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AIRROC matters

LEVERAGING LEGACY LIABILITY

2016 Commutations & Networking Event

TRUMPET LITTLE RHODY • PANEL WOES • CYBER REGS • ROCKIN' GOOD TALE • DRP "ON DEMAND"
PELICAN BRIEF • ALL IN ON EVENT • SURVEY SAYS! • FLAHERTY AND STACK HONORED

Harried Holidays

Peter A. Scarpato

Its 6:15 am, Saturday morning, with Christmas Eve but a week away. The season's first snow fall coats parked cars and lonely sidewalks. An idyllic winter scene. The house is quiet. My daughter, in from New Orleans for the week, is all snuggled up in her bed. And, as the holiday poem goes, not a creature is stirring, not even a mouse. Except, the "rodent" hooked to my computer darts back and forth on the kitchen table as I try, through weary eyes and coffee close by, to finish this article and all else needed for our issue. Did I cut it too close? Maybe.

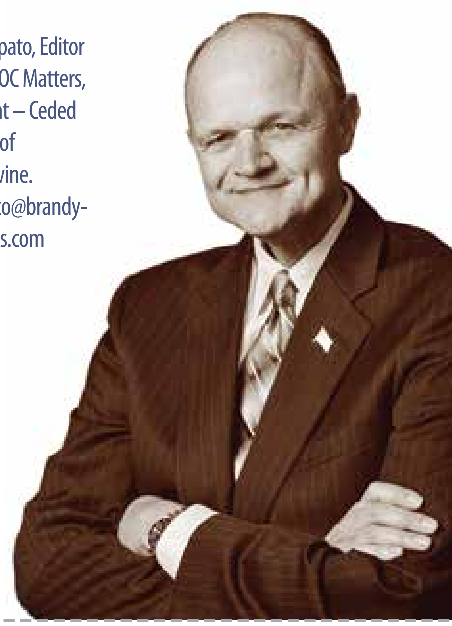
We begin with yet another installment of important musings on the best thing from Rhode Island since Meredith Vieira: Insurance Business Transfer. In, *Can U.S. Insurance Companies Afford Not to Restructure?* Luann Petrellis makes the case for increased adoption of legislation permitting carriers to restructure run off liabilities and release capital for other opportunities. Next is, *Sixth Circuit Follow Up,* Michael Goldstein and Nick Horsmon's continuing examination of Sixth Circuit judicial rulings where courts intervene in previously sacrosanct arbitration proceedings. Our own Francine Semaya provides a timely update on the NAIC's amended version of its draft Insurance Data Security Model Law in, *Cybersecurity: What are insurance Entities Required to Do?*

Ever wonder where AIRROC came from? Well, wonder no more. Our Chair, Leah Spivey, recounts the cherished story in, *The Invention of AIRROC,* of which she gave the premier public reading at the recent October Commutation Event. And for those of us who could not attend the Mayer Brown and White & Williams co-sponsored training presentation on the Dispute Resolution Procedure, no worries. AIRROC now offers a website video of the entire session – a prerequisite for our Certified Legacy Insurance Professional ("CLIP") designation – *On Demand.*

Not only fashionistas offer a hot new look. Our segment on the October event, *AIRROC 2016 Commutations and Networking Forum,* sports a new, bold-colored banner, a striking reminder of the forum's clear relevance to the run off industry. This section covers the gamut of education sessions on emerging risks, overburdened long term health care companies, Rhode Island's IBT and Brexit. Of special note is the self-explanatory *Summary of Results: EY and AIRROC Survey on the US (Re) insurance Runoff Market.* The article is a helpful guide to the survey's insightful conclusions.

We next pay tribute to, *AIRROC Person of the Year 2016: Bill Flaherty.* This article traces the formative steps in Bill's career, his opinions on run off past, present and future, and his strong support for AIRROC. As we do every year for the past five, we honor promising, up-and-coming industry graduates in the name of our first Executive Director. This year, *AIRROC Awards Trish Getty Scholarship* to Taylor Stack, a senior majoring in Risk Management and Insurance at Temple University. We also cover our St. Baldrick's Foundation fundraiser and, of course, Present Value.

Have a safe and bountiful holiday season and prosperous New Year. And, let us hear from you. ●



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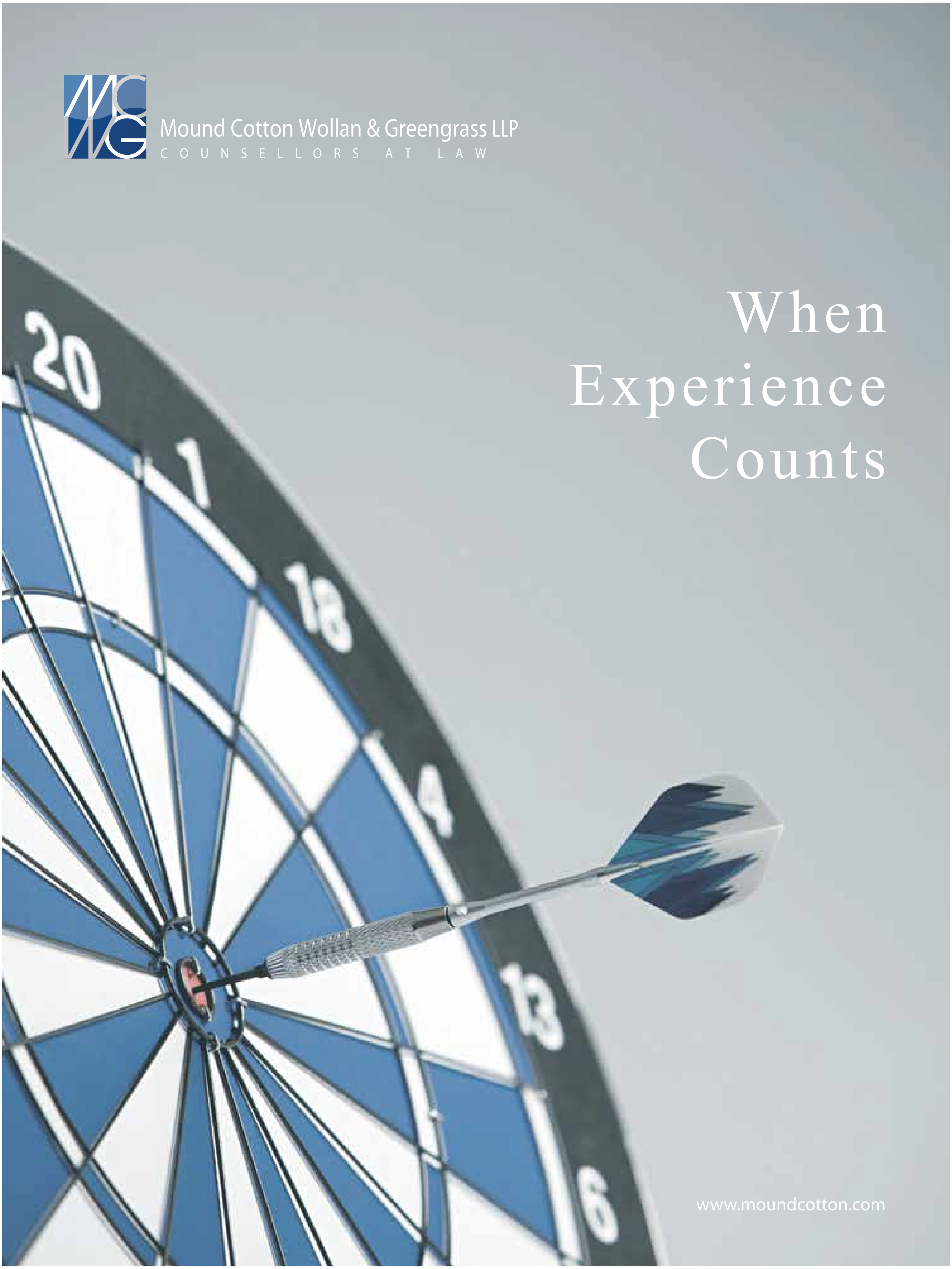

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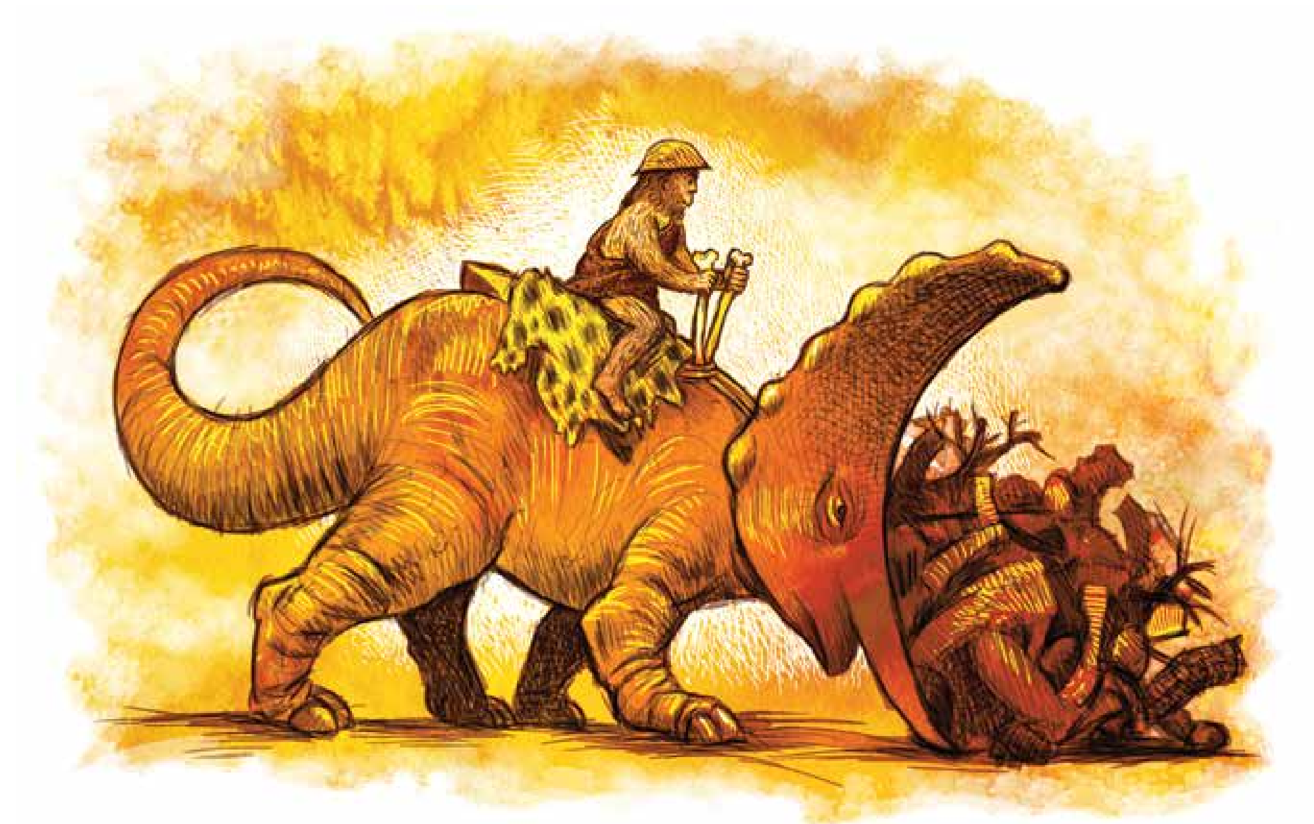
AIRROC

Can U.S. Insurance Companies Afford Not to Restructure?

Part 3: The case for expanding the Rhode Island Insurance Business Transfer to other lines of business



Current global market conditions have increased pressure on business leaders to focus on efficient capital management with an eye towards long-term trends. Rhode Island's amendments to Insurance Regulation 68 are the first step in providing greater flexibility to the U.S. insurance market to take part in the advance restructuring game. The U.S. lags behind the UK in the available tools and mechanisms at their disposal to achieve business transfers that provide an effective and definitive exit solution. Although the U.S. has moved judiciously on this front, it is poised to make more gradual steps forward.

Entire industries are being challenged like never before to open up, innovate and reinvent themselves. In a world where everything is changing, the biggest risk is standing still. This is as true for the insurance industry as it is for any other industry seeking to stay competitive in a growing global economy.

The global game of (re)insurance is evolving at an accelerating pace. There are significant restructuring activities going on in the global and U.S. market. In 2013, Fitch Ratings, when referring to accelerating restructuring in the life insurance industry, stated that there is an "ongoing trend in the industry where many insurers are taking steps to refocus operations and discontinue or divest businesses that have underperformed and/or no longer provide a strategic fit. Some of this product rationalization has also been driven by persistently low market interest rates, which have lowered the relative profitability of some traditional products while also lowering the cost of borrowing if debt is used to finance the acquisition of these businesses … We expect this rationalization process will continue to create opportunities for both traditional players looking to strengthen existing core business, reinsurers with an expertise in block acquisitions, and nontraditional players (e.g., private equity)."

The pressure is now on all insurance carriers to manage their capital more efficiently. It is expected that continuing market conditions, such as the low interest rate environment, globalization, competition and other market trends, will force many insurance companies to continue to undertake significant restructuring activities. According to the 2015 Swiss Re Sigma Report, in Europe "the introduction of regulations such as Solvency II will encourage insurers to restructure in pursuit of capital efficiencies and/or economies of scale or scope. Similarly, the influx of alternative capital will continue to stimulate deals, especially if financial investors become active sellers as well as buyers."

Moving discontinued or capital-absorbing product lines to another business's balance sheet is a huge advantage to an insurance group that has found itself with multiple portfolios of discontinued business, developed over many years and in many formats that can be resource-draining and possibly problematic to the modern insurance organization. Throughout the world there are many jurisdictions that have a restructuring tool to achieve this type of transfer. The most familiar is the Part VII Transfer in the UK — a court sanctioned novation of policies from one carrier to another carrier used by insurers to rationalize portfolio and corporate restructurings and to assist in the closure of businesses in run-off. Generically, this mechanism is referred to as an insurance business transfer.

An insurance business transfer involves the substitution of one counter party for another within the same contract. Its greatest value is the potential to conclusively relieve the transferor of its policy obligations and vest these in the transferee. As a restructuring tool, it is extremely advantageous to a sophisticated insurance industry in allowing firms to adapt themselves to changing business environments through group reorganization to streamline the corporate structure, to gain operational costs savings and efficiencies, to exit problematic lines of business, to bring finality to the business, and to achieve more efficient capital management and improved capital and solvency metrics by releasing excess capital tied up in insurance portfolios.

Prior to August 18, 2015, when the state of Rhode Island (RI) passed Amendments to Insurance Regulation 68 (IR 68), it was virtually impossible to achieve this type of transfer in the U.S. The RI Amendments to IR 68 set forth a process for transferring commercial property and casualty (P&C) runoff business from one entity that does not have to be a RI company to another company that does have to be a RI insurance company. This transfer process results in a novation of the transferred policies affected by a court order from the RI Superior Court after a robust regulatory and judicial review process. The insurance business transfer mechanism allowed under the RI regulations (RI IBT), is modeled after the UK Part VII transfer, UK legislation that was enacted in 2001 and applies to all lines of business.

The pressure is now on all insurance carriers to manage their capital more efficiently.

Since the Part VII legislation was enacted in 2001, hundreds of successful transfers have been completed, none of which have subsequently encountered financial difficulties. In a recent interview with David Scasbrook, Head of P&C Runoff Solutions for Swiss Re, Scasbrook commented that, "Transactions have largely been entered into by companies in run-off or those with a very specific need. And those needs can be categorized into three main reasons: strategic orientation, so companies that have exited a line of business or are acquiring another company and wish to insulate themselves from the results of that company's prior year liabilities. People also enter into these transactions for operational reasons and then more commonly capital management reasons." The Part VII transfer provides the UK insurance market with an effective restructuring tool, making it a vibrant market that is attractive to investors.

Since the UK adopted the Part VII transfer, similar laws have become more prevalent in other parts of the world. In the UK, as well as other jurisdictions that have a similar transfer process, companies have the ability to exit and enter lines of business more easily and to restructure their operations so that they may more efficiently and effectively deploy their capital and achieve greater operational efficiencies. In an Insurance Day article by Rasaad Jamie, Jamie states that, "According to Arndt Grossmann, chief executive of Darag, a specialist run-off insurer based in Germany, which acquires closed books of business from other insurers and reinsurers, the market continues to expand especially in terms of transaction volume, fueled by the increase in discontinued business held by European insurers."

Prior to the approval of the Rhode Island Amendments to IR 68, there was no effective mechanism to transfer portfolios of business from one insurance carrier to another insurance carrier and achieve complete finality for the transferring company. For many years, loss portfolio transfers (LPT) have been the preferred runoff solution. While LPTs provide economic benefits to the transferring company, they do not provide legal finality. Also, Assumption Reinsurance statutes are available in some states and provide for a traditional novation. However, these statutes are viewed as cumbersome and time-consuming and are not widely used outside the rehabilitation process. In some cases, management may choose to sell companies in runoff, but frequently this is not an effective solution because the runoff may be embedded in a much larger portfolio of active business. The court-sanctioned novation process set forth in the RI IBT provides companies with an effective means to transfer all or part of a portfolio to another company achieving complete finality for the transferring company while also adequately protecting the rights of policyholders through a robust regulatory and judicial review process.

Can U.S. Companies Afford Not to Restructure? (continued)

Currently the RI IBT is restricted to commercial P&C runoff business. The RI IBT was written pursuant to RI's "Voluntary Restructuring of Solvent Insurers Act," which limits the application of transactions to commercial P&C business. However, there is no compelling justification to limit the application of the RI IBT to commercial P&C business. The exclusion of other lines of business such as life, workers' compensation, long-term care, etc., leaves carriers holding these liabilities with nowhere to turn to effectively restructure their runoff business.

The RI IBT transfer mechanism is an effective restructuring tool that could be applied to all lines of business to help companies increase capital efficiency, as well as address problem lines of business (i.e., long-term care). Real and tangible benefits can be gained from an insurance business transfer mechanism, and the decision to proceed with a transfer can be a catalyst and form the cornerstone for achieving operational and financial improvements for both the transferring and assuming parties. In order to stay globally competitive, the U.S. insurance industry needs a restructuring tool that allows companies to transfer business from one company to another company and provides a clean exit for the transferring company. The RI IBT is a game changer, providing the U.S. market with a new tool to compete in the global market.

The UK experience shows that the insurance business transfer concept is a successful business model for the transfer of all lines of insurance business. In the U.S., the insurance business transfer, as a strategic restructuring tool, is only nascent as we find ourselves to be new players in an advanced restructuring game. RI took the first step in passing regulations allowing for insurance business transfers of commercial P&C runoff business. When RI and other states adopt legislation providing for insurance business transfers that apply to all lines of business, companies will have the ability to efficiently and effectively restructure all their runoff liabilities. Going forward, organizations will increasingly utilize the concept of an insurance business transfer as a strategic tool to allow insurance groups, captive insurance companies and others to exit certain lines, or portfolios of runoff business to unleash capital for better emerging opportunities, and to free management attention and oversight to more core activities.

Final Part of a 3-part series. Parts 1 and 2 appeared in the Fall and Winter AIRROC Matters, 2015.

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Sixth Circuit Follow-Up

Michael H. Goldstein & Nicholas H. Horsmon

Court Interventions in Arbitration Proceedings

In the Fall 2016 edition of AIRROC Matters, we discussed a series of contentious arbitration disputes between Meadowbrook and National Union that led to a noteworthy Sixth Circuit decision concerning the involvement of courts in arbitration proceedings and the impact of ex parte *communications.*

In August 2016, in *Star v. National Union*, 2016 WL 4394563, at *1 (6th Cir. 2016), the Sixth Circuit issued another opinion involving the parties that vacated an arbitration award because of improper *ex parte* communications between a party-appointed arbitrator and counsel.

In 2011, Meadowbrook demanded arbitration based on National Union's failure to pay workers-compensation claims amid accusations of overbilling. The parties entered into arbitration before a three-member panel. During the organizational meeting, the Panel ruled that all *ex parte* communications would cease with the filing of the initial brief. The Panel issued an Interim Award in National Union's favor, after which National Union's arbitrator began communicating *ex parte* with National Union's attorney.

Meadowbrook filed a supplemental brief addressing the Interim Award. National Union subsequently filed a motion to strike. *Ex parte* communications between National Union's arbitrator and National Union's counsel resumed while Meadowbrook's appointed arbitrator was on vacation. As a result, no discussions among the entire Panel occurred. Despite the lack of deliberation with Meadowbrook's arbitrator, National Union's arbitrator drafted an order granting National Union's motion to strike and sent it to the umpire, but did not copy Meadowbrook's arbitrator on the e-mail. Although the draft was eventually sent to Meadowbrook's arbitrator, the other Panel members issued the order without receiving a response.

Because the Interim Award provided that National Union could recover attorney's fees, National Union submitted a bill of costs. Meadowbrook's review of these time sheets exposed the *ex parte* communications. Meadowbrook filed an emergency motion with the Panel to stay all proceedings. Although this motion was denied, the motion drew a lengthy dissent from Meadowbrook's arbitrator. Ultimately, Meadowbrook filed with the Panel a motion to disband the panel. The Panel denied the motion, with Meadowbrook's arbitrator dissenting. The Panel, by a 2-1 majority, subsequently issued a Final Award ordering Meadowbrook to pay National Union an additional $9 million plus attorney's fees.

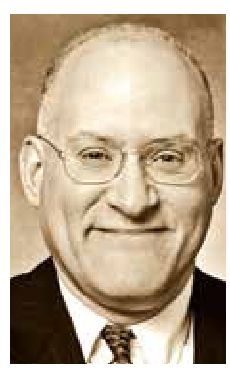
Meadowbrook then filed suit in the Eastern District of Michigan urging the court to vacate both awards, citing the *ex parte* communications and the "disenfranchisement" of Meadowbrook's appointed arbitrator. The Court ruled against Meadowbrook and entered an order confirming the Panel's awards, finding that Meadowbrook "fail[ed] to allege specific instances of misconduct" and "fail[ed] to develop" its argument regarding disenfranchisement.

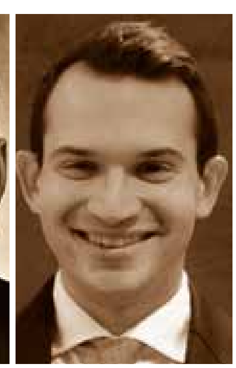
In August 2016, the Sixth Circuit reversed the District Court and vacated the Panel's awards, holding that, under Michigan law, an arbitrator engaging in "misconduct prejudicing a party's rights" is grounds for vacating an award and that this standard "clearly encompasses such ex parte communications."

The Sixth Circuit, citing Michigan Supreme Court precedent, found that "National Union violated the unequivocal ban on ex parte communications three times" and that "the parties and the Arbitration panel—sophisticated businesspeople all . . . settled on this ban at *National Union's* urging." Additionally, the Sixth Circuit found that "[b]ecause [the ex parte communications] violated the plain terms of the parties' scheduling orders, Meadowbrook need not demonstrate prejudice for us to vacate the Arbitration Panel's two awards."

The Sixth Circuit further opined: "The rule is very strict in excluding any communication to an arbitrator, made ex parte after the case is submitted; and when such communication, which may affect the result, is made, it is not usual to enter into an inquiry as to whether the arbitrator was in fact influenced by it or not." The Court emphasized that "[w]hen [the two majority panel members] issued a Final Award over [Meadowbrook's arbitrator's] dissent . . . Meadowbrook found itself liable for millions more than it had anticipated when the arbitration commenced. Put simply, this was an arbitration in which 'the coincidences all broke one way.'"

The Sixth Circuit's recent decision constitutes another meaningful development in the growing body of case law evidencing the federal judiciary's willingness to intervene in arbitration proceedings when courts find that a party has been prejudiced or disenfranchised as a result of the behavior of counsel or party-appointed arbitrators. ●





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Cybersecurity

What are insurance entities required to do?

While US regulators attempt to require insurers to be more aggressive in protecting consumer data from cyber attacks, in August the NAIC'S Cybersecurity Task Force released an amended version of its draft Insurance Data Security Model Law.

The NAIC model law proposes to establish "uniform" standards for data security and investigations, in addition to how to notify about a data breach. The model law would be applicable to all insurance entities, producers and other parties, not only insurance companies. The model law would require a very comprehensive written "information security program" and each licensee's board of directors would be responsible to oversee and approve the program and ensure its compliance with the law. It was hoped that the NAIC model would establish uniformity among state laws and regulations; however, because it states that it would not "supersede existing state laws and regulations" any chance for uniformity across state lines becomes moot. Not only does there exist at least 47 states with breach notification issues, but layers of federal laws as well. Compliance will be a nightmare for all insurance entities, big or small.

Contrast the NAIC model law with New York's proposed regulation entitled "Cybersecurity Requirements for Financial Services Companies." The New York proposed regulation has caused significant concerns among the industry, especially with an effective date of January 1, 2017. The regulations, according to recent industry comments, would cause an undue hardship and burden on all insurance entities and third parties doing business with insurance entities. Producers, for example, would be required to have a separate plan to conform to each of its insurers' plans as well as its own plan to comply with the regulation as a covered entity.

Of major concern with the New York proposed regulation is the potential extraterritoriality reach. For example, if the insurer cannot segregate its New York customer data from data that includes more than New York risks, then the financial institution must comply with the onerous regulatory requirements in other states where it conducts business. In addition, there is a short window of time once the regulation becomes effective for covered entities to develop and initiate a compliant plan.

If New York's regulation's effective date is not postponed, and the NAIC is not able to amend its proposal to preempt state laws and regulations and have such model law adopted at its December National meeting, insurance entities and third parties doing business with covered entities, may be faced with up to 50 states varying laws and regulations to comply with. If ever there was a reason to have "uniformity" among the states, it is now. The industry clearly recognizes the need for cybersecurity regulations, and the need to move quickly, but in order for all required entities to comply across state lines, the regulators must agree on one platform. ●

Francine Semaya, flsemaya@gmail.com

The Invention of AIRROC

Leah Spivey

Once upon a time a long, long time ago in a land not so far away lived a girl who was smart, talented and poor. She loved to play with other children but was limited in what she had to offer. Back in those days no one had real toys to play with, they didn't even have rudimentary ones like marbles. So for toys they used rocks.

Unfortunately, this little girl was so poor she didn't even have a rock to play with, but she noticed that the rich kids had all kinds of rocks, big ones small ones, and brightly, colored ones. Some even had silver and gold rocks. They would collect the rocks and those with the most or biggest rocks were the clear winners.

The way the children would play with their rocks would mostly be by throwing them at each other or smashing one child's rock against another child's rock. Some would lose their rock to their opponent. Others would outright take rocks from another when the other was not watching. The game was called Hard Rock and the kids back then thought this was the only way to have fun.

But, the little girl did not like the game as she thought that it was unfair. When the poor children tried to enter the games with the fragment of rock they might find they were always disappointed. The poor children were either quickly defeated and left with no rock at all or no one would even want to play with them. The little girl decided instead of trying to play she would just collect rock fragments and did so until her pile became quite large and valuable. Other poor children saw her and started doing the same. However, they still longed to play with each other, so the little girl and her friends created a new game.

This game would require teams instead of individuals to play together and the goal was to have every team win not just those with the most, best or biggest rocks. The game was also different because it was collaborative. The children would share what they had learned about gathering rocks, getting the most out of their rocks, maintaining their piles, and ridding their piles of the rocks for which they had no use by trading them with other children who might value them more. There seemed to be no end as to the different ways in which they might combine their piles to make them easiest to manage and sweep away when they eventually disintegrated. They also came up with an easy way to settle disputes that was much less painful and did not cost nearly as much as the Hard Rock game.

Unfortunately, even though the new game looked like more fun and the poor children offered to have the rich kids join in, only a couple of them would do so at first. So, instead of being allowed to join the Hard Rock players to form a larger all-inclusive group having another game to play, the poor children had to form their own group with their new game. When they did, it attracted beings like horses and dogs and elephants that helped the children clearly find, identify, manage and move their piles.

As history would have it, the strangest thing began to happen, some of the rich kids became poor, and more and more of the still rich kids started segmenting their rocks, began to play the new game and the brightest among them even joined the new group. However, the new game was so inclusive that you did not have to join the group to be able to play. Everyone was welcome to build something great out of very little and learn how to extract value from the piles of fragments once regarded as a loss.

So, you must have figured out by now that this new game and group was called AIRROC and is still played today. It allows all of us children, rich or poor and others, who are still playing with rocks to do so in the most mutually beneficial way. I would like to thank that little girl and her friends for giving us such a fun, fascinating and fruitful game to play. ●

Leah Spivey is the Head of Business Runoff Operations for Munich Reinsurance America. lspivey@munichreamerica.com

Now "On Demand"

DRP Workshop

No worries if you could not make the DRP (Dispute Resolution Procedure) Workshop on September 22nd, co-sponsored by Mayer Brown and White & Williams, in New York City. Even if you forgot to set your DVR to record it, AIRROC is pleased to announce that the entire presentation - both the live DRP mock presentation and the video segments of a mock traditional arbitration, arbitrated by Sylvia Kaminsky - will be available "on demand" on the AIRROC website.

This will be the first on demand training that AIRROC offers. "We decided to make a DRP session the focus, as one of the requirements for AIRROC's Certified Legacy Insurance Professional (CLIP) Designation is the completion of an AIRROC DRP training session," said Executive Director, Carolyn Fahey. If you are interested in learning more about the CLIP designation, visit the AIRROC website at www.airroc.org/clip-home.

However, future productions of this dramatic series will continue and, if you have an opportunity to attend, you will enjoy a chance to go behind the curtain and chat with other participants about using the DRP process. Speed, cost-efficiency, and process efficiency are features of the program that make it preferable, depending on the dispute, to a traditional arbitration. Attending the program will enable you to discuss when the DRP is the way to go and how to tailor the process to suit your business needs. The September 22nd workshop also included substantive discussion of the allocation and billing issue presented in the mock arbitration, including an analysis regarding which arguments and facts were persuasive to Ms. Kaminsky, the mock arbitrator.

Future sessions are in the planning stage and AIRROC hopes you will provide your opinion on how we can make the DRP and the training as beneficial to your business as possible. Please contact Carolyn Fahey at Carolyn@airroc.org with any suggestions. ●

photos / Jean-Marc Grambert


Dodge


Goldsmith

News & Events

Regulatory News

NAIC

There were five contested elections for insurance commissioner on November 8, 2016. The results are:

Delaware: Democrat Trinidad Navarro, Sheriff of New Castle County, was elected as Insurance Commissioner. Navarro had defeated incumbent Karen Weldin Stewart in the primary.

Montana: Republican State Senator Matthew Rosendale won as Montana Commissioner of Securities and Insurance. Incumbent Monica Lindeen (D) did not run for re-election.

North Carolina: Republican Mike Casey unseated incumbent Democrat Wayne Goodwin as North Carolina Insurance Commissioner, the first time a Republican has held this office in the state's history.

North Dakota: Republican John Godfread won as North Dakota Insurance Commissioner. Incumbent Adam Hamm (R) did not run for re-election.

Washington: Incumbent Mike Kreidler (D) won his fifth term as Washington State Insurance Commissioner.

Also, at its December National Meeting, the NAIC named former Pennsylvania commissioner **Michael Consedine** as its CEO effective in early 2017. While commissioner, **Consedine** was the NAIC's representative to the EU–U.S. Insurance Dialogue Steering Committee and was active in the International Association of Insurance Supervisors (IAIS), where he served on their Executive Committee.

Andy Beal, current acting NAIC CEO, will continue in his role as Chief Operating Officer and Chief Legal Officer.

Cybersecurity

In August the NAIC'S Cybersecurity Task Force released an amended version of its draft Insurance Data Security Model Law. Now on the table are competing approaches by the Federal Government, the NAIC and New York State. The issues raised by these competing approaches, which will have significant impact on insurers and their vendors, are discussed in the article on page 10 of this issue.

Solvency II

The insurance industry has been warning of the potential consequences for US insurers and reinsurers if Federal and International regulators are unable to come to an agreement on standards for applying Solvency II to US entities. Now there is specific evidence of these concerns with Germany's action banning Missouri domiciled Shelter Re from continuing to do business in Germany without establishing a licensed branch in Germany. According to the US insurance industry, the implications for internationally active US insurers without a "Covered Agreement" to protect them, coupled with the consequences of Brexit, could be significant. On the other hand, the NAIC and the state insurance commissioners believe that the state-based insurance regulatory system should be granted equivalence without a "Covered Agreement." In reaction to Germany's position, the NAIC is itself looking into the issue of reciprocity in view of the actions of German and UK regulators, which could lead to even more international regulatory confrontations.

And this does not even begin to take into account the effect of a new administration in Washington!

Industry News

This year's election season seems to have contributed to a slow pace of corporate moves and combinations, as companies and regulators seek signs of direction for the future. There have been a few significant transactions, however.

In October, **Sampo Japan ("Sampo")** agreed to acquire Bermuda insurer **Endurance Specialty Holdings ("Endurance")** for $6.3 billion, the second largest acquisition by a Japanese insurer. **Sampo** will pay $93 per share, a 40 percent premium to the average share price at the time of the announcement. According to announcements of the transaction, the Bank of Japan's embrace of negative interest rates has made overseas investments more attractive for Japanese companies, and a relatively strong yen made the purchase easier. **Endurance** provides property and casualty insurance in the United States, as well as reinsurance and specialized coverage in areas like agriculture.

Contrasting with Sampo's expansion into developed markets is **American International Group's ("AIG")** sale of **United Guaranty Corp. to Arch Capital Group Ltd. ("Arch")** for $3.4 billion including $2.2 billion in cash and the rest in **Arch** securities. This transaction is consistent with Chief Executive Officer Peter Hancock's efforts to simplify AIG and free up capital in light of persistent pressure by activist investors Carl Icahn (Icahn Partners) and John Paulson

(Paulson & Co.) to divest key units in an effort to shed AIG's designation as a "systemically important financial institution."

In October, **China Oceanwide Holdings Group Co., Ltd. ("China Oceanwide")** announced an agreement to buy U.S. insurer **Genworth Financial, Inc. ("Genworth")** for $2.7 billion in cash. **China Oceanwide** said the Chinese firm will pay $5.43 per share to acquire all the Richmond, Virginia-based firm's outstanding shares. **Genworth** has mortgage insurance operations in the US, Canada and Australia and a life insurance business in the US, including a troubled long-term care book of business. Some recent Chinese bids for insurance interests have attracted intense regulatory scrutiny overseas and in the US.

Finally, in December **Liberty Mutual Insurance Co. ("Liberty Mutual")** agreed to acquire Ironshore Inc. ("Ironshore") from Chinese conglomerate Fosun International Ltd. for about $3 billion. Hamilton, Bermuda-based **Ironshore** is a specialty and surplus lines insurer with gross premiums written of $2.2 billion in 2015. Ironshore is the sixth-largest U.S.-based surplus lines insurer with $1.01 billion in nonadmitted premiums, according to *Business Insurance's* latest ranking. **Liberty Mutual's** existing surplus lines operation, Liberty Insurance Surplus Corp., reported $342.2 million in nonadmitted premiums in 2015.

New Member

AIRROC is pleased to welcome new member, DARAG Deutsche Versicherungs- und Rückversicherungs-AG **("DARAG"). DARAG** is the first German insurance company to specialize in taking on inactive business, i.e. discontinued insurance portfolios that are no longer generating premiums, from direct insurance and reinsurance companies. It has been in existence since 1949 and dedicated exclusively to all aspects of the run-off business, whether acquisition, management or solutions. As a dedicated legacy entity, **DARAG** is a natural addition to the AIRROC family.

People on the Move

AIRROC Board member, **Sylvain Villeroy de Galhau,** was appointed CEO of AXA Liabilities Managers effective October 1, 2016. Sylvain joined AXA in 2000. He joined the AXA Liabilities Managers Executive Committee as Chief Financial Officer in 2007; and was appointed CEO of AXA Liabilities Managers UK and Head of Acquisitions in 2013. In his new position as CEO of AXA Liabilities Managers, he will continue to support the growth of AXA Liabilities Managers business by leading the fund-raising and acquisition strategy.

After more than 30 years with the Stroock & Stroock & Lavan LLP law firm, **William Latza,** has been named the Chief Compliance Officer & General Counsel of Lemonade, Inc., the newly licensed, innovative peer-to-peer insurance entity in New York. Bill can be reached at bill.latza@lemonade.com. ●

WINTER 2017 MARK YOUR CALENDAR

February 1-7, 2017
American Bar Association Midyear Meeting
Miami, FL
www.americanbar.org

March 14-15, 2017
AIRROC Spring Membership Meeting
New York, NY
www.airroc.org

April 8-11, 2017
National Association of Insurance Commisioners (NAIC) Spring National Meeting
Denver, CO
www.naic.org

May 8-10, 2017
Insurance & Reinsurance Legacy Association Ltd. (IRLA) IRLA Annual Congress
Brighton, UK
www.irla-international.com

July 18-19, 2017
AIRROC Summer Membership Meeting
New York, NY
www.airroc.org

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.

A Pod of Pelicans

Carolyn Fahey

Message from the Executive Director

Our cover for this issue features five white pelicans. Pelicans by nature are collaborative, social, savvy, and global. Without a doubt similar parallels could be drawn for the AIRROC constituency, making the pelican a fitting cover illustration. Let's look at those terms in relation to AIRROC NJ 2016.

COLLABORATIVE: The event itself is a true collaboration. The AIRROC Board and Event Committee plan each year together. The education features – special events, fundraising, and the scholarship – happen only because many individuals work together to bring these to fruition. The post-event survey also points to the collaborative nature of the delegates – 65% reported that they met with seven or more companies and 83% made progress on either commutations or project plans with whom they met.

SOCIAL: Why does the industry attend AIRROC NJ? The top two reasons from our attendees are: 76% for networking and 53% for commutations. Working hard and playing hard go hand in hand at AIRROC. It is always satisfying to watch our delegates hard at work and at the end of the day enjoying the time together to catch up and share a story and laugh. AIRROC provides an invaluable social connection, which facilitates getting the job done. Just look at the photos from the event in the pages of this magazine and you will see it yourself.

SAVVY: AIRROC members see the benefits of being present. As much as we are "more productive" in the workplace with the rising use of technology the personal relationships we have are increasingly important. AIRROC provides the platform to meet in person and enhance those relationships. That's just smart business.

GLOBAL: Pelicans live on every continent except Antarctica. As runoff becomes an increasingly global business, AIRROC's importance is heightened. We had attendees from the U.S., U.K., France, Italy, Germany, Malta, Switzerland, and more. The reach of those companies that joined us truly is global.

Join the pelicans and come to AIRROC! ●

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

AIRROC Board of Directors & Officers 2017

Back Row – left to right: Jose Martinez, Jr., Secretary (CNA); Andre Lefebvre (Arrowpoint Capital), Peter Scarpato (Brandywine Group); Karen Amos (Resolute Management Services); David Kenyon (Swiss Re). **Middle Row – left to right**: Michael Baschwitz (Zurich); Katherine Barker, (Armour Risk Management); William Teich (The Hartford); Marianne Petillo, Treasurer (ROM Re); Ivan Jaffa (RiverStone ReSources. **Front Row – left to right**: Ed Gibney (R&Q); Leah Spivey, Chair (Munich Re America); Michael Fitzgerald, Vice Chair (QBE North America); Carolyn Fahey, AIRROC Executive Director; Bill Littel (Allstate). Not Pictured: Sylvain Villeroy de Galhau (AXA Liabilities Managers UK).

COMMUTATIONS & NETWORKING FORUM

APPLAUSE, APPLAUSE FOR THE EVENT!

The New Brunswick Heldrich Hotel was the scene once more for our Commutation and Networking Forum. Hundreds gathered for three days of business, food and fun in a now familiar setting. And AIRROC continues to shine as the platform where things get done!

photos / Jean-Marc Grambert

The AIRROC Education Committee did it again!

The featured speakers at AIRROC NJ 2016 found themselves presenting to a packed room and had lots of interaction from the audience with the use of a new technology which enabled them to submit answers to questions with the use of their cell phones. The interactive, interesting and insightful sessions were one of the highlights of the October event for many. A brief synopsis of what was discussed appears in the following pages. Speaker materials can be accessed on the AIRROC website or the AIRROC APP.

Emerging Coverage Issues Driven by the Sharing Economy

Summary by Ben Gonson

The second session of the Education Day was entitled "Emerging Coverage Issues Driven by the Sharing Economy". Marcus Doran, COO of Armour Risk and Education Day Co–Host, moderated the panel consisting of: Gerry Finley, Senior VP of Casualty Underwriting at Munich Re; Joseph LoParrino, Manager of US P&C Actuarial Services-PwC; and Amy Kallal, Partner with the law firm of Mound Cotton Wollan & Greengrass LLP. The hour long session was very detailed and the 60 slides shown may be reviewed on the AIRROC website. Home sharing (Airbnb) and ride sharing (UBER) were the main types of sharing discussed, followed by emerging opportunities, including "blockchain" and peer-to-peer insurance.

Joe LoParrino discussed the current landscape, noting that technological advances and resource scarcity were at the heart of the sharing economy. $15 billion had been invested in the sharing economy as of 2013; however, only 19% of the total U.S. population had engaged in a sharing economy transaction. Almost everyone in the audience had used UBER, while only a few people had been involved with home sharing.

Gerry Finley then discussed underwriting considerations. He noted that the transportation network company (TNC) connecting the buyer and seller resists assuming any liability. Furthermore, traditional policies do not insure, or specifically exclude or limit coverage for, certain exposures that may arise from the sharing activity. In addition, legislative and court battles lie ahead.

Insurers have been somewhat responsive to the coverage gaps that sharing activities have created. Graduated coverage is available for UBER drivers based on the stage of the ride share process. Liability exposure for ride sharing depends on three scenarios: where the driver is logged in but not yet matched with a passenger; where the driver is in route to pick up a match and; where the passenger is in the vehicle. While ride sharing exposures are generally covered in the basic commercial auto policy, most drivers rely on their personal auto policy where gaps in coverage currently exist. For its part, UBER offers liability coverage up to $1 million per incident and physical damage coverage to the driver's vehicle that occurs during a trip up to $50,000.

Meanwhile, the traditional homeowner ISO policy form (HO3) currently excludes business use and only covers "occasional" rental. The two major risks in the home sharing Airbnb context for short-term rentals are property damage or theft to the host's property and potential bodily injury to guests. Airbnb offers both types of coverages as of January 2015.

Page 18 (from left): Leah Spivey, Munich Re America; Karen Amos, Resolute Management Services.

(panel left to right): Joseph LoParrino, PwC; Gerry Finley, Munich Re America; Amy Kallal, Mound Cotton Wollan & Greengrass LLP; Marcus Doran, Armour Risk Management.

Page 19 (from left): Amy Kallal, Mound Cotton Wollan & Greengrass LLP (top middle) Vince Bodnar, LCTG; (bottom middle) Doug Greer, Alvarez & Marsal (far right) Mark Goodman, Freeborn & Peters; Doug Greer, Alvarez & Marsal; Vince Bodnar, LCTG.

Topical subjects and spirited dialogue punctuate another successful Event

Amy Kallal discussed the legal landscape regarding whether drivers are independent contractors instead of UBER employees in detail. A California court in O'Conner v. Uber (see slide) held that the drivers were presumptive employees because they perform services for the benefit of UBER. This case apparently settled; however, various states have made their own determination of employment status.

The panel ended with a brief discussion on the emergence of blockchain and peer-to-peer insurance. Blockchain involves a shared digital ledger that constantly grows as new blocks are added to it. The decentralized ledger keeps a record of each transaction that occurs across a network, with the blockchain's integrity hinging on strong cryptography. Banks, investment firms and insurers are investing considerable time and resources to develop the technology, which started with Bitcoin. Numerous insurance issues arise with blockchain, including security, regulation, fraud and terrorism. Peer-to-peer insurance is not a new concept. However, new technology is lowering the barriers to entry for the average person. Lemonade recently launched its peer-to-peer platform that provides limited coverages in limited jurisdictions. While it is in its infancy, it will be interesting to watch it address issues such as multistate regulation and longer tailed exposures. Who knows, maybe a run-off opportunity!

Is Long-Term Health Care the Next Run-off?

Summary by Ben Gonson

The third session of the Education Day was entitled "Is Long-Term Health Care the Next Run-off?" Mark Goodman, Partner with Freeborn & Peters, moderated the panel consisting of Vince Bodnar, Chief Actuary of Long Term Care Group, Inc., and Doug Greer, Senior Director at Alvarez & Marsal. The hour-long session was detailed and the 40 slides shown may be reviewed on the AIRROC website.

Many people in the audience had not bought long-term care ("LTC") insurance, which is designed to cover long-term services and supports, including personal and custodial care in a variety of settings. As noted in the description of the session, the panel discussed the size of the market, pricing considerations, regulatory response, concerns and challenges.

Vince Bodnar advised that 7 million Americans have LTC insurance, although 45 million will need such insurance by 2025. LTC is a $720 billion market in 2016, only 3% of which is privately insured. One-third of LTC is paid for by Medicaid and Medicare. Only 10 or more companies are writing new LTC policies now. 70 companies have runoff LTC blocks. Incurred claims will continue over time and current policy reserves of $103 billion will increase.

Doug Greer discussed the evolution of LTC insurance using slides demonstrating the changing format of the coverage provided and the growth in the industry that started in the mid-1980s, with rapid growth from 1995-2002 (130 insurers). The market contracted starting in 2003. Slide 7 lists the ten largest insurance group "closed blocks" – i.e. runoff opportunity.

Vince Bodnar explained that the crash of LTC insurance was caused by a number of factors:

- Its design makes it a very risky product;
- Environmental developments – very low lapse and mortality factors, unforeseen drop in interest rates and emergence of assisted living facilities;
- Insurers exiting from the market – total premium of $1,033 million as of 2001 and $320 million as of 2014;

Educational Panels (continued)

- High new business premium rates – premium cost is out of range for most of the middle class; and
- Challenges getting regulatory approval for rate increases – only a third of the rate increases requested is approved.

The financial distress in the LTC insurance market was briefly discussed. In 2008 Conseco transferred 140,000 LTC policies to a state trust. The Penn Treaty (2009 rehabilitation) is expected to become the most expensive LTC liquidation with $3 million covered by a guarantee association.

Although high interest exists in buying runoff LTC books (mostly from Asia and/or private equity backed-reinsurers), few deals are occurring as it is difficult (1) to find price points both parties can agree with and (2) to completely off-load risk. In terms of future outlook, LTC services will evolve. Baby boomers will demand change and not expect help from their children. Emerging technology will make LTC more efficient and less labor intensive. LTC costs will continue to rise and it will be easier to reduce benefits than to ask regulators for large premium increases.

Page 20 (clockwise from left) panel/audience; Christopher Brennan, New Jersey Department of Banking and Insurance's Office of Solvency Regulation; Karen Boisvert, Swiss Re America; Mory Katz, Pro Global Insurance Solutions; (bottom) Al Bottalico, Locke Lord; Elizabeth Kelleher Dwyer, Rhode Island Superintendent of Banking and Insurance .

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Rhode Island Regulation 68

Summary by Joseph C. Monahan

AIRROC's New Jersey Commutations and Networking Forum included a panel presentation entitled "Rhode Island Regulation 68 – A View Of It In Practice." Locke Lord LLP's Al Bottalico moderated the panel, comprised of: Karen Boisvert, Swiss Re America's Senior Vice President, Casualty Underwriting; Rhode Island Superintendent of Banking and Insurance Elizabeth Kelleher Dwyer; Christopher Brennan, Legal Specialist with the New Jersey Department of Banking and Insurance's Office of Solvency Regulation; and Mory Katz, Managing Director of U.S., Pro Global Insurance Solutions, plc.

As amended in August 2015, Regulation 68 provides another option for the management of run-off liabilities in the form of "insurance business transfers" or "IBTs", which require either re-domestication to Rhode Island or the formation of a new company domiciled in Rhode Island. As Ms. Dwyer explained, in order to undertake an IBT, an insurer must be solvent and adequately reserved. Moreover, the Regulation applies only to commercial property and casualty lines of business. An application for approval of the IBT plan must be submitted to the Rhode Island regulators. Assuming the proposed IBT receives that regulatory approval, the plan is then submitted for court approval. Ms. Dwyer emphasized that a carrier considering an IBT under Regulation 68 should first discuss its plans with her office before applying, as such communication will help to move the process along more smoothly. Ms. Dwyer's goal is to complete the review and approval process within 90 days, and that, depending on the time of year and completeness of the application, the process could potentially be accomplished in as little as one month. After that, she estimated that the requisite court approval could take approximately nine months to a year, but that it may go faster as the Rhode Island court gains more experience with the procedure.

The focus of the approval process is the protection of policyholders and the regulators require confirmation that all policyholders have received proper notice of the plan. As part of the application, the applicant must file an actuarial re-port, and Rhode Island will hire its own actuary to review and analyze that filing.

Delegates come to deal, learn and grow.

Ms. Dwyer's office will provide the court with an opinion regarding the plan and will monitor the plan's implementation in order to ensure policyholder protection, and she emphasized that the Insurance Department will oppose an IBT if it appears the new entity will be undercapitalized or have insufficient reserves.

Ms. Boisvert explained that Regulation 68 allows for legal finality with respect to run-off, and likened it to Part VII Transfers in the United Kingdom. She further noted that the Regulation allows for a transfer of the balance sheet and provides for capital relief along with regulatory oversight to protect policyholders. She indicated the procedure can be used both for internal consolidation and to facilitate the acquisition or transfer of legacy books of business between parties.

Mr. Brennan expressed that this is uncharted territory, such that New Jersey does not have protocols in place to evaluate a proposed IBT. He did note, however, that before New Jersey would give up oversight of anything that would impact policyholders, his office would take a very close look at the proposal. That said, he expressed that New Jersey is in favor of anything that will help the market and free up capital so long as policyholders are protected in the process. He stressed that New Jersey intends to work closely with Rhode Island as a second set of eyes. Like Ms. Dwyer, he emphasized the importance of communication with the New Jersey regulators in advance of submitting an application for an IBT. In so doing, the company should be ready to explain why the proposal is not harmful to its policyholders, and should focus on the adequacy of reserves. The panel agreed that a company considering an application under Regulation 68 should consult with the regulators in any state where there is a large block of policyholders.

Mr. Katz spoke on behalf of Pro Global, a U.K. based company with offices in the U.S. that was the first to apply under Regulation 68 to allow it to accept IBTs for purposes of managing legacy books. He indicated that Pro Global has significant experience with Part VII Transfers in the U.K. The name of its Rhode Island domestic will be ProTucket. Mr. Katz stated that client demand was behind Pro Global's decision to submit its application and opined that he believes the market for such transactions will prove to be substantial.

Brexit – Impacts and Implications

Summary by Joseph C. Monahan

The education sessions at AIRROC's New Jersey Commutation and Networking Event included a panel discussion regarding the implications for the insurance industry of the United Kingdom's recent vote to withdraw from the European Union, otherwise known as "Brexit." Michelle George, Partner with Chadbourne & Parke (London) LLP moderated the panel, which was comprised of: James Ferris, Director with PwC; Carolyn Coda, Swiss Re's Deputy Head of Government Affairs Americas; Pascal Salelles, AXA LM's Global Head of Commutations; and Frank Schmid, Head of Property & Casualty Inforce Management, AIG.

The panelists generally agreed that it is difficult to handicap what Brexit will mean for the insurance run-off industry at this point, as there still remains much uncertainty. In fact, Mr. Schmid observed that there is still some chance the U.K. will not complete its withdraw from the E.U., as any final deal negotiated under Article 50 of the Treaty on European Union will have to be ratified by the British Parliament. Much will depend on whether the negotiations between the U.K. and the E.U. will result in a "soft Brexit" or "hard Brexit." A soft Brexit would see the U.K. participate as

Page 21 (from left): Frank Schmid, AIG; Pascal Salelles, AXA LM; (far right) Frank Schmid, AIG; Pascal Sallelles, AXA LM; Carolyn Coda, Swiss Re; Michelle George, Chadbourne & Parke; James Ferris, PwC.

COMMUTATIONS & NETWORKING FORUM

Educational Panels (continued)

a member of the European Economic Area (“EEA”), similar to Iceland, Norway, and Lichtenstein, or at least participate in the European Free Trade Association (“EFTA”), which includes Switzerland along with the three EEA countries. A hard Brexit is a situation where the U.K. does not participate in either of these organizations but instead relies in its trade relations with the E.U. on World Trade Organization rules, supplemented by bilateral trade agreements. Given the immigration issues that seem to have motivated much of the Brexit vote, the panelists agreed that a hard Brexit is the most likely outcome. In the meantime, the uncertainty as to what form Brexit will take has its own negative implications.

A hard Brexit would jeopardize the ability of a U.K. company to do business throughout the E.U., using an element of E.U. membership known as “passporting,” which allows financial services to be sold in the E.U. without the need to seek further authorization from each E.U. country where it seeks to do business. This could pose a hardship on U.K.- based insurers. For instance, if the company had run-off operations in Europe, and the U.K.’s passporting rights were cancelled, the U.K.-based company would need to establish a European-based affiliate in order to facilitate access to the European market. The panel pointed out that in 2014, across the E.U., only 13 percent of insurers’ cross-border market entries occurred via passporting, the balance having occurred via the establishment of subsidiaries. For insurers that currently access the E.U. through the London market, much will depend on the ability of Lloyd’s to continue to provide such access, possibly by establishing a subsidiary in the E.U.

An alternative to passporting, known as “equivalence,” is available, through which reinsurance services outside of the E.U, but in a regime deemed “equivalent” to the E.U.’s, can be sold. Equivalence is not available for insurance, so for those entities without a European presence, it would be necessary to establish and provide insurance via a European subsidiary, then reinsure to the equivalent regime. This could at least mitigate the loss of passporting rights, but it is not yet clear what this would look like in practice. It is likewise not yet apparent what impact Brexit will have on the U.S. market, although some panelists expressed skepticism that it would have a significant effect.

The panelists agreed that the situation is a fluid one, with many questions left to be answered before any clear impacts on the ongoing and run-off markets can be fully understood. ●

Joseph C. Monahan is a Partner in the Philadelphia office of Saul Ewing LLP. jmonahan@saul.com

Page 22 (from left): Michelle George, Chadbourne & Parke; James Ferris, PwC; Pascal Sallelles, AXA LM; Frank Schmid, AIG; Carolyn Coda, Swiss Re.

Page 23: audience; (middle) Luann Petrellis, EY; (bottom) Marcus Doran, Armour Risk Management; Jay Votta, EY; Luann Petrellis, EY.

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Summary of Results: EY and AIRROC Survey of the U.S. (re)insurance Runoff Market

One of the highlights of the Education Session at AIRROC's October Forum was the first "reveal" of the results of the AIRROC/EY jointly produced (re)insurance runoff survey. The first of its kind in the US, the results highlight the ongoing challenges faced by insurers and reinsurers that are strategically managing their legacy business. Kevin Gill, Luann Petrellis, and Jay Votta from EY opened the Education Day at AIRROC NJ 2016 with the insights and new data from this study.

With the trend of legacy players becoming more and more intertwined with the live markets, being able to illustrate the size and depth of the U.S runoff market is increasingly important. "While AIRROC constituents know the importance of legacy, many of us face challenges with illustrating to our companies and colleagues how we impact the live insurance market," said Carolyn Fahey, Executive Director of AIRROC. "Every company has legacy – but the definitions can be as varied as the business plans of the companies themselves."

Below is more detail on the survey and what we learned…

In early 2016, Ernst & Young LLP teamed up with AIRROC to conduct a survey of industry experts on the current state of the U.S. insurance runoff market and predictions for the future. The goal was to understand the key strategic objectives for companies with runoff business, how the runoff business is managed, and options for dealing with the many challenges of runoff business.

Survey (continued)

The Survey primarily targeted members of AIRROC, the only U.S. based non-profit association focusing on the legacy sector of the insurance and reinsurance industries. The survey respondents were predominantly senior executives and management of U.S.-domiciled insurers and reinsurers with runoff business, as well as runoff acquirers and foreign carriers with U.S.-domiciled policies in runoff. Respondents came from a variety of organizations, including midsized carriers and some of the largest international organizations.

From the survey responses, we identified five key findings.

1. Finality is at the top of the agenda for managers of runoff business.

The majority of respondents reported that runoff business is being managed through the use of strategic runoff plans indicating that runoff managers are taking a structured approach to runoff business. A full 88% of survey respondents reported having a strategic runoff plan in place. This acknowledges that management sees the importance of a strategic runoff plan and that opportunities are available to deal proactively with runoff business.

Finality is at the core of these plans. The majority of survey respondents identified finality as the most important objective for runoff plans. The respondents identified long-tail claims, availability of exit mechanisms, and counterparty interest as the most important concerns influencing their ability to gain finality for runoff liabilities. This validates senior management's frequently cited frustration with the lack of progress in managing runoff claims and the limited available options to address legacy liabilities. Many owners of long-term runoff portfolios — for example, those containing asbestos exposures — believe they have no viable exit option for restructuring runoff business. Notably, 73% of respondents reported that their runoff is expected to take more than 10 years, suggesting that finality is a somewhat elusive goal that requires a long-term pursuit.

These findings highlight the need for more efficient and effective exit options for companies continuing to grapple with managing discontinued businesses. Currently, the most frequently utilized "exit solutions" include loss portfolio transfers (LPTs) and commutations.

> A full 88% of survey respondents reported having a strategic runoff plan in place.

While these may be effective options for certain blocks of business and parties, for others they do not provide the comprehensive exit solution most companies are seeking. A new development last year is the approval by Rhode Island of regulations providing for insurance business transfers (IBT), which offer both economic and legal certainty for the transferring company. While time will tell if companies decide to use the Rhode Island regulations to reach their goals the survey respondents as well as industry "buzz" indicate that there is great interest in the possibilities.

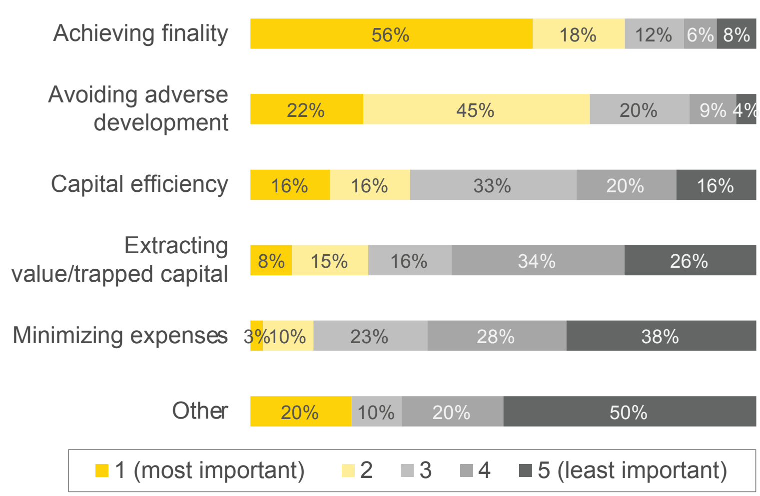
2. Restructuring is becoming more significant in the U.S. runoff market, and finality is the key driver influencing runoff restructuring activities.

Restructuring activity in runoff is becoming more significant in the US runoff market as there is a growing market to acquire runoff business. Worldwide, acquisitions of P&C runoff business have increased in the years since the financial crisis, especially from 2011 to 2013. The U.K. has been a core market for legacy acquisitions — no surprise given its favorable legal and regulatory environment. With the U.K. non-life runoff sector reaching maturity, legacy acquirers are reportedly looking to expand in the U.S., where the size of runoff portfolios is significant.* Notably, 52% of survey respondents reported total gross runoff reserves in excess of $1 billion.

* Swiss Re Sigma No.3/2015 M&A in insurance: start of a new wave?

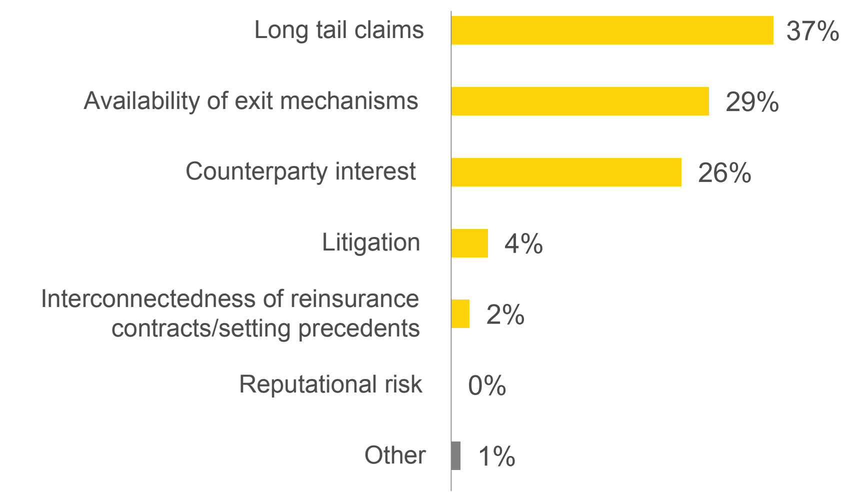
What are the key objectives of your or your client's organization's strategic run-off plan?

Please rank the top 5 objectives, with 1 being the most important.



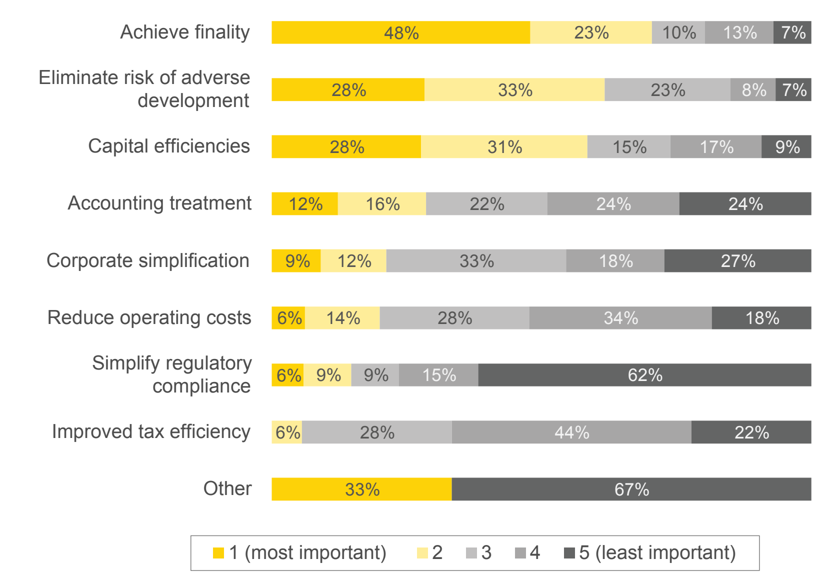
Numbers may not add due to rounding

In your opinion, what is the single most important concern influencing the ability to gain finality for run-off liabilities in the US?



What are the key drivers that influence or would influence your or your client's organization's run-off restructuring activities?

Please rank the drivers on a scale of 1 to 5, with 1 being the most important.



Numbers may not add due to rounding

Survey respondents also identified finality as the key influence in runoff restructuring activities, with elimination of the risk of adverse development and capital efficiencies also cited as key influencers. The interrelatedness of finality, adverse development risk, and capital efficiencies highlights that respondent organizations want to focus on core business and exit non-core lines. Companies appear willing to consider new tools and approaches to address the challenges of runoff; multiple respondents believe that Rhode Island's IBT regulation will be the single most significant development in the U.S. runoff market over the next three to five years.

Most respondents expect the amount of restructuring activity to remain roughly constant with the last three years, although a greater number of respondents expect an increase in restructuring activity than a decrease. Notably, many respondents (42%) have not restructured in the last three years. For those that have, the majority of deals average less than $50 million. These responses indicate a need for new restructuring tools in the runoff industry. Companies are looking for ways to restructure their runoff business to achieve finality and release excess capital.

Whether the entity is a small P&C company or an international insurance group, there is a continual need for effective restructuring tools to optimize capital deployment as well as to manage runoff liabilities. Historically, Berkshire Hathaway has dominated the market. Three of the larger insurer groups — representing 50% of losses incurred in 2013 from asbestos and environmental — engaged in large loss portfolio transfers with Berkshire Hathaway's National Indemnity.1 While larger insurance groups can afford to enter into these sophisticated reinsurance transactions, there are fewer options for many small and midsized insurance companies. The new Rhode Island runoff regulations may become a viable tool leading to more transactions among midsized and smaller firms.

3. Commutation remains an important part of the runoff toolkit.

Nearly three-quarters, or 72%, of survey respondents have considered an exit option, acknowledging that managing runoff business to expiration does not provide control over the timing of closure for the business with the result that liabilities remain on the balance sheet and capital is tied up rather than being redeployed to core areas or returned to shareholders.

Survey (continued)

Survey respondents report that the acceleration of runoff through commutation is the most common strategy for dealing with legacy business. A full 83% of respondents report considering commutation, with loss portfolio transfers cited by 76%. Commuting policies and contracts on an individual basis is a lengthy process, as confirmed by the overwhelming majority of respondents reporting that the expected duration of runoffs will exceed 10 years.

> A full 83% of respondents report considering commutation, with loss portfolio transfers cited by 76%.

Other exit options being considered are novation (50%), policy buyback (41%), sale (39%), and the Rhode Island IBT regulations (30%). Since finality is the primary objective of most runoff plans, the industry appears to be looking for alternatives to commutation and LPTs to achieve a more efficient and effective exit that provides finality. The survey results show hopefulness that the Rhode Island IBT regulations will provide an effective exit solution and will expand to other states.

4. Asbestos claims continue to plague the industry.

Respondents cited adverse loss experience as the most important challenge facing runoff businesses, with the overwhelming majority of respondents citing asbestos claims as the most frequent challenge to effective runoff. The survey responses indicate that the majority of runoff portfolios are reserved for asbestos claim exposures with the mean percentage of total reserves for asbestos claims at 41.6%. Respondents indicated environmental claims exposure would be another frequent challenge. It is clear that respondents expect asbestos and environmental liabilities to continue to strain capital going forward.

5. Future developments include ongoing focus on finality, asbestos concerns and IBT regulations.

Most survey respondents indicated that Cyber and CTE (head trauma) claims are most likely to create the next major exposure for the industry. Whether either of these exposures will rise to that of asbestos is uncertain, but clearly the industry is concerned.

> Companies appear ready and willing to consider new tools and approaches to address the challenges of runoff.

Many survey respondent identified Rhode Island's Regulation 68 providing for Insurance Business Transfers as the most significant development in the runoff market over the next three to five years. Given the stated importance of finality in runoff portfolios, the industry appears to be considering these new regulations as a means to reach their goals.

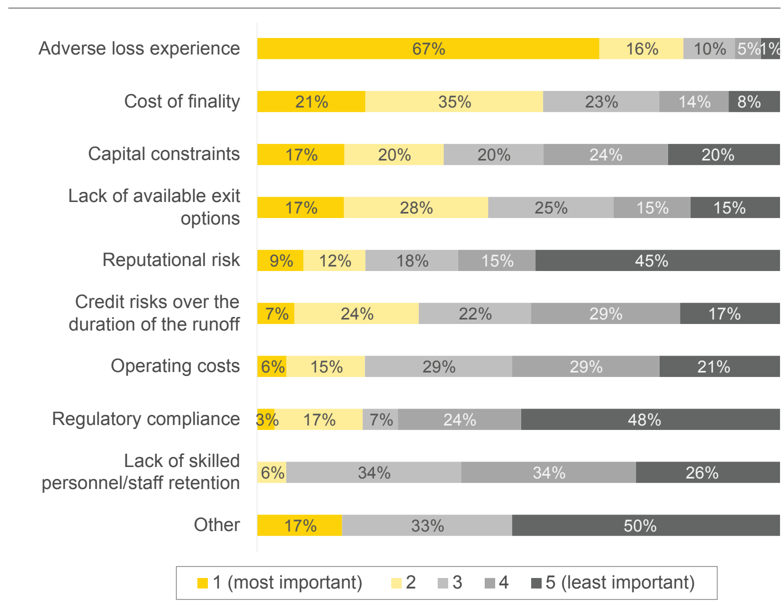
Conclusion

Finality is at the top of the agenda for insurers with runoff business. While many companies continue to use commutation and loss portfolio transfers as "exit" solutions for runoff business, these options alone do not provide the finality that most companies are seeking. Companies appear ready and willing to consider new tools and approaches to address the challenges of runoff.

Certainly, that's one reason many respondents expect Rhode Island's IBT regulation to be the single most significant development in the U.S. runoff market over the next three to five years. The future may prove to be an exciting time for runoff business in the U.S., with new restructuring tools enabling more efficient management of runoff business and focused solutions being applied to runoff liabilities. ●

Written by Luann Petrellis, EY Insurance Advisory Practice.Luann.petrellis@ey.com or lpetrellis@outlook.com

Please select the five most important challenges facing US insurers and reinsurers with run-off business with 1 being the most challenging.



Numbers may not add due to rounding

AIRROC Person of the Year 2016:

Bill Flaherty

Our process of writing a profile of the Person of the Year began, as it always begins, with an interview of our star, Bill Flaherty, and questions that lend themselves to a description of his career.

But the storyline of Bill's career is epitomized by the fact that this interview may be only the second time in his career he has been interviewed. The first was when he entered the job force as a CPA and auditor at KPMG Peat Marwick in 1979. Every role since then, producing a stellar career in the run-off industry, has been an evolution of his skills in applying the bedrock principles of auditing to capital management and implementing a broad-frame view for economic growth by leveraging run-off assets.

In 1990, he was lured away from KPMG by John Fitzpatrick, the CFO of Kemper, to join Kemper Corporation, becoming the head of internal audit. By 1993, his position had evolved into CFO of Kemper Reinsurance Company, a position he held until 2001. Kemper Re had been acquired by GE in 1998 and renamed GE Reinsurance Corporation. In 2001, Bill's role at the company changed to leading a new dedicated team responsible for commutations across the GE Insurance Solutions U.S. entities. When Swiss Re bought GE Insurance Solutions (GEIS), they broadened Bill's playing field by adopting the GEIS liability management structure. He is currently Senior Vice President, Head of Liability Management for the Americas. At Swiss Re, Bill is the leader of fifteen professionals responsible for portfolio management activities related to Swiss Re's legacy property-casualty reserves in the Americas.

Since 2001, Bill describes his own career as being one where "every deal is a new deal." That gives him the opportunity to utilize his financial skills and work across all the functions within his own company (underwriting, actuarial, claims, finance) to execute transaction for the mutual benefit of Swiss Re and its clients. He has immense respect for professionals in the run-off industry. He is grateful to have worked for organizations, GE and now Swiss Re, that understand and support proactive management of legacy portfolios. He also takes great pride in being instrumental in the development of a global dedicated team within Swiss Re that manages its inforce P&C reserves.

He views commutations as an efficient dispute resolution mechanism that allows the parties to resolve a dispute in a way that serves both sides' financial goals. This perspective may be why he has been responsible for the commutation of over $3 Billion in reserves over the last 10 years.

Bill Flaherty is currently Senior Vice President, Head of Liability Management for the Americas at Swiss Re.

Bill has supported AIRROC since its inception. He believes members get excellent value for their membership both from the education agenda and the networking/deal-making opportunities, and he believes this is particularly critical for bringing younger people into the business and growing their careers. He intends to advocate for the organization with a view of increasing membership by medium- and smaller-sized companies and he hopes AIRROC will strengthen its outreach in this area.

Finally, he credits his wonderful wife and three children for his success. They have supported and encouraged his career and they are a constant source of joy and pride.

The AIRROC Person of Year Award is sponsored by Butler Rubin, which has done so for the past 11 years. AIRROC is grateful for their ongoing support and this opportunity to pay tribute to leaders in the industry such as Bill Flaherty.

AIRROC Awards Trish Getty Scholarship

5th Annual Award Recipient Taylor Stack

AIRROC presented the Trish Getty Scholarship to a very deserving Temple University student this year. The 5th Annual award recipient is Taylor Stack, who is a Senior majoring in Risk Management and Insurance. In presenting the honor, Ed Gibney shared some remarks from the namesake of the scholarship, former Executive Director Trish Getty. Although she wasn't able to be there in person, Trish applauded Taylor for her accomplishments to date, and stated that she hoped to have the chance to meet her someday. Ms. Stack has a 3.8 GPA at Temple and is an active member of Gamma Iota Sigma, the fraternity for professional risk management, insurance and actuarial students. She has already gained real-world experience through her internship at Lockton Companies in New York during the summer of 2016, where she worked alongside associates, completing projects in seven different product lines including property, casualty, employee benefits, legal, and financial services. In addition to academic pursuits, Taylor has collaborated with administrators and fellow students to co-found a cooperative café on the Temple U campus, which garnered the team a national "Top Student Leadership Project" award. She also spent a semester abroad in Costa Rica. The $5,000 annual scholarship was established by the AIRROC Board of Directors in honor of Trish Getty, the founding Executive Director of AIRROC. It is awarded to a student studying Insurance, Risk Management, or Actuarial Science who is in need of financial aid for tuition. In accepting the award, Ms. Stack thanked the audience and explained how honored she was to have been chosen for this award and how vital this type of aid is to help in developing the next generation of talent for the insurance industry. ●

AIRROC Hosts Fundraiser

For the St. Baldrick's Foundation

As part of our "AIRROC Gives Back" initiative, AIRROC hosted a fundraiser for a worthy cause during the annual Commutations & Networking Forum at the Heldrich Hotel in New Brunswick, New Jersey. The event featured champagne and cupcakes and offered a way for attendees to take a brief respite from their afternoon meetings. For this annual outreach event, we chose to donate the proceeds to the St. Baldrick's Foundation to assist in their efforts to combat childhood cancer.

AIRROC delegates cumulatively donated $500 to the organization, and AIRROC matched what was collected. In total, a gift of $1,000 was sent to the foundation. Carolyn Fahey, Executive Director of AIRROC, said that hosting events like this is a way for "AIRROC and our members to take a few minutes to reflect on their successes and pay it forward to a worthy charity." St. Baldrick's works closely with leading pediatric oncologists to determine the most promising research to fund that will make the greatest impact for children with cancer.

The St. Baldrick's Foundation was chosen this year as its legacy lies in the reinsurance industry! After several businessmen came up with the idea in 1999, the annual reinsurance industry's St. Patrick's Day party, held at Jim Brady's pub in Manhattan in 2000, became the first St. Baldrick's event. The goal of shaving 17 heads and raising $17,000 turned into 19 bald heads and $104,000 donated to fund the research of the Children's Oncology Group. Since their start, St. Baldrick's volunteers have raised more than $200 million in research grant funding. "AIRROC was very pleased host this charitable event, and I personally am grateful to all who contributed," said Fahey.

To learn more about St. Baldrick's events and ways that you can help, please see their website: www.stbaldricks.org







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AIRROC's VISION is to be the most valued (re)insurance industry educator and network provider for issue resolution and creation of optimal exit strategies.

AIRROC's MISSION is to promote and represent the interests of entities with legacy business by improving industry standards and enhancing knowledge and communications within and outside of the (re) insurance industry.