NCIGF℠
National Conference of
Insurance Guaranty Funds

nolhga
National Organization of Life & Health
Insurance Guaranty Associations

November 21, 2007

Re: **Treasury Review of Regulatory Structure Associated with Financial Institutions: Request for Comments (TREAS-DO-2007-0018)**

I. The Commentators. The following comments are delivered jointly by the National Conference of Insurance Guaranty Funds (NCIGF) and the National Organization of Life and Health Insurance Guaranty Associations (NOLHGA) pursuant to the Request for Comments issued by the Department of the Treasury on October 11, 2007.

II. The Interests of the Commentators. NCIGF and NOLHGA are both deeply involved in a specialized area of the financial services regulatory structure: coordinating the provision by their memberships of specified protections to insurance consumers in situations where the insurer owing obligations to consumers has entered insolvency (liquidation) proceedings. In some ways, NCIGF and NOLHGA and their members perform a function in the insurance market that is roughly analogous to the function of the FDIC with respect to its member and insured depository institutions. NCIGF's members are principally concerned with protecting consumers of failed property and casualty insurers. NOLHGA's members are principally concerned with protecting consumers of failed life or health insurers.

NCIGF and NOLHGA neither support nor oppose any specific regulatory reform proposals that have to date been the subject of public discussion within Congress or the Department of the Treasury. However, in light of the increasing attention given in recent years to the possibility of an augmented federal role in supervising (or directly providing) regulation of the business of insurance, NCIGF and NOLHGA believe it important that the Department and other interested parties have a clear understanding of the nature of the current guaranty protection mechanisms protecting insurance consumers; the track record, resources, and financial capacity of those mechanisms; the ability of those mechanisms to adapt to various proposals for regulatory change; and the implications for consumers and others of certain specific concepts for establishing alternative consumer "safety net" mechanisms.

III. Further Inquiries Invited. The information contained in this response is necessarily concise and summary in form. Representatives of NCIGF and NOLHGA would be happy to respond – in writing or in person – to any specific requests for follow-up information or data.

IV. Summary of Commentators' Perspective. NCIGF and NOLHGA take no position on legislation permitting "optional federal chartering" (OFC) for insurers, nor any other specific proposals for insurance regulatory reform at the federal level. However, NCIGF and NOLHGA believe that, should OFC legislation be adopted, the optimal approach to providing a financial safety net for insurance consumers whose companies fail would involve continued reliance on the current guaranty system, both for companies keeping their state charters as well as for those opting for a federal charter. The same conclusion has been reached by the drafters of OFC bills currently introduced in the Senate and the House. That conclusion is sound for the following reasons: (i) the current system has been tested and proven successful in hundreds of insurer insolvencies over the past four decades; (ii) the system is experienced and fully staffed with experienced personnel in place in every state; (iii) the system has ample financial and operational capacity; (iv) reliance on the current system would eliminate the need to expend federal tax dollars to create, staff, and maintain a new federal bureaucracy; and (v) the current system could easily, logically, and fairly be adapted to cover companies choosing a federal charter, since it *currently* covers the companies that would elect such a charter change.

V. Background Information. In order to understand the current insurance safety net system, it is important to understand several background facts about the system and the environment in which it operates. The following are among the more critical facts:

History of State Regulation. Insurance has been regulated almost entirely at the state level throughout U.S. history. Initially, that was at least in part a consequence of an 1869 ruling of the United States Supreme Court (*Paul v. Virginia,* 75 U.S. (8 Wall) 168 (1869)) to the effect that the transaction of insurance business did not involve "interstate commerce" and, therefore, was beyond federal regulatory authority. When the Supreme Court reversed the holding of *Paul v. Virginia* in 1944, holding insurance to be "interstate commerce" in the case of *United States v. Southeastern Underwriters,* 322 U.S. 533 (1944), it became clear that the federal government had the power to regulate insurance. However, Congress opted largely to maintain the status quo – state regulation – by enacting the McCarran-Ferguson Act in 1945, 15 U.S.C. §§ 1011-15, under which Congress re-established the primacy of state insurance regulation *except* to the extent Congress might explicitly choose to regulate the field. OFC legislation would constitute such an express Congressional decision to regulate insurance.

Bifurcation of the Consumer Insurance Markets. Although it is customary to refer to the insurance industry as though it were monolithic, in fact the industry is divided into several quite distinct segments. The most significant and clearest distinction is between those companies writing direct property and casualty business, on the one hand; and those writing direct life and annuity business, on the other. While a relatively small number of insurance holding company structures include separate subsidiaries that write both life and annuity and property/casualty business, for the most part companies specialize in one such line or the other. The contractual commitments embodied in property/casualty contracts are fundamentally different than those embodied in life and annuity contracts. Those fundamental differences are reflected in completely different systems for

marketing, operations, accounting, and investments; and also in separate and distinct regulatory frameworks for property/casualty and life and annuity insurers. In addition, the financial safety net system currently in place across the country is similarly bifurcated: the property and casualty insurance guaranty associations that comprise NCIGF's membership operate separately from the life annuity and health insurance guaranty associations that comprise the membership of NOLHGA.

The Executory Nature of Insurance Contracts. Insurance contracts typically comprise a complex of promises to insurance consumers that, taken as a whole, are quite different in nature from the simple commitment inherent in, for example, a depository account with a bank or thrift institution. In the case of a deposit account (savings or checking), a primary consideration is the availability of funds on a "demand" basis to meet current daily needs of the depositor. As a consequence, the primary objective of a consumer "safety net" system, as provided by the FDIC for federally insured depository institutions, is the provision (within program limits or "caps") of immediate liquidity for the account. When a bank fails, in effect the FDIC replaces dollars with dollars, which permits fulfillment of the deposit account promise of immediate liquidity.

By contrast, the principal objectives of most insurance contracts – whether property/casualty or life and annuity – have little to do with current liquidity and everything to do with protection against events that may occur long after the financial failure of a consumer's insurance company. The protections vary tremendously with the type of insurance contract written and the facts of the consumer's situation, and may range from the provision of legal defense or indemnity for a consumer owning a homeowner's policy to the continued provision of life insurance at stable rates (perhaps established decades earlier) for a consumer who may be medically uninsurable at the time his life insurance company fails.

In order to fulfill the promise embodied in an insurance contract, it is not enough merely to replace dollars with dollars; instead, it is necessary to replace insurance with insurance, which is the role served by the current guaranty association system.

Safety Net Requirements When an Insurer Fails. In order to meet the fundamental requirement of the banking safety net – assuring depositor liquidity by being able to replace dollars with dollars almost instantaneously – the FDIC requires a high level of pre-funding and a relatively low level of operational banking expertise and resources.

However, since the focus of an insurance consumer safety net is not liquidity protection but rather the performance, over a number of years, of the executory contracts in force when an insurer fails, the focus of an insurance safety net must be on the delivery of technical insurance expertise backed by sufficient financial resources to honor the contractual commitments of the failed insurer as they come due over a period of years. That is precisely the focus of the current guaranty association system.

The Current System for Insurer Insolvency Administration. Just as insurance companies are regulated almost entirely at the state level, it is also at the state level where

the current regulatory system provides for the receivership of a failed insurer and for the related consumer "safety net" provided by the members of NCIGF and NOLHGA. In particular, the receivership of a failed insurance company is administered by the insurance commissioner of the single state where the company is chartered – in effect, its state of incorporation – pursuant to the insurance receivership laws of that state, and under the supervision of a court in that state.

The Elements of the Current Insurance Guaranty System. Individual insurance consumers today are protected against specified losses from an insurer's insolvency by the guaranty associations that now exist in each state.[1] Protection for consumers generally is provided by the guaranty association of the state where the consumer resides or, in the case of property insurance, where the property is located. When insurers doing business in multiple states fail, the activities of the multiple affected guaranty associations are coordinated by their national membership organizations – NCIGF, in the case of property and casualty insurers, and NOLHGA, in the case of life and health insurers.

Thus, although the receivership of a failed company may be administered by an entirely different state – the state where the company was chartered or "domiciled" – and although primary responsibility for regulating the financial health of the failed company is also vested in the state where it was domiciled – each individual guaranty association responds to an insolvency by protecting the residents of that association's state, wherever the failed company may have been domiciled, regulated, or placed in receivership. To illustrate, while a failed insurer that did business nationwide may have been domiciled in one state, *e.g*., Illinois, its consumers receive "safety net" protection from the guaranty associations in the states where they reside (or where the insured property is located). The protections provided from as many as 50 or more guaranty associations are coordinated through NOLHGA and NCIGF.

The Guaranty System in the Context of the Overall Regulatory Scheme. Guaranty associations are creatures of state statute whose responsibilities to protect consumers are "triggered" by the entry of a court order placing an insurer into liquidation proceedings when the insurer is found insolvent. Delivery of the protections mandated by statute is generally administered by a state guaranty association executive director (often assisted by staff or outside consultants), working in coordination with the receiver of the failed insurer. Performance of those guaranty association functions is overseen and guided by independent Boards of Directors drawn from the insurance companies doing business in the states, and funded in the first instance by assessments levied upon those insurers doing business in the state. Although most guaranty associations are subject to the supervisory oversight of their state insurance commissioner, they are not generally[2] or in

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[1] Every state has an insurance guaranty association that provides protection for the failure of a property or casualty insurer, and also an association that protects against the failure of a life or health insurer. One state (Wisconsin) combines those functions within a single association, while a few other states have additional guaranty associations providing protections for certain specific types of business.

[2] The form of most insurance guaranty associations is that of a special, non-governmental, not-for-profit corporation established by specific state enabling legislation. However, in four states (Arizona, Arkansas,

any meaningful sense operated by state government, and they do *not* have a role (even in their own states) in monitoring or policing the solvency of insurers. Similarly, guaranty associations almost never serve as the receiver of a failed insurer. Instead, the receiver of a failed insurer is by statute the insurance commissioner of the state where the insurer was granted its charter, and most commissioners in that role appoint a "special deputy receiver" to handle the details of receivership administration.

VI. The Current Guaranty System and Financial Institution Regulatory Structure.

At page 3 of the Request for Comments, the Department states that it is important to evaluate financial institution regulatory structure and "(C)onsider ways to improve efficiency, reduce overlap, strengthen consumer and investor protection, and ensure that financial institutions have the ability to adapt to evolving market dynamics... ."

The nature of a financial safety net mechanism developed in conjunction with an overall scheme of financial institution regulation bears directly on the measure of protection afforded consumers. The nature and operation of the system (currently and historically) also bears a relationship to the efficiency of the regulatory system; the extent of overlap it contains; and its ability to adapt to future developments. Several topics raised by the Request for Comments are to some extent addressed generally in the background summary, "Overview of the Current Insurance Guaranty System," attached as Appendix A. Other more specific issues raised by the Request for Comments are addressed below.

Consumer Protections Provided by the Current Guaranty System. The current system provides insurance guaranty association protection for individual insurance consumers purchasing traditional personal lines contracts in amounts at least equal to, and in many cases, substantially higher than, current levels of protection afforded to insured bank and thrift depositors. (Details of benefit levels are described generally in Appendix A.) However, guaranty association protection of insurance benefits is essentially different from bank deposit insurance in the sense that the principal focus of the insurance safety net is the fulfillment of the insurance promise to the consumer, and not merely the assurance of liquidity of deposited funds. See "Background Information – The Executory Nature of Insurance Contracts," above.

The current system is funded in the first instance by assessments levied by each state guaranty association upon the insurers who do business in that state, up to annual statutory limits that are a percentage of a company's recent premium volume in the state.[3]

New York and Pennsylvania), at least some elements of the guaranty mechanism are operated as part of state government.

[3] Guaranty associations also fund the performance of their obligations to some extent through the application of subrogation rights; i.e., they "step into the shoes" of consumers they protect and, having discharged the duties owed the consumers by the failed insurer, take the consumers' place as creditors of the insolvent insurer. Consequently, guaranty associations often receive distributions of some assets that eventually become available over the course of a receivership, although those distributions seldom fully satisfy the claims owed to guaranty associations, and usually are paid – to whatever extent they are paid – years after the guaranty associations have satisfied their obligations to consumers.

In effect, the system allocates the cost of providing the consumer safety net ratably among the insurers in the state, based upon insurers' relative market shares of business. Applying the statutory limits on permitted assessments determines how much funding is available for a given state guaranty association. That funding has almost always proved considerably more than adequate to meet all financial requirements of all guaranty associations in all insolvencies.[4] In the several instances where extreme catastrophes (e.g., Hurricane Andrew and its effects in Florida) have tested the financial capacity of the guaranty association in an individual state, the system has responded with creative solutions that assured full and prompt protection of every consumer at the full, statutorily mandated levels.

Efficiency and the Current Guaranty System. Efficiency in this context is best considered by asking where and how must consumer protection be determined; how it is in fact determined under the current system; and whether the delivery of such protection involves a prompt, direct, effective path to protecting the consumer, rather than redundant or duplicative bureaucracies or impediments to and delays in protection.

Insurer insolvencies are fundamentally different from bank failures, particularly on the liability side of the balance sheet. Insurer liabilities primarily comprise the multi-dimensional promises made to consumers under many types of insurance contracts, typically employing a number of different, non-standardized policy forms even within a single insurer.[5] By contrast, bank liabilities represented by deposit accounts are considerably simpler, essentially one-dimensional, and relatively homogenous.

Moreover, in the case of failed insurers – particularly property/casualty insurers – the liabilities (promises to consumers) are intricately involved with local property conditions and the local tort, health-services delivery, and judicial systems.

Any insurance safety net system would have to specify *ex ante* the benefits that would be made available to consumers were an insurer to fail. Then it would have to provide for the delivery of the benefits in individual cases of insurer failures.

The definition of benefits is relatively straightforward. Under the current system, benefits are defined in the state law establishing each individual guaranty association. Those laws, in turn, are adapted to local conditions by each state legislature from model legislation promulgated by the National Association of Insurance Commissioners

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In addition, in some states, insurance companies are entitled to some measure of state tax relief in respect of assessments that they pay to state insurance guaranty associations.

[4] In 2006, the last year for which such figures were available, the aggregate assessable premium (i.e., the financial capacity to assess for that single year) for NOLHGA's member guaranty associations was $8.1 billion, and the costs actually required in order for life and health guaranty associations to protect consumers in that year were $25.5 million. In 2005, the last year for which such figures were available, the aggregate assessable premium for NCIGF's member guaranty associations was $6.8 billion , and the assessments actually required in order for property/casualty guaranty associations to protect consumers in that year were $989 million.

[5] It is assumed for purposes of this discussion (though perhaps debatable) that asset challenges in an insurer receivership are roughly comparable to asset challenges in the liquidation of a commercial bank.

(NAIC).[6] Some details of the benefits provided under the current system are described in Appendix A.

However, while the definition of safety net benefits may be fairly simple, the *delivery* of those benefits is inherently quite complex. Under both the current system and under any other hypothetical insurance safety net model, delivery of benefits requires the provider of the safety net to work closely with the receiver of each individual failed company to determine, on a contract-by-contract basis, the contractual liability of the failed insurer to each consumer, as well as the proper application of safety net protections (e.g., the statutory obligations of a guaranty association) to that consumer's contractual claim which in turn depends on considerations of law and other factors unique to the state where the claim arises.

The resolution of the consumer's claim against insurer assets and the application of safety net benefits to that claim involve an irreducible quantum of technical analysis that is required under the current system and that would be required under any competing model. However, it must be noted that the *current* system has an infrastructure of experienced analysts and administrators on the ground now in every state: individuals experienced both in working with receivers to analyze insurance contractual commitments to consumers and the application of safety net benefits to such consumers. Moreover, those individuals trained in the current system are also familiar with the complex of local laws and conditions that affect or define the benefits owed to consumers. Even under a federal regulatory model, the claims of consumers in a receivership would still largely turn on local conditions and laws, meaning that a federal safety net essentially would have to replicate the knowledge and experience bank of the current system in order to protect consumers.

Finally, protections provided to consumers under the current system are administered locally, and not determined or administered by a remote federal bureaucracy. Today, a consumer's safety net protection is provided by the guaranty association of the state in which the consumer (or the insured property) resides, as determined by that state's statutes, and as supervised by that state's insurance commissioner.

Regulatory "Overlap" and the Safety Net Function. Regulatory "overlap" is not an issue under the current system. The system now provides that the insurance guaranty association for the state where the consumer resides (or where the insured property is located) is exclusively responsible for providing the specified consumer safety net protections. There is no overlapping responsibility for the provision of those protections.

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[6] The OFC bills pending in the House (H.R. 3200) and Senate (S. 40) would not explicitly mandate the provision of specific benefits by state guaranty associations, but rather would establish "minimum standards" that guaranty associations must satisfy in order to achieve "qualified" status. Those standards are essentially similar to the current NAIC models for state property casualty guaranty funds and life and health guaranty associations. If a state were to fail to achieve "qualified" status, its consumers would be protected by a "fallback" federal mechanism, the National Insurance Guaranty Corporation, provided for in the OFC legislation. Of course, if all states achieved qualified status, that fallback would never be used.

In addition, as noted above, the current guaranty system separates the provision of the consumer safety net from the financial solvency regulation of insurance companies whose consumers are protected by the safety net: Financial solvency is regulated principally by the insurance commissioner for the state where a company is domiciled.[7]

Suggestions have been made in the past – though not recently – that federal insurance regulatory reform might include some type of FDIC-type system to provide a consumer safety net for those whose policies might someday be issued by federally chartered insurers. Such proposals do carry with them an issue of regulatory overlap, to the extent they propose the creation of a parallel federal safety net mechanism, separate and apart from the current guaranty system.

The current system encompasses all companies that are direct writers of insurance in the United States (including those that might opt for a federal charter, were such an option available). Proposals for an FDIC-type system contemplate a division of the financial capacity of the safety net system between a federal system, funded by assessments on federally chartered companies; and a state system, funded by assessments on state-chartered companies. By "splitting" the capacity now available to the current system into two (presumably) more limited pools, less funding would be available in both pools to protect consumers whose companies might fail.[8]

Adaptability of the System to Future Developments. A number of interested observers have concluded that the current guaranty system is highly adaptable to any of a wide range of potential developments in the insurance market and in the regulatory environment. The clearest example is the legislation currently introduced with bi-partisan sponsorship both in the House and the Senate providing insurers with the option of converting to a federal charter (and back to a state charter), in much the same way that is now permitted for banks. Both the House and Senate versions of OFC legislation provide that the insurance consumer safety net would continue to be provided by the current guaranty system, so long as state guaranty associations "qualify" by not discriminating between federally- and state-chartered insurers and their consumers, and so long as state guaranty associations provide a minimum level of protection essentially similar to that provided now in most states.

The logic of that position follows from several considerations. The first is that the current system is recognized as tested and proven, having effectively provided protection for millions of consumers in hundreds of insurance company failures of all types. In

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[7] No changes to this basic "architecture" would be brought about by the OFC bills now pending in the House and Senate; under those bills, financial solvency of federally chartered companies would be regulated by a federal insurance commissioner, and the safety net function would be provided by qualified state guaranty associations (or, if a state failed to qualify, by the "fallback" National Insurance Guaranty Corporation). Companies that maintained their current state charters would continue to be regulated for solvency primarily by the insurance commissioner of their domiciliary state.

[8] It might also be asserted that creation of a federal safety net mechanism would implicitly establish a federal guaranty – presumably backed by federal tax dollars – that would stand behind whatever assessment funding might be available to the federal mechanism.

addition, the system is in place, experienced, fully staffed, and would require the creation of no new bureaucracy and no "learning curve" in order to protect consumers. Moreover, the current system is *already* protecting consumers of the very companies that likely would obtain federal charters by opting to convert their current state charters to federal charters. Furthermore, reliance on the current system would require no federal tax expenditures for establishment, staffing, and maintenance, and no federal guaranty (explicit or implicit) of consumer protections. Finally, the current system, as now constituted, has and would continue to have ample financial capacity to protect consumers of all companies (whether chartered by states or by a federal regulator).

In effect, the concept reflected in the current OFC bills in the House and Senate (continued reliance on the existing guaranty system) would simply treat federally chartered companies as though their charters were issued by a "51st state." To illustrate, the Virginia guaranty associations *now* protect consumers of insurance companies doing business in Virginia whose charters are issued by the state of Illinois or any other state. If, under the pending OFC legislation, an Illinois company were to shift its charter to become regulated at the national level, the same Virginia consumers of that company, under the same contracts, would continue to be protected at the same levels, by the same guaranty association, and supported by the same premium base, as was the case before the company elected to move its charter.

VII. Concluding Observations. The current United States insurance guaranty system is a proven, mature, capable, flexible, and well-financed system that has protected millions of insurance consumers for decades and that is well-suited to continue protecting insurance consumers for the foreseeable future, regardless of how insurance regulation may develop and evolve.

The commentators would welcome the opportunity to review with the Department in greater detail any of the matters addressed in these comments.

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APPENDIX A

Overview of the Current Insurance Guaranty System

Over the past few years, increasing attention has been given to the possibility of an alternative federal system for regulating insurers, and a number of hearings on improving insurance regulation have been held in both the House and Senate. On July 25, 2007, Representatives Melissa Bean (D-IL) and Ed Royce (R-CA) introduced the "National Insurance Act of 2007" (H.R. 3200), which would establish a federal chartering option for life and property/casualty insurance companies and agents. Their 333-page bill is substantially similar to a Senate bill (S. 40), which Senators Tim Johnson (D-SD) and John Sununu (R-NH) introduced on May 24.

The particulars of these and other regulatory reform proposals differ, but each is principally motivated by the desire to create a more uniform and modern regulatory system to address perceived deficiencies in state regulation. While the existing insurance guaranty system was not one of those perceived deficiencies, the proposals all recognize the essential need to provide an insolvency safety net for insurance consumers. The Congressional bills would rely upon the existing insurance guaranty system to provide that safety net for policyholders of federally-chartered insurers, in the same manner that the system currently protects policyholders of state-chartered insurers.

The existing guaranty system is established, experienced, and successful in protecting policyholders from the adverse financial effects of insurer insolvencies. The experience gained and efficiencies achieved in the course of protecting policyholders over the past several decades are substantial. Given this experience, the guaranty system is well positioned to protect the nation's insurance consumers, regardless of the system used to regulate insurers.

HOW THE INSURANCE GUARANTY SYSTEM WORKS

Guaranty associations are organizations created by state law to protect policyholders if their insurance company becomes insolvent. If an insurer becomes insolvent and there are insufficient funds to meet policyholder obligations, the appropriate guaranty associations assess insurers licensed in their states that write the same type of insurance written by the insolvent company. The guaranty associations use money collected from assessments to pay claims and provide other insurance benefits for policyholders of the insolvent insurer, resident in their states, up to specified limits. When life or health insurers are liquidated, the life and health insurance guaranty associations arrange for the continuation of coverage under life and annuity (and certain health) contracts, and the adjudication and payment of claims on most health contracts issued by the failed carrier. When property or casualty companies are liquidated, the property/casualty guaranty associations adjust and pay claims in respect of consumers' policies, and they also pay or provide for a legal defense under liability policies.[1]

[1] Under insurance liquidation laws, virtually all property and casualty insurance contracts, and many health insurance contracts, are cancelled as of the date of liquidation, leaving the guaranty associations responsible for the adjudication and payment of claims that had accrued prior to liquidation. Life and

GUARANTY ASSOCIATION STRUCTURE

Generally speaking, every state has a property/casualty association, and a life and health insurance guaranty association each created by state law, overseen by the state's insurance regulator, and typically operated as a non-profit association.[2] The membership of each property/casualty guaranty association comprises the property and casualty insurance companies licensed to do business in that state, and the membership of each life and health insurance guaranty association comprises the life and health insurance companies licensed to do business in that state. Each guaranty association is governed by a board of directors, the members of which in most states are elected by the association's member insurers and approved by the state's insurance commissioner.

While each state's law establishes the coverage for the residents of its state, nearly all states have guaranty association laws adapted to local conditions by each state legislature from the model property/casualty and life and health guaranty association statutes promulgated by the National Association of Insurance Commissioners (NAIC). Most property/casualty guaranty associations provide coverage on a per claim basis for personal injury and property damages up to $300,000 and provide full benefit coverage for workers' compensation claims. Three states provide higher limits, and six states have somewhat lower limits. Most life and health guaranty associations provide coverage at limits of at least $300,000 for life insurance death benefits, $100,000 for life insurance cash surrender values, $100,000 for annuity withdrawal or payment values, and $100,000 for health insurance benefits.[3]

NATIONAL CONFERENCE OF INSURANCE GUARANTY FUNDS (NCIGF)

NCIGF is an organization of 55 property and casualty insurance guaranty associations, representing the 50 states, the District of Columbia, and Puerto Rico. NCIGF coordinates the activities of its member guaranty associations, monitors litigation that may affect guaranty associations, coordinates with the property and casualty insurance company trade associations on state legislative matters, conducts education and training seminars for guaranty associations, provides financial information concerning the guaranty system, serves as a clearinghouse of relevant information, and provides a national forum for discussion and liaison with the NAIC and insurance receivers.

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annuity contracts covered by guaranty associations typically are not cancelled upon liquidation, and the life and health guaranty associations (within coverage limits) arrange for those contracts (as well as certain health insurance contracts) to be honored as long as policyholders choose to keep them in force.

[2] In Wisconsin, the property/casualty and life and health guaranty association functions are performed within a single entity. In addition, several states have separate guaranty mechanisms to provide protection in respect of certain specific types of benefits or programs, such as workers' compensation insurance or health maintenance organizations. In most states, there are two organizations – a property/casualty guaranty association protecting policyholders of property/casualty insurers, and a life and health guaranty association protecting policyholders of life and health insurers.

[3] Under several of the optional federal charter proposals, life and health guaranty associations will need to meet "federal minimum standards" for coverage limits. These minimum standards are the same as the above-cited coverage limits with one exception. That exception is the limit for health insurance coverage, where the proposed federal minimum standard is set at $500,000 for medical insurance, $300,000 for disability insurance, and $100,000 for other types of health insurance.

NATIONAL ORGANIZATION OF LIFE AND HEALTH INSURANCE GUARANTY ASSOCIATIONS (NOLHGA)

NOLHGA, headquartered in Herndon, Virginia, is made up of the nation's 52 life and health insurance guaranty associations representing the 50 states, the District of Columbia, and Puerto Rico. NOLHGA was created in 1983 to act as the national representative for guaranty associations in developing and coordinating national plans for resolving the complex issues inherent in protecting policyholders in multi-state insolvencies. When an insurer is declared insolvent, NOLHGA assembles a task force of guaranty association members representing the states whose residents are affected by the insolvency. This task force, with the support of NOLHGA staff and legal, actuarial, and financial experts, develops a plan for guaranty associations to provide coverage to policyholders on a consistent, cost-effective, and timely basis. In most cases, this plan involves the guaranty associations making payment to a financially sound insurance company to assume the insolvent company's covered policy obligations. The task force also supports the receiver's efforts to realize value in respect of the company's assets in a manner that maximizes assets available for creditors. At each step in the process, NOLHGA works closely with its member guaranty associations, insurance regulators, receivers, and other interested parties to build consensus on action necessary to protect policyholders and resolve the insolvency fairly and equitably.

INSURER INSOLVENCIES AND THE GUARANTY ASSOCIATIONS

Property and casualty insurance companies sell policies that provide coverage for losses to property, for legal liability to third parties caused by the insured's conduct, and for the cost of defending liability claims against the insured. Life and health insurance companies sell policies of whole-life and term insurance, annuities, and health insurance.

Prior to the establishment of the first modern insurance guaranty associations in about 1970, claimants waited until a liquidation proceeding concluded before receiving even a fraction of their promised benefits.

Today, every state has a property/casualty insurance guaranty association that steps in immediately upon liquidation to pay the claims of and defend the lawsuits brought against the residents of that state for all types of claims covered by the association, up to the limits of the association's coverage. Likewise, every state has a life and health insurance guaranty association that, upon liquidation of an insurer, provides for the payment of claims on health insurance policies and the continuation of contractual protections from life and annuity contracts up to the limits of the association's coverage.

HISTORY OF SUCCESSFUL PROTECTION OF CONSUMERS

The existing insurance guaranty system has a proven track record of protecting policyholders in the event their insurance company fails. Since the early 1970s, the property/casualty insurance guaranty system provided protection to policyholders in more than 450 cases of insurer insolvencies, paying a total of approximately $21 billion in claims and expenses. Since 1988, the life and health insurance guaranty system has participated in approximately 100 multi-state insurer insolvencies. In those cases, guaranty associations have guaranteed more than $21 billion in coverage benefits and

assessed their member insurers over $6 billion to protect more than 2.2 million insurance consumers. Despite this level of insolvency activity and expense, the insurance guaranty system has met all of its obligations and promptly provided protection to all consumers for whom they are responsible in each and every case of insurer failure.

THE GUARANTY SYSTEM IS WELL POSITIONED TO DEAL WITH FUTURE INSOLVENCIES

The nationwide network of life and health insurance and property/casualty insurance guaranty associations has proven extremely effective at achieving its principal mission — the protection of policyholders. As with any effective organization, the insurance guaranty system has evolved over the years and operates with a high level of cooperation, coordination, and consistency that comes only with experience.

NCIGF and NOLHGA have also evolved over the years into national coordinating mechanisms that have established effective and credible working relationships with both insurance regulators and industry members. NCIGF and NOLHGA each employs a complete complement of full-time staff professionals who are well versed in the technical and practical complexities inherent in any insolvency.

Among the key benefits of the insurance guaranty system are the efficiency and cost savings achieved as a result of the functions performed by NCIGF and NOLHGA. The resources and coordination they provide help minimize costs by facilitating a national response plan for protecting policyholders in multi-state insolvencies. This coordination of effort also reduces the length of time it takes to resolve a multi-state insolvency and provide policyholders their statutorily prescribed benefits.

While NCIGF and NOLHGA serve as the national coordinating bodies for protecting policyholders, their individual guaranty association members are aware of and sensitive to local circumstances and respond quickly to the concerns of resident policyholders when an insolvency occurs. The volume of calls and letters from concerned policyholders is understandably high in the aftermath of an insolvency. The staffs of the individual guaranty associations are able to respond quickly to explain coverage benefits and the claim submission and payment process; provide status reports; and resolve specific inquiries. NCIGF's member associations understand their state tort law and court systems and how to adjudicate claims promptly and efficiently. NOLHGA's member associations are familiar with the local standards and practices applicable to provision of life and health insurance benefits. For these reasons, the existing insurance guaranty system is able to enjoy the operational efficiencies of a national system, while effectively responding to the often-local concerns of insurance consumers experiencing financial and other stresses associated with the failure of their insurance company.

Given its significant experience, operating efficiency, and credibility, the current insurance guaranty system is well positioned to protect the nation's insurance consumers from future insolvencies of life and health and property/casualty insurers, regardless of whether those insurers may be regulated under a federal system or by the states.