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N.Y. Regulators Hope to Create New Trend by Selling Off Insolvent Company

NEW YORK March 13 (BestWire) — New York regulators are hoping their plan to sell an insolvent insurance company to the highest bidder becomes a road map for others to follow.

Regulators would like to sell Midland Insurance Co., which has been in liquidation since 1986, to the highest bidder. The company currently has about $1 billion in assets and about $2.9 billion in liabilities. Mark G. Peters, special deputy superintendent in charge of the New York Liquidation Bureau, said it could take state regulators another decade to wind the company down.

Private companies might be able to liquidate the company faster, while paying policyholders a larger percentage of claims than state regulators could. It would be the first time the assets of an insolvent company were sold to private investors in the United States, but similar plans have been successful in Europe.

"Our hope is that if it works, this will become a template for use again," Peters said.

The idea is that a private entity would be able to gather more assets than regulators. For instance, about two-thirds of the company's assets are reinsurance recoverables, and regulators have garnered about $200 million in old claims last year.

"But we don't have ongoing relationships with the various reinsurers. We aren't buying reinsurance again next year. Whereas the kind of financial institutions we are meeting with do, so they may well be able to collect a higher percentage of those reinsurance claims than we could, which would allow them to make more money than we would," Peters said.

Also, regulators primarily invest in Treasury notes, whereas private investors have more flexibility in what they can invest in, and may be able to generate a higher return. "There's about $300 million in cash. A large financial institutions might invest that money...and can presumably make more money on this than we can, which is what allows them to bid at a higher price than what we can estimate we can return to policyholders," Peters said.

So far, about a dozen potential buyers, including investment banking houses, private equity entities and insurance companies, have met with regulators to express an interest in buying Midland.

"Basically, a lot of people are looking to buy something like this now because it is an investment that's uncorrelated to the stock market. Whether you make money on this or not, it doesn't depend on how the stock market does," Peters said.

Not that regulators would let just anyone bid.

"We have no intentions of selling Midland to someone who will return it to us a year later," Peters said. Regulators have created a rigorous bidding and vetting protocol. The New York Liquidation Bureau, which manages more than 60 insolvent insurance company estates for the New York State Insurance Superintendent, is seeking public comment on draft Request for Proposal documents seeking bids for Midland. After the 45-day public comment period, the draft RFP documents will be submitted for court approval. Once approved, the liquidation bureau will post the final RFP documents on its Web site, www.nylb.org.

Under the terms of the proposed sale, the purchaser would pay just a percentage of Midland's liabilities, in the form of a guaranteed distribution to policyholders with resolved claims. Buyers can theoretically turn a profit if they settle claims for less than they are worth on paper and get reinsurers to pay any money owed. Under the proposed RFP documents, the buyer would also pay policyholders a pro rata percentage of any profits made.

The bidding process will require prospective buyers to say how much they'd give to policyholders through the guaranteed distribution and profit sharing. Those percentages will be the primary basis for competition among bidders.

Regulators hired Milliman Inc. in October to analyze the Midland estate to determine how much policyholders would receive if the state continued to handle the liquidation. That analysis will help regulators review the bids from private investors, and ensure that policyholders would receive a better payout if the company were sold (BestWire, March 6, 2009).

"Once we have qualified the bidders, they will be given access to a war room with all of Midland's documents, reinsurance contracts, proofs of claim, insurance contracts. And then they'll come up with bids," Peters said.

One group who stands to gain the most if the plan is successful is the state guaranty funds, who pay the claims from insolvent insurers and then become a creditor to the estate of the insolvent insurer.

"Anything you can do to strengthen the financial security of the guaranty funds is and of itself a good piece of public policy," Peters said.

The Midland estate has already paid two dividends: 10% in March 2006 and 5% paid in June 2007. Overall, the two dividends were $84.8 million of Midland's assets.

Founded in 1959, Midland wrote a "substantial amount of excess coverage for major Fortune 500 companies," the liquidation bureau said. Midland also acted as a reinsurer.

The company's $2.9 billion in unsettled claims involve thousands of policyholders nationwide, including corporations seeking reimbursement for payments to victims suffering from asbestos exposure, defective breast implants, and HIV-tainted blood products, regulators said.

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