



LEGISLATIVE POSITION

Professional Insurance Agents of New York State Inc.

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PIANY supports reforms to New York's insurance security funds to ensure adequate protection for policyholders in the event of insurer insolvency.

PIANY recommends that the Insurance Department undertake the following steps to follow up on the legislatively-mandated report on the state's insurance security funds, based on an evaluation by outside consultant RSM McGladrey in 2005-2006:

An assessment of progress made to date on each of the report's recommendations.

Further study focusing on that portion of the state's insolvency system which was not a part of this evaluation, i.e., the Liquidation Bureau's operations in its role as receiver.

A report to the public, summarizing the findings of such assessment and any further study, including the status of progress on previous recommendations, any further recommendations and future plans.

Preparation of legislation to accomplish those steps which require legislative action.

Regarding legislation, PIANY offers the following positions:

Support for merging the Public Motor Vehicle Liability Fund with the larger and more financially secure Property Casualty Insurance Security Fund.

Support for time-barring claims against insolvent insurers to provide greater certainty and speedier resolution to the liquidation process.

Support for more closely tying funding caps and assessments to projected cash-flow needs, which pre-supposes systematic development of actuarial projections regarding such needs.

Opposition to changes that would reduce the current protection provided to New York's policyholders, including lowering the current \$1 million limit or eliminating protection for certain policyholders based on their net worth.

Discussion: financial health of funds

PIANY believes that no action should be taken that reduces the current level of protection provided by New York to its policyholders and claimants. These financial caps already are decades old, and their value clearly has diminished over the years relative to the exposure of policyholders to loss. Part of the value of using New York-licensed insurers, for which the statutory and regulatory scheme embodies an overwhelming preference, is the assurance of financial oversight. When, despite such oversight, one becomes insolvent, the state should make every effort to see that the insurer's obligations are honored.

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PIANY strongly opposes excluding from such protections certain policyholders based on net worth. The suggested threshold amounts of \$25 or \$50 million really do not automatically define an entity that can withstand a major financial loss. In any case, we believe even consideration of such exclusion is an inequitable approach, given the many questions that surround the current operations of the Security Funds.

PIANY's major concern is with the PMV fund, which, according to the consultants "is impaired and clearly has been for a prolonged period of time." It is disturbing that claimants are not being paid timely, and policyholders are not being defended in legal actions related to potential claims. We view the prolonged lack of action providing redress for claimants and insureds as a serious breach of the public trust.

PIANY supports the findings of the outside auditors that "Currently, the PMV Fund is too small to be self-sustaining." Based on the report's findings that merging the PMV Fund with the main property-casualty fund would result in assessments on motor vehicle premiums that would "still only be at approximately the 1% level," after finding a separate financial solution to the PMV's current backlog, PIANY strongly supports this approach.

Moreover, PIANY is concerned about the potential effect on all funds of any future, large insolvencies. The consultants' report mentions this potential with respect to Kemper. Recently, news reports also question whether the Royal and SunAlliance run-off may end in insolvency—possibly leaving unpaid claims connected to the World Trade Center attacks. We would recommend proactive investigations into the facts regarding these carriers and a report on the Department's findings. (Since neither company is actively writing business, the traditional sensitivity of such reporting because of its potential effect on the company's continued viability should not be a factor.)

Discussion: NYLB Operations

Key to the health of the Security Funds is the effective management of the New York Liquidation Bureau. Only one aspect of NYLB responsibilities was audited by outside consultants who submitted a report in 2006 after studying the role of the NYLB in its management and accounting of the Funds and the claims payments made on their behalf. The NYLB's other role is that of receiver on behalf of the liquidated companies' estates—i.e., the aggressive pursuit and collection of reinsurance recoverables and other revenues due to New York from ancillary jurisdictions, creditors, etc. The audit results suggest that all functions of the NYLB should be evaluated.

In 2005, the Legislature reacted to a public crisis that occurred that year in funding of the insolvency funds, by requiring the Superintendent to study the funds and report, with recommendations, to the Legislature. The mandate included an outside audit. The audit was conducted in 2005-2006; based on its recommendations, the Superintendent reported to the Legislature on May 1, 2006.

Even a cursory reading of the outside auditor's report suggests a striking lack of leadership, oversight and effective procedures and technology for an operation that employs 350 people and oversees the estates of 60 defunct insurance companies. Even where auditors report optimistically about "several initiatives of the [Liquidation Bureau's] new management regime (led by Jody Hall)," it should be understood that former Special Deputy Superintendent Hall was discharged in August, 2006 and indicted in December, 2006 for actions alleged to have been committed in her role at the Bureau. With this in mind, here are a few of the shortcomings cited by the auditors:

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There has been a current lack of continuity in the senior and executive management structure of the NYLB. [i.e., In the preceding four years, three Special Deputy Superintendents, including Hall, and four Chief Financial Officers] . . . Currently, difficulty exists for management in terms of implementing longer-term business plans, strategies, etc. . . .given recent turnover in senior level positions.

There does not appear to be any centralized monitoring/management/strategic planning for the Security Funds.

The NYLB would benefit from access to actuarial resources since none are currently available to the NYLB.

During our review, procedures did not exist to test the accuracy of the TPAs' data integrity practices.

The NYLB had not previously attempted to evaluate the ultimate liability of the Funds for known estates.

[While] there are regulatory mechanisms to which the NYLB is subject . . . this regulatory oversight does not extend to annual audited financial statements or quarterly filings with a third party regulator.

A consolidated financial statement for the Security Funds does not currently exist. . . Neither a general ledger, nor a comprehensive set of financial statements is maintained for the three funds in Albany . . . The only statements that are prepared are the Income and Disbursements Statements, which are included in the Annual Report to the Superintendent each year.

The NYID . . . prepares Income and Disbursement tables for each of the three funds for inclusions in the Annual Report to the Legislature. . . . When shown to several NYLB personnel, they were unaware of these tables, which implied this information is not shared openly between the two areas prior to inclusion in the Annual Report. . . . Data provided to the Legislature should be reconciled to other records.

Prior to our evaluation, NYLB management had never previously produced the kind of analytical data from its own data bases or loss data from the TPAs needed to perform an actuarial analysis. . . . Note that all of the data we have placed reliance upon for purposes of the actuarial assessment have come from ad hoc system extracts rather than regular data runs that would have been tested and validated over time, thereby enhancing reliability.

[Regarding TPAs which were first hired to accommodate the large insolvencies of Reliance and Reliance,] The NYLB previously had never requested Type II SAS No. 70 audit reports from the TPAs. [The auditors then go on to discuss their subsequent inability to secure such reports for three of the five current TPAs.] . . . Appropriate oversight and monitoring of the TPAs is required.

TPA data should be obtained by the NYLB on a regular basis. This data should be reconciled/balanced and tested. . . . There should be a clear feedback loop between what is passing through the NYLB systems and what is being recorded in the Fund's bank accounts.



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These amounts should be reconciled on a monthly basis to ensure the integrity of both sets of data. The NYID – T&A would have to produce this data timely to permit this control.

There is not a regularly scheduled, automated link between the TPAs' processing NYLB's claims and the NYLB claim system. . . . Since claims system data appears to tie directly to the estate reports prepared by the NYLB Finance Department, it would appear that these estate reports are distorted by the lack of timely data for those estates for which TPAs are settling claims.

These findings suggest there is a great deal of room for improvement at the NYLB and its relationships with the TPAs, if NYLB continues to rely on their services going forward. It appears from the audit report that attention needs to be given to the question of oversight and selection of TPA's and standardizing their contracts.

When the Superintendent reported to the Legislature on May 1, 2006 on the findings, a scant two pages of this 13-page report were devoted to a discussion of "Administrative Reforms." Even this discussion conceded that reform was "a 'work in progress'" at the time of the report. Given the subsequent departure of Deputy Superintendent Hall, it is reasonable to wonder how much progress actually was accomplished during the second half of 2006. PIANY believes New York's reputation for effective, transparent government operations could be tarnished by a continued inability to address the serious shortcomings detailed in this report.

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