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Insurance Company Failures of the Early 1990s—Have We Learned Anything?

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Summary: The early 1990s saw the failure of three major life insurance companies in North America—Executive Life, Mutual Benefit, and Confederation Life.

The panel looks back at the settlements of these insolvencies and how different policyholders fared. Changes in the insurance industry, credit analysis, and marketplace resulting from these failures are discussed. The panel also represents the changes in regulation designed to prevent or lessen the impact of future insolvencies and tries to assess the likelihood of a major failure in the future.

Mr. Victor Modugno: I hope that by the end of this session you will answer the question, Have we learned anything?, in the affirmative. I am currently employed by Transamerica. From 1986 to 1990 I was employed by Executive Life, and I have first-hand experience in one of the failures we will be talking about. I wrote a book on that. A condensed version of the book was made into a study note for the SOA.

We have assembled an outstanding panel. We have a representative of a rating agency, a state regulator, and a guaranteed investment contract (GIC) purchaser.

Our first speaker is Murray Becker. Murray retired at the end of last year after a long and distinguished career in what is now called stable value investments, formerly referred to as GICs. We were very fortunate to get Murray to come out of retirement

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to be on this panel. He had client's money invested in all three of the failures we will be discussing. He played a key role in the rehabilitation plan for Mutual Benefit.

Murray is the former president of Becker & Rooney, a consulting and investment management firm that specialized in stable value investments. He is considered the founder of the GIC service business, having developed a specialty practice in this area, beginning in 1972. He is a graduate of the Wharton School with a degree in management. He began his career at MONY, where he advanced to director of group pensions. He is a former vice president of Johnson & Higgins, a former partner of Kwasha Lipton, and a former vice president of J.P. Morgan Investment Management.

Mr. Becker is a Fellow of the Society of Actuaries and has served as President of the Actuarial Society of Greater New York. He has also served on the SOA's Committee on Pensions and on its Education & Examination Committee. He is currently a member of the Actuarial Advisory Committee of the New York City Retirement Systems. Mr. Becker is the recipient of the Pension World Advisor of the Year Award for 1986 and was voted 1996 Most Respected GIC/Stable Value Professional by the Investment Management Institute.

Murray will give an overview of the three failures: Executive, Mutual Benefit, and Confederation. He will discuss the outcome for GIC policyholders and changes in the stable value business.

Out next speaker is John F. Gies, Chief Life/Health Actuary of the Connecticut Insurance Department. Jack Gies joined the Connecticut Insurance Department in 1992. He directs the life/health actuarial valuation function for the department and supervises activities of consultants and staff providing actuarial analysis and examination services. He is also a member of the Life and Health Actuarial Task Force of the NAIC, as well as several NAIC and American Academy of Actuaries working groups. Before joining the department, Mr. Gies was vice president and actuary with Connecticut Mutual Life Insurance Company where he managed apportionment of earnings for participating policyowners. Mr. Gies is a Fellow of the SOA who has spoken at several SOA meetings and seminars. Jack will discuss what regulatory changes took place after these failures.

Keven W. Maloney is a vice president and-senior analyst in the Finance, Securities and Insurance Group at Moody's Investors Service. He joined the firm in December 1996 and currently concentrates on the credit ratings of U.S. life insurance companies. Prior to joining Moody's, Keven was vice president and director of

research at Fiduciary Capital Management. He began his career with Wright Investors' Service as an equity analyst.

Keven received a B.A. from Manhattanville College and earned an M.B.A. from Fordham University. Keven will give the rating agency point of view of changes following these failures

Our first speaker is Murray Becker.

Mr. Murray L. Becker I'm going to give a brief description of each of the three defaults. I'm going to discuss what the issues were in terms of rehabilitating or liquidating the insurance company. I'm going to then discuss, in each case, the issues affecting GIC policyholders, and what the financial outcomes were. After doing that for each of the three companies, I'm going to talk about the impact of the three insolvencies on what is now called the stable value business.

I'm not going to discuss the outcome for individual policyholders, which is outside of my area of specialization. In general, individual policyholders came out OK in all three cases because of state guarantee coverage.

As background, I just want to talk a little bit about GIC funds or stable value funds. A GIC fund is nothing more than a fund that has a collection of individual GIC contracts put together in a portfolio. Each contract has its own crediting rate, and the participant gets what appears to be a guarantee of principal and rate of return, which is the weighted average interest rate of all the individual contract holdings. A stable value fund is more general and has synthetic GIC contracts as well as real GIC contracts. Synthetics are contracts in which you have a bond investment or a series of bond investments or a portfolio of bonds in which a third party guarantees principal and interest. The investment performance of the underlying bonds that are either actively managed or held to maturity are used to produce the same kind of investment return that the participants expect, which is a fixed interest rate over an interval of time.

Prior to the Executive Life Insurance Company (ELIC) default there was no such thing as a stable value fund and all GIC funds presupposed that there never would be a default. The problems that would be created by default were more or less unthinkable. Everyone took the view that if you had a default, you would defeat the fundamental premise of a GIC fund which was that principal would be guaranteed, and only the rate of return would vary over time.

No one ever thought GIC defaults could occur. It's hard to imagine that people could think that way today. No one thought that the leading insurance companies

that were carrying AAA ratings could default in a short period of time. Most GICs were for five years or less, so who could imagine that a AAA investment could be not only downgraded but go into insolvency within the five years of the time frame.

Looking back now it's quite clear that a default in 100% of a GIC fund is not automatically going to be a problem. It boils down to what percentage of the fund is invested in the defaulted contract. If the percentage is low enough, then the financial magnitude of the loss is not too great. Then all you need is some kind of technique that every actuary would be familiar with to convert the loss of principal into an equivalent lower interest rate and somehow or another find a way to credit the lower interest rate to amortize the default over a period of time so that at the participant level, there would be no loss of principal. There would only be a lower interest rate and you wouldn't have a nightmare. You would simply have, like any other investment, slight disappointment in the return of the investment.

That's clear now; it wasn't clear then. Executive Life was seized by the California insurance department in April 1991. The single most important cause was excessive exposure to junk bonds. The amount of junk bonds was well beyond any reasonable level at a time when the junk bond market was going into, for a variety of reasons, a total state of collapse. There were also financial reinsurance treaties that allowed reinsurers off the hook in the event there would be a claim. And what's common in all of these defaults was insufficient capital to support the risk that the insurance company was taking.

In the case of Executive Life, one of the first things that happened was a GIC policyholder group formed. One of the initial issues was whether a GIC, in which there is really nothing that you would call insurance, would be given policyholder priority in an insolvent insurer. So the policyholder group—to emphasize the policyholder status—called itself the Group Annuity Policyholder's Protective Association (GAPPA). Membership in this group was limited to plan sponsors almost exclusively, but not quite entirely. Essentially it was a plan sponsor group. Consultants in the business who were experts were precluded from membership because some of the plan sponsors thought that there might be a conflict of interest. Consultants in this business want a thriving guaranteed investment contract marketplace. They would be more interested in saving their business than saving the participants. That's exactly what happened regardless of whether that argument has any merit or not. I personally avoided all the work and aggravation that comes from having to deal with the issues that affect the policyholder, but we were able to follow it from the sideline.

One of the other characteristics here is that at the moment of default, no one had the foggiest notion of what the recovery value of an Executive Life contract would

be. If I had to pick a number out of the air, I would have guessed about 70% of your money, but I didn't have any basis for that. That was just a guess. It turned out that that would have been an accurate guess, but I would have said that it was somewhere between 50%, and maybe 80%, but no one knew. You had offers for Executive Life contracts, at maybe 25¢ or 30¢ on the dollar. You were a fool if you took it.

The question you have as a plan sponsor or as an advisor to plan sponsors in such circumstances is: what do you do with participant entitlements in a defined contribution plan? GICs are used almost exclusively in savings plans or profit sharing plans where participants have an account balance. There was nothing in the law or in the plan that permitted you to do this. However, what appeared to be the only sensible solution would be to freeze the Executive Life holdings and create two accounts for each participant—one a frozen account owning an interest for whatever it was worth in Executive Life and another account representing all the other GICs in the fund. When a participant terminated, retired, made a loan, or was otherwise entitled to withdraw money from the plan, the participant could only withdraw money from the non-Executive Life part of the plan. This had the advantage of not having had any value placed on the Executive Life contract. In general, there were no legal problems created by the fact that nothing in ERISA permits you to do this and nothing in the plan gave the plan sponsor authority to do this. You can probably justify it on the grounds that the fiduciary for the plan is subject to a higher calling that transcends both the law and the plan document, but in any case, that's what was done.

Now, this was in April 1991. By May 1991, it was quite clear that when you did this, there were two serious side effects. One is that the participant thought every nickel that was in Executive Life was gone and they would never see it and there was not a whole lot the employer could do about it because the employer couldn't even guess at what the recovery value would be. Second, until Executive Life was liquidated in full, no matter how many years that would take, the participant would not be able to get their money out of the plan, so it was like an ongoing hardship that would last well beyond the time frame of the actual default.

The lesson that could be used in other defaults is to find some other way to do it other than freeze the contract. To wrap up the Executive Life situation, there was a big conflict because Executive Life had also issued municipal GICs, called muni-GICs, for municipal bonds. These were issued to municipalities for investment of proceeds of taxable municipal bond issues. All GICs from Executive Life had annuity provisions in them. In a savings plan there's always some hope that a participant might some day elect an annuity, but I've never seen one. It could happen. In the muni-GICs, there was no participant to elect a GIC. Naturally the

GAPPA group wanted to have policyholder status and deprive the muni-GICs from the same status thereby giving the GIC and other policyholders a much larger percentage of the assets. The muni-GICs won that battle in court. In other words they got *pari passu* treatment. All GICs were considered policies and got the same status as any other kind of policy.

The outcome was that Executive Life was acquired by European insurers and became Aurora National. In March 1994, almost three years after the default, there was a substantial cash distribution, but not all of it. The total value at that time was roughly 86% of the account balance at the time of default. There was no interest over that interval. If you worked backwards to the present value of the recovery in relation to what would have happened if you got paid in full, it was roughly 70¢ on the dollar. So my original guess was pretty accurate. The participants, of course, all thought they got more since nobody knew how to take into account the loss of interest.

I'm now going to move on to the Mutual Benefit case that occurred in July 1991. Anybody who paid attention to ELIC knew what not to do. The primary cause of default in Mutual Benefit's case was excessive investment in commercial mortgages and real estate in an environment of a weakening economy, corporate downsizing, empty office spaces, and all the other things with which you're probably familiar. It was exacerbated by a lack of diversification. Mutual Benefit had four jumbo real estate investments and all four went sour. Of course, the capital ratio was insufficient to support the risks on the assets side.

To compound the problem there was almost a total lack of liquidity so that a run on the bank, which was emerging in 1991, triggered by Executive Life, would have driven the company in the ground. It was just a matter of time, so the New Jersey department took it over. A policyholder group was formed. This time it more or less included everybody who was willing to volunteer to put in time to represent policyholders. The group was called the Association of Mutual Benefit Life Insurance Contractholders (AMBLIC). I was on the steering committee of this group. There were two major constituencies. Both were group pension policyholders. One was all the GIC business that Mutual Benefit wrote and the second was all the 403(b) business that Mutual Benefit wrote. Together they united, even though they had, in some cases, divergent interests. The GIC side had all kinds of professional expertise. The 403(b) side had tremendous public sympathy because you had tens of thousands of hospital workers and teachers with 403(b) contracts. Fortunately, the hospital workers were in New Jersey where political influence mattered the most.

Another difference in the Mutual Benefit case, is it was almost certain that the insurance industry would put together some kind of bail-out package that would have the effect of converting the losses into lower interest rates as I described earlier. This was accomplished through the mechanism of putting everything that wasn't guaranteed by state guarantee funds, which was 80–85% of the GICS, and a proportionate amount of assets into a separate account guaranteed by a consortium of insurance companies. The remaining general account contracts had the implicit backing of the state guarantee funds. There was a strong guarantee package put together for everything in the general account. There was a weak guarantee package, guaranteeing mainly principal and not too much interest, but you would get whatever the asset delivered and it was put in the separate account side. You had these two parallel plans going. It all depended on the same assets, but one was strongly guaranteed with limited upside potential. The other was weakly guaranteed with more upside and more downside potential.

The primary insolvency issue here was different. Unfortunately the New Jersey law didn't give policyholders priority over general creditors and Mutual Benefit had a lot of general creditors. As a result of that, New Jersey passed a law and gave the commissioner authority to apply it retroactively to cover the Mutual Benefit case, if, in the judgment of the insurance commissioner, the interest of the public warranted that that be done. That was controversial and sounds like it ought to be unconstitutional to a non-lawyer like me, but in fact, there were a lot of precedents in the law where such things can be done, so that was an issue that was litigated. The judge sided with the policyholders and upheld the law as being constitutional giving policyholders priority on the assets. He did give the stock of the emerging company, the new Mutual Benefit, which is called MBL Life Insurance and Annuity Company, to the creditors who otherwise would have gotten nothing.

The outcome turned out to be surprisingly good. The general account contracts with a strong guarantee package got all their money back and a 5.21% interest rate over a period of time that will end this year. The default occurred in 1991, so they got 5.21% during the eight years from mid-1991 to mid-1999. The separate account policyholders, who everybody thought would do worse because the assets were so poor, got 6.21% over that period of time. Given where interest rates are today that wasn't such a bad outcome either. Mutual Benefit has been acquired by Sun Life, which in turn has been acquired by AIG and that ties it up.

Confederation Life was seized in August of 1994. This was a very unusual situation. You had cross-border issues. Michigan was the state of entry in the U.S. for Confederation Life. Under Michigan law a trust is to be maintained with assets sufficient to meet U.S. liabilities, so it's collateralized. U.S. policyholders have first claim on the trust assets as well as a residual claim on the general account of the

Canadian company. Unfortunately, in violation of Michigan law, the trustee accepted assets that were IOUs from a subsidiary of Confederation Life in lieu of real assets in the Michigan Trust, so there was a hole in the Michigan Trust.

Without getting into all the gory details, the structure was very weak to protect policyholders. You didn't even have a policyholder claim for the missing assets because the entity that owed it to you was a subsidiary of Confederation Life, which was not an insurance company and therefore you were a general creditor of the subsidiary.

In the end, through this liquidation, all the GIC policyholders will have gotten what's defined in the plan as full recovery. This would be 100% of the interest guarantee through the time the GIC contract would have matured and then 5% interest thereafter. That's defined as full recovery. In some cases, plans with guarantee fund coverage will do better than that.

I want to just wrap up with the effect on the GIC/stable value marketplace. There are a lot of negative effects, especially if you view it from the interests of insurance companies. First, the plan sponsor community no longer views even the leading credits in the life insurance industry as utterly safe havens. Second, a large number of plans sponsors abandoned the whole notion of GIC funds or stable value fund; instead they'd rather have bonds or money market funds or both, which seem to be the worst of all worlds, but at least they're not promising something that can't be delivered.

From the viewpoint of the insurance industry exclusively, it has lost its monopoly and has to compete for business against the notion of synthetic GICs. There are some plan sponsors that have gone to 100% non-GIC stable value funds. In other words, everything is synthetic. And from the point of view of intermediaries in the business, who in this day and age control most of the stable value business, there is a widespread belief that the insurance industry doesn't stand behind its products. If I had time, I could tell you why.

There are some positive effects. The principal of diversification has been reaffirmed. If you have a default, it's very easy now to make sure that you have continuity of the principal guarantee even through a default. If you have a small loss, it converts into a modest reduction in interest credited. That's all there is and no aggravation.

The plan sponsors love synthetic GICs, particularly in the large companies where they've gotten a better product. Intermediaries who are in the business like it too. The ability to live through a default without aggravation has been established,

although there are a lot of plan sponsors who don't understand that. If they did, they might reconsider their view on GICs.

And finally, credit worthiness has now been established as something you must pay attention to and so you have a sounder way of looking at guarantee products than we had in the past.

Mr. John F. Gies: Murray's presentation is about as detailed as you can get with regard to these companies. My perspective—the regulatory perspective—is a little bit different. For one thing, we're dealing with a whole array of companies, and different businesses. In Connecticut we have 130 domiciled companies, so as a regulator you're looking at life insurance companies, annuity companies, combination companies, and group pension companies. Identifying riskiness and identifying insolvent companies is like flying a plane. Usually, this regulatory job is unremitting boredom with moments of extreme panic. The hope is that the financial statements would give us early warning of insolvencies. They don't always for a number of reasons and I'll try to develop that theme during my presentation.

I'll provide a definition so that some subsequent statistics have some meaning. An impaired company is any action involving any number of activities: receivership, conservatorship, cease and desist order of suspension, license revocation, and administrative order. There are a number of regulatory actions that would constitute an impairment that supports these statistics. There are guarantee fund assessment data. I include them only to give you a sense or a perspective on the amount of insolvency under our current regulatory framework.

The data that were available to me included a 10-year period of time on the life and health companies. There were $5.8 billion of life and health guarantee fund assessments in the period covering 1988–97, and for the property and casualty (P&C) industry, $6.5 billion. Executive Life was a lot more expensive to the guarantee funds ($2.3 billion) than Confederation Life ($0.2 billion) and Mutual Benefit ($0.1 billion) due to the manner in which the insolvency was handled. Executive Life, of course, involved the liquidation of assets and the incurring of losses, which were then supported by the guarantee funds. The other two entities were managed more on a going concern basis. They were held and the assets had a period of time to recover and the guarantee funds escaped some significant cost there, but nevertheless, it seems to me that on the life and health side, we had 113 companies involved in that $5.8 billion of guaranteed fund assessment.

So we asked the question, why do insolvencies happen? I would characterize these as symptoms and not sources. The familiar litany of inadequate pricing and surplus

growth, affiliate problems, and misstated assets are the most common. Fraud and reinsurance are mentioned every once in a while.

Other surveys have been done. The historical data seem to indicate that small companies tend to comprise most of the insolvencies and newer companies tend to comprise most of the impairments. Another characteristic is unusual growth. Health companies are more risky than annuity companies or life companies, but that's generally anecdotal.

As to why insolvencies or impairments happen, I would focus on poor risk management. These are familiar items to most of you. Underwriting cycles, investment-related businesses and risky assets, and policyholder and contractholder put options create a risk and, of course, there's management capacity. The underwriting cycles, the GIC cash-flow underwriting, the underpricing of products, (most recently in the property and casualty industry with its workers' compensation market) result in too competitive pricing. We've had periods where individual disability income, with the guarantees that were provided, has created risk. I think even in the triple X term insurance market there's real competition in pricing. It's a commodity. If your prices are not the best, you're not getting the business, and all of this is putting stress on the products and on the companies. Now we have variable annuities with all kinds of guarantees being added in order to attract market share. They, of course, create risks that are often not reflected in the balance sheet.

Investment related businesses, large case pension markets, equity-indexed annuities, and interest-sensitive products are very close to the banking industry and create risk. What has the NAIC done? First of all, we have to talk about the scope and range of our minimum financial standards. Clearly the annual statement filing is very complete. Some would say it has too much information. It needs to be revised to be made more meaningful. Every state has minimum capital requirements. We talked about risky assets. We have an asset valuation reserve (AVR) and an interest maintenance reserve (IMR). We have a risk-based capital mechanism to identify the riskiness of assets. Let's not forget the prescriptive liability valuation that presumably incorporates so-called conservatism on the liability side of the balance sheet. Codification is attempting to make our rules uniform and more consistent. We have the actuarial opinion, which is a very interesting development, and I think very helpful in this whole regard.

We have developed model regulations dealing with surplus relief, and we tried to close those loopholes so that the balance sheets are in fact truly stated, perhaps not misleading, but truly stated. The NAIC has developed an accreditation review, which has done a marvelous job in terms of firming up the state insurance departments in the work that they do in supervising and overseeing the business.

Then there are the guarantee association mandates. So we have a whole array of overlapping standards addressed to appropriate financial reporting and deal with troubled companies.

I would identify three as key NAIC efforts. The Holding Company Act is very important in dealing with affiliates: disclosure, disclosure, disclosure. Let's understand what companies are doing when they perform these cross-company transactions.

The accreditation program under frequency and quality of the examinations. This is a risk-based assessment process and more and more insurance departments are being asked to perform a risk-based analysis as opposed to a pro forma balance sheet. The actuaries have a very important role to play in that aspect. Finally, there is risk-based capital (RBC) and the actuarial opinion. Here I'm thinking in terms of an integrated approach to identifying the capacity of companies to satisfy their obligations.

So in summary, what is the cause of impairments? Obviously, it seems that this is a chicken-and-egg question. Which comes first? Basically it's a confluence of adverse events. The common threads in these adverse events are poor management practice, i.e., unidentified risk or misunderstanding of risk. It's usually characterized by fast growth and aggressive pricing. It's often driven by competition and the reach for market share. It's often accompanied by ignorance, fraud, or deception on the part of management. The result is misstated balance sheets, delayed recognition, delayed corrective action, and obviously the existence of inadequate reserves.

Now for the remedies. You won't hear this from regulators often, but it's a remedy that's increasingly taking hold. It's not a question of mandated risk avoidance or prescribed practices. I think it's more nearly a question of appropriate risk identification, quantification, transparent financial reports, and disclosure. At the core, this is an asset/liability management issue. It has short-term and long-term aspects.

Clearly there are limits to the expertise and knowledge base of actuarial professionals and companies fail for reasons other than things and topics that actuaries are expert at. I think we ought to consider the role of the actuarial opinion and analysis in addressing these insolvency issues. In particular, the newest emerging development is the unified valuation system (UVS). It's an American Academy of Actuaries project. It places greater emphasis and importance on the role of the actuary in providing expert opinion. It's an integrated opinion. The UVS embraces an integrated asset adequacy analysis that recognizes, for example,

remote contingency high-benefit cost risk that the current system captures only sporadically. I'm thinking of variable annuities with guarantees, possibly long-term-care contracts, or any number of areas where the current financial system strains to capture the risk and to put it on the balance sheet. The UVS system is not a point-in-time measurement. It's dynamic. It asks for five-year projections on various scenarios. It deals with this concept of degree of confidence. Can we say that our reserves represent an 80–85% confidence level, and can we then talk about the assets in addition to reserves? It is that part of surplus, which is in fact working capital, which provides 95–97% confidence? Can we begin to quantify, using stochastic models, the riskiness in our asset/liability mix?

The UVS embraces the U.S. penchant for markets, which are prudently free of regulatory barriers, but are moderated by identification and exposure of unhedged risk. That's fairly unique. If you look to Canada or if you look to the U.K., you'll find a different regulatory system where the regulator has much more power to intervene and to get at management. The U.S. is more of a capital-based market and in our country you have the freedom to succeed or to fail. That's the way we've run our businesses. This represents a real paradigm shift. It's built and very much dependent upon an independent review and strengthened actuarial standards of practice. As you can imagine, the actuary would be very important to this.

Mr. Keven Maloney: We did a study on insolvency. Any company can default. In Moody's database we have upwards of 100 years of data on company failures. The oldest failure occurred in 1937. It was a subsidiary of a railroad company, but real failures didn't really come about en masse until the 1970s and 1980s. It has been smaller companies, with under $100 million in assets, that really don't have the capabilities to manage a company. They don't have the employees or the sophistication of larger companies. And that's true across all industries, not just insurance.

We can look at insurance company defaults versus bond defaults over a 10-year period using 1989 as a start date. We take the top 400 insurance companies in the U.S. and measure them over a 10-year period of time comparing their default rate against other failures in Moody's database: investment grade or noninvestment grade. It shows a very good picture for the insurance industry—there is very low frequency of default.

What if we were to take the top 400 companies in each year and simply measure year intervals. It's not cumulative like the defaults. It has more peaks and valleys. It shows that the insurance industry followed the same trend of the economy, and it isn't too hard to imagine that that would be the case. Defaults have definitely

leveled off. The last major one was in 1997. There was a peak or turn-up in 1998 with the all-corporate category, which has to do with the problems in Asia.

We can discuss estimated default values of GICs and bonds. For bonds, Moody's uses the market price 30 days after a default as a measure of the ultimate recovery value of a bond. For the three major defaults of the 1990s, we used the discounted present value using accrediting value or simulation of that accrediting value as a discount factor. So it's a little bit like apples and oranges, but it's probably the best that anybody is going to come up with and it paints a pretty good story. Both Mutual Benefit and Confederation Life paid or are going to pay about 89–90¢ on a dollar. Executive Life was much less at 68¢ on a dollar. You can compare that against what bondholders received. Mutual Benefit bondholders probably received about 50¢ on a dollar and on our discounted present value base, this is about 30¢. For Confederation Life, it was about the same. For the Euro bond notes, which were outstanding, there is about 30¢ on a dollar on discounted present value bases. The worst case scenario is First Capital. It paid six cents on a dollar, which on a discounted present value base is about three cents. They even liquidated a BMW as part of the settlement. There obviously weren't a lot of assets left.

Three out of the four rated insurance companies that defaulted were not rated investment grade at least a year before they defaulted by Moody's, so those weren't a surprise. Executive Life had been downgraded into the B category and into the B category months before it defaulted, and those ratings show a high level of default. B would expect a 25% default rate over say a five- or six-year period. B would be 40%, so it was sort of expected.

First Capital, which was another major default was always noninvestment grade. Southwestern Life was always a noninvestment credit. The fourth was a surprise. I should take a step back. We didn't rate Confederation Life. We had discussions with management, but there was never a formal rating. If we did rate it, it wouldn't have been high. It would have been much different than the other rating agencies.

The fourth, Mutual Benefit, was a surprise. We didn't expect the run to occur and I think that it was probably a failure on our part to analyze the potential of liabilities becoming very liquid. In some cases, there were asset problems and asset/liability problems. Sixty percent of their assets were in mortgages. They were very illiquid and when the real estate market tanked, it took them down. They also had a lot of private placements. They had some venture capital money that didn't turn out too well. I think they had a controlling interest in Carter Halley, which went down. There were a lot of interesting assets. Thankfully it was not a typical insurance company. Moody's view has really changed about how liabilities will respond to a crisis of confidence in the insurance industry.

There are several common characteristics of insolvent companies. Much of this is repetition of what was said before, so I'll go through it fairly quickly. Illiquid investments are one of the biggest. When you develop any sort of problem and all your assets are liquid, it doesn't leave you a lot of room. You just can't run a company that way.

We're seeing throughout the insurance industry and in other industries, too, like financial service industries, a move to have liabilities be more liquid. A good example is annuities. Insurance companies are writing much more annuities than life insurance. If you look at the liabilities on an insurance company's balance sheet, they're mostly annuities at this point. Those can run very quickly, whereas somebody can't really qualify for a good rate for life insurance after a certain age. It stays around for 20–40 years. Annuities tend to turn over rather quickly. Individual annuities tend to have a seven-year surrender charge. After the seven years is up, or the surrender charges go away, you see a huge lapse rate so it's a much shorter liability. Whenever there's a crisis of confidence, policyholders tend to be very quick to move money, especially institutions. I don't think Fidelity is going to wait around to see if an insurance company is going to make it. They'll pull.

Another development that happens in some insolvent companies is a decline in new business, and that was the case with Executive Life. Not only was there surrendering of any possible policyholder liability, but there is also no new business. So it became a situation of trench warfare trying to maintain assets and keep the money in.

Another characteristic is previous rapid spread based product growth. What I'm talking about here is annuities. In most insolvencies that we've looked at with insurance companies, there tends to be an aggressive growth pattern, probably by offering very attractive crediting rates to policyholders and then not being able to back that up because the assets don't perform as expected. Eventually there is a negative spread earned.

High debt leverage is another characteristic. Confederation Life had a very high debt-to-total-capital ratio. If you looked at Mutual Benefit you probably would have seen a similar instance. First Capital was another example and so was Southwestern Life where there was a lot of debt. When things turned down, the whole company unraveled.

Poor underwriting really has to do more with spread-based products. Excessive credited rates offered to policyholders and general mismanagement covers everything. If you put a finger on anything as to why a company defaults, it's really mismanagement and the inability to foresee how certain actions will affect the

future of a company. Equitable is a good case, where they wrote tons of 10-year guaranteed rate GICs, and it almost took the company down. They couldn't foresee that interest rates would fall 10%, as a result they couldn't cover the spread and I think they lost about $1.5 billion just in that one product line.

What has changed since the early 1990s? Disclosure has definitely improved, especially for mutual companies. I remember going to see a large eastern mutual insurer for which I was to do credit analysis in the early 1990s. Their response was we're so and so, we're the best, we'd never default. And some of those companies actually became troubled, even though they didn't default. A few were acquired by strong rivals, and, as a result, capital is definitely stronger. We've seen capital improve across the board at most large companies, and that's really positive. I think that's really a reflection of the environment and a very positive earnings momentum has developed from falling interest rates. I think the insurance industry's management is becoming much more aggressive with risk and also competing against other financial service providers.

Investments are definitely more diversified. You don't see companies with 50% of their assets in commercial mortgages. You don't see 70% of assets in high-yield bonds. The most aggressive companies might have 15% in high-yield bonds and a much more diversified portfolio. Commercial mortgages might have the highest exposure, at about 35%. Now a market has developed where you can securitize mortgages, however, in the early 1990s that wasn't the case. We're seeing a lot more liquidity in the commercial mortgage market. In the next downturn in the market, there will be losses. There will probably be a better result because of the liquidity being enhanced due to development of Real Estate Investment Trusts (REIT) and other co-mingled trusts that have been securitized.

Earnings have rebounded quite well, and I think that is a function of a very positive market environment. Risk management has definitely evolved. There is much more sophistication, especially in some of the larger insurance companies. They have developed quite elaborate asset/liability management models and contingency plans. Four or five years ago, nobody had contingency plans in the event certain scenarios would occur, such as a run on the bank or a run where people want their money back very quickly and are exercising the options in their policies.

Once again, the capital markets have been quite favorable. This has been probably the most unique time since the 1950s where you see very low interest rates and a strong equity market. It's almost impossible not to make money if you're an insurance company at this point. On the other hand, what happens when things turn around? You'll see some companies become stressed, though I think the larger

companies are definitely well positioned for a number of reasons. I'll get to that later.

As far as trends, what's going on in the industry and how that's going to affect the potential for insolvency include consolidation, convergence and globalization? There is consolidation within the industry, where you're seeing larger companies acquire smaller companies. It tends to be the more highly rated companies acquiring lower-rated companies. There are exceptions to the rule, but that's usually the case. You've also seen convergence of banks, investment banks and insurance companies. A good case in point is Citicorp. We don't expect to see that model being duplicated throughout the whole industry. We would expect at least some insurance companies to be acquired by banks in the future.

We are seeing globalization. Life insurance is still very much a local business. What's sold in the U.S. is much different than what's sold in England or in France. However, you're seeing global enterprises being created. They have operations in several different countries, and they are developing might and power from that.

Regarding demutualization and the mutual holding company structure, I can't go as far as saying that there won't be any mutuals in five years, but there will be a lot less. As these mutuals demutualize, some of them will be acquired because they'll go at a price-to-book value of under one. After a few years, if management can't get the stock price up to a level of say 1.5 or 2 of book, there will be blood in the water. They'll be bait for other companies that have higher multiples and are interested in growing.

The product focus has also changed to separate accounts and equity-based products. A positive for the industry is that more fee-based products means less risk. Spread base is probably the more common product that an insurance company could sell. However, insurance companies do not really manage live equity products. It's outsourced to a third party, so they're giving up the asset management technique that they've developed over the years. If you went back ten years ago, most of what insurance companies sold was what it managed internally. That's not the case today. Distribution has also changed quite radically. You're seeing the tie model where you have the career or even a PGA agent with a strong tie to the company. You're seeing that being almost dissolved where the independent regional broker/dealer is really the source for variable annuity production. The banks are becoming quite powerful as distributors, and as they become more and more powerful, they're going to demand more of the slice of the pie from the insurance company in order to distribute the products. Distribution really controls the key characteristics of an insurance company and giving that up to third parties is a negative trend.

Most insurance companies are definitely well along the way to solving any Y2K problems. We don't expect any large companies to have an issue.

The strengths include good asset quality. The average bond rating of an insurance company is in the A category. That's very high quality. Earnings momentum should continue. The insurance industry is in the retirement forum, and that is expected to grow quite significantly in the next 20–30 years. Insurance companies should be able to attract some assets. Efficiencies are improving for some. You're definitely seeing insurance companies talk more and more about being efficient and that should make for a stronger company in the long run.

This is fairly unique to the insurance industry, but it tends to have a very predictable premium and benefit flows. I'm talking about life insurance; it's a very long-tailed liability. That's a strength that the insurance industry has over other financial service providers that don't have that long liability. There is a stream of income that will come in every year, and there's tremendous imbedded value in certain business lines, especially life insurance where the mortality tables were quite conservative. There is better value in whole life policies or whole life blocks and in other life insurance blocks, though that's not the case across the whole industry.

There is an expanding market for retirement products. That's a 20-year plus trend that we would expect to see play out over, say to 2015 or 2020. Insurance companies should be able to gather some assets and should be able to compete quite well against other financial service providers, especially because of the tax-deferred status of variable annuities. It's quite an attractive product and we're still seeing growth in that business: $100 billion was sold last year and $115 billion might be sold this year. This is a growth market that should continue to grow for an extended period of time. So all that bodes well for the insurance industry and insolvencies, as a result, should be less because of the strength.

Challenges include a market environment that is quite competitive. We're seeing banks and other financial institutions encroach upon life insurance companies common ground, i.e., the sale of asset management products. There's excess capacity within the life insurance industry. There are really too many companies, especially small companies. That's a concern. Some of those will have to be acquired. Migration of consumer preferences toward equity-based products plays against the insurance industry because they're not known as an equity manager. If you look at variable annuities, most of that is outsourced to third parties, and you would expect that trend to continue.

Another challenge is that liability duration is definitely being shortened. As annuities continue to grow, we'll see the liability duration of insurance companies

definitely contract more and more, and we also expect to see increased financial leverage as companies acquire other companies by issuing debt. That's also a negative trend.

Those that have distribution are going to prosper. Those that don't are going to suffer. That's probably going to be the major key to success in the future. Falling long-term interest rates is a positive now because everybody seems to have unrealized gains on their books. If interest rates rise, you're going to see those turn into losses and some companies obviously are going to suffer as a result.

Could large insolvencies occur again? Our expectation is, yes, they could under certain circumstances. We don't expect it to occur, but a good example is what's happening in Japan and Korea. Obviously, the product profile is different, but under certain very stressful scenarios, the insurance industry would suffer just like any financial service company would. You'd see insolvencies. We don't expect to see any major insolvencies. There are obviously some companies that we rate as investment grade that have a higher level of default probability than others, but for the large insurance companies, we don't see anything out there that really would crater them in a short run. To say never is a long time. It's possible that 20 or 30 years out, if some companies don't change and refocus, they could become troubled.

Mr. Modugno: I will ask the first question. The decade of the 1990s had three major failures. I don't think we've seen anything like that. In the 1980s you had Baldwin United; in the 1970s, it was Equity Funding, but there has been nothing like that and we didn't even include First Capital, which was also a major failure. So for the decade of 2000 compared to the decade of 1990, do you see more equal or less spectacular failures? I'll ask each panelist to answer that in order.

Mr. Becker: My vote is for substantially less among the upper tier companies. Insurance companies have learned that they have to have more capital when they're taking more risk. They are much more diversified than they have been in the past, so I just don't see a repeat of the 1990s.

Mr. Gies: I don't think I disagree with that, although I am impressed with the changes in the industry, the more bank-like our products become. We do like guarantees. We are, in fact, insurance organizations, and so the kinds of risks that we're dealing with are relatively new. I think it's important that the regulatory framework move and change and more accurately assess what the real risks are and rely less on *pro forma* financial reports. Central to that is an actuary, a peer review process, and a pretty insightful assessment of risk.

Mr. Maloney: I would agree with Jack and Murray that there's likely to be fewer insolvencies than you see in the early 1990s. I think the insurance industry has definitely progressed toward being more risk managers. However, I would couch that by saying, we're seeing more and more companies become bank-like and more spread-based providers and less insurance providers. If you look at the average insurance company, they're more of an annuity house than they are an insurance company. That's really more of a banking investment type of business, which has a higher risk level. As of now, I can't think of any large life insurance organization, besides one or two that we already rate below investment grade, that really could suffer considerably in the short run and wind up in default.

Mr. Gene Eckstut: Let's say insolvencies occur because there is a problem in one of the investment markets. It could be real estate or junk bonds. Let's say a company is overinvested in one pot and that pot became bad and then they were in trouble. In the three insolvencies, it was noted that two of the insolvencies in the long run didn't lose that much money or didn't cost the guarantee funds that much money because they managed the investments until the investment market recovered a little bit (for example, real estate). In the case of Executive Life, it seemed like California just jumped in and said, "Oh, we're just going to sell all these assets at the bottom of the market," and therefore they froze the loss. My question is, why did they do that?

Mr. Modugno: Murray and I might have differences of opinion on this. This was an indirect result of Proposition 103 where we had an elected commissioner who was in the process of running for governor. He wanted front-page news. If ELIC had just held those assets instead of selling them at the bottom of the market, they would have had full recovery. I'll let Murray get his point in.

Mr. Becker: I agree with what Vic said, but the insurance industry had a role. The insurance industry thought of Executive Life as a pariah investing outside of the norms of the business. It felt that whatever happened to Executive Life policyholders, they deserved it. This is an incredible point of view, but it got translated into real losses for the industry because the default was recognized. The losses were established, whether the assets were sold or not. The guarantee funds have to make up the difference, and the guarantee funds are, I believe, 50% supported by the industry. That locked in the loss. Now, it didn't take the industry long to learn that they had a hand in screwing up Executive Life by not jumping in and saying, "Wait a minute, we'll help with a workout." So the industry did jump in to help Mutual Benefit several months later and the leaders like Metropolitan, Prudential and some others said, "Look, we'll work with you to work something out." In many ways the Mutual Benefit bail-out was designed to avoid losses by the guarantee funds by essentially taking away the instant loss and using the asset

recovery model and amortization over a period of time to do it. Confederation Life didn't work out quite the same way, but there was a very strong industry interest in minimizing the losses and working out the assets. I would say that there's a mixed responsibility in which, in the end, everyone lost because of the way Executive Life was handled.

Mr. Gies: I would just add to Murray's comments. As I reviewed the literature, there was a learning process here. The National Organization of Life and Health Guarantee Associations (NOLHGA), and the companies learned through the Executive Life failure and then subsequently through some of the other failures that there were different ways of approaching the problem. What if the concern had been what's best for the policyholders? What is our promise to the policyholders? It's essentially benefits, like life insurance and annuity payouts, not cash. I understand that cash is part of the overall mix in the U.S. and part of our contracts, but if they initially had that better understanding of what ultimately the promise is, maybe the decision process might have been different too, but maybe not. But I do think now that there is a mindset that managing these impaired corporations for the benefit of the policyholders is a much better way to go.

Mr. Maloney: Regarding Executive Life, it was obvious that the sale of assets lost value for the policyholders. I think I remember reading that it was about $1.5 billion that was given up from the sale of assets quite quickly. Garamendi was the Insurance Commissioner for the state of California; he was a novice, and he didn't really understand the insurance industry. He had worked for a bank. I met him once or twice. He just had a different outlook on what was going on than somebody who was inside the insurance industry. He also was a political animal, so I think he gave up a lot of value to policyholders by selling out so quickly, and he sold to Leon Black. He was the one who created a lot of stuff in the first place. He knew what the value of it was. Why would you sell it? It's like selling to the shark. You're going to get bitten. I think it was mishandled.

Mutual Benefit and Confederation had more of a professional management team that came in. My concern is that these insolvencies take a long time to resolve. Eight years is a long time to wait to get your money back. If you said that to a bondholder, he wouldn't accept it. One year or a year-and-a-half is really what you want to spend in any sort of workout to get your cash out. Also, you had a lot of different interests in Executive Life. You had joint service and Goldman Sachs had bought a lot of the muni-GICs at 10¢ on a dollar. It was looking for the big pop. Whether it was 68¢ or 50¢, it wanted cash back quickly; it didn't matter. It is going to make a ton of money. I think there were a lot of different interests in Executive Life that you didn't see in the other failures. As a result, you saw policyholders probably treated in a better way.

Mr. Modugno: There was an industry bailout proposal that would have managed the money, and I think Garamendi chose the French. There was a proposal from NOLHGA to take over and manage the assets on an ongoing liquidation basis. He chose the French over that. Any other questions?

From the Floor: Clearly an Executive Life discussion could go on all day. I had one observation, if I could just digress for a moment. This is directed to Kevin and then anybody else can jump in. You mentioned smaller companies at least five times. We represent the National Alliance of Life Companies. First you said that smaller companies have a greater default rate, and I was waiting to see you illustrate that. Second, you said that larger companies are better situated for the future. You didn't explain why. Third, you said that you don't expect any large companies to have a Y2K issue. I didn't know whether you meant we should be worried about large companies having them or you did expect small companies to have them. I was wondering if that was the case. Fourth, you said that there were too many smaller companies and I don't think there are enough small companies. I was wondering why there are too many. Fifth, you said that for the large companies you didn't see anything that would crater them in the short run. I am just wondering if that was because we should be concerned if a large company fails or because you thought that for small companies, you did see problems. Generally there seems to be a bias that small companies have serious problems or are going to have serious problems and yet there was no demonstration of that. I was just wondering if Moody's has anything or any of the other commentors would like to comment on specifically what data can support the statement that smaller companies have these kinds of problems that we should be worried about.

Mr. Maloney: Across the industry, smaller companies have a higher default rate and the insurance industry is no different. I could provide you with some specifics as to why. I'm talking about companies with assets under $100–150 million. There are more of them than there are of larger companies and they tend to fall at a faster rate. There were four defaults in 1998, and they're all very small companies. There weren't any large companies that defaulted. If you went back 20 to 25 years, we do have some data. Unfortunately, the NAIC wasn't very good at keeping track of data, so it's really not available beyond 20–25 years. It just isn't available. There are a lot of these smaller companies with $50 million or $25 million of assets that are not very well regulated. No offense, Jack. A lot of them are domiciled in Arizona. They tend to not pass under people's radar screens, and when a default occurs, it's not on the front page of *The New York Times*.

You had several other questions but I failed to write them down. There's substantial evidence that smaller companies do have a higher rate of default. Does that mean that it's three or four times the default rate of large companies? No. And can a

small company survive over a period of time? Sure. Our feeling is that the insurance industry is becoming much more sophisticated and that a smaller company probably doesn't have the resources to climb up that scale. Some will but others won't. I think you'd agree that a company that has $100 million of assets in this day and age is probably not going to play very well against larger companies. They're not going to have the sophisticated asset/liability management process. They're not going to have the many actuaries that a larger insurance company has. That's not to say that they can't survive or thrive. It just means that they're going to have a tougher time at it.

Mr. Gies: Kevin, I want you to know that the 130 companies in Connecticut are very well regulated. I also want you to know that you have been referred to as a regulator as well. Doug, my research showed that three quarters of the insolvencies were companies with $5 million or less in capital. There are more companies, so a number like that doesn't indicate that they're more likely to fail. There are more small companies than there are large, but I do think that regulatory resources are oftentimes more directed to the large companies because they can afford the kind of attention and because their products are typically multi-line. Typically financing the regulatory review is more easily supported at the large company than it is at the small company. Of course we have that Section 7 and Section 8 differential that we're dealing with as well.

Mr. Kenneth W. Hartwell: I have a two-part question for the panel that's related to risk. I don't know all the details, but in the not-too-distant past, there was a major failure of a fund that dealt with derivatives, although it was run by two Nobel prize winners. I think what happened is that some way-out contingency that they felt would never occur, did occur. Are there some comments on the possibilities of that happening in the insurance industry? Second, we've heard a number of comments about people not having enough capital, and there's a lot of pressure on the insurance industry now to produce high return on equity (ROE). Some of them are even producing 2%, at least according to the published financial statements. One way to increase your ROE is to reduce the denominator. One very prominent company that used to be rated AAA got downgraded, and I think it was done voluntarily. The chairman made a statement last year that he wasn't going to let another downgrade stand in the way of a further acquisition. He was praised by the equity analysts for having that attitude.

Mr. Gies: Ken, I think your point is very well taken on long-term capital management (LTCM). We are concerned about and naturally would be concerned about the more sophisticated products and the exotic instruments and the little understood financial instruments that tend to support some of today's insurance products. I don't know how to get at that question other than to have the

appropriate financial engineer working on it, supplying an opinion and a peer review process. I think there's a real need to have the actuarial profession as part of that equation. My other comment would be that, in the U.S. system, failures are tolerated, so we have all the benefits of innovation and freedom to create products and to create new investment vehicles. We tolerate failures as opposed to prescribing activities and telling people what they can or cannot do ahead of time, but your point is very well taken. We don't know what can't be known. We're going into that field more and more, so there is no questions that there will be surprises in the future.

Mr. Becker: I just had the one comment on the capital ratio. Our view of the insurance industry is that when you're in the GIC buying business you essentially have to be a credit analyst. We would say an insurance company can be leveraged as it wants to be. We're only going to deal with the insurance companies that have a high enough capital ratio to provide a lot of comfort. The norms of the industry now are in high single digits in terms of the capital ratio as opposed to mid-single digits of eight or nine years ago when defaults began. As long as there are plenty of high single digit, fairly large insurance companies that look to us as well diversified companies that carry AA or better ratings, that's where our money will go. If somebody wants to make more profit and have a better ROE, they'll be in a different marketplace.

Mr. Maloney: On the issue of LTCM, a number of insurance companies actually had investments in that organization. None had anything extreme. The highest I know of is about $25 million, and interestingly, those that got into it early in the first round of investments, which I think was in 1996, there was a payout in late 1997. They got most of their cash out. Most of them took their cash out, so what they lost was any earnings. Most of them actually recorded maybe a 5%, 6%, 7%, or 8% return on that investment, and they expected to get out of it even above that when the workout is completed. I think a hedge fund is much different than an insurance company. I would hope so. I can't see the same sort of events affecting an insurance company just because the liability mix is much different. They're not leveraged three, or four-to-one like a hedge fund is. There's just not that level of debt outstanding.

As far as the high ROE, I would agree with you 100%. A company that's earning under 10% is under a lot of pressure to get that up to 12% or 15%, or they'll get taken over. They know that. It's a very vicious world out there. I have heard one insurance company chairman tell me that they wanted to take a dividend on this life insurance operation because we have too much equity and so we'll never get to that 10% level. They actually took a dividend up to the parent company. They knew they couldn't increase earnings so they took the equity out to get to the 10%. We

would think this is a negative from a credit perspective, but the equity analysts seem to like it. What really drives the decision-making is equity analysts. They own the company.

Mr. Stephen L. Pontecorvo: This question is directed toward Keven. You talked a lot today about the regulators' contributions to the insolvencies that have occurred. The study notes that I read for a lot of exams said that the rating agencies certainly didn't help the situations and maybe even contributed to them because of their very late and rapid adjustments at a point that was probably too late in time. I was hoping you could talk a little bit about whether or not Moody's has adjusted the way they rate the insurance companies in that respect and possibly have a better grasp on forewarning people before the problem is too late.

Mr. Maloney: I think the one we missed was Mutual Benefit. We had rated it AA2, which is a very high rating, several months before it defaulted. At the time it defaulted, we had downgraded it to A3. That happened on approximately May 15 or something, and the company defaulted in July. It obviously didn't help matters to downgrade the company, but if you read the press release it basically said that we didn't know about the huge real estate portfolio. We found out and we had to rate the company accordingly. Obviously it didn't help matters, but I think you have to do what you have to do. When you find out some information, you have to incorporate it into the rating. Moody's has been rating different companies for 100 years, not so much insurance companies but other industries. It's a difficult situation because you don't want to create the run. By the same token, you have information that's going to affect the rating. You have to release it to the public. Moody's investor service is for investors. It's for credit rating or credit decisions. I don't know what else to say about that. Obviously, it wasn't a happy situation, and I'm sure it led to further problems with the company.

Mr. Becker: I'd like to just say a little word from the point of view of the investor in GICs. We were concerned that the credit rating agencies, in general, didn't anticipate the defaults earlier, especially our firm that had largely relied on them up until about a year or so ahead of the beginnings of defaults. The problem was what happened after Executive Life and Mutual Benefit, when credit rating agencies and especially Moody's began downgrading companies that were considered AAA. There were two or three notches at a time in blocks. In Moody's case, maybe 10 companies would get downgraded all at once and in an environment that was already panicky. This made it look to the world like no insurance company was safe and that everything was at risk.

Unfortunately, none of the excessive downgrades were corrected for a couple of years, which seemed to us to be a political situation where you didn't want to look

stupid, having overreacted in the first place. I think that in the early 1990s, the insurance industry and employer marketplace looked like a very shaky industry, not because of the early defaults, but because of the subsequent actions that occurred. I don't blame the credit agencies that are downgrading when it's appropriate, but I do think that it has to be done carefully.

Mr. Maloney: Maybe I should respond to that. Downgrading companies in block obviously didn't help the insurance industry, but it had to be done. Our feeling at the time was that there was a massive change in the public's perception of the insurance industry. Prior to that event, the feeling was that people wouldn't turn in their policy. You had people outside the door of Mutual Benefit asking for their money back. Nobody expected that, and we didn't either. So we had to reflect that in the ratings and there were block downgrades. At this point, the ratings are quite legitimate.

Mr. Becker: I have no problem with Moody's today.

Mr. Maloney: I was on the other side. I didn't work for Moody's at the time. I remember asking my current boss, "How could you do this?" And he said, "Well, we did it to everybody." It was done across the board, and as it turns out, it was the best thing to do at the time in a bad situation. I think it created more credibility for the ratings in the long run because now it's much more legitimate. An A-rated credit is much more legitimate today than it was five or six years ago. I think it really connotes the level of potential loss.