SENATE COMMITTEE ON INSURANCE

Senator Susan Rubio, Chair
2021 - 2022 Regular

Bill No:	AB 2154	**Hearing Date:**	June 22, 2022
Author:	Cooley		
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Urgency:	No	**Fiscal:**	Yes
Consultant:	Erin Ryan		

SUBJECT: California Insurance Guarantee Association

DIGEST: Simplifies the California Insurance Guarantee Association's (CIGA) bonding authority and deletes a sunset on that authority; provides a statutory mechanism for use by CIGA to impose a surcharge on new licensees and existing licensees that begin writing a new line of business; and clarifies CIGA's obligation to cover cyber security insurance policy claims in the event of the insolvency of a company writing this type of insurance.

ANALYSIS:

Existing law:

1) Establishes CIGA to pay "covered claims" of insolvent member insurers up to $500,000 per claim for all insurance policies except workers' compensation claims, which are unlimited, as specified.

2) Requires each insurer admitted to transact insurance in this state in three specified classes of insurance, including workers' compensation, auto and homeowners, and all other property/casualty insurance, to participate in CIGA as a condition of doing business.

3) Requires CIGA to allocate levy assessments and claims payments and costs based on the three categories of insurance.

4) Defines "covered claims," and expressly limits CIGA's authority to make payments to only those claims that are specifically enumerated.

5) Authorizes CIGA to levy an assessment of up to 1% of direct written premium of insurers in each assessment category to pay covered claims.

6) Authorizes the California Department of Insurance (CDI) to issue bonds on behalf of CIGA to provide for rapid payment of covered claims that arise as a result of a natural disaster.

7) Creates the Insurance Assessment Bond Fund (IABF), and specifies that proceeds from the sale of bonds in #6 above and insurance assessments to repay those bonds are to be deposited in the IABF.

8) Authorizes CIGA to issue up to $1.5 billion in bonds through the Infrastructure and Economic Development Bank (IEDB) by January 1, 2026 to pay workers' compensation claims and efficiently manage its cash flow needs, as specified.

9) Establishes the Workers' Comp Bond Fund (WCBF), and specifies that proceeds from the sale of bonds in #8 above shall be deposited in that Fund.

10) Authorizes the CIGA board of directors to request the IEDB to issue bonds when it determines that the insolvency of one or more workers' comp insurers will result in covered claims in excess of CIGA's capacity to pay from current funds.

11) Allows CIGA to levy an assessment on workers' compensation insurers, based upon direct premium collected, for the purpose of paying off the bonds.

12) Requires member insurers to recoup the premium assessment charge through a surcharge on premiums charged for insurance policies in the year following the premium charge.

This bill:

1) Would repeal the provisions relating the issuance of bonds by the CDI to pay covered claims after a natural disaster.

2) Would authorize CIGA to ask the IEDB to issue bonds if it determines the insolvency of member insurers writing auto and homeowners' insurance and all other insurance will exceed CIGA's ability to pay covered claims from current funds.

3) Would authorize CIGA to levy an assessment on member insurers writing homeowners' and auto insurance and other insurance to pay the principal and interest on the bonds issued for that claims category, which would be recouped by insurers through a surcharge on applicable policies.

4) Would create the Homeowners' and Automobile Bond Fund and the Other Bond Fund into which the proceeds from the sale of bonds would be deposited.

5) Would specify that obligations under a policy issued to cover cyber security are covered claims, but limits CIGA's liability to $1,000,000 or the policy limits, whichever is less.

6) Would require an insurer to recoup the premium charge amount through a surcharge of premiums, even if a premium charge has not yet been paid to CIGA because the member insurer had no direct written premium for that category of insurance for the prior year.

7) Would require the CIGA board, whenever it requests the IEDB to issue bonds, to within 60 days of the request report to the Assembly Committee on Insurance and the Senate Committee on Insurance, and annually thereafter while bonds remain outstanding:

    a) The amount of the bonds requested;

b) The reason for the requested bonds;

c) Details of covered claims obligations requiring the issuance of bonds; and

d) Planned bond repayment assessments.

Background

According to the Author:

> AB 2154 allows the California Insurance Guarantee Association (CIGA) to have an efficient funding mechanism when responding to catastrophic events such as wildfires or insolvency in the insurance market. In particular, this bill streamlines the process by creating one set of procedures and creates a track record that will make such funding readily accessible and less costly. AB 2154 also sets forth a new member surcharge to address a potential gap in the CIGA statute to address and avoid unfair competition issues. Additionally, AB 2154 clarifies CIGA's obligation for cyber security insurance in the event of an insolvency of such coverage.

CIGA was created by legislation in 1969 as an association of insurers that makes payments to policyholders of property/casualty, workers' compensation and "miscellaneous" insurers when a member insurance company becomes insolvent and is unable to do so. It is a statutory entity that depends on the establishing legislation for its existence and for a definition of the scope of its powers, duties and protections. All states have an insurance guarantee association, and most, including CIGA, are based on the National Association of Insurance Commissioners Model Act of 1969.

CIGA is funded by premium surcharges upon applicable lines of insurance. CIGA issues no policies, collects no premiums, makes no profits, and assumes no contractual obligations to insureds. Generally speaking, CIGA accepts the assets and liabilities of companies and makes payments from the assets, earnings on investments, and assessments levied on member insurance companies. Since its inception, CIGA has never failed to pay a claim.

CIGA is unique as a regulated entity, even among California's hybrid state/private entities such as the California Earthquake Authority and the State Compensation Insurance Fund, because by statute it is actually established by insurance companies as an involuntary association as a condition of those companies transacting insurance business in California. The purpose of CIGA is to pay "covered claims" of member companies that have failed. CIGA's total liability for any single claim is $500,000, other than claims for workers' compensation, which are not limited. CIGA does not have to pay a claim if other insurance is available to pay the claim.

CIGA maintains three separate funds that guarantee different lines of insurance: property/casualty, workers' compensation, and "other." The funds are assessed and maintained separately, with an assessment on property/casualty insurance providing the resources to pay claims of insolvent property/casualty insurers and assessments on workers' compensation insurance providing the resources to pay claims of insolvent workers' compensation claims. CIGA only levies the assessment to cover its claims and costs, and so has not always levied the maximum allowable assessment. If one of the funds is under-funded, CIGA can levy an additional assessment up to the maximum to replenish it. CIGA also relies on distributions from insolvent estates and investment income. The Conservation and Liquidation Office of the CDI actually controls and liquidates the insolvent insurers' estates, and determines when or if CIGA receives any distributions from the estate. CIGA cannot count on any such proceeds until actually received. Estate recoveries usually occur many years after CIGA has paid claimants and often represent only a fraction of what it has paid for the covered claims. The rest is paid by assessments on member insurers.

As a result of a crisis in the workers' compensation market in the late 1990s and early 2000s and the insolvency of 27 workers' compensation insurers, most of CIGA's claims volume have been workers' compensation claims—claims that have no cap. Workers' compensation is a "long tail" line, meaning the ultimate payment on individual claims is not known for a long time after the policy is issued, possibly decades. Injured workers have a right to up to lifetime medical benefits to remediate a workplace related injury. Some workers with severe injuries may be entitled to a lifetime pension. CIGA did issue bonds to pay workers' compensation claims after the wave of insolvencies, but does not currently have any outstanding bonds for this purpose.

CIGA to date has never had to request CDI to issue bonds to pay natural disaster claims. At the same time, although insolvencies among property/casualty insurers are rare, increasing wildfire losses, climate change, and the ever-present earthquake threat could change that quickly and lead to the need for CIGA to respond quickly to pay covered claims of insurers other than the workers' compensation category.

Last year, the Legislature approved yet another extension of CIGA's workers' compensation bonding authority to 2026. There is no sunset date on the natural disaster bonding authority. This bill seeks to streamline and consolidate CIGA's bonding authority into one bond issuer—the IEDB, while maintaining the separate issuance and repayment mechanisms for the three separate categories of insurance covered by CIGA, and eliminates the need for periodic legislative review of the sunset.

CIGA currently has no authority to require new insurers or insurers writing a new line of business to collect a bond repayment assessment in its first year of writing coverage in one of the three categories because the assessment amount is based on the previous year's written premium. According to CIGA, this creates an unfair competition issue because the new insurer, by not having to include the surcharge in its premiums, has a competitive price advantage over established insurers in that line of business. This bill would require new insurers and those writing in a new line of business to collect the relevant assessment on its policies and remit within 60 days of the end of the calendar year.

Cyber insurance is a relatively new line of insurance, and current statutes are silent on the issue of whether the insolvency of an insurer writing such policies would be considered covered claims for purposes of CIGA. In addition, it is not clear in which category cyber insurance would fall. CIGA notes this is not a problem unique to California, and believes clarification is needed to remove any ambiguities as to coverage and the amount of the coverage cap. This bill expressly adds cyber insurance as a defined covered claim, includes it in the “other” category of claims, and sets a maximum cap of $1 million for any claim, up to the policy limits.

Related/Prior Legislation

AB 1541 (Committee on Insurance, Chapter 305, Statutes of 2021) extended for three years CIGA’s authority to issue bonds not to exceed $1.5 Billion in order to cover workers compensation claims obligations

AB 822 (Cooley, Chapter 85, Statutes of 2015) provided that the laws governing CIGA do not require a final determination of a claim in an insolvent insurer’s liquidation proceeding before a covered claim may be submitted to CIGA.

AB 2710 (Cooley, Chapter 137, Statutes of 2016) simplified the methodology used by CIGA to calculate assessments on member insurers.

ARGUMENT IN SUPPORT:

CIGA writes in favor of the three changes as follows:

> (1) CIGA Bonding Authority. CIGA believes it would be more efficient going forward to combine these two provisions into one. They both have the same end goal (i.e., provide funds to CIGA to pay covered claims) but they go about it in very different ways. Since CIGA has a track record for issuing workers compensation bonds, CIGA believes it makes sense to fold the natural disaster bonds into the sections that deal with the workers’ compensation bonds. With this change, in the future when CIGA needs bridge funding for any purpose, it has one statute, one set of procedures and a track record that should make such funding relatively quick and less costly.
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> (2) Cyber Coverage by CIGA. CIGA believes that if a carrier were to go insolvent that wrote cyber policies there would be a question as to whether such policies would be considered covered claims as the current statutes read. In addition, there are issues as to whether the benefits provided under such policies are even insurance, as often future credit monitoring for customers whose personal information has been breached is one measure of damages. Under current law, CIGA covers specific lines of insurance identified in Section 1063. It is not clear which line, if any, cyber insurance claims would fall. Finally, it is not clear how CIGA's $500,000 cap per covered claim would apply in such situations. This is not just a California problem. All guaranty associations are facing similar issues. CIGA believes clarification in California is needed to remove any ambiguities as to coverage and the cap.
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> (3) New Member Surcharge. There is a potential gap in the CIGA statutes that should be addressed out of concerns for fairness when CIGA access its member insurers in respond to an insurer insolvency. When a company becomes licensed to write business in California and it writes a line of business where a surcharge is being applied in its first and second year of

writing, that company should be collecting a surcharge even though it had not received an assessment from CIGA. The new company would not have received an assessment from CIGA because the assessment is based on the previous year's writings which in the case of a new insurer there were none. The surcharge needs to be collected anyway to avoid an unfair competition issue. Any surcharges collected needs to be remitted to CIGA to be used to pay future insolvencies. CIGA proposes the statute be amended to make it clear that any new company in California must collect a surcharge (assuming a surcharge has been approved by CIGA) for this first two years of business and remit such surcharges collected to CIGA.

SUPPORT:

California Insurance Guarantee Association (Sponsor)

OPPOSITION:

None received

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