN MAGNUSON: A great controversy has been generated in Oregon among those of the Insurance Industry. This issue is centered around Senator Magnuson's bill, S. 2236, which would create a federal insolvency fund for property and casualty insurance companies. There is unanimous sentiment among Oregon's insurance industry, including the State Commissioner, that such a program is not needed at this time in Oregon. Therefore, I would like to submit to the Committee the following letter from the Insurance Commissioner to me wherein he addresses himself to the merits of S. 2236. It is my belief that this Committee and other interested parties could benefit from the Commissioner's expertise in this area.

MARK O. HATFIELD.

DEPARTMENT OF COMMERCE,
Salem, Oreg., January 19, 1970.

Hon. MARK O. HATFIELD,
U.S. Senator from Oregon,
Senate Office Building,
Washington, D.C.

DEAR SENATOR HATFIELD: Senator Magnuson has introduced Senate Bill 2236 which, if enacted, would create a federal insolvency fund for property and casualty insurance companies.

The bill certainly seeks a laudable end—protecting insurance buyers against the insolvency of their property and casualty insurers. It is based upon the concept of the Federal Deposit Insurance Corporation. Nonetheless, it is my belief that the bill is unnecessary at this time and, further, contains within it the implicit destruction of the present system of state regulation of insurance in favor of an expensive and unnecessary federal system which will stultify rather than enliven an important socio-economic service.

Let me give you some of the specific reasons for my opposition to the bill.

While any loss to a policyholder is a matter for public concern, the losses due to insolvencies which are asserted as the justification for the bill are overstated. The figures used represent the sum of the gross potential liabilities of insolvent insurers, without regard to the actual loss payments those companies were able to make, or the alternative recoveries made from other sources by claimants. As an example of the latter, most states, including Oregon, require auto insurance policies to contain an "uninsured motorist" clause of a type which provides that the insured's own company will reimburse him if the insurance carrier of the person who is liable to him is insolvent. The failure to recognize this, and other offsets, results in a manifold overstatement of the actual loss to claimants.

The states can better handle the concern of insolvency themselves. California and Michigan already have done so by providing that all property and casualty

insurers licensed to do business in those respective states constitute a pool to provide for the payment of any funds due to policyholders or claimants from any insolvent property or casualty insurer admitted to do business in those states. The National Association of Insurance Commissioners, at its meeting in December of this year, adopted a model insolvency protection bill using this approach, and made a policy statement that each state would enact such a bill in order to protect its citizens. It is my intention to offer this model bill, modified to meet Oregon legal standards, to the 1971 Legislature as the most important legislative request of the Insurance Division. I am sure the preponderance of the insurance industry will support this bill in Oregon and elsewhere, rather than a federal scheme.

The National Association of Insurance Commissioners operates an established, time-tested system for the examination of insurance companies for solvency and solidity. The fifty states cooperate in the examination of all insurance companies in all lines of business. Senate Bill 2236 would create a duplicative system of federal examination for property and casualty insurers only, with permission to set federal standards which might or might not conflict with the standards being used.

The NAIC Valuation of Securities Office, in New York, annually prepares a compilation which sets forth the value to be assigned to various securities for the purpose of computing the solvency of an insurance company upon examination. An issue might be raised against the reliability of state examinaitons in that the Valuation of Securities office was misled in the Community National Life Insurance Company case, resulting in a false picture of solvency. But, the Securities and Exchange Commission, a federal agency, was likewise fooled by the same people who succeeded in misleading the NAIC's security office. Further, NAIC responded promptly and effectively when the problem arose to strengthen the evaluation procedures for securities and prevent a recurrence.

The cost of the proposed federal bill would be excessive, in my view. Oregon policyholders would be required to pay an extra "tax" in the form of increased insurance premiums of $318,000 per year (based on 1967 figures). This amount equals two-thirds of the entire Oregon Insurance Division's current budget for one year. This tax would be a continuing one and would far exceed the costs of a state operated, post-assessment insolvency fund such as the one contemplated by the NAIC model bill. Oregon has had only one property and casualty insurance company insolvency in the last decade. That was the Pioneer Mutual Insurance Company, which went under as a result of the 1962 Columbus Day windstorm. The Pioneer Mutual failure was directly attributable to the fact that it lacked catastrophe reinsurance coverage. Had the proposed state insolvency bill been in effect at the time of the Columbus Day storm, the losses to those policyholders would have been compensated at less cost to Oregon premium payers than a single year's premium required from them to the federal insolvency fund.

I should point out that even if the bill were to pass, it covers only property and casualty insurers, and states would still have to provide regulation for life insurance and health insurance companies. This could very easily bring about absurd situations. For example, we frequently must resolve differences between casualty insurers and health insurers as to who is responsible for hospital bills after an accident where there is no liable third party. If the federal government controlled the casualty insurers and the state the health insurers we might find that the federal people say the health insurer should pay while the state says the casualty insurer should pay. Since neither government could control the company it thought responsible, no one could force payment and the insured would be left holding the bag (or the hospital bill). Under the present system the state decides (within the policy terms) who should pay, and they pay.

When I see the administrative problems and time delays that exist in the Welfare and Unemployment Compensation systems and compare those systems with the capacity of well-financed, well-staffed state insurance departments to meet problems in a timely and economical manner, I become more and more convinced that the regulation of insurance, which achieves a national character through the interstate cooperation engendered by the NAIC, ought to remain in the hands of the states. I do not mean for a moment to suggest that Senator Magnuson wants to bring property and casualty insurance under federal control, but I am convinced, and so are others much more experienced in the business than I, that it is the inevitable and end result of the passage of S. 2236.

Sincerely,

CORNELIUS C. BATESON,
Insurance Commissioner.

STATE FARM MUTUAL AUTOMOBILE INSURANCE CO.,
Bloomington, Ill., February 20, 1970.

Hon. WARREN G. MAGNUSON,
Chairman, Senate Commerce Committee,
Old Senate Office Building,
Washington, D.C.

DEAR SENATOR MAGNUSON: In view of your Committee's consideration of S. 2236 and the problem of insurance company insolvencies, we would like to take this opportunity to bring to your attention a proposal which we believe is directly responsive to this problem.

We share in the concern for those who innocently suffer financial loss through the insolvency of insurers. The findings of interested legislative committees dramatically reflect the fact that present regulatory controls for insolvency are inadequate and need to be improved. Those findings indicate that the primary objectives of any remedial legislation should be to devise regulatory safeguards which will prevent or minimize, in the first instance, the occurrence of insolvencies. The factual record developed by the Senate Antitrust and Monopoly Subcommittee demonstrates that most of the insolvencies of the past decade have resulted from the unscrupulous conduct of a limited number of individuals. They have dissipated good assets—through wasteful practices, through high commissions to controlled agencies, through the substitution of poor securities for sound securities, and, in some cases, through outright fraud.

When this can occur in a business which has an elaborate regulatory system, then obviously regulation for solvency needs to be improved. The regulators need early warning devices that sound alarms before a company's financial condition becomes critical. Means must be found to insulate the regulator from any tendency to temporize, vacillate or procrastinate when conditions exist which are leading a company toward insolvency.

These considerations have led State Farm to propose a concept which will, we believe, safeguard the ability of an insurer to satisfy, at all times with sound assets, its obligations to its policyholders and claimants. In brief, we propose the creation of a custodial arrangement under which each insurer would maintain with an independent custodian, such as a bank, cash and marketable securities equal to its reserves for losses, loss adjustment expenses, and unearned premiums. This requirement that custodial deposits be maintained is designed to guarantee that assets needed to pay claims and other obligations arising out of the insurance contract will be available when needed. It should prevent many insolvencies and reduce the impact of those which may occur. Thus, the regulator is furnished with a new and invaluable tool in regulating for solvency.

There are several precedents for an approach of this nature. For example, the Dominion of Canada requires that companies doing business in Canada maintain, in a special deposit, assets sufficient to cover liabilities incurred in Canada. The State of New York, more than half a century ago, enacted a requirement that all alien companies doing business in New York maintain, in a trusteeship account, assets sufficient to cover all liabilities and the minimum capital and surplus applicable to the lines of business engaged in by that company. The countries of Mexico and Germany each maintain similar requirements.

We suggest that any meaningful legislation addressed to the general problem of insurance insolvency should include a specific requirement for the creation of such custodial accounts. State Farm's proposal is described in detail in Exhibit G, attached to our testimony before the Antitrust and Monopoly Subcommittee presented on December 9, 1969. We would be happy to furnish a copy of that statement if this would be helpful to your Committee's consideration of this problem.

Respectfully,

DONALD P. MCHUGH,
Vice-President and General Counsel.