compute the amount for contingencies referred to in this section on a consolidated basis and prorate the total amount for contingencies to each such insurer in proportion to the premiums earned by each such insurer, if:

(a) they are affiliated through ownership, where each such insurer is wholly owned by or wholly owns one or more of the other insurers in such group, or,

(b) they pool substantially all their business with each other and the commissioner certifies that such computation on a consolidated basis will more accurately reflect the financial condition and affairs of such insurers.

(6) Every insurer or fund, including fraternal benefit societies, authorized to transact insurance in this state on the effective date of this section shall be allowed two years after the effective date of this section in which to comply with the requirements of this section. Any such insurer which fails to meet the requirements of this section at the end of such two years may be granted one extension of an additional two years in which to comply by the commissioner if the commissioner is satisfied such insurer is safe, reliable and entitled to public confidence and would materially suffer from a forced conversion of its assets to comply with this section.

DISCUSSION BY S. C. DuROSE

In this paper, the author proposes certain premises which are said to be the basis for insurance investment regulation and then describes and discusses some of the shortcomings of the persent approach to investment regulation. He also suggests certain principles for achieving his concept of the purposes of insurance investment regulation. Also attached to the paper are copies of legislation proposed in the state of Michigan for the creation of a post-insolvency assessment type fund and for the regulation of insurer investments. It is my opinion that the primary interest of the Society as respects this paper is the author's rationale and discussion of insurance investment regulation.

The author calls attention to the fact that, in most states, there is at present no acceptable solution to the handling of the social problem of paying claimants in event of the liquidation of an insurer. Attention is also directed to deficiencies in the present insurance accounting system and in financial reporting. The author deals with these matters in the framework of insurance investment regulation. The paper is of value in that the author presents rather unusual and novel concepts as to the purpose of insurance investment regulation and as to present deficiencies and proposed remedies. I happen to agree with much of what the author has said but, on the other hand, I disagree with several of the premises upon which he has constructed his dissertation.

The author points out several problems involving holding companies which he quite correctly exposes to the light of day. He also identifies some of the niceties of reinsurance that are currently attracting the scrutiny of insurance regulators. However, I must confess that I do not share his conclusion that all facets of these problems can be properly resolved solely through the regulation of insurer investments. I agree with a great many of the points that the author makes but I cannot agree that the regulation of insurer investments such as is proposed would resolve the many complex problems involved with upstream and downstream holding companies, deficiencies in uniform accounting and financial statement reporting, and the methods and practices of management in the conduct of an insurance business.

The basic premise of the paper seems to be that "The purpose of regulation of insurance investments is clearly to assure the solvency of insurers." I do not believe that the regulation of insurer investments can be boiled down to that one statement of purpose nor do I believe that this actually states the purpose of investment regulation either in the past or in our current business climate. The regulation of investments cannot, by itself, "assure the solvency of insurers." It is my observation that non-life insurers generally become insolvent as a result of a failure to adequately recognize or disclose reserves for unpaid claims, unearned premiums, and other contractual liabilities. Life insurers become insolvent because of a failure to properly control expenses. Neither of these causes of insolvency can be eliminated by regulation of investments.

In 1965 the Wisconsin Legislature passed legislation setting up the Insurance Laws Revision Committee of the Wisconsin Legislative Council for the purpose of rethinking and rewriting the Wisconsin insurance laws. Spencer L. Kimball, Dean, University of Wisconsin Law School, has been staff director of this project since its inception. The various chapters of the revised Wisconsin Insurance Code typically go through a drafting sequence of a working draft, preliminary draft, first draft, second draft, third draft, and usually a fourth draft, before final action by the Insurance Laws Revision Committee and then consideration by the Legislative Council. After favorable consideration by these committees, the draft is then prepared in bill form for introduction to the Legislature. Dean Kimball has prepared a separate chapter on the regulation of investments that is presently in the third draft stage. In this draft, he suggests that there are four general objectives for the regulation of investments of insurers. Briefly, they are:

1. To seek to prevent incompetent management from making speculative or otherwise unsuitable investments that endanger policyholder interests.
2. To seek to stabilize the financial position of insurers to prevent them from being unduly vulnerable to shifts in economic circumstances.
3. To assert a degree of control with respect to concentration of economic power.
4. To accomplish specific social objectives such as investment in public housing or in urban renewal.

I agree that many statutes are not completely clear in defining solvency or insolvency of an insurer. The regulation for solvency would seem to involve a great many facets of the insurance business other than the mere regulation of investments. It would seem to me that additional matters in the regulation of an insurer for solvency or insolvency include the efforts of the insurance regulator in the areas of uniform accounting; specifications of the format for monthly, quarterly, and annual financial reports; rate regulation; reinsurance contracts; examination of insurers; licensing; and annual review of the performance of management and their methods and practices in the conduct of an insurance business, including the maintenance of the financial solidity of the corporation. There are various tests of performance as respects solvency. When a company fails certain of these tests, or does not show a proper rating by one of these tests, then it is indicated that the company is insolvent. The problem of insolvency is to devise adequate tests to show either insolvency or a predictable trend in that direction. The regulation of investments, while building in safeguards against insolvency, would not in itself prevent insolvencies.

In a technical legal sense, it would appear that a commissioner would have difficulty in going before a court to request liquidation and receivership of an insurer on the basis that the insurer was not solvent because it had not conformed to the requirements of an investment law. I would think that the lawyers would, in general, have to proceed on the more affirmative basis that the insurer was, in fact, insolvent and unable to meet its obligations. In this connection, it is of interest to note the definition of insolvency contained in section 645.03 (14) (b), Wisconsin Statutes, as follows:

"645.03 (14) 'Insolvency' means:

"(b) For any insurer, that it is unable to pay its debts or meet its obligations as they mature or that its assets do not exceed its liabilities plus the greater of 1.) any capital and surplus required by law to be constantly maintained, or 2.) its authorized and issued capital stock. For purposes of this subsection, 'assets' includes one-half of the maximum total assessment liability of the policyholders of the insurer; and 'liabilities' includes reserves required by law. For policies issued on the basis of unlimited assessment liability, the maximum total liability, for purposes of determining solvency only, shall be deemed to be that amount that could be obtained if there were 100% collection of an assessment at the rate of 10 mills."

Chapter 645 of the Wisconsin Statutes is the Insurers Rehabilitation and Liquidation Act which was enacted by the Wisconsin Legislature in the 1967 session and is the work of the Insurance Laws Revision Committee under the direction of Spencer Kimball. This is a comprehensive Act which gives to the Commissioner of Insurance a great number of tools or procedures for coping with the whole spectrum of complex problems in the area of delinquency in insurance companies. I will not attempt to recite the substance of this chapter but I would commend it to all members of the Society for study.

It is not possible for me to attempt a critique of the proposed investment regulation law. I am not familiar with Michigan insurance law, and without having a knowledge and understanding of the context of the law into which the proposed chapter will be inserted it is difficult to formulate valid comments. I note, for example, that the proposed legislation seems not to contain a definition of either solvency or insolvency. Presumably some other statute would contain such a definition.

In summary, I believe that the author has done a service by identifying some significant issues in the insurance business today, and, in any event, his ideas are different and thought-provoking. I agree with the deficiencies he has noted in the accounting and regulatory system that we have. I do not agree that the author has properly identified the basic purposes of the regulation of insurance investments nor would I agree that the author has proposed appropriate solutions to achieve the purposes that he has identified. I believe that the author has oversimplified the many facets of insurer regulation for solvency and solidity and, having done this, he attempts to ascribe too great curative powers to his solution to the oversimplified problem. However, I believe that there is merit in what the author proposes when considered in the more limited context of investment regulation. Within such a framework, his points are worthy of serious consideration.

Actuaries should, on occasion, climb down from their ivory towers and mingle with the natives struggling to keep alive in the jungle down below. Papers such as this and a caustic critique and attendant discussion serve such a purpose and thereby broaden the perspective of insurance actuaries.

DISCUSSION BY CLYDE H. GRAVES

Mr. Bailey, in his paper "Insurance Investment Regulation," has undertaken a large order. He has attempted, as he stated in his introduction, (1) to review the purpose and present method of insurance investment regulation, (2) to describe some of the shortcomings of the present methods, (3) to suggest some principles for achieving the purpose of insurance regulation, and (4) to present suggested legislation designed to remedy some of the present shortcomings.

The discussion of the purpose and present method of insurance investment regulation is much too brief. Mr. Bailey states that "The purpose of regulation of insurance investments is clearly to assure the solvency of insurers." Recently, New York, Wisconsin, as well as Michigan, have restudied the question of investment regulation and in Wisconsin and Michigan bills are currently being considered, while New York has just amended its laws to deal with investment and holding companies. In a draft on "Regulation of Investments" prepared for the State of Wisconsin Legislative Council, it is stated that the laws regulating investments of insurers have a number of objectives and it goes on to mention four: (1) To prevent management from making speculations or otherwise unsuitable investments