MAINE INSURANCE GUARANTY ASSOCIATION

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Testimony to the Joint Standing

Health Coverage, Insurance and Financial Services Committee

in Opposition to LD 694

March 15, 2021

Senator Sanborn, Representative Tepler, and esteemed Members of the Committee, my name is Barbara Law, and I am the Executive Director of the Maine Insurance Guaranty Association ("MIGA"). This testimony in opposition to LD 694 is focused on the potential impact of the proposed legislation - if enacted - on MIGA's member insurers and certain current and potential future policyholders and claimants. I also seek to provide the Committee with information regarding the source of funding of business insurance and other claims in the event insurers with liabilities created by the proposed measure were to subsequently be ordered liquidated based upon finding of insolvency.

Created in 1970, MIGA is Maine's Property and Casualty insurance insolvency safety net – acting as the state-created payer of last resort to provide important protection to Maine policyholders and claimants from insurance insolvency losses. MIGA is part of a national system of statutory state Property and Casualty insurance guaranty funds and associations that collectively provide a safety net by discharging certain policy obligations of insolvent insurers.

Like similar organizations in other states, MIGA operates pursuant to its own authorizing statute, which specifically defines and limits MIGA's obligations and provides for funding essential to MIGA's protections. <u>See</u> 24-A MRSA § 4431, *et seq*. MIGA is an association whose members are all Property and Casualty insurers licensed to write insurance in Maine. In short, MIGA is funded in the first instance by assessments on those member insurers, as further explained below.

The state-based Property and Casualty insurance guaranty funds are a vital component of the insurance consumer protection framework, especially in volatile economic times. The operations and funding of the guaranty fund system are dedicated to supporting insurance consumers impacted by the failure of an insurer. Guaranty funds deal effectively with the time-sensitive needs of insurance consumers, and in doing so, help maintain public confidence in the insurance promise.

Property and Casualty guaranty funds were established with a specific purpose in mind: to provide timely compensation as defined by statute to policyholders and claimants if an insurance company becomes insolvent and is ordered into liquidation. The primary source of funding for the state guaranty funds is intended to be the assets of the company that failed. However, those assets are not available immediately because collecting them and administering all creditor claims against the estate is a complicated and multi-year process. State guaranty funds are constructed to avoid what can be the lengthy time-period between liquidation and recovery of the insolvent carrier's available assets, as well as address shortfalls that would leave covered claims otherwise unpaid.

The Property and Casualty guaranty fund system[1] has proven over many years of operation that it has the capacity to handle high volumes of claim payments. Guaranty funds step in upon the entry of an order of liquidation to provide timely payment to consumers who often have losses that need to be addressed immediately.

To date, COVID-19 has not affected the ongoing work of MIGA, nor of the guaranty fund system as a whole. Guaranty funds are fulfilling their mission to protect policyholders impacted by insolvencies, both prior to and during this period. This mission has been fulfilled over the course of the last 50 years. MIGA alone has paid approximately $201 Million in claims since inception, and has, in turn, recouped approximately $117 Million from the assets of insolvent insurers, with assessments of $82 Million largely making up the difference.

In recent years, insurance company insolvencies have been infrequent. Companies are conservatively managed, and their solvency is closely monitored by state insurance regulators. State regulators – especially Superintendent Cioppa and his staff - do a highly effective job using modern data-driven techniques and examinations of the company's books and records to intervene at the earliest signs of an insurer's financial impairment. Still, insolvencies do occur for various reasons, including the underpricing of insurance products or the recurrent payment of benefits that exceed the terms of coverage in the insurance contract. This is precisely why LD 694 raises concerns related to insurer insolvencies.

The additional insured losses potentially arising from LD 694, if enacted into law, would result in systemically and drastically underpriced commercial insurance business. APCIA projects that the proposed legislation would generate additional monthly business interruption losses in Maine between $400 Million on the low end to $1.7 Billion on the high end. These projected losses per month suggest a yearly total of billions of dollars of additional covered business interruption losses. Losses in this range would clearly far exceed the total amount of commercial premium collected during the corresponding period under Maine business policies which cover business interruption. Under the

[1] A separate system exists for life, health and annuity insurance products – the mechanism operates somewhat differently but the purpose is the same – protection of insurance consumers.

circumstances, it would be reasonable to anticipate that LD 694 could serve as a catalyst for insolvencies of multiple insurers that are otherwise financially sound.

Any insolvencies of insurers licensed in Maine, regardless of domicile state, would result in the cancellation of all the insurers' in-force policies[2] and trigger MIGA coverage, which provides its statutory coverage benefits upon such an event. MIGA then becomes responsible for all open and new (through the date of policy cancellation) covered claims arising under the Maine Property and Casualty policies of the insolvent insurer(s). Businesses located in Maine with an insolvent insurer and seeking to recover business interruption losses under the proposed legislation would consequently look to MIGA for payment. Thus, the financial impact of any insurers rendered insolvent by the proposed legislation would therefore shift in large part to MIGA's remaining member insurers and the insurance buying public.

This shift would occur because the liquidity needs associated with MIGA's insolvency protections are financed by assessments imposed upon premiums of solvent insurers writing insurance in Maine. As a practical matter, the assessment base will be reduced to the extent of the market share held by any insurers rendered insolvent by LD 694. This will result in remaining member insurers (including, as explained below, some that do not even write commercial or business interruption insurance) bearing a disproportionate share of statewide insurance losses. Moreover, MIGA's member insurers are specifically authorized to include these assessments as an element of premium rates in Maine. See 24-A MRSA § 4447. In this way, the costs of MIGA's insolvency protection are passed through to the insurance-buying public in Maine in the form of higher rates for their insurance.

It is important to underscore that a large cross-section of Maine policyholders ultimately would bear the additional cost of the business interruption and other claims of any insurers rendered insolvent by the proposed legislation. MIGA's assessment mechanism is structured with three separate accounts: "Auto," "Workers Compensation," and "Other." See 24-A MRSA §4436. Commercial business insurance falls under the "Other" account, which means that the cost of business interruption claims paid by MIGA would be assessed on all Maine premiums included in the "Other" account. Notably, in addition to commercial/business insurance premiums, the "Other" account also includes homeowners insurance and other personal insurance policies, such as personal liability umbrella policies. Thus, through the "Other" account, some of the business interruption insolvency costs driven by proposed legislation would be imposed upon Maine consumers, as well as on other business/commercial policyholders generally.

The provisions of LD 694, if enacted, would also directly threaten to undermine MIGA's foundational mission to promptly pay covered claims. MIGA's assessments are subject

[2] The extent to which market displacement, and/or affordability and accessibility issues, may emerge based on this act alone in Maine's personal and commercial insurance markets is beyond the scope of this testimony.

to a statutory cap of 2% applied on an annual basis. See 24-A MRSA §4436. While the exact extent of any insurer insolvencies that would be driven by the proposed legislation is difficult to foresee with any precision, inserting additional business interruption losses of even a fraction of the magnitude of the projected losses could drive MIGA's assessments in the 'Other' account up to the capped level. MIGA's 2020 assessment capacity in the "Other" account - its largest account - was slightly under $22 Million, which at that level would only be sufficient to cover a small percentage of additional losses projected by APCIA.

The consequence of covered losses exceeding the assessment cap would be multiple years of assessments persisting at the capped level. That level of ongoing assessment burden could impair MIGA's liquidity and delay its ability to fully pay claims to existing and prospective claimants – including a homeowner or injured party under a personal property or liability insurance claim – resulting in their claims not being fully paid when such obligations become due. MIGA's enabling statute provides direction in the event of such a shortfall but the proscribed remedy is to pay claims proportionally until sufficient assessments are made to pay the claims in full. If the effect of LD 694 on the industry is in the range as APCIA predicts, such overwhelming losses might mean MIGA could take many assessment years to "catch up" due to business interruption claims alone.

Finally, this testimony thus far has focused the discussion on the direct impact of the proposed legislation on the MIGA mechanism that provides protection against insolvent business interruption coverage. Most insurers, however, do not write just business interruption coverage, but write multiple lines of insurance. That means that if the proposed legislation were to drive multiple insurers insolvent due to the additional business interruption losses those insurers are forced to shoulder, their insolvency would also affect the other lines of insurance they write, most of which would be covered by MIGA. Accordingly, such business interruption-driven insolvencies could potentially impose substantial additional costs on Maine policyholders through higher assessments in the Auto and Workers Compensation accounts. The scope and amount of these additional costs would depend upon the lines of business written by an insolvent insurer and the depth to which the business interruption losses under the proposed legislation would drive the insurer into insolvency.

In closing, please let me stress that MIGA is a robust insolvency protection mechanism, well-designed to appropriately fund insurer insolvencies occurring in the ordinary course of events. This testimony is not intended to suggest or imply otherwise. MIGA has never failed to pay its covered claims for lack of capacity, nor does it come close to hitting its assessment limit under ordinary circumstances. On the other hand, as we respectfully suggest, the analysis set forth above demonstrates, MIGA was not designed to be a substantial funding source to reimburse policyholders for widespread business losses caused by a 100 Year Pandemic with community spread. We respectfully suggest it would be bad public policy with undesirable results to ask MIGA, albeit indirectly, to fulfill that role, but such a request is a probable consequence of the proposed legislation if enacted. MIGA therefore urges the Committee to vote Ought Not To Pass on LD 694.

Respectfully submitted,

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