4. (2 points)

   a. (0.5 point)

      Briefly describe two examples of mandatory corrective action that an insurance commissioner may impose on an insurer.

   b. (0.5 point)

      Briefly describe administrative supervision, and briefly describe one reason regulators may be reluctant to take this action.

   c. (1 point)

      Fully describe receivership, including an explanation of rehabilitation and liquidation.

CONTINUED ON NEXT PAGE

Candidates were expected to be able to list four distinct factors that might be used to assess the effectiveness of an insurance regulatory framework. Common errors include: • Stating "protect policyholders" as the top priority of insurance regulation but not describing a factor for assessing effectiveness • Simply stating "act in the public interest" without explaining further and describing a factor for assessing effectiveness • Listing multiple factors that describe the same general concept. For example a candidate might list "a competitive insurance market", "insurance availability and affordability", and "financial strength and stability of insurers". Each of these is an acceptable answer, but they all describe a healthy insurance market. • Listing features that might exist within a strong regulatory framework but are not used to assess effectiveness, such as checks and balances, standardized procedures, and data quality.
Part b
Candidates were expected to describe/define the three reasons for regulatory failure. A common mistake included writing something for fallibility that did not convey simple human error. For example: "regulators fail in their assessment of financial indications" or "did not detect an insolvency".
Part c
Candidates were expected to provide three strengths of the US regulatory system with a brief description explaining how the strength might mitigate one of the causes of failure from part b. Common errors include: • Stating "most insurance commissioners are elected" as a strength. The vast majority of states appoint their commissioners. • Answers relating to guaranty system. Guaranty funds are in place to benefit policyholders after a company fails and the question asked for strengths that could help to prevent failures. • Listing a strength, but failing to describe it and/or linking it to part b. • Listing "duplication", "peer review" and "peer pressure" as three separate strengths.

FALL 2019 EXAM 6U, QUESTION 4	
TOTAL POINT VALUE: 2	**LEARNING OBJECTIVE: A2**
SAMPLE ANSWERS	
Part a: 0.5 point	

SAMPLE ANSWERS AND EXAMINER'S REPORT

Sample responses (any two):

- Perform certain actions to reduce its liabilities, such as purchasing reinsurance or restricting available limits that can be sold.
- Restrict new-business or runoff existing business. May require an insurer to improve their position before taking on new risks.
- Reduce its general and commission expenses
- Increase its capital and surplus
- May require insurer to not give out dividends to policyholders/stockholders
- Require insurer to invest in less risky assets (e.g. prohibit certain investment practices)
- File reports concerning the value of its assets
- Document the adequacy of its premium rates

Part b: 0.5 point

Administrative Supervision occurs when the insurer must seek approval before making certain business decisions. (i.e. the regulator will "oversee" insurance company operations).

Sample responses for reasons regulators may be reluctant to do administrative supervision:

- Regulator may believe the insurance company will recover on its own, so it would not act
- Regulators may be reluctant because when policyholders find out about this (or brokers) they may be less willing to place business with them, therefore making the situation worse.
- The consequences of regulator intervention may otherwise prompt policyholders to leave and give insurer and the regulator a bad reputation
- May not want to interfere with a politically connected insurance company
- Regulators may be reluctant because this is time-consuming and require a lot of effort and personnel
- Reluctance comes in because this could lead to the loss of jobs and could hurt the local economy (Forbearance)
- Regulators may believe an insurer has been unlucky and hit with a one-time setback that it can resolve on its own.
- Regulatory forbearance may cause regulator to be too lenient

Part c: 1 point

Receivership is a type of bankruptcy where Commissioner becomes/assigns a receiver to take control of the insurance companies assets and liabilities. It can have two outcomes: rehabilitation or liquidation.
Rehabilitation is an attempt to save the company. Commissioner will try to reduce liabilities, increase assets. They usually look for an outside investor to inject capital.

Liquidation occurs when assets are insufficient to pay liabilities and the insurer ceases to exist. Assets are liquidated and paid out to stakeholders based upon an appropriate prioritization.

EXAMINER'S REPORT

The candidates were expected to know various examples of mandatory corrective action, be able to describe administrative supervision, and know why regulators may be reluctant to do this.

Also, they needed to describe receivership and its two possible outcomes (rehabilitation and liquidation), and then define both.
Part a
Candidates were expected to list two examples of mandatory corrective action. Common errors include: • Stating "increase rates", or any variation of that, since that is not something for which insurer and its' domiciliary regulator have complete control. • Giving rehabilitation or liquidation as examples of mandatory corrective action. • Giving two examples of limiting new or renewal business, which was duplicative. • Giving examples of incorrect actions, such as replacing management, requiring rate increases, or removing the license to do business.
Part b
Candidates were expected to describe administrative supervision, and provide a reason why regulators may be reluctant to pursue this course of action. Common errors include: • Describing receivership instead of administrative supervision. • Stating that administrative supervision comes only after corrective action failed, with no description of what it is, and describing it by using the word "supervising" without context explaining the actions. • Use of vague descriptions, such as the regulator is "stepping in", "monitoring", "watching", or "participating" in the company operations (i.e. no clear notion that they are acting in an approval capacity).
Part c
Candidates were expected to describe receivership, and note that its two possible outcomes are rehabilitation or liquidation, defining each of them. Common errors include: • Failing to include outcomes • Defining liquidation by saying assets were liquidated, with no further context.

FALL 2019 EXAM 6U, QUESTION 5	
TOTAL POINT VALUE: 2.5	**LEARNING OBJECTIVES: A3, C2**
SAMPLE ANSWERS	
Part a: 0.5 point	