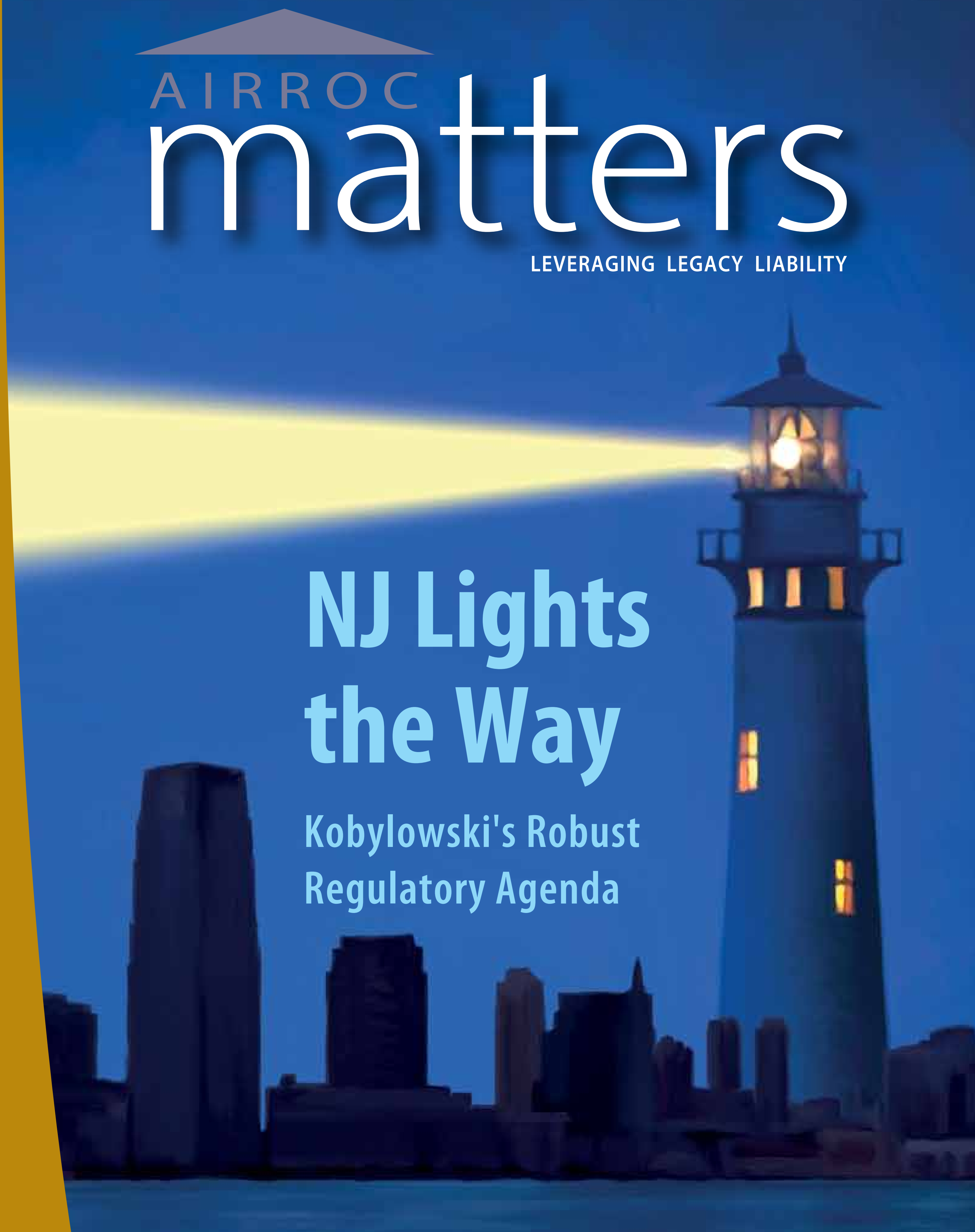
www.airroc.org Vol. 10 No. 2 Summer 2014

AIRROC matters

LEVERAGING LEGACY LIABILITY



NJ Lights the Way

Kobylowski's Robust Regulatory Agenda

A SESSION ON CESSIONS • IS LIMA WORKING? • EXCLUSION CONFUSION
FOCUS ON GIBNEY • THE "BUZZ" IN LEGACY • CONTINUING EDUCATION

Show the Way…Others Will Follow

Peter A. Scarpato

Transfixed upon a distant shore, the lighthouse pierces the darkness so others find their way. A fitting image and tribute to our featured article, Fran Semaya and Fred Pomerantz's interview of *Commissioner Kobylowski* on *NJ's Robust Regulatory Agenda*. The Commissioner sat down with Fran and Fred, offering insights into NJ's regulatory approach to a number of topics, including the National Flood Insurance Program post-Hurricane Sandy, the success of NJ's post-Sandy mediation program, the FSOC, captive insurance in the Garden State, enterprise risk management and many others. We truly appreciate Commissioner's time and candid comments.

Next, Barbara Murray, former AIRROC Run-off Person of the Year, provides valuable operational tips in *Cede it Right the First Time: 10 Practices of Effective Ceded Reinsurance Claims and Accounting Teams*. Covering the necessary culture, technology, financial and operational skills, and team approach, Barbara's article is a must read for anyone in the business of ceded reinsurance. What follows is Karen Deibert, Robert Romano and Jonathan Bank's take on *The Low Down on LIMA: The Legacy Insurance Management Act*. This "low down on LIMA" analyzes the pros and cons of Vermont's newly enacted law, finally concluding that it lacks finality.

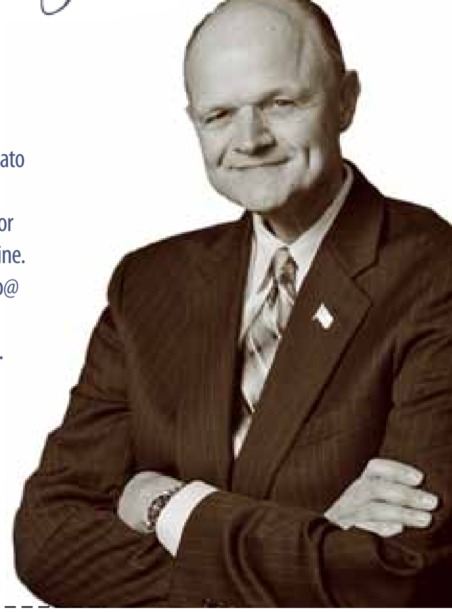
Andrew Lewner and Lauren DiLeonardo take aim at the misfire of early asbestos exclusions in *Ready, Fire, Aim! The Effect of Asbestosis Exclusions.* The article pays tribute to the perils wrought by the best laid plans of insurers who attempted to exclude coverage for asbestos-related illnesses from policies issued in the 1970's and 1980's. Next, this edition's Spotlight feature gets down and friendly with Ed Gibney. In *Gabbin' with Gibney*, Ed opens up to reveal the secrets of his prowess and personality.

In *What's the "Buzz" in the Legacy Industry?*, Executive Director Carolyn Fahey puts her ear to the grapevine, giving us the scoop on recent developments, ADR, regulatory trends and issues for the future. She also offers a whimsical, "colorful" romp in *Seeing Red: From Apples to Sox…*, culminating in her announcement of the location of this year's October event, the Heldrich Hotel and Conference Center in New Brunswick, NJ.

The newest member of our senior editorial team, Assistant Editor Michael Goldstein (welcome Michael!), gives us his valuable AIRROC *Educational Session Summaries/NY*, where a record setting attendance received valuable updates on lead paint litigation, sports-related brain injuries, cases impacting corporations, and other topics. We're also all over feedback from AIRROC's April 9, 2014 regional education session in Boston, the result of a partnership between AIRROC, Edwards Wildman LLP, Alvarez & Marsal, and the Boston Chapter of the CPCU.

Wrap it up with Present Value's coverage of people and companies in the news, and there you go…another great edition. Enjoy.

Let us hear from you. •

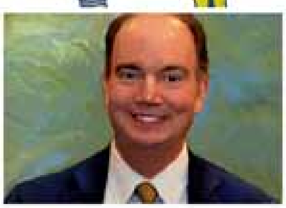


Peter A. Scarpato is VP of Ceded Reinsurance for ACE Brandywine. peter.scarpato@brandywine-holdings.com.

AIRROC matters

Vol. 10 No. 2 SUMMER 2014 www.airroc.org



Illustrations / Rafael Edwards
Photos NY / Jean-Marc Grambert
Photos Boston / John Kennard

AIRROC Board of Directors and Officers

AIRROC Executive Committees

Commissioner Kobylowski

NJ's Robust Regulatory Agenda

Fran Semaya and Fred Pomerantz had an illuminating discussion with NJ Insurance Commissioner of Banking and Insurance Kenneth E. Kobylowski (above), getting an in-depth picture of New Jersey's positions in the regulatory arena.

Fran Semaya: *Thank you so much for agreeing to do this interview. I'm here with my colleague, Fred Pomerantz and we are thrilled that you were able to find time for us today. We're going to start with Superstorm Sandy and its aftermath. So Fred, I'm turning the first question over to you.*

Fred Pomerantz: *Thank you, Fran. Commissioner, the U.S. Senate voted recently to delay implementation of the Biggert-Waters Act for four years and several members of the House are calling for immediate repeal. That's because since the law went into effect in October 2012, the price of flood insurance has risen dramatically for thousands of homeowners across the country.*

Because homeowners in New Jersey filed the largest number of FEMA flood aid claims – and the state of New Jersey is second only to New York in the amount paid to homeowner claimants impacted by Sandy – what reforms, if any, to the Biggert-Waters Act would you, as New Jersey Insurance Commissioner, like to see?

Kenneth Kobylowski: I think, Fred, that the National Flood Insurance Program (NFIP) isn't working as well as anyone envisioned. It's now some $23-$24 billion in the red. For years, it wasn't collecting premiums that accurately reflected the risk that the properties presented. In a few cases it may actually be charging too much. The pricing is all over the place.

Going beyond Biggert-Waters, we really need to look at the entire NFIP program and the way flood insurance is provided in this country. We have long advocated for a private flood insurance market that's more readily available to consumers because, frankly, the private marketplace is much better at serving insurance consumers.

Even if we get away from what Biggert-Waters does and doesn't do, we need to take a look at the entire provision of flood insurance in this country.

Semaya: *Just to continue that train of thought a minute, do you think that in New Jersey alone – that property insurers who write property and related liability insurance in New Jersey, would be willing to write flood insurance through the private market?*

Kobylowski: What I've heard anecdotally, Fran, is that they've never gotten involved because they never thought they could compete premium-wise with the NFIP. I think they're starting to rethink that and since Sandy, again, anecdotally, we've heard that insurers are willing to take another look at the opportunities for them in flood insurance in New Jersey.

In the aftermath of Sandy you're going to see in New Jersey properties that are constructed with better materials and other mitigation components, so I think they're going to be better at withstanding damage from floods. For companies that are really forward-thinking, this is a great opportunity for them.

Since Sandy, a couple of new companies have entered the market, including some that write exclusively on the coast. Those companies inspect and underwrite each specific property and I think the companies are really forward-looking. This could provide them a great opportunity.

Semaya: *Great news. So as one who lives just a little bit in from the coast, I'm glad to hear that. Still focusing on Sandy, New Jersey – not unlike New York – has implemented a mediation program to handle the disputes between insurers and* *policyholders on claims related to damage caused by the storm.*

How successful has the program been in New Jersey, and how many claimants have utilized the process?

Kobylowski: The program, overall, has been very successful. A little bit of background on the program. It's being administered by the American Arbitration Association and our mediation program is open to all insurance claims — other than flood claims under the NFIP.

It includes homeowners, personal auto, commercial property claims, commercial auto claims and business interruption claims. It is a very broad program and broader than what was implemented in states in the aftermath of Katrina.

We are at a 67% success rate. We have 832 claims in the mediation program to date. I think what is important is that when we do our exit survey, 91% of the people who participated in the program rated it either a 4 or 5 on a scale of 1 to 5, with 1 being terrible and 5 being excellent.

So, I think consumer satisfaction with the program is evident. I think our success rate is probably about where I expected it to be. Frankly, I'm a little bit disappointed in the number of people who have chosen to participate and I encourage more people to take advantage of it.

Pomerantz: *What happens when the insurer and the policyholder are not able to resolve claims in the mediation process?*

Kobylowski: If they're not able to resolve the claims, Fred, the policyholder has the option of filing a lawsuit against the insurer. The mediation program is intended as one last option before having to file. We know the lawsuit's going to be time consuming, expensive and inefficient.

We really believe that the mediation program should be tried by policyholders who still have open claims. It's going to give them a relatively expeditious, economical way to try to resolve claims before they have to file suit. There's a $750 fee that the insurance company pays. The only cost to the policyholder is if they choose to bring their own attorney or their own adjuster to that mediation.

Semaya: *When you say 67% of the mediations have been successful, is it that the insurance companies tend to pay out more than they were willing to pay, or is it that they're just reaching a compromise? From the results of the survey can you tell which way the trend is going?*

We really believe that the mediation program should be tried by policyholders who still have open claims.

Kobylowski: I don't know, Fran, if it's that the companies are paying out more than they expected to pay. I think it's, perhaps, when everybody sits down at the table with an impartial, experienced third-party who reviews all of the materials provided and can come up with a number to get it resolved, that makes sense to both the company and the policyholder, the parties in many cases will choose not to litigate. In some other cases, the insured is presenting new information that changes the way the insurer views the claim. That results in a payment, where there had previously been a denial, or in an additional payment.

Semaya: *We've heard, compared to some of the other states, that it's working and it is quite good, so my hat's off to you and to the AAA for that.*

Pomerantz: *The next topic is insurers designated as "systemically risky." What was your initial reaction when Prudential was identified as a potential SIFI, and what role, if any, did the New Jersey Department play in the evaluation made by the Federal Reserve in considering whether to designate Prudential Financial as "too big to fail?"*

Kobylowski: My initial reaction, Fred, was disappointment because I think it was the wrong decision by FSOC. When you look at Prudential's assets and businesses, it is clear to me that they are not "systemically important." The vast majority of its assets are insurance assets. It has very little counterparty risk. In addition, it's highly unlikely that there will ever be a run on an insurance company similar to a run on a bank. There are just so many safeguards in the regulatory system to prevent that. Also, the insurance business is fundamentally different from the banking business. So insurer failures don't cause the same problems that bank failures cause.

We provided information to FSOC because we are Prudential's lead regulator.

We tried to help FSOC understand Prudential's business. Then, when they were initially proposed for designation, we made a very strong argument explaining why, under Dodd-Frank, the proposed designation was incorrect.

I, along with Connecticut Commissioner Leonardi, attended the appeal hearing at Treasury when Prudential appealed the designation. So we both felt very strongly, as did Arizona, — who is the other significant regulator here in the United States — that Prudential should not be designated as "systemically important." I was disappointed with Treasury's decision.

Pomerantz: *A recent International Monetary Fund Working Paper entitled "What is Shadow Banking" proposes a new and broader range of activities that are to be considered as shadow banking — including any non-traditional financial activities, including insurance, that need private or governmental guarantees to operate. As Commissioner, what is your view of this proposal?*

Kobylowski: Well, I'm not familiar, Fred, with that particular paper but I think, just in general terms, the business of banking is very different from the business of insurance and at this Department, as in a number of other states, we regulate both banking and insurance. So we see it from both sides.

And I would venture to say that they're almost 180 degrees diametrically opposed just in terms of the way they operate,

Commissioner Kobylowski (continued)

their liquidity needs and things of that nature. As a result, they're regulated completely different. There's the banking doctrine — the "source of strength doctrine" — in which every entity within a bank holding company system is deemed to be a source of strength for every other entity within that system.

That concept is diametrically opposed to how insurance regulation works, where we focus on the solvency of each separate legal entity within an insurance holding company system. In fact, we wall off each separate legal entity so if there's any financial trouble at a particular legal entity, it's less likely to spread to other entities throughout the system. Insurance regulation is ultimately about policyholder protection and making sure that each entity has the assets available to pay claims when called upon.

So, until it is recognized that the regulation of banking and the regulation of insurance are completely different, I think we're going down the wrong path.

Semaya: *Thank you. We're going to move now to a topic that I know is near and dear to New Jersey, the New Jersey captive market.*

Back in 2010, New Jersey adopted legislation to become a captive domicile. One of the things the legislature left out was the provision in the original bill that would have permitted the formation of RRG captives. Do you have any background or understanding as to why the legislature removed that provision and does it place New Jersey at a disadvantage with other captive jurisdictions, for example, Washington DC, which is a very big RRG captive market?

Kobylowski: I really don't have any inside knowledge on that. I just chalk it up to the legislative process. There are just so many entities here in New Jersey that can really benefit from the traditional captive model that I don't think the inability to create RRG captives has been a hindrance whatsoever. We have licensed at least 17 captives with more in the pipeline from a really broad spectrum of industry: the chemical industry, telecommunications, really a broad spectrum, which is the focus. So I'm extremely pleased with the way the captive market's evolving here in New Jersey.

Semaya: *Does it concern you that a lot of states are "jumping on the bandwagon"? New Jersey's got a pretty good handle on it but Delaware is growing by leaps and bounds. I think it was recognized as the Number One state for new captives in this past year.*

I know that over the years that Vermont has been the leading US captive jurisdiction – both in number and knowledge of the captive market. Hawaii has been around for a long time. D.C. also has been around a long time as has South Carolina, but there are a lot of other states that have entered the captive market recently. And so, does this continued growth throughout the U.S. concern you, as a regulator, or the NAIC?

> *[T]here are plenty of companies that could avail themselves of the New Jersey captive model.*

Kobylowski: I really would prefer not to speak for the NAIC, but from my own viewpoint, we in New Jersey viewed our captive initiative as focused on the traditional captive model where you have, for example, a chemical company that wants to self-insure some of its risk. We're focused on captives as a tool to make New Jersey an even more attractive place in which to do business. Being able to form a captive here is yet another reason for a business to remain in or relocate to New Jersey.

Forming a captive makes a lot of sense for a lot of companies. And we really believe in New Jersey that there are plenty of companies that could avail themselves of the New Jersey captive model. Some of the other more exotic captive models really weren't within our focus.

So we aren't focused on trying to generate captives from outside the borders of New Jersey. We think that right now, there's enough business here in New Jersey on the captive side where we are focused. Other states are more amenable to different models of captives. I can tell you that we have turned down some captive models that we just didn't think were appropriate.

Semaya: *That is an admirable approach. When New York issued its report in June entitled "Shining a Light on Shadow Insurance" and made a huge issue of captives and life insurance, this really encouraged other regulators, and the NAIC, to take on their own investigation into what I'll call "shadow insurance." Did you have a reaction? Did New Jersey react as I know the NAIC did along with some other states?*

Kobylowski: I think at a certain level, Fran, we were already there, again, because as I said earlier, we really never focused on the more exotic captive models. From my perspective, that was not on our radar screen. We knew they were out there and as I said earlier, we've turned down some captive models that we just didn't think were appropriate. We focused more on the traditional captive model, of non-insurance entities setting up a captive to self-insure part of its risks. That's always been our focus.

I guess that's always been a place where New Jersey was at, even prior to the New York report.

Semaya: *Are you sitting on the NAIC committee that's looking into this?*

Kobylowski: No.

Semaya: *Is there anything else on captives that you'd like to share? Are you finding any particular regulatory issue that might be evolving as a result of the move into the captive market, or is it just the same regulatory issues as you would find with any other insurance company?*

Kobylowski: In a state that's taken our regulatory approach, the issues are usually straightforward. Plain vanilla stuff. Indeed, traditional captives can really pose fewer regulatory concerns. The more that a captive operates simply as an alternative to pure self-insurance, the less reason we have to worry.

Pomerantz: *Moving on to the Holding Company Model Act and enterprise risk*

Commissioner Kobylowski (continued)

management: New York recently published regulations, subject to comment, which apply to most large insurers. Do you agree or disagree that the requirements for an enterprise risk management report should apply only to insurers, say, with a minimum, annual premium threshold or group-wide annual premium threshold?

Kobylowski: Yes, Fred. I think that makes some sense, because I think what you really don't want to do is to hit small companies over the head with a lot of unnecessary regulatory burdens. At the same time, we are dealing with a national model that resulted from compromise and a lot of discussion with stakeholders, and we want to advance uniformity. So, to me, you have to think about what makes sense, on balance.

Pomerantz: *What plans does New Jersey have to implement enterprise risk management and ORSA reporting?*

Kobylowski: We haven't enacted either yet – either the Holding Company Model Act or ORSA. In New Jersey, I can tell you it is on our radar and under discussion. That is probably as far as I can go.

Pomerantz: *In the definition under the Holding Company Model Act, a holding company, per se, even the smallest insurer, which is wholly-owned by a pass-through holding company, would be considered a controlled insurer depending on premium volume potentially would have to report its enterprise risk management program and comply with ORSA reporting. What's ironic is that huge, publicly-owned insurance companies whose shares are so widely held that perhaps there is no 10% or greater shareholder, could theoretically escape the requirements for ERM and ORSA reporting. Do you have any reaction to that?*

Kobylowski: Well, that needs to be looked at, although we have the Holding Company Model Act, which I know a number of states have adopted. I think at last count it was almost half.

I can tell you that, at the NAIC level, we are looking at amendments to that act already. So I think there's always the opportunity to make it better and I think those may be some of the things that we're looking at to try to make that model law as effective as possible.

> *[S]upervisory colleges can't be overlooked. They're enormously helpful.*

Semaya: *I know one of the issues that has come up – and you may not be there yet with the drafting of New Jersey's ORSA law — is the New York regulation on the issue of confidentiality. New York is issuing the ORSA law by regulation. The Department is taking the position it cannot add in a confidentiality provision — that the NAIC Model Act and to my knowledge, other state statutes, include taking the position that you cannot include a confidentiality provision in a Regulation.*

It is our understanding that New York is relying on the provisions in New York's General Obligations Law that protect work product, proprietary information and trade secrets. When New Jersey does formulate its ORSA law — whether by regulation or by amendment to the Holding Company Model Act or a separate act — will you take into consideration the importance of a confidentiality provision?

Kobylowski: Yes. To me, that's extraordinarily important. We take very seriously here protecting proprietary information.

Semaya: *Glad to hear that and I'm sure many of the insurers will feel the same.*

Let's move on to principle-based reserves.

Kobylowski: Fran, before you get to that, maybe just one other thing on the whole issue of enterprise risk management is the value of supervisory colleges.

I don't think we can overstate the importance of supervisory colleges. I know that Connecticut has been a leader in not only organizing but participating in them and it's my opinion as a regulator that the supervisory colleges are enormously valuable. All indications are that the companies feel the same way.

We recently completed the Prudential supervisory college with regulators from Connecticut, Arizona and Japan. The buy-in from Prudential, and the time that we received from the top down at Prudential, including its CEO, COO, CFO, CRO and General Counsel, along with the presidents of their business units, was invaluable and enormously helpful to us.

So whether we're talking about enterprise risk management or holding company structures, the supervisory colleges can't be overlooked. They're enormously helpful.

Semaya: *I have spoken to Commissioner Leonardi about supervisory colleges as well. I don't know if you attended the EU-US dialogue that was held at the NAIC on the Saturday right before the start of the December National Meeting, but there was a panel, including Commissioners Leonardi and Consedine, along with Steve Johnson from Pennsylvania, focused on supervisory*

colleges. I found it rather fascinating when Steve Johnson banged on the table and said, "We don't need ComFrame because we have our supervisory colleges and they work." The insurers that participated on this panel agreed that the supervisory colleges were beneficial to the insurers as well.

But one issue is whether or not the FIO Director, Mike McRaith, should have a seat at the table at the supervisory colleges. First, according to Dodd-Frank, the FIO director is not an insurance regulator and the FIO does not regulate the business of insurance. That's still left to each of the states. In your opinion, what role, if any, should the FIO or any other organization like the IAIS, or any other important non-regulatory body, have vis-à-vis the supervisory colleges?

Kobylowski: Well, I was not, unfortunately, at the session in D.C. in December but I understand that it was a very good session with a lot of thoughtful discussion.

My opinion is FIO should not be at the table. They're not a regulator.

Pomerantz: *I wonder, in light of the FIO's report on modernization with its many recommendations, whether FIO is not overstepping the balance of federal regulation and whether those recommendations can be achieved without repealing or significantly amending the McCarran-Ferguson Act.*

Kobylowski: I guess I'll let the FIO report speak for itself. My reaction is that it is clear that state-based insurance regulation works and it's clear that state-based insurance regulation needs to exist because it does work. If the point of the recommendations is to address the causes of the financial recession we had a few years ago, I think we really need to re-examine what exactly precipitated that financial recession. It's clear to me that the cause was not insurance or insurance companies.

Semaya: *And I think that one of the things that always bothers me is that "New York insurer AIG" is always the reason everything toppled and we all know that's not the case.*

As you are aware, I chair the TIPS Federal Involvement in Insurance Regulation Modernization and Health Care Task Force of the American Bar Association and we proposed, and were successful in having, the ABA adopt a policy supporting that the FIO should not be regulating the business of insurance but should be advisory to the industry and be the "voice" of the U.S. in international matters, because it's becoming harder to deal on global insurance issues with 56 regulators having a voice. There is strong industry support for an "appropriate" international role for FIO.

Kobylowski: Yes. I can understand that when you say you're dealing with the 56 regulators, you also have to remember the EU is 26 separate entities which do not always speak with one voice.

So I think we need to be mindful of that. It's not as if the members of the EU represent one view and we are 56. So I think that point needs to be made. In addition, there is far more uniformity of solvency regulation among the 56 U.S. jurisdictions than they get credit for. The notion that we're going in 56 different directions couldn't be farther from the truth.

Semaya: *That is an excellent point.*

Pomerantz: *Do you believe that consensus can be reached among 50 state regulators on the acceptability of PBR as an improvement over the formulaic approach to setting reserves that's currently enforced instead of viewing it as an all-encompassing solution to existing problems within the U.S. regulatory system?*

Kobylowski: I'm hopeful that we will get to a resolution on that. I think PBR is important and the way to go. I think we all need to use our talents as regulators and our experience as regulators to right-size reserves. I think it's clear to everyone that the formulaic approach is leading to inappropriate levels of reserving and we need to address that.

We need 42 states and 75 percent of the premium volume and I think we'll get there. I think we'll get there because it's the right approach.

Semaya: *It's interesting you say that because you need about 75% of the premium, but it appears that two states that are very adamantly opposed to PBR are New York*

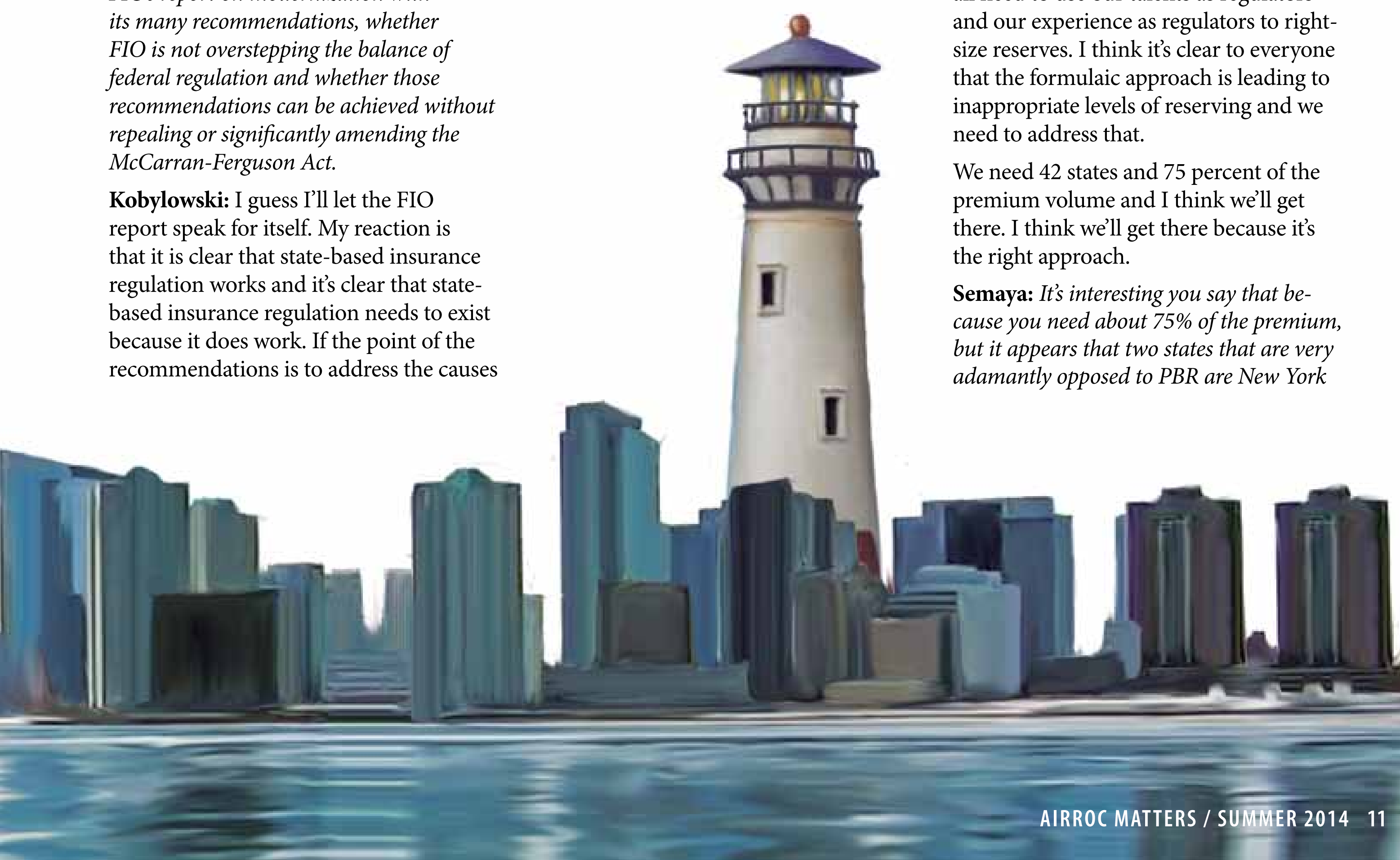


illustration / Rafael Edwards

Commissioner Kobylowski (continued)

and California, where a very large percentage of the premium generated. It almost appears that those states are looking to have some form of federal regulation on how PBR should be applied. How does this impact the uniform trend that the NAIC is trying to adopt?

Kobylowski: I think insurance regulation should be state-based. I'm not in favor of any federal regulation, but, yes, New York and California haven't yet gone in the direction of PBR so it's something that we all have to consider.

Reasonably intelligent people can always differ on a topic but I think that PBR is important and I think it is moving in the right direction to rightsizing reserves. It's not going to be simple or happen overnight, but I think it is the right approach and it is moving in the right direction.

Semaya: *That's helpful. We're going to turn to the NAIC for a couple of minutes. NAIC has received some negative press, if you will, after the last NAIC meeting, particularly after being challenged by Commissioner Leonardi on governance issues and requesting an independent audit.*

What committees does New Jersey participate on this year that you find very important and where does New Jersey have a leadership role?

Kobylowski: We are on the Life and Annuities (A) Committee, the Financial Condition (E) Committee, and on the International Insurance Relations (G) Committee. I also Chair the Financial Stability Task Force.

Semaya: *You're involved with some very significant committees.*

Kobylowski: I think they're all important and I think New Jersey – because we're Number 8 in terms of written premium– should be heard on these issues and other issues important to the industry.

> *So while the IAIS has a global capital standard in mind, I'm not sure that it would lead to better regulation or better regulatory products.*

I think being on the International lnsurance Relations (G) Committee and in view of the international scope of, and our regulatory authority over, Prudential, it is vitally important to New Jersey that the NAIC views it that way as well.

Semaya: *The NAIC doesn't have any real regulatory power, except in promulgating uniform financial statement blanks that all insurers use.*

What do you see as the appropriate role that NAIC can play as we deal with the very important issues raised by the FIO report and other proponents of federal involvement in regulation?

I know for example, you believe and support that PBR should be a state-based issue and not regulated by federal law. Where do you see the NAIC now with all these controversial issues? What role does the controversy surrounding the NAIC play in your thinking and how can it benefit state regulation as opposed to feeding the criticism of state regulation by both the federal government and even some state regulators?

Frederick J. Pomerantz is a Partner at Wilson Elser Moskowitz Edelman & Dicker LLP. fred.pomerantz@wilsonelser.com

Francine L. Semaya. Esq. is a Legal and Insurance Regulatory Consultant. flsemaya@gmail.com

Kobylowski: I don't view the issues that Commissioner Leonardi raised in December as bad. I think any successful organization should always examine its governance structure and how it operates. If an organization doesn't do that, then you really need to question the strength of that organization. Anyone who is sitting in a leadership role at any organization of significance should always be examining how things are done in a governance structure.

So to me, that only demonstrates the strength of the NAIC. We are constantly examining ourselves and looking at ways that we can improve so I don't view Commissioner Leonardi's point in December as being a criticism of the NAIC. I think it shows the strength of the NAIC and the strength of the regulators that comprise the NAIC. I don't think it really has to do with the perceived outside attacks on state-based regulation, whether from the federal government or the international regulators. I think it's just something that every strong organization does routinely and the NAIC is an extraordinarily strong organization with extraordinarily bright people. It is something that the NAIC should be doing.

Semaya: *Where do you see U.S. insurance regulation five years from now?*

Kobylowski: I see the state-based system being as strong as ever because I always get back to the bottom line, Fran – it works. We have 150 years of state-based insurance regulation that works. I think five years from now, it's going to be stronger than ever.

Pomerantz: *A lot of effort and time has gone into trying to come up with some kind of global regulatory standards for financial regulation, in particular for insurance. I'm just wondering whether that is a realistic goal and also whether the establishment of global standards or even the establishment of a global regulator would generate a political power struggle? If so, how would political accountability work?*

Kobylowski: That's an excellent point, Fred. I'm not a fan or a proponent of some type of global capital "one size fits all approach." I think that part of the strength of the system is that we have divergent views and ways of regulating based upon all of our collective experiences. That just adds to the strength of the system.

So while the IAIS has a global capital standard in mind, I'm not sure that it would lead to better regulation or better regulatory products. No one's ever convinced me of that yet.

Semaya: *Do you think that there is a chance that the states can continue to work together as they move toward more uniformity?*

If the commissioners and the NAIC work together for more national uniformity, not federal, but national, will it strengthen the core of insurance regulation as well as make the federal government pull back?

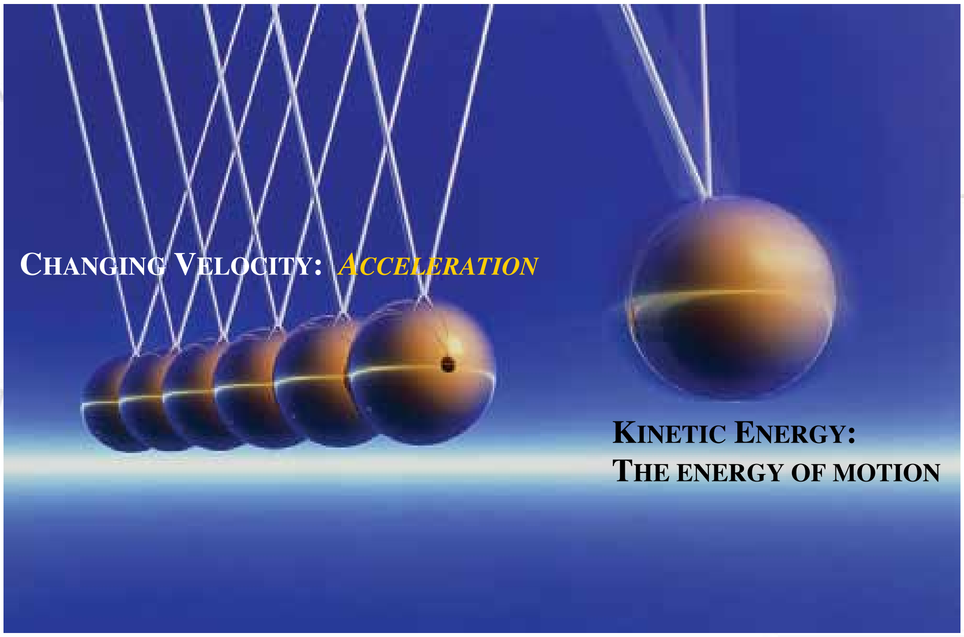
Kobylowski: I would really approach that, Fran, from the standpoint of the companies and how much of a burden we are putting on the companies to have to deal with varying requirements in the different states and the fact that all of that adds to cost, which ultimately ends up on a consumer's plate.

So, yes, I think there is a lot to be said for uniformity among the states and that's something that we at the NAIC discuss all the time because we all are aware of the burdens that different requirements put on the companies. That's why we are working towards even more uniformity. I think that's a very important point.

Semaya: *That's a positive note in which to end. It's been a pleasure speaking with you.*

We hope this was enjoyable for you and that we leave you with a positive feeling.

Kobylowski: Thanks very much, Fred and Fran. It was really my pleasure.



DEVONSHIRE

Devonshire is a (re)insurance management, audit and consulting company with offices in California and New York. The company specializes in reinsurance, including ***accelerated*** run-off management, audits of ceding companies and coverholders, operational support and consulting.

devonshiregroup.com

Cede It Right the First Time

10 Practices of Effective Ceded Reinsurance Claims and Accounting Teams

illustration / Rafael Edwards

"We apply reinsurance recoveries to the oldest balance due regardless of which claim the reinsurer is actually paying."

"What do you mean we paid 40% more than our contractual limit and the reinsurer is refusing to reimburse us?"

These are just two examples of issues that can generate significant obstacles in effectively managing an insurance companies ceded reinsurance asset. The complex contractual structures of reinsurance programs and individual reinsurance agreements; cumbersome ceded reinsurance processes and systems; and evolving reinsurance accounting rules create challenges for those responsible for determining, reporting, and collecting reinsurance cessions. It can be difficult to determine how to manage reinsurance obligations efficiently and effectively within available resources while also trying to meet operational goals in a constantly changing external environment. Meeting these challenges requires the successful incorporation of human and technical resources, as well as, the appropriate implementation of processes and controls. In order to optimize the effectiveness of ceded reinsurance programs and the associated accounting, ceded reinsurance teams should strive to implement the following practices.

1. Establish a clear culture of learning and adapting

Critical to an organization's profitability is the ability of management and lower level employees to learn from past behavior and integrate learning into the company's daily culture. Adapting to change and incorporating knowledge from past successes and mistakes will help an organization identify future opportunities and potential risks.

The goal of the ceded reinsurance team is to identify and secure the reinsurance asset. In order to achieve this goal, each individual team member must understand the role in the overall process. For example, employees who develop a quarterly bordereaux not only view themselves as processors of information, but as individuals who carry out critical functions necessary for the company to seek and record the proper reinsurance assets. These employees also understand the a) necessity of securing the reinsurance asset, b) contractual relationships, and c) other team members' roles. This enables them to identify red flags that may require further investigation. Having a good grasp of the overall process and their role in the process helps employees gain an understanding of how reinsurance impacts surplus and liquidity and, more importantly, the organization as a whole. If individuals at all levels focus on finding solutions to business challenges, then an organization is much more likely to prosper.

2. Understand placement profiles and identify reinsurance relationships

A successful ceded reinsurance team understands the company's reinsurance programs and the goals for current reinsurance placements. Effective ceded reinsurance leaders promote an understanding of reinsurance programs at all staff levels. This helps staff to identify claims that fall outside of the developed processes and controls and uncover opportunities for missed cessions. Teams that thoroughly document ceded reinsurance placements on an individual program basis within a sound and tested system, will have quick and accurate retrieval of placement information. Effective ceded reinsurance teams encourage staff managing individual programs to have a working knowledge of the coverage the reinsurance contracts offer, as well as, the nature and structure of the specific reinsurance program.

Companies often fail to identify cessions because of siloed approaches to managing various types of protection (facultative, treaty, excess of loss, or quota share). For example, when a claim exhausts facultative protection and the company fails to identify additional coverage that may be available under a reinsurance treaty. Another commonly missed cession occurs in the context of non-concurrent coverage, due to placement issues or exiting initiatives, including covered periods, layers of protection and treatment of expenses. Individuals responsible for billing initiatives in successful ceded reinsurance teams understand these issues and, as a result, can avoid inappropriate billings and overstatement of reinsurance assets on the balance sheet.

3. Master technology and data

While many insurance organizations have data quality issues resulting from operating multiple claims and reinsurance systems, a well-managed ceded reinsurance team is knowledgeable about the basic operations of all available systems and sources of data. To understand which systems feed or impact the data (e.g., application of deductibles or loss sensitive premiums), as well as, what causes differences in timing. This knowledge can enable the ceded reinsurance team to consistently pull and organize data, create net and gross calculations, and incorporate predictive analytics when identifying red flags in certain books of business or types of claims. The individuals inputting data into the systems will have a thorough understanding of the data (definition and need for the various fields of information, the purpose and goal of the system, and databases fed by their inputs) and will be able to consult internal and external subject matter specialists to address data and/or coverage interpretation issues in a timely manner.

To optimize resolution initiatives, it takes a proactive approach to litigation and arbitration management, and communicates outcomes to internal stakeholders.

4. Manage the reinsurance program with an understanding of the financial statement impact

A financially healthy insurance company has financial statements with transparent reinsurance footnotes, fully collateralized Letters of Credit (LOC) that are replenished on a timely basis, and no Schedule F penalties. Such an organizations' reinsurance staff understand the impact of Schedule F, why there is a penalty, and how the penalty is calculated. The company identifies poorly performing reinsurers (those with balances due over 90 days) and pursues outstanding balances beginning 60 days from the date of invoice. On a quarterly basis, the ceded reinsurance team reviews Schedule F balances and the associated penalties, establishes targeted collection goals, and addresses variances of planned to actual recoveries. In addition, at least twice yearly, the team verifies collateral and seeks replenishments one quarter in advance. The team also vets financial statement footnotes on reinsurance topics with other company stakeholders involved in financial reporting such as the Chief Financial Officer.

5. Conduct regular, ground up account and broker reconciliations

An effective ceded reinsurance team is confident in the accuracy of its brokers and vendors' data and logic used in calculating cessions and applying payments. This team has an established process to reconcile data periodically through an independent — "ground up" approach rather than just a "roll forward" methodology — and regular reviews of retained losses against reinsurance placements to identify missed cessions. In addition, it resolves differences promptly and appropriately documents the resolution.

6. Maintain an enhanced process for evaluating credit risk

To determine the creditworthiness of prospective and current reinsurers, an effective ceded reinsurance team reviews information available from a variety of sources such as reports from multiple rating agencies, recent reinsurer financial statements, and other available industry resources. They evaluate and test their evaluation methodology regularly, and upon identification of an at-risk reinsurer, review management strategy, including potential exiting transactions, credit risk adjustment, and the associated balance sheet impact.

7. Appropriately manage disputes and record risks

In order to facilitate the analysis of possible outcomes and recording of disputed risk reserves (i.e., "allowances"), effective ceded reinsurance teams can identify disputed ceded reinsurance matters and quickly evaluate and discuss the relevant coverage issues and exposures with both internal and external stakeholders. Such a team maintains supporting documentation detailing the basis of the disputed risk value and tracks revisions and the associated drivers. The team also reviews documentation to identify opportunities for improvement with respect to existing and future cessions. To optimize resolution initiatives, it takes a proactive approach to litigation and arbitration management, and communicates outcomes to internal stakeholders.

8. Continually advance processes and controls

Effective ceding reinsurance teams develop manuals that cover the processes related to their reinsurance programs, including accounting for cessions,

10 Practices… (continued)

effectuating and crediting invoices, limit impairment, collateral requirements, preparing financial statements / reports, and entering / interpreting data. In addition, these manuals document current processes and controls clearly in a user-friendly fashion and provide updates in real time. The companies also test controls and review for consistency with leading industry practices. Moreover, they train appropriate staff in both processes and the controls and encourage individuals at all levels of the organization to identify opportunities to enhance operations and improve efficiencies.

9. Clearly document accounting records and collection initiatives

An effective ceded reinsurance claims and accounting team documents reinsurance collection activities, including contract interpretation, cession calculation, notice, billing, loss reporting, and reinsurance audits, in an accurate, timely, concise, factual and retrievable manner. Such a group communicates expeditiously, both internally and externally, and quickly escalates issues and shares resolution-oriented plans.

10. Team, cross train and plan for succession

Successful ceded reinsurance teams work consistently with other departments within the organization to manage current issues and plan effectively for the future. Incorporating a multidisciplinary approach, whether formal or informal, provides an effective means of addressing a variety of issues, including direct and reinsurance contract wording, potential loss development on existing claims, calculation of ceded IBNR, and financial reporting. Cross training should coincide with teaming opportunities to promote individual career development, expand bench strength and ultimately maximize resource capabilities. Going hand-in-hand with cross training, succession planning not only is important to plan for advancement, but also prepares the team through mentoring programs and forecasting exercises for anticipated and unanticipated events that may require a change in leadership and staffing.

A ceded reinsurance team who effectively implements these ten practices likely will optimize its ability to identify all applicable cessions and timely secure its reinsurance asset; appropriately address issues as they arise; efficiently and effectively manage its data; ensure accurate, timely and transparent financial reporting; and effectuate mutually beneficial dealings with stakeholders. ●

Barbara K. Murray is a Director in the PwC Actuarial & Insurance Management Solutions. barbara.k.murray@us.pwc.com

The Low Down on LIMA

The Legacy Insurance Management Act

Effective February 19, 2014, Vermont enacted legislation, the Legacy Insurance Management Act ("LIMA"), to facilitate what some had hoped would become a US version of Part VII of the UK Financial Services and Markets Act 2000 ("UK Part VII") which has become a well-known vehicle to transfer books of assets and liabilities between insurers in the UK and elsewhere ("Part VII Transfers").

Following the success of Part VII Transfers, operators of run-off insurers in the US and abroad have been searching for ways to transfer similar blocks of US insurance (and reinsurance) business to insurers in the US.

A previous legislative enactment in Rhode Island effective in 2004, the Voluntary Restructuring of Solvent Insurers Act ("Voluntary Restructuring Law"), dealt with the subject by creating a vehicle whereby solvent Rhode Island-domestic insurers (including those that re-domesticate to Rhode Island) could commute liabilities for commercial property and casualty business in run-off and terminate operations. Despite a 2011 Rhode Island Superior Court case that confirmed certain aspects of the Rhode Island approach *(In Re GTE Reinsurance Company)*, this legislation has not been widely used as potential assuming insurers reportedly have been reluctant to re-domesticate to Rhode Island. Moreover, issues continue to exist under the Voluntary Restructuring Law regarding its legal certainty and enforceability outside of Rhode Island.

LIMA approaches the issues of run-off transfers from a different perspective, but again probably fails to create the legal certainty needed to be of great use to the market.

In a Part VII Transfer, the High Court of England and Wales (the "High Court" or the Court of Session in Scotland) orders the transfer and permits UK insurers, as well as certain insurance branch operations of a UK, EEA (European Economic Area) or non-EEA insurer, to transfer books of assets and liabilities (including US non-admitted and reinsurance business) to qualified overseas transferees. Part VII Transfers of liabilities governed by UK law and sanctioned by the High Court have the benefit of finality.

LIMA approaches the issues of run-off transfers from a different perspective, but again probably fails to create the legal certainty needed to be of great use to the market.

LIMA, on the other hand, was designed to create a unique niche management industry in Vermont for the run-off of US commercial insurance and reinsurance legacy business written by US and overseas non-admitted (i.e., unlicensed) insurers and reinsurers that would like to exit such business ("Legacy Business"). As discussed below, a transfer pursuant to LIMA ("LIMA Transfer") probably lacks finality.

LIMA has several distinctive features that distinguish it from UK Part VII. These features are:

1. LIMA requires that a Vermont-domiciled company be established specifically to assume Legacy Business. LIMA permits any Vermont entity, including specialized non-insurers, such as investment companies, to be formed to assume Legacy Business. One of the chief industry proponents of LIMA has observed that foundations, institutional endowments, family trusts and other investors with long investment horizons may perceive LIMA as creating an attractive investment opportunity.

2. Unlike UK Part VII which is broad in scope, a LIMA Transfer is restricted to closed blocks of non-admitted commercial property and casualty insurance business and reinsurance. To be considered a "closed block," all such business is required to have been expired for not less than 60 months and have no active premiums yet to be paid. Surplus lines business meeting such requirements and, presumably, direct and industrial insured exemption business if placed with an eligible surplus lines insurer, is a focus of LIMA. Workers' compensation, life, health and other kinds of personal lines insurance/reinsurance are specifically excluded from a LIMA Transfer. The fact that qualifying reinsurance must have had no active unpaid premium outstanding for 60 months may create practical impediment against including reinsurance in the transfer, in light of the possible long-tail of premium payments under some contracts.

3. Key to both the LIMA Transfer and Part VII Transfer processes is that notice of the proposed transfer is required to be given to policyholders and reinsurance counterparties. LIMA and UK Part VII notices, however, differ in potential consequence. Pursuant to LIMA, policyholders and reinsurance counterparties are permitted to opt out of the transfer. A Part VII Transfer may be achieved without permitting parties to opt.

4. The LIMA approval process is solely regulatory. Approval is conferred by Final Order (the "Final Order") of the Vermont Insurance Commissioner (the "Commissioner"), which is appealable to the Vermont Supreme Court. In contrast, the UK Part VII process requires approval of both the UK

domiciliary regulator, the Prudential Regulation Authority, formerly known as the Financial Services Authority (the "PRA") and the High Court.

5. The Final Order issued pursuant to LIMA effects a statutory novation of only those policies and reinsurance agreements in the closed block that have not been excluded from the transfer by opt out or otherwise. The UK Part VII process which, as noted above, requires both PRA and High Court approval of a transfer, effects a court-ordered novation of all policies and reinsurance agreements that comprise the closed block.

6. Unlike UK Part VII, LIMA contemplates that regulatory oversight of the assuming company will be tailored by the Commissioner on a case-by-case basis, and that the Final Order will include the terms and conditions of the oversight of the closed block and operation, management and solvency of the assuming company.

When considering strategies for exiting US legacy business, non-admitted insurers and reinsurers should carefully consider whether (i) an exit mechanism is structured to assure finality; (ii) the transfer would be enforceable in all relevant US jurisdictions; and, (iii) in the case of overseas insurers and reinsurers, the transfer provides the basis for the early termination of US surplus lines or reinsurance trusts which may secure the business to be transferred. An overview of each of these considerations follows:

(i) **Prospective transferors should recognize that finality may not be assured by LIMA.** The objective of exiting a closed block would be defeated by orphan business excluded from a LIMA Transfer by policyholder or reinsurance counterparty opt out. Furthermore, prospective transferors should be alert to the possibility, albeit remote, that the Vermont Supreme Court could unwind a LIMA Transfer on appeal.

(ii) **Whether a LIMA Transfer would be enforceable in all relevant US jurisdictions is unclear.** Courts would apply the constitutional principle of full faith and credit if asked to examine whether a Final Order is enforceable outside Vermont. Article IV, Section 1 of the US Constitution mandates that full faith and credit be given "in each State to the public acts, records, and judicial proceedings of every other state." It is unclear whether a regulatory "Final Order" alone would be recognized and enforced in any other US state without a court order.

(iii) **A LIMA Transfer may be insufficient to support the early termination of a prospective transferor's US surplus lines or reinsurance trusts.** Overseas surplus lines insurers are required to maintain US surplus lines trusts to secure their US surplus lines business. Many such trusts are extant which cover legacy business in run-off. Similarly, an overseas reinsurer of US cedents may maintain letters of credit, funds withheld, a cedent-specific trust or a US multi-beneficiary reinsurance trust to collateralize US ceded liabilities so that its US cedents may take statutory credit for the reinsurances ceded. Transfer of liabilities to an insurer of other entity that has not satisfied the credit for reinsurance or other requirements for termination of trusts or release of collateral may be ineffective for the practical realization of the transfer.

Challenges of Regulation and Oversight of LIMA Transfers

As LIMA has not yet been tested, there are many issues to be resolved by the Vermont Department of Financial Regulation ("DFR") and prospective insurers wishing to attempt business transfers. Regulatory issues are likely to arise if an assuming company is not an insurer. US cedents domiciled in states other than Vermont who are parties to inward reinsurance agreements included in a LIMA Transfer will expect that the assuming company continue to collateralize their reinsurance liabilities by posting letters of credit or by other acceptable means. The associated costs of providing such collateral could be significant.

We expect that the legacy business exit mechanism created by LIMA will evolve, perhaps by regulations promulgated pursuant to LIMA, to ensure that the vibrant niche management industry envisaged by the DFR is realized. ●

Karen S. Deibert *(not pictured)* is Of Counsel at Locke Lord LLP. kdeibert@lockelord.com

Robert A. Romano is a Partner at Locke Lord LLP. rromano@lockelord.com

Jonathan Bank is Of Counsel at Locke Lord LLP and member of the AIRROC Matters Publication Committee. jbank@lockelord.com

Ready, Fire… Aim!

The Effect of Asbestosis Exclusions

illustration / Rafael Edwards

Introduction

Since the late 1970s, the insurance industry has almost universally sought to exclude coverage for asbestos-related illnesses from insurance policies. Unfortunately for some insurers, the "asbestos" exclusions used in policies during the late 1970s and early 1980s have proven to be less comprehensive than intended, leaving insurers potentially vulnerable to unintended asbestos exposures.

One of the earliest asbestos exclusions commonly used in policies drafted prior to the mid-1980s excluded coverage for bodily injury claims arising from exposure to "asbestosis" or "asbestosis or similar diseases." While asbestosis is the name of a particular disease caused by exposure to asbestos, during the early years of the insurance industry's reaction to the flood of asbestos litigation, the term was often used generically to describe *all* diseases caused by exposure to asbestos.

Over the last few decades, insureds under policies containing "asbestosis" exclusions have challenged the scope of those exclusions, arguing that an exclusion for "asbestosis" does not exclude claims related to other diseases, such as mesothelioma or cancer. This article examines how U.S. courts have treated "asbestosis" exclusions, as well as reinsurance implications for an insurer that ultimately pays asbestos-related claims it thought were excluded at the time of underwriting.

History Of Asbestos/Asbestosis Exclusions In The Insurance Market

Asbestos was widely used in a variety of products from the late 1800s through much of the twentieth century. *See Borel v. Fibreboard Paper Products Corp.*, 493 F.2d 1076 (5th Cir. 1973) at 1083, n.3; Obremski, Cynthia M., *"Toxic Tort" Litigation and the Insurance Coverage Controversy, Federation of Insurance Counsel Quarterly*, Vol. 34, No. 1, p. 11-12 (Fall 1983). Although the dangers of asbestos were known as early as the 1930s, it was not until decades later that a significant number of plaintiffs injured as a result of asbestos exposure sought to hold manufacturers legally accountable. *See id.* at 12; Gallo, A. Andrew, *Asbestosis: Assessing Insurer Liability for Indemnification and Defense Costs, Federation of Insurance & Corporate Counsel Quarterly*, Vol. 37, No. 1, p. 43 (Autumn 1986).

The onslaught of asbestos-related litigation during the 1970s and 1980s was prompted by the Fifth Circuit's landmark decision in *Borel v. Fibreboard Paper Products Corp.*, 493 F.2d 1076 (5th Cir. 1973). *See* Gartland, Peter (ed.), *Lloyd's Prepares for Asbestosis Claims, Reinsurance, The Monthly Reinsurance Magazine*, Vol. 12, No. 6, p. 336 (Oct. 1980). In *Borel*, an industrial worker brought suit against several manufacturers of insulation materials that contained asbestos, alleging that he had contracted the diseases of asbestosis and mesothelioma due to exposure to the manufacturers' products. The jury found the insulation manufacturers jointly and severally liable for the asbestos-related diseases that developed from the use of their products. *Borel*, 493 F.2d at 1095, 1106-7. The jury's verdict was upheld by the Fifth Circuit Court of Appeals.

In the ten years following the *Borel* decision, 20,000 new asbestos lawsuits were filed, prompting underwriters and brokers to act quickly to exclude bodily injury claims arising from asbestos exposure from future liability policies. Gallo at 43, n.2. While, generally, the Insurance Services Office (ISO) – a New York-based trade organization that drafts standard insurance policy language and files it for approval with state regulators – institutes changes in insurance policy language to ensure uniformity amongst its member insurers, underwriters in the late 1970s and early 1980s, observing the high volume and potential costly nature of asbestos claims, did not wait for ISO to craft standard exclusions. *See* ISO's Policy Language and Rules (visited Dec. 6, 2013) http://www.iso.com/Products/Overview-of-ISO-Products-and-Services/ISO-s-Policy-Language-and-Rules.html. Instead, underwriters and brokers began drafting *ad hoc* exclusions using varied language. Significantly, some of the

exclusions drafted post-*Borel* used the term "asbestosis" in place of "asbestos." *Celotex Corp. v. AIU Ins. Co., et al.*, 175 B.R. 98 (Bankr. M.D. Fla. 1994) provides the "asbestosis" exclusion language that appears in policies written by various insurance companies during the late 1970s and early 1980s. *See id.* at 103, n.1-2. *See also Carey Canada, Inc. v. Columbia Casualty Co.*, 940 F.2d 1548, 1551 (D.C. Cir. 1991) (noting that the appellee insurers began issuing "policies with variously worded asbestos-related exclusions" in October 1977 "in the face of thousands of lawsuits").

Through the early 1980s, asbestosis – a non-malignant disease caused by "prolonged and heavy asbestos exposure" (Obremski at 3) – was thought to be the most common of the asbestos-related diseases. Environmental Issues Task Force at Commercial Union Insurance Companies, *Asbestos—A Social Problem, Viewpoint, The Marsh & McLennan Quarterly*, Vol. XI, No. 1, p. 31 (Spring 1982). Thus, while some policies excluded coverage for all bodily injuries caused by "asbestos" exposure, others excluded coverage for injuries "arising out of asbestosis and related diseases arising out of asbestos products." *Celotex*, 175 B.R. at 104, n.3. It was not until the mid-1980s that insurance industry asbestos exclusions began to be more standardized.

Evidence suggests that underwriters who drafted exclusions in the late 1970s and early 1980s using the term "asbestosis" intended to eliminate coverage of all bodily injury claims resulting from asbestos exposure. Indeed, it was common during that time to use the terms "asbestosis" and "asbestos" interchangeably. *See* Gallo at 45, n.9. ("The term 'asbestosis' will be used throughout this paper to describe all the asbestos-related diseases including asbestosis, mesothelioma and lung cancer."); Ratner, Patricia E., *Insurance Coverage of Asbestosis Claims-Running for Cover or Coverage*, Emory L.J., Vol. 32, p. 901 (Summer 1983) ("All asbestos-related diseases in this comment will be referred to as 'asbestosis.'"); Gartland at 336 ("The spate of *asbestosis* claims now emerging in the US has led Lloyd's non-marine underwriters to set up a working party to examine their future effect on the market.") (emphasis added). *But c.f.* Neild, Peter, *Asbestos: A Problem for Liability Insurers, Journal of the Chartered Insurance Institute*, Vol. 71, p. 114 (1974) ("Because of the legal significance of the difference between asbestosis and mesothelioma the use of the word asbestosis to describe the mere presence of asbestos bodies should be avoided.").

Interpreting Asbestos/Asbestosis Exclusions

The use of the term "asbestosis" in place of "asbestos" in exclusions during the late 1970s and early 1980s has given rise to disputes between insurers and their policyholders. *See id.* at 102-03; *Carey Canada*, 940 F.2d at 1552-3; *UNR Industries, Inc. v. Continental Ins. Co.*, No. 85 C 3532, 1989 WL 265493, at *2 (N.D. Ill. Jan. 11, 1989); *The American Insurance Co. v. American Re-insurance Co.*, No. C 05-01208 JSW, 2006 WL 3412079, at *6-7 (N.D. Ca. Nov. 27, 2006). Policyholders have argued that "asbestosis" exclusions preclude coverage of only those injuries arising from the singular disease asbestosis, and that insurers are obligated to reimburse losses arising from other diseases caused by asbestos inhalation, such as cancer. Insurers have argued that the intent of "asbestosis" exclusions was to exclude *all* claims related to diseases caused by exposure to asbestos. Courts that have addressed this issue have reached different conclusions about the merits of these arguments.

Celotex Corp. v. AIU Ins. Co., et al., 175 B.R. 98 (Bankr. M.D. Fla. 1994), involved a policy that excluded liabilities resulting from "asbestosis and other diseases that result from asbestosis." *Id*. at 111-112. The policy holder argued that the plain language of the policy unambiguously excluded only "asbestosis" claims. The insurers sought to introduce considerable evidence showing that the intent of the parties at the time of underwriting was to exclude all asbestos bodily injury liability. *Id*. at 103. Ultimately, the court held that the term "asbestosis" is unambiguous and refers to "a singular disease," finding that the "only reasonable interpretation" was

Asbestosis Exclusions (continued)

that the exclusion precluded "asbestosis" claims and refused to consider any extrinsic evidence. *Id.* at 110.

By contrast, other courts have been willing to consider extrinsic evidence to analyze the meaning of the an exclusion for "asbestosis." In *UNR Industries, Inc. v. Continental Ins. Co.*, No. 85 C 3532, 1988 WL 121574 (N.D. Ill. Nov. 9, 1988), for example, the court initially found that the "asbestosis" exclusion unambiguously excluded only claims arising from the disease asbestosis and issued a summary declaratory judgment on that basis. *UNR Industries, Inc. v. Continental Ins. Co.*, No. 85 C 3532, 1988 WL 121574 (N.D. Ill. Nov. 9, 1988) at *14. The insurers moved to amend the judgment and presented parole evidence demonstrating that there were "many instances in which medical, legal experts, and other insurance companies (Continental, in this case) have used the term asbestosis to mean 'asbestos-related' even though it can be shown to be incorrect from a technical point of view." *UNR Industries, Inc. v. Continental Ins. Co.*, No. 85 C 3532, 1989 WL 265493 (N.D. Ill. Jan. 11, 1989) at *2. The court granted the insurers' motion and vacated the declaratory judgment, concluding that an issue of fact existed as to the meaning of the term asbestosis, such that summary judgment was not appropriate. *Id.* at *2.

Other courts have similarly allowed insurers to present extrinsic evidence as to the intent and/or understanding of the parties at the time of underwriting. *See AstenJohnson, Inc. v. Columbia Casualty*, 562 F3d. 213, 219-222 (3d Cir. 2009) (holding that the court could properly consider extrinsic evidence regarding trade usage of the term "asbestosis" and that the insured was not entitled to summary judgment on its declaratory judgment claims); *Highlands Insurance Co. v. The Celotex Corp.*, 743 F. Supp. 28, 31-32 (D.D.C. 1990) (finding that the court was required to consider extrinsic evidence of the parties' intent where the "asbestosis" exclusion at issue was ambiguous on its face).

Finally, at least one court has held that an "asbestosis" exclusion excludes coverage for all asbestos-related diseases.

Finally, at least one court has held that an "asbestosis" exclusion excludes coverage for all asbestos-related diseases. In *Carey Canada, Inc. v. Columbia Casualty Co.*, 940 F.2d 1548 (D.C. Cir. 1991), the District of Columbia Circuit Court, relying on evidence of the parties' subjective intent, upheld the district court's factual finding "that all parties knew and understood that the 'asbestosis' exclusions [at issue] applied to all asbestos-related disease claims." *Carey Canada, Inc. v. Columbia Casualty Co.*, 940 F.2d 1548, 1553 (D.C. Cir. 1991). With respect to the first policy at issue, which excluded claims arising out of "all asbestosis operations," the court concluded that the exclusion was ambiguous on its face and found that the district court had properly considered the extrinsic evidence of the parties' intent to exclude asbestos-related diseases aside from asbestosis. Thus, the court enforced the insurer's broader interpretation of the "asbestosis" exclusion. *Id.* at 1554-1555. As to the other two policies at issue, however, the court remanded the case "for further findings to determine whether the term 'asbestosis' was used ambiguously in the public record and the insurance industry" at the time the parties entered into those policies. *Id.* at 1558.

Reinsurance Implications

In light of the inconsistency with which courts have interpreted "asbestosis" exclusions, it is possible that an insurer could be called upon to pay asbestos-related bodily injury claims that it believed at the time of underwriting were excluded from coverage. In such a situation, it is important for the insurer to understand whether its reinsurance, where applicable, will respond to such losses. Although there have been no reported cases addressing this issue, the first place an insurer should look to determine its reinsurance coverage is the terms of the relevant reinsurance agreements.

Indeed, if the reinsurance agreement contains its own, broadly-worded asbestos exclusion, depending on the other relevant terms, it is possible that the loss, while otherwise properly billed, will be excluded from reinsurance coverage. Many reinsurance agreements, however – in particular facultative certificates – do not contain their own exclusions, but instead provide that they are governed by the "terms and conditions" of the reinsured policies. In such a case, if the underlying policies contain only an "asbestosis" exclusion, then the reinsurance agreement would only be viewed as having an "asbestosis" exclusion, and not a broader exclusion.

In addition, most reinsurance agreements contain follow-the-fortunes and/or follow-the-settlements clauses, which broadly provide that the reinsurer is required to follow the loss payments and/or settlements of the reinsured. Although determining whether asbestos losses paid in the face of an "asbestosis" exclusion are properly billed under a reinsurance agreement is a fact-intensive process, the absence of a broad asbestos exclusion and the presence of a follow-the-fortunes and/or follow-the-settlements clause in the reinsurance agreement would likely support such a reinsurance billing. ●

Andrew S. Lewner is a Partner, and Lauren V. DiLeonardo is an Associate in the Insurance and Reinsurance Arbitration/Litigation Practice Group of Stroock & Stroock & Lavan LLP. alewner@stroock.com, ldileonardo@stroock.com

Gabbin' with Gibney

Ever affable, Ed Chats about Teamwork, Coaching, Humor and the Business

"Perfection is not attainable. But if we chase perfection, we can catch excellence." – Vince Lombardi

Our Spotlight member is not only Vice Chair of the AIRROC Board but an avid sports fan from baseball to basketball to golf. It is no wonder he likes to quote Vince Lombardi. Ed plays golf, coached his sons' baseball and basketball teams for many years and currently directs a basketball league for 750 children in his parish. During our chat with Ed, we saw a lighter side demonstrated by highlights of a recent golf trip to England and Scotland with his son, a friend and his friend's son. At one point, the four searched through second-hand clothes at a local thrift shop to find decent jackets and ties in order to satisfy the dress code of the Muirfield Clubhouse. The next day, having no further need for the clothes they had bought, they donated the items back to the thrift store. During that same trip, they were in Liverpool for the Open Championship and made a little Beatle's Tour side-trip, donning Beatles "mop" wigs during the excursion to model their Beatlemania. Ed gleefully relayed these vacation memories making for an amusing conversation.

What lessons have you learned from working in the reinsurance industry?

My love affair with work really took off when I started working on something called "commutations" in February 1990. Early on I thought, well, it is my responsibility to pull everything together myself and sought little input. Soon, however, I learned that in order to execute a successful commutation strategy it truly takes a team approach. You must build a support group stressing that it takes a dedicated team of people from various disciplines to execute a successful commutation strategy. Coordinating the efforts of the accounting, audit, claims, actuarial, and legal areas and making all feel that they are contributing to a successful run-off is critical.

If you could have a second career, what would it be?

I would absolutely be a High School teacher and coach. I was greatly influenced by the Irish Christian Brothers that taught and coached me at Essex Catholic High School in Newark. I even thought seriously for a time about joining the order. I have taught religious education classes at our parish and have always loved teaching in the work environment. I also coached my three son's baseball and basketball teams for many years.

What do you like best/worst about your current position?

My last day at CNA was 31 December 2013. I totally enjoyed the 9+ years I spent there executing the commutation strategy we built. Mike Fitzgerald brought me on board back in 2004 and we had tremendous success. He stressed a team-approach to run-off; we had such a solid group of people in all disciplines, with whom I enjoyed working. I learned so much in my time at CNA and, honestly, there was nothing I didn't like about the job. I am very much looking forward to my next challenge.

What industry publications do you read on a regular basis?

I enjoy reading Business Insurance and Insurance Insider but my favorite publication by a very wide margin is AIRROC Matters. We have such a dedicated group of people that bring that together. I no sooner finish reading the current issue that I can't wait till the next is published!

What educational sessions or conferences do you attend and why?

For the past several years, I have attended only the AIRROC events. In 2013 alone, we held eight events, all with terrific education agendas. This organization just offers so much to run-off professionals like me. The opportunity to learn, the ability to network, and to progress commutations is best right here!

What is your favorite book?

I would have to say, *Unbroken*. "It is an unforgettable story of one man's journey into extremity, and a testament to the resilience of the human mind, body, and spirit." – Laura Hillenbrand

What is your favorite quote?

I have two favorite sports-related quotes. "Hey, Dad? You wanna have a catch?" – Ray Kinsella, Field of Dreams and "Perfection is not attainable. But if we chase perfection, we can catch excellence." – Vince Lombardi

What is your favorite leadership manual/book?

Who Moved My Cheese? by Spencer Johnson, M.D.

What might (someone) be surprised to know about you?

I do like poking fun at myself. Maybe that is why I still have a flip-phone (for anyone who watched the 2014 Winter Olympic coverage, so does Bob Costas!). Anyway, I don't have any contacts stored because if I dial a number once I never forget it! I am also a Beatle's fanatic and have a passion for the game of golf.

What sorts of trends do you see?

The most fascinating area for me is cyber risk. More and more companies are offering coverages and end-to-end risk management solutions to help clients prevent and safeguard against data breaches, computer hacking, employee error, etc. I believe that this area of insurance is going to grow significantly

Tell us how you first got involved with AIRROC.

CNA was one of the original member companies when AIRROC was formed in 2004. At that time, I was asked by Art Coleman to be the Secretary of the organization. I am very proud to have eventually been elected to the Board of Directors and most recently to Vice-Chair.

What was your first impression of AIRROC?

I have been impressed from the start by the passion exhibited by so many leaders in our industry to make AIRROC the very meaningful and vibrant organization that it is today.

If you could change one thing about AIRROC, what would it be?

A couple of years ago I would have said that we need to expand the education that we offer to the run-off industry and to reach further down into organizations to develop the next generation of leaders. But now, with what we have been able to achieve in this area under Carolyn Fahey's guidance, I wouldn't change a thing.

The interest in AIRROC seems to be growing. Why do you think that is?

It is very easy to see that the value-added to organizations far exceed the cost involved in joining.

What would you like to see in the Magazine?

I like this Spotlight idea a lot, and totally enjoyed the first one featuring my good friend, Diane Myers. I hope to see more of these in the future. ●

Connie D. O'Mara, connie@cdomaraconsulting.com
and Bina Dagar, bdagar@ameyaconsulting.com

What's the "Buzz" in the Legacy Industry?

As Executive Director of AIRROC, I am afforded the chance to interact with and learn from all types of individuals involved in the run-off/legacy arena — a very dynamic and important sector of the financial services industry.

In its 9th year, AIRROC continues to be a relevant organization to our constituencies — companies with legacy business in their portfolio. Membership is on a corporate level; and given the impact and importance of legacy business to the entire industry, AIRROC has attracted many talented and experienced participants. The Association has 47 members, including:

• Major US and international insurance and reinsurance companies

• Well-known rehabilitations, receiverships and liquidations that impact a significant portion of US and overseas business

• Insurance/reinsurance brokers

• Third-party administrators and run-off managers that handle business for the risk-bearing companies

AIRROC also welcomes entities ineligible for membership such as Corporate Partners, allowing them to get involved with supporting our initiatives.

In my daily work, I have many opportunities to collaborate with AIRROC's board members, speak with employees of AIRROC member companies, and gain insights from many others involved in making our organization successful. I often question them about their overall impressions of the present and future state of the run-off market. The "Buzz" heard around the industry is what follows. Note: this does not represent the views of AIRROC or of any particular AIRROC member – but is an attempt to catalog reflections from numerous conversations with individuals deeply involved in the legacy realm.

Recent Developments/Observations

• A trend toward firms whose actuaries and their models are driving exposure analysis to the point of mechanizing the process. Decision-making and financial reporting is being impacted (and not necessarily in a positive way). Models can't replace a thorough analysis of subjective factors including good judgment based on experience.

• While resources in the run-off sector always appear to be limited, staffing levels of many run-off operations have been further reduced relative to past workload levels. As workloads increase, efficiency, effectiveness, and proper asset/ liability management are impacted.

• Presently, there is more acquisition activity and less commutation activity. If you are not selling or buying legacy liabilities, you might feel left out of the run-off world at this time despite the need to continue to complete commutations in this relatively low interest rate economy.

Dispute Resolution

• This important area continues to generate many complaints.

• While AIRROC (and other association groups) have procedures aimed at addressing problems inherent in the arbitration process, the biggest challenge lies in getting both parties to agree to use such processes.

• Despite the fact that most arbitrated disputes ultimately settle before hearing – but well after the parties have spent considerable time and expense in the process – parties continue to avoid procuring the assistance of an experienced, industry mediator to get them there quickly, efficiently, and early.

• The "gamesmanship" that accompanies negotiations can sidetrack the quick resolution of disputes. When the company in the "weaker" financial position, tries to pursue recovery of small balances through one of the streamlined techniques, the "stronger" company sometimes won't agree, knowing that the expense of normal arbitration will make the other party's pursuit of such balances cost prohibitive.

• Another tactic of large ceding companies is to require an arbitration panel or court of law to tell parties whether it is proper for the reinsurer to pay less than 100% of their billing. Reinsurers are not always in a stronger financial position than their ceding companies, so this approach can "water down" the goal of getting the dispute resolved.

• The industry would be better served if more players would give the streamlined methods a try.

Regulatory Concerns

• Generally, companies feel that too much time, energy, and operational resources are tied up with compliance and management of regulatory requirements to the point where they cannot perform their regular function in an effective manner.

• Complex regulations are confusing and hard to understand and implement in a practical way.

• Particularly noted is the new ORSA regulation – which will be the most taxing to those who do not already have a robust risk management infrastructure in place.

Challenges/Questions on the Horizon

• Finding ways to position investment portfolios for eventual interest rate increases while dealing with the more immediate ongoing low investment returns.

• Medical cost inflation, especially on the pharmacy side, for legacy workers' compensation claims.

• The uncertainly of knowing if the Affordable Care Act will drive more medical expense cost shifting into the workers' compensation market.

• Will there be changes to tax policy that helps or hinders the overall financial health of industry?

• Is the business of run-off running off, or will there be a new set of either "unforced errors" or extreme calamities (or both) within the industry to create the next wave of growth for run-off and restructuring? If history is any guide, the industry will probably encounter the latter by the end of the decade.

• Can we influence the insurance and reinsurance world to see a run-off strategy as necessary to bolster ongoing business in active companies?

If only we had a crystal ball to foresee the future! While AIRROC cannot answer these unknowns for our constituents, we will continue to do what we can to support the industry, provide networking and meeting opportunities, and educate on the cutting edge topics that companies face every day.

As we forge ahead, AIRROC will continue to provide highly ranked educational programs, workshops, and business meetings. In the first half of 2014, we have hosted member focused education events in Chicago, New York, and Boston. For the second half of the year, look for us in New York and Chicago for second programs, as well as in New Jersey and Washington, DC. In 2013, over 850 individuals attended AIRROC meetings and 96% of the attendees ranked the education sessions and content good or excellent. AIRROC's attendees are diverse with 65-70% of the participants coming from risk bearing carriers. Another focus for us this year will be website enhancements, more cutting edge commentary and content in AIRROC Matters, and expansion of key member services.

Learn more on our website at www.airroc.org. ●

A version of this article originally appeared in the Runoff & Restructuring 2014 Yearbook published by Iskaboo.

Seeing Red: From Apples to Sox…

As I always do when it is time to pen my quarterly column, I reflected on where AIRROC and I have been in the last few months and noticed the color red had prominence in my itinerary.

In March, I was in the "Big Apple" for the first Membership Meeting of 2014 — a great day of networking followed by a second day of education. We heard two sessions on lead paint as well as updates on the NFL Litigation, key U.S. court rulings, and an insurer's standing in Chapter 11 cases.

A few weeks later, I traveled to the home of the "Red" Sox for AIRROC's first Boston-based Regional Education Day, co-hosted by Edwards Wildman LLP, Alvarez & Marsal, and the Boston Chapter of the CPCU Society. The event was enthusiastically enjoyed by all.

Now, I'm seeing other colors. They are our June Regional Education Day in Chicago (our blue logo) and the Summer Membership Meeting in July — fireworks, perhaps? Registration for both is now open on the AIRROC website.

Finally, I am pleased to announce that the October Commutation and Networking Forum will be held at the Heldrich Hotel and Conference Center in New Brunswick, New Jersey from October 19th – 22nd. Registration will open June 1, 2014.

So from my perspective a "rosy red" outlook for AIRROC in the coming months. Looking forward to crossing paths with our members and supporters very soon… ●

Carolyn Fahey joined AIRROC as Executive Director in May 2012. She brings more than 20 years of re/insurance industry and association experience to the organization. carolyn@airroc.org

Thanks to Our Corporate Partners




AIRROC Educational Session Summaries / New York

Record Attendance for AIRROC's Spring Membership Meeting

Nearly 150 individuals from AIRROC constituencies attended the March 11-12 Spring meeting on the 29th floor of "30 Rock." Hosted by AIRROC counsel Chadbourne & Parke, our members had a productive day of networking and business meetings followed by a day of education on several interesting topics. Read on!

Get the Lead Out!

Lead Paint (Part 1): The Epidemiology and the Litigation

Benjamin Blume, a Partner at Carroll McNulty & Kull, moderated this panel consisting of Patrick Connor, President of Connor, and J. Marks Moore III, Principal at Semmes, which examined the medicine, research, and litigation trends of lead poisoning and the sources of lead in the environment.

Lead Paint (Part 2): The Anatomy of Lead Paint Claims – Insurer and Reinsurer Perspectives

Amy Kallal, a Partner at Mound Cotton Wollan & Greengrass moderated this panel consisting of Craig Brown, Vice President and Deputy General Counsel of RiverStone, Gregory Caruso, Vice President of Munich Re, and Mitchell Gibson, Claims Expert and Vice President, Swiss Re, in which experienced insurance and reinsurance claim handlers shared their experiences and lessons learned in the handling of lead paint claims.

Please visit AIRROC's website at AIRROC.org for a complete summary of the lead paint panels.

Ain't That a Kick in the Head…

The Latest on Concussion Liability and Sports-Related Brain Injuries

Robin Dusek, a Partner at Freeborn & Peters updated AIRROC members on the current status of litigation arising out of brain injuries sustained by athletes, as well as, the insurance coverage actions that have been filed in response thereto. Ms. Dusek initially provided an overview of the human brain's response to a concussive trauma and what some scientists have found can result when such events take place on a repetitive basis, as they often do with athletes.

More specifically, studies have shown that such events can result in chronic traumatic encephalopathy (or "CTE"), a progressive degenerative disease characterized by the destruction of brain tissue and the accumulation of "tau" protein. Ms. Dusek explored the findings of a researcher at Loyola University who issued two studies in which he concluded that (1) there is no credible scientific data to support an increase in neurological risk from playing professional football, albeit, a surprisingly high percentage of players exhibited clinically significant impairment, and (2) no cause and effect relationship has been demonstrated between CTE and concussions or participation in "contact" sports.

Ms. Dusek proceeded to provide an overview of athletes who have been diagnosed with CTE; namely those participating in football, ice hockey, WWE wrestling, baseball, and most recently, rugby and soccer. Conclusive CTE diagnosis is complicated by the fact that it must await post-mortem analysis, and some athletes who have taken their lives when faced with the disease appear to have purposefully avoided damaging their brains in the process in order to preserve them for scientific analysis.

Ms. Dusek then discussed lawsuits filed by athletes against the NFL, individual NFL teams, NFL team physicians, the NCAA, Riddell (a football helmet manufacturer), the NHL, the D.C. United soccer team, and high schools with sports programs. Notably, the litigations against the NFL, NHL, NCAA, and Riddell have been certified as class actions. These in turn have resulted in a multitude of insurance coverage litigation currently venued in California, New York, and a recently dismissed action in the U.S. District Court for the District of Kansas. Despite settlement of the class action against the NFL, there is no question that this will continue to provide fertile grounds for both wrongful death and insurance coverage litigation for years to come.

Summarized by Michael H. Goldstein

From the Courtroom to the Boardroom

U.S. Court Rulings: A Look at Recent Cases Impacting Corporations

Partners Rich Dodge and Fred Reinke of Mayer Brown discussed recent court rulings that may impact the way corporations conduct themselves in the U.S. The presenters discussed *Daimler AG v. Bauman*, – U.S. –, 134 S.Ct. 746 (2014), in which the U.S. Supreme Court reversed the Ninth Circuit Court of Appeals' holding that the alleged malfeasance of an Argentine subsidiary of Daimler AG (a German corporation) could subject Daimler AG to general jurisdiction in California. This led into a discussion of *Walden v. Fiore*, – U.S. –, 134 S.Ct. 1115 (2014), in which the U.S. Supreme Court again reversed the Ninth Circuit Court of Appeals' holding that personal jurisdiction was proper over a U.S. law enforcement agent who had seized funds in the Atlanta airport from travelers on their way to Nevada as the police officer lacked minimal contacts with Nevada for the court to exercise personal jurisdiction over him in that state.

The presenters then discussed *Global Reinsurance Corp. v. Equitas Ltd.*, 18 N.Y.3d 722 (2012), in which the New York Court of Appeals reversed the Appellate Division and dismissed plaintiffs' case because, *inter alia*, New York's anti-trust laws under the Donnelly Act (N.Y. G.B.L. § 340, *et seq.*) could not be invoked by a German reinsurer as having extraterritorial application to London marketplace retrocession agreements. This led to a discussion of *United States Fidelity & Guaranty Co. v. American Re-Insurance Co.*, 20 N.Y.3d 407 (2013), in which the New York Court of Appeals examined the "follow the settlements doctrine" and modified the holding of the Appellate Division — in line with the lower court's dissenting opinion — finding an issue of fact as to whether USF&G was unreasonable in (1) allocating the settlement amount by attributing nothing to the "bad faith" claims made against it and (2) in how it valued certain claims for settlement purposes.

The presenters then provided an overview of emerging trends and claims such as the issue of anti-terrorism extra-territorial jurisdiction where acts that actually take place outside of the U.S. can support causes of action in American courts. Specifically, *Rothstein v. UBS AG*, 708 F.3d 82 (2d Cir. 2013), in which the Second Circuit Court of Appeals affirmed that plaintiffs had Article III standing to bring suit against a Swiss bank (operating in the U.S.) — that unlawfully furnished currency to Iran — alleging that this constituted aiding terrorism against Israel. However, the Second Circuit dismissed the plaintiffs' Complaint as they failed to state a claim under the private right of action provision of the Anti-Terrorism Act (18 U.S.C. § 2331, *et seq.*). Finally, the presenters concluded with a brief overview of coverage issues related to claims for breaches of cyber-security.

Chapter 11: Where Do YOU Stand?

Insurers' Chapter 11 Standing

Presenters Ted Zink and Francisco Vazquez of Chadbourne & Parke, provided an overview of insurers' standing in Chapter 11 bankruptcy proceedings. The presenters began with the "actual case or controversy" requirement of Article III of the U.S. Constitution and flowed into the concomitant "standing" requirement. More specifically, the Constitutional standing requirements are three essential elements: (1) "injury in fact" (concrete, particularized – actual or imminent), (2) causal connection between the injury and the conduct complained of, and (3) that it be "likely" that injury will be redressed by favorable decision. There are also "prudential" limitations on standing which remain within the court's discretion and are principally concerned with whether a litigant (a) asserts the rights or interests of a third-party, (b) presents a claim outside the scope of interest protected by the specific law invoked thereby, or (c) advances questions of wide public significance equating with generalized grievances more appropriately left to the legislature.

The presenters then explained that standing in Chapter 11 bankruptcy proceedings is dictated by Section 1109(b), which provides that a "party in interest. . . may raise and may appear and be heard on any issue . . ." Notably, this does not abrogate

photos / Jean-Marc Grambert

AIRROC Educational Session Summaries / NY (continued)

the above constitutional standing requirements, but rather coexists with these requirements. Section 1109(b)'s list of who may constitute a "party in interest" does not include an insurer; however, it is non-exhaustive and this lack of inclusion is obviously not determinative of an insurer's status. A bankruptcy court does require, however, that an entity have a "sufficient stake" (*i.e.*, a pecuniary interest that could be adversely affected by the issue before the court) in the outcome of the proceeding to participate therein. Yet, because of concerns related to multiple parties delaying reorganization, not every "party in interest" may be deemed to have standing to be heard on every issue before the court. Moreover, while a party denied bankruptcy standing may then acquire appellate standing to challenge that determination, appellate standing has a stricter requirement than "injury in fact" as it requires both direct effect and financial injury. The same holds true for an insurer trying to participate in its insured's proceedings.

Regarding an insurer's standing, it is important to understand that potential liability on a policy does not serve to automatically trigger "party in interest" standing and the relevant court will consider prudential limitations in determining insurer standing and thus whether it may be heard either inside or outside the context of the reorganization plan. The presenters then walked the attendees through bankruptcy court opinions that have assessed the issue of insurer standing as to all types of issues raised in Chapter 11 bankruptcy proceedings. Notably, courts will not grant an insurer standing to object to a reorganization plan confirmation if it is "insurance neutral." *See, e.g.*, *In re Combustion Engineering, Inc*. Conversely, insurers will have standing to object to reorganization plans that directly affect them. *See, e.g.*, *In re Quigley Co. Inc*. or *In re Thorpe Insulation Co*. Finally, the presenters walked the attendees through *In re Fuller-Austin*, in which the language of the reorganization plan was amended in order to specifically indicate that the rights of the insurers would not be affected by the confirmation of the plan, thereby eliminating the insurer's standing to participate in the proceeding. ●

Michael H. Goldstein is a Partner at Mound Cotton Wollan & Greengrass, mgoldstein@moundcotton.com

ADVERTISERS IN THIS ISSUE

Find out how your company can benefit from advertising in AIRROC Matters. Contact Carolyn Fahey: tel 703-730-2808 or email carolyn@airroc.org.

CONTINUING ED

AIRROC Goes to "Beantown"










photos / John Kennard

On April 9, AIRROC took our Regional Education to Boston for the first time. The partnership between AIRROC, Edwards Wildman LLP, Alvarez & Marsal, and the Boston Chapter of the CPCU proved to be a success with over 75 in attendance and a diverse set of presentations of relevance to the industry…so, from the 29th floor of Edwards Wildman's offices in the Prudential Center, we spoke with attendees and sponsors to get some perspectives on how the day went.

Carolyn W. Feehey

Edwards Wildman was pleased to continue our long time support of AIRROC by hosting the 2014 Boston Regional Education Day. The speakers worked hard to present topics of interest and practical value to AIRROC members and other attendees in a format that was interesting and engaging. The level of attendance and the spirited audience interaction was very gratifying. We believe AIRROC plays an important role in the industry. We look forward to hosting, sponsoring and attending future AIRROC events.

– Nick Pearson, Edwards Wildman

Great location and comfortable setting, easy to see and hear speakers. Interesting topics to broader run-off industry. Nice range of topics, including good training opportunity for arbitration process for people who are newer to the reinsurance dispute process. Overall, very good program.

– Linda MacDonald, The RiverStone Group

The Boston Regional Education day was a tremendous success as it covered topics that provided interest to a diverse group of participants. The feedback I received was that the topics discussed – Solvency II, Sanctions and Cyber Risk – impact the operations of both run-off and "live" (re)insurers. As the interests of both groups converge, the role of AIRROC - and future conferences it hosts - will grow as it continues to provide a forum for thought-provoking topics to the insurance industry.

– Rudy Dimmling, Alvarez & Marsal Insurance and Risk Advisory Services, LLC

The AIRROC education day introduced new timely topics such as the Vermont Captive Legislation and Cyber Risk and expanded on topics previously presented bringing knowledge more current on Solvency II and OFAC. The OFAC discussion was particularly illustrative with one of the speakers highlighting his recent experiences in the Ukraine.

– Brenda Craven, The Hartford

I always enjoy a good mock arbitration. I like being able to see both sides of the story in a relatively unbiased manner. It helps me to think outside of the box more when interpreting reinsurer inquiries, etc.

– Barbara Gounaris, The Hartford

News & Events

Regulatory News

ERM and ORSA

As part of the NAIC's Solvency Modernization Initiatives, the NAIC adopted "The Risk Management and Own Risk Solvency Assessment Model Act" (No. 505) (the "ORSA Model Act") in September 2012. In order to be effective, the requirements of the ORSA Model Act are expected to be adopted by the states as of January 2015. The adoption of the ORSA Model Act, to a large degree, was in response to the International Association of Insurance Advisors ("IAIS") financial standards, as part of enterprise risk management mandates. ORSA is required to be a "Confidential", self-internal assessment of an insurer, which identifies the insurer's material and relevant risks in its business plan and the ability of its financial resources to support these risks. ORSA is closely intertwined with the insurers' enterprise risk management and part of the holding company corporate governance requirements, and is intended to be an important regulatory tool to facilitate understanding and measurement of risk that is inherent in an insurer's business of insurance.

The ORSA Model Act does not apply to all insurers, but focuses on any U.S. insurer that writes in excess of $500 million of written and assumed premium or insurance holding company groups that together write in excess of $1 billion of annual direct written and assumed premiums.

The biggest concern during the NAIC drafting process and now during adoption in the various states is *confidentiality*. The industry's position is that these materials are not otherwise public and must be protected once filed with the regulators because the ORSA reports will be largely based on sensitive, internal document records and internal analyses. The ORSA Model Act, in Section VIII clearly identifies the "ORSA Summary Report and all documents, materials or other information in the possession or control of the Department of Insurance…" to be recognized as "proprietary" and to include "trade secrets."

Most if not all states have indicated that they have or will incorporate a strong confidentiality provision. In New York, confidentiality has been addressed in Regulation 203; adopted as an emergency regulation. Although the New York Regulation parallels the NAIC ORSA Model Act, after not including the confidentiality protections provided for in the Model Act and in the Acts adopted by other states, and from concerns expressed by the industry, the emergency regulation now includes a confidentiality provision, but it appears to be restricted to "trade secrets" and is still not as expansive and clear as it could be.

To date only 7 states have adopted a version of the Model Act: Iowa, Maine, New Hampshire, Pennsylvania, Rhode Island, New York and Vermont. In a recent AIRROC Matters interview of New Jersey Commissioner Kobylowski, he advised that New Jersey is working on its proposed law and Confidentiality is of significant importance to the Department.

Industry News

Most industry pundits have been predicting increased merger and acquisition activity among insurers for 2014. For the first third of the year, however, the activity has been remarkably slow. Through April 2014 there has been no major insurance company M&A activity announcement. The most significant acquisition in this period has been **Arthur J. Gallagher & Co.'s** acquisition of the insurance brokerage and premium funding operations of Perth, Australia-based conglomerate **Wesfarmers** for A$1,010 million (about U.S. $933 million). The acquisition, which according to Gallagher's chief executive, is its largest acquisition in its history and will make Gallagher one of the largest brokerage firms in Australia and New Zealand.

On the corporate side, the biggest splash was the hostile $3.2 billion offer by Bermuda-based provider of property and casualty insurance, **Endurance Specialty Holdings Ltd.**, to buy **Aspen Insurance Holdings Ltd.** after Aspen's board of directors turned down the offer as an "ill-conceived" proposal that under values the company. According to its press release, Endurance offered to pay $47.50 per share, 21% more than the April 11th closing price of $39.37. As of the deadline for this column, Aspen has steadfastly rejected Endurance's various overtures to discuss a proposal.

XL Insurance (Bermuda) Ltd. has entered into a definitive agreement to sell its wholly owned subsidiary, XL Life Reinsurance (SAC) Ltd. to **GreyCastle Holdings Ltd.** a newly formed Bermuda company, for $570 million in cash. According to XL, upon completion of the transaction, XL Life Reinsurance will reinsure the majority of XL's life reinsurance business via 100% quota share reinsurance. XL's life reinsurance business was placed into run-off in 2009. The transaction is expected to be completed in the second quarter of 2014 subject to satisfaction of regulatory conditions. GreyCastle's third party investors reportedly include large family offices and university endowments.

If you are aware of items that may qualify for the next "Present Value," such as upcoming events, comments or developments that have, or could impact our membership, please email Fran Semaya at flsemaya@gmail.com or Peter Bickford at pbickford@pbnylaw.com.

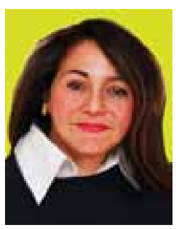
Francine L. Semaya & Peter Bickford

People on the Move

Tad Montross, Chairman, President and CEO of General Re Corp., has been elected chair of the board of directors of the Reinsurance Association of America. Mr. Montross succeeds Tad Walker, President and CEO of PartnerRe North America, as chair to serve a one-year term. The RAA also announced that Mr. Montross, who previously served as RAA vice chair, has been succeeded by **Henry Klecan**, President and CEO of Scor U.S. Corp. and Scor Reinsurance Co., and **Michael Sapnar,** President and CEO of Transatlantic Holdings Inc., is serving as RAA secretary-treasurer.

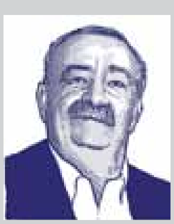
Peter B. Steffen, recently joined Freeborn & Peters LLP as a Partner in its Litigation Practice Group and as a member of its growing industry team that serves all areas of the global insurance and reinsurance marketplace. Pete concentrates his practice on complex commercial litigation and arbitration, specifically advising clients on reinsurance, accounting liability and regulatory matters.

Carroll McNulty & Kull LLC (CMK) has added a team of nine lawyers from the firm of Wenick & Finger, P.C., which closed earlier this year, "to enhance its professional liability and commercial general liability practice, and to add a medical malpractice defense concentration to its New York office." Four of the lawyers are joining the firm as members. They are **Frank Wenick, Barbara Finger, Robert Coppersmith** and **Susan Noble**. CMK's practice areas include insurance coverage, insurance defense, construction, admiralty and maritime, healthcare, medical malpractice defense, commercial disputes, commercial transactions, employment, international trade, and workers compensation. For more information, visit www.cmk.com.



Pina Albo was appointed as a member of the Board of Management of Munich Re effective October 1, 2014, responsible for its Europe and Latin America Division. Until year-end 2014 her responsibility will be in conjunction with Georg Daschner, who will be retiring. Pina has been the President of the Reinsurance Division in the USA at Munich Reinsurance America, Inc. since 2009. She joined Munich Re in 1992. ●

IN MEMORIAM



Edward Meehan, Vermont's first captive insurance director, has died. Mr. Meehan, who came to Vermont from the Massachusetts Division of Insurance, helped develop Vermont's captive industry from its earliest days in the 1980s. When he left state government in 1991, Vermont was far and away the leading venue in the domiciliary US captive market. Susan Donegan, commissioner of Vermont's Department of Financial Regulation, said in the statement that: "Vermont would not be a global leader in captive insurance without his contribution."

SUMMER 2014 MARK YOUR CALENDAR

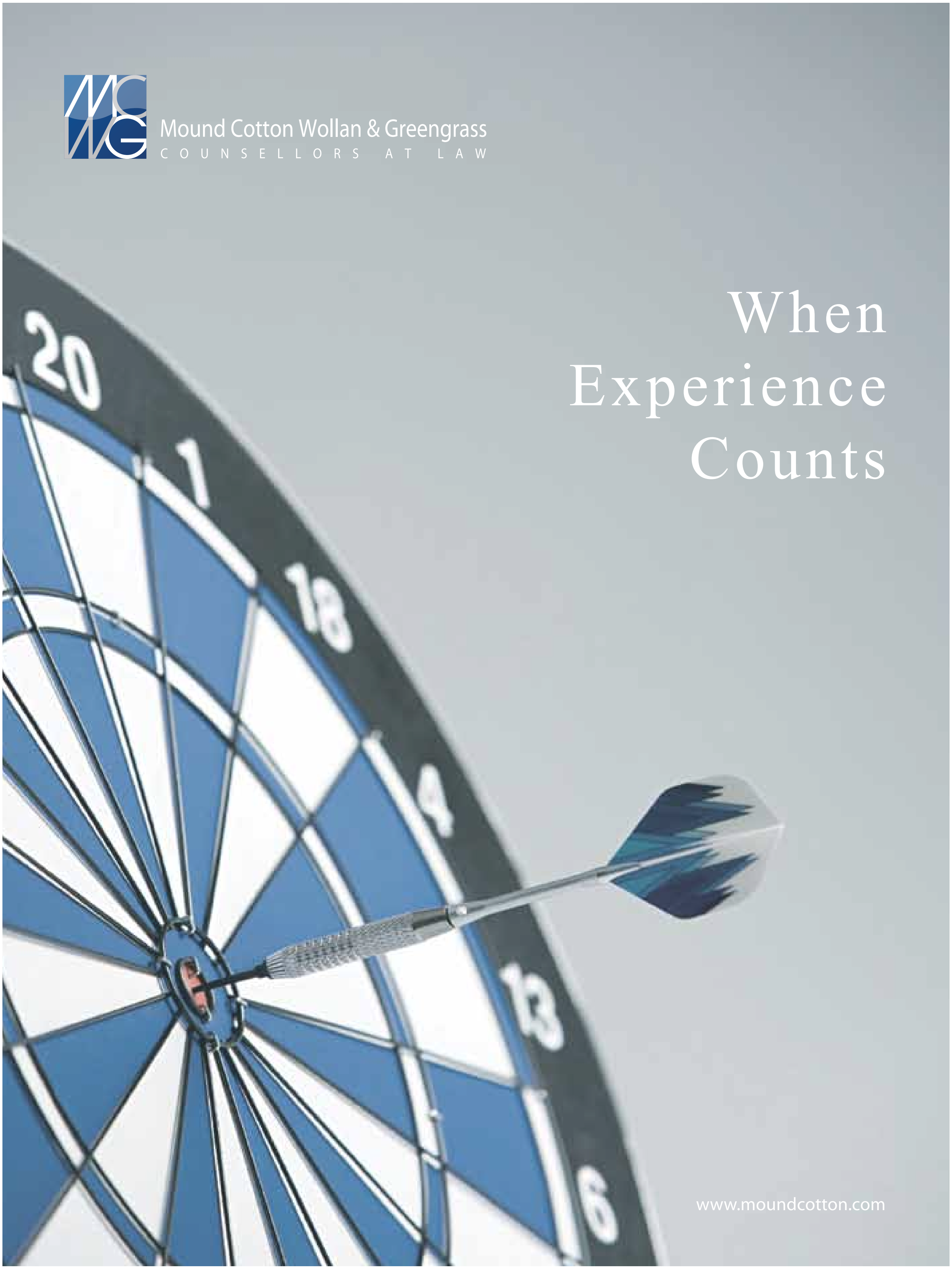
JULY 15-16
AIRROC Summer Membership Meeting
New York, NY
www.airroc.org

AUGUST 16-19
NAIC Summer National Meeting
Louisville, KY
www.naic.org

SEPTEMBER 23
DRP Workshop
Philadelphia, PA
www.airroc.org

OCTOBER 16
IRLA Annual General Meeting
London, UK
www.irla-international.com

OCTOBER 19-22
AIRROC Commutation
& Networking Event
New Brunswick, NJ
www.airroc.org


Mound Cotton Wollan & Greengrass
COUNSELLORS AT LAW
When
Experience
Counts
www.moundcotton.com