9. (2.25 points)

   a. (0.5 point)

      Describe how a guaranty fund provides services to policyholders.

   b. (0.5 point)

      Briefly describe two challenges that could arise for state guaranty funds if a national multiline insurer were to become insolvent.

   c. (0.5 point)

      Explain why insurers are prohibited from including information on guaranty funds in their marketing materials.

   d. (0.75 point)

      If a state were to eliminate its guaranty fund, briefly describe a potential consequence to each of the following stakeholders:

      - Policyholders
      - Insurers
      - Regulators

CONTINUED ON NEXT PAGE

QUESTION 9	
TOTAL POINT VALUE: 2.25	**LEARNING OBJECTIVE: B2 / B3**
SAMPLE ANSWERS	
Part a: 0.5 point	
• Handles claims of insolvent insurer OR Pays claims and returns unearned premium of insolvent insurer • Provides temporary coverage in case of insolvency	
Part b: 0.5 point	
• Difficult to distribute loss across states OR coordinating payment across multiple state guaranty funds OR each state would need to agree to the proposed settlement amounts from the guaranty fund OR Laws and processes are different between states, so it is difficult to determine the allocation to each state • May need to assess annually for several years OR There is a limit on the assessment by written premium per year so may need to assess for more than one year	
Part c: 0.5 point	
• Guaranty fund has limited coverage OR policyholder may not be fully indemnified • Moral hazard OR distorting competition OR existence of guaranty fund does not prove financial strength OR insurer grows irresponsibly OR policyholders would be less likely to seek a financially strong insurer	
Part d: 0.75 point	
Policyholders (any one of the following): • Would not be paid for claims/unearned premium in the event of an insolvency • Reduced premium because insurer would no longer be paying guaranty fund assessments • Would have incentives to seek stronger insurers Insurers (any one of the following): • Would not have to pay assessments • Would charge lower rates because they would not be paying assessments • Would have lower costs because they are not paying assessments • Regulators would increase capital requirements • Weak insurers would lose business to insurers with higher financial ratings OR Strong insurers would gain business from weaker insurers Regulators (any one of the following): • Stronger solvency monitoring • Stronger rate and solvency monitoring • Lose NAIC accreditation • Increased complaints from policyholders • Will increase minimum capital requirements on insurers	
EXAMINER'S REPORT	
Part a	
The candidate was expected to know that the guaranty fund continues insurance coverage until policyholders find new insurers and that the guaranty fund handles claims and refunds unearned premium for policyholders of an insolvent insurer. Most candidates were able to state that the guaranty funds pay the claims of insolvent insurers.	

Fewer candidates also knew that they provided temporary coverage. The most common errors were restating the question as an answer and rewording the same answer in two different ways.
Part b
The candidate was expected to give two short explanations of what would be unique if a national multi-line insurer were to become insolvent. The candidate was expected to demonstrate knowledge of two of the three following statements: each state involved needs to approve the final settlement; coverages and laws are different by state making it difficult to allocate the loss among state guaranty funds; the guaranty fund may need to assess annually over several years to recover the shortfall. Common errors included: • Making statements that were not unique to multi-state like increasing premium to recoup assessments, assessment costs shifted to policyholders, slower claim settlements, and lines not covered • Draining the state fund or assessment is insufficient – this is a misunderstanding of the assessment cap, the cap is a maximum per year but the guaranty fund can assess insurers annually until the insolvency is fully funded • How to allocate among policyholders – state law determines how much policyholders are entitled to – the issue is how much each state guaranty fund agrees to contribute. • How to assess insurers – the issue is how much each state's guaranty fund agrees to cover and then that state assesses the insurers in their state according to state guaranty fund law.
Part c
The candidate was expected to give two brief or one full explanation of why insurers are prohibited from marketing the guaranty fund. Common errors included: • Every insurer has access to the guaranty fund (the guaranty fund is for the benefit of the policyholders, not the insurer) • The prohibition is state law (restates the question)
Part d
The candidate was expected to give a short explanation of the effect of the elimination of the guaranty fund on policyholders, insurers, and regulators. Common errors included: • Attributing the benefit of the guaranty fund to the insurer rather than the policyholder, • Stating that the policyholder wouldn't be paid for their losses without also demonstrating their knowledge that this is only true in the case of insolvency • Assuming that small insurers are weak insurers • Insurers will strengthen their financial position without stating that this would be a reaction to increased regulation or competitive demands.