STATE OF MISSISSIPPI
OFFICE OF THE COMMISSIONER OF INSURANCE

HOMESITE INSURANCE COMPANY v. MISSISSIPPI WINDSTORM UNDERWRITING ASSOCIATION (MWUA)	**NO. 08-5812**
ONEBEACON INSURANCE GROUP v. MWUA	**NO. 06-5481**
RLI INSURANCE COMPANY v. MWUA	**NO. 08-5813**
ZURICH AMERICAN INSURANCE COMPANY (for itself and its associated and affiliated insurance companies that are members of MWUA) v. MWUA	**NO. 06-5407**
FARMERS INSURANCE GROUP OF COMPANIES (including its subsidiary Foremost Insurance Group) v. MWUA	**NO. 06-5406**
AEGIS SECURITY INSURANCE COMPANY v. MWUA	**NO. 08-5792**

CONSOLIDATED FINDINGS, CONCLUSIONS, AND ORDER

These matters came on for hearing before the Commissioner of Insurance (hereinafter "Commissioner"), through his designee, Lee Harrell, Deputy Commissioner of Insurance, on the 10th and 11th days of December, 2008, pursuant to appeals filed by each of the above-named companies from decisions of the Mississippi Windstorm Underwriting Association (hereinafter "MWUA" or "Windpool"). The specific issues raised by each company will be set forth in more detail below. Having considered all of the testimony and evidence produced by the parties herein, the Commissioner makes the following Findings of Fact and Conclusions of Law, to wit:

Factual and Procedural Background

Pursuant to statute, the MWUA issues property insurance policies in George, Hancock, Harrison, Jackson, Pearl River, and Stone Counties. Miss. Code Ann. § 83-34-3 provides that

the MWUA consists of "all insurers authorized to write and engaged in writing property insurance within this state on a direct basis. Every such insurer shall be a member of the association and shall remain a member so long as the association is in existence as a condition of its authority to continue to transact the business of insurance in this state." Members are assessed monies on a yearly basis to cover the expenses, losses, etc. of the MWUA. Credits are given for voluntary writings in the six coastal counties.

During the assessment process for claims resulting from Hurricane Katrina, the MWUA became aware that some member companies had incorrectly reported their premiums and/or credits, so in January and February, 2006, the MWUA Board allowed companies to resubmit or "true-up" their 2004 reports. Notice was sent to all member companies giving them until March 1, 2006, to submit corrected and/or additional information. (This date would, in effect, allow companies to submit corrected 2004 and 2005 numbers, since the 2005 numbers were already due on March 1, 2006.) The six appeals herein, while raising somewhat different issues in each case, all stem from the above-described assessment process.

All six appeals were filed in a timely manner, and all companies, with the exception of RLI Insurance Company (hereinafter "RLI"), entered into Stipulations with the MWUA regarding the procedural history of each case. Counsel for RLI and MWUA were unable to finalize stipulations prior to the hearings herein, so RLI submitted its "Record Before the Mississippi Department of Insurance" as an exhibit to its Joinder [joining in the appeals of all other insurers herein], setting forth the procedural history of its appeal. Also, each party agreed on the record to adopt the record made by all other parties, in effect creating one consolidated record. This was done, in part, to effectuate the Order of the Chancery Court of the First Judicial

District of Hinds County, Mississippi, entered on May 14, 2008.

The purpose of the Chancery Court's May 14th Order was to consolidate the two appeals filed by Union National Fire Insurance Company (hereinafter "Union National"), as well as to "consolidate all [other pending] appeals and also allow any interested [MWUA] member company to join in this action." In other words, the Chancellor recognized that altering one member company's assessment would have an impact on all the other member companies' assessments, so a plan was devised whereby the appeals pending before the Department could be moved along as quickly as possible, with the ultimate goal of those appeals being consolidated with the appeals currently in Chancery Court. There are a total of eight companies with viable appeals: Union National (two appeals in Chancery Court); United States Fire Insurance Company, A Subsidiary of Crum & Forster Holding, Inc. (hereinafter "Crum & Forster," in Chancery Court), and the six companies herein. The time for appeals has now expired.

Miss. Code Ann. § 83-34-1, *et seq.* are the authorizing statutes for the MWUA. Section 83-34-13 provides that, "Within forty-five (45) days after the passage of this chapter, the directors of the association shall submit to the Commissioner for review and approval a proposed plan of operation. Such proposed plan shall...grant proper credit annually to each member of the association for essential property insurance voluntarily written in the coast area; and shall provide for the efficient, economical, fair and nondiscriminatory administration of the association...Such proposed plan may include...plans for the assessment of members to defray losses and expenses...and for such other provisions as may be deemed necessary by the commissioner to carry out the purposes of this chapter." Pursuant to the above language, the Plan of Operation was duly adopted and approved by the Commissioner on October 1, 1987.

Miss. Code Ann. § 83-34-29 states that, "The association is authorized to promulgate rules for the implementation of this chapter, subject to the approval of the commissioner." The resulting MWUA Manual Of Rules and Procedures (hereinafter, "MRP") was promulgated and approved by the Commissioner on October 1, 1987.

In other words, the aforementioned statutes authorize the overall MWUA and set forth the broad parameters by which same is to be operated. The Plan of Operation, which includes both the Plan of Operation and the Articles of Agreement, refines the parameters of the operation and gives general operating procedures. The Manual of Rules and Procedures[1] gets even more specific and sets forth the guidelines for applications, procedures for processing applications and placing insurance, and the like. More specifics of the operations of MWUA will be provided within, as needed.

Findings and Conclusions

Standard of Review

While the Commissioner has some degree of statutory oversight over certain aspects of the MWUA, these matters were before the Commissioner simply as appeals by Appellants of adverse rulings of the MWUA, pursuant to Miss. Code Ann. § 83-34-19. Further, while the statute provides for an appeal from an order of the MWUA, it and the other insurance laws of the State of Mississippi are silent on the appropriate procedures and standards for review.

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[1]The MRP was revised by the MWUA on October 1, 2007, to make same compatible with the statutory changes that were adopted by the Mississippi Legislature in its 2007 Session, to respond to problems in operations brought to light after Hurricane Katrina. For purposes of this appeal, however, the MRP adopted on October 1, 1987 controls.

Consequently, we adopt the standards set forth in Mississippi State Tax Commission v. Mississippi-Alabama State Fair, 222 So. 2d 664 (Miss. 1969); and Thomas v. PERS of Mississippi, 2005-CC-02184-COA (Miss. Ct. App., June 26, 2007), which are whether the decisions of the MWUA were: 1) arbitrary or capricious; 2) based on substantial evidence appearing in the record; 3) were beyond the power of the body to make; or 4) were violative of some statutory or constitutional right of the Appellants. If all four tests are met, the decisions of the MWUA must be upheld. *Id.* These standards make sense for this type of review in that the process by which the governing rules of the MWUA were established involved an administrative agency, namely the Department of Insurance; these appeals are to an administrative agency; and the MWUA is the body charged with the administration of the Windpool statutes. The MWUA is the entity with the knowledge and expertise in the day to day operations of the Windpool, and it makes sense that those decisions should be afforded great deference.

In cases, such as those herein, where there were no transcripts made and/or no formal hearings below, and, therefore, no testimony to review, the appellate body is permitted to hear testimony and to review the facts *de novo*. However, even though the facts are reviewed *de novo*, the appellate body still gives deference to the overall decision of the underlying agency. See Cook v. Board of Supervisors of Lowndes County, 571 So. 2d 932 (Miss. 1990); Leigh v. Board of Supervisors of Neshoba County, 525 So. 2d 1326 (Miss. 1988); and Mississippi Insurance Underwriting Association v. Standard Products, 271 So. 2d 405 (Miss. 1972).

Finally, there is significant overlap among the issues raised by the parties herein, and many of those issues have previously been addressed by the Department in the orders entered in the Union National and Crum & Forster appeals. There are, however, differing factual issues

raised by each of the parties. Consequently, a section will be devoted to the issues and factual allegations raised by each appellant herein.

Homesite Insurance Company (hereinafter "Homesite")

Specific Issues Raised

1. Not Being Allowed to Claim Credits after March 1, 2006

The primary complaint raised by Homesite was that the MWUA did not allow the Company to resubmit its 2004 numbers after the March 1, 2006 deadline to do so had passed. While there is significant overlap involving the issues, they basically fall into three groups: that said failure violated the Company's due process rights, was beyond the authority of MWUA, and was arbitrary and capricious.

Due Process

In cases of this nature, minimal due process must be afforded, consisting of notice and an opportunity to be heard. *See, e.g., State Oil & Gas Bd. v. McGowen*, 542 So. 2d 244, 246 (Miss. 1989)," as cited in PERS v. Wright, 949 So. 2d 839, 843 (Miss. 2007).

On August 31, 2005, MWUA made its first Hurricane Katrina assessment. Based on the percentages of participation calculated by MWUA, Homesite's share of the assessment totaled $17,450.00, which Homesite paid on September 23, 2005.

On December 2, 2005, the MWUA sent out a second round of assessments to member companies related to Hurricane Katrina claims. Homesite's second assessment was $497,325.00, which it paid on December 9, 2005.

Subsequent thereto, the MWUA was advised by a number of member companies that the

companies' submitted 2004 premium information was incorrect or incomplete. On January 11, 2006, the MWUA Board passed a motion related to Hurricane Katrina assessments, which granted member companies "a single opportunity to submit corrected and/or supplemental information for their 2004" reported direct and voluntary premiums. On January 17, 2006, a letter was sent by MWUA to all member companies stating the above, as well as, "In light of these apparent incorrect premium reports, the MWUA Board of Directors determined it to be equitable and fair to allow all member companies the opportunity to provide any necessary corrections or additions to their 2004 premium reports," with a copy of the Board's motion attached thereto. The motion went on to explain how the resubmission was to be made.

On February 1, 2006, a second letter went out to all member companies from the MWUA, referencing the January 17, 2006 letter, and providing forms for reporting 2004 Net Direct Premiums and 2004 Voluntary Premiums, as well as instructions for filing same. Both letters, as well as the motion, stated that in order to be considered, all corrected information must be submitted to the MWUA no later than March 1, 2006. The sentence, "All reports or information submitted after March 1, 2006 will not be considered," was highlighted in bold and underlined in the February 1, 2006 letter.

On April 17, 2006, MWUA made a third assessment to cover the then $545,000,000.00 in Katrina losses. This assessment was based on the recalculated percentages of participation, prepared after receipt of the corrected/additional information received by March 1, 2006. Homesite was assessed $876,354.00, which it paid on April 28, 2006. On July 6, 2006, Homesite appealed the MWUA assessments to the MWUA Board. Said appeal was amended on December 5, 2007. A final order was issued by MWUA on June 13, 2008, and Homesite

appealed said order to the Department on July 3, 2008.

Homesite alleges that it did not receive either the January 17, 2006, or the February 1, 2006 letter. It admitted that it received the three assessment letters, as well as the March 1, 2006 letter regarding the 2005 Insurer's Report to MWUA, to be used for the 2006 percentages of participation. This March 1st letter stated that said Reports were due by May 1, 2006, and informed member companies that voluntary premiums could be reported either quarterly or annually, but final voluntary writing reports are due March 1 of the year after voluntary premiums were written. This is a standard letter, albeit with some revisions, sent to all companies each year and really had nothing to do with the "true-up" period set forth in the January and February letters; but it is Homesite's position that this is the first time since it became licensed to do business in Mississippi in 2000, that it realized it could take credits for voluntary premiums written in the six coastal counties.

According to Homesite's Brief (Section II, p. 3), "In July 2000, MWUA member company Royal Special Risks Insurance Company was sold by the Royal and SunAlliance Group, Inc. to Homesite Insurance Company. Royal Special Risks Insurance Company was renamed Homesite. MWUA was advised of this on April 12, 2002." This information was confirmed by the Department's records. In 2003, Homesite began writing homeowners insurance for property located in Mississippi.

Joe Shumaker, the current Manager of MWUA, testified at his deposition on September 29, 2008, that the standard procedure when a new company becomes a member of the MWUA was to send them what has been referred to as a "welcome to the Windpool letter," an "undated letter," or simply the "welcome packet." This letter, found at Exhibit 1 to Shumaker's testimony,

discussed how voluntary credits and farm credits should be reported and the time frames for doing so. As was brought out during the December 10, 2008 hearing, Homesite alleges that it never received the welcome packet, and does not have a copy of same; consequently, they had no notice of any of the reporting time frames, or the procedure by which to file for credits. The MWUA's response was that if Homesite did not receive a packet it would have been because they simply acquired the interests of Royal SunAlliance and were not, in the eyes of the MWUA, a new company. As to the mailings of the January 17 and February 1st letters, Joe Shumaker testified at his deposition, and same was reiterated at the December 10th hearing, that said letters were sent to all the companies on the member company list - the same list used for mailing the assessment letters, annual report statements, and the like, and that the addresses on said list were those provided by the individual companies on their annual reports.

Homesite asserts that the reason it did not file for its voluntary credits was because it did not receive the January 17th and February 1st letters, giving companies the opportunity to "true-up" their numbers. Miss. Code Ann. § 83-34-9; Section IX of the MWUA Plan of Operation; and Section VII of the MWUA Manual of Rules and Procedures all state that a member shall receive credit annually for essential property insurance voluntarily written in the coastal counties. If a company is to receive credit annually, it makes sense that somehow the MWUA must be made aware of those credits, also on an annual basis. These documents are publicly available to anyone. The fact of the matter is that even though Homesite had been licensed to do business in Mississippi since July of 2000, and had been writing insurance in Mississippi since 2002 or 2003, it never sought to determine the procedure by which said credits could be taken. Had they read the governing statutes alone, they would have been aware that credits were available and

could have taken appropriate steps to find out more about that subject.

It is the responsibility of the member companies to submit the appropriate documentation to the MWUA to receive credits. Section VIII of the MRP sets out "Accounting Procedures" for both the "Servicing Companies" (those companies writing the actual MWUA policies) and for "Participating Companies" (members of the MWUA by virtue of their writing property insurance in Mississippi). Subparts 2(A) and (B) of the "Participating Companies" section states:

> A. A company shall participate in writings, expenses, profits and losses in proportion that its net direct premium written in this state during the preceding calendar year bears to the aggregate net direct premiums written in this State. Such calculations shall be carried to five decimals.
>
> B. A participating company shall annually receive credit toward participation in the Association for Essential Property Insurance written in the "Pool". Each participating company **in order to receive such credit**, shall set up the necessary statistical procedures whereby they can accurately determine **and furnish to** the Association their voluntary writings. Such information shall be verified to the satisfaction of the Association and shall be submitted in a form mutually agreed on by the Company and the Association. (Emphasis added.)

In other words, it is incumbent on the participating company, if it wishes to receive credits, to set up procedures within the company to "accurately determine and furnish to" MWUA its voluntary writings. The MWUA has no other way to determine what a company's voluntary writings are, unless same are submitted to MWUA by the company.

As stated in previous findings, Hurricane Katrina and its aftermath brought imperfections in the MWUA system into focus, but, as will be discussed further herein, it also shed light on company operational issues as well. Homesite points out that there is no proof that they ever received the January 17th and February 1st letters, and they maintain that they did not receive

same. Homesite concedes, however, that they received the two assessment notices sent prior to January, and the assessment letter sent in April, as well as the March 1, 2006 letter with the annual report forms. Nonetheless, the failure of Homesite to timely file for credits is not due to its not receiving the January and February true-up letters, or even its not receiving the "welcome packet." Homesite knew enough to know that it had to file annual reports of premiums with MWUA, which it did on a yearly basis. The failure was because it did not familiarize itself with the whole of the governing statutes, the Plan of Operation, and the Manual of Rules and Procedures, all publicly available documents. Those documents, by referencing the annual credits available for voluntary writings in coastal counties, would have put Homesite on notice that further investigation into the matter was needed.

MWUA Did Not Have the Authority to Set a Deadline for the Filing of Credits and/or To Deny Credits

The arguments made by Homesite on this point are: 1) receipt of the voluntary premium writings credit is mandated by statute; and 2) because there is no time line or deadline in which to request the credit, the March 1, 2006 deadline for receiving credits exceeded MWUA's authority. If any deadline were to be construed, a reasonable deadline would be three years from the date of filing. These arguments are similar to those previously made by Union National, and the Department will, therefore, refer to its prior rulings on this issue.

Homesite points to the statement found in both Miss. Code Ann. § 83-34-9 and Section IX of the MWUA Plan of Operation, that, "A member shall annually receive credit for essential property insurance voluntarily written" in coastal counties. This representation of what the statute and Plan of Operation say is accurate as far as it goes, but it does not delineate the full

extent of the MWUA's powers.

As stated above, Miss. Code Ann. § 83-34-1, *et seq.* comprise the authorizing statutes for the MWUA, and same provides for the passage of a plan of operation by the MWUA Board. Said Plan of Operation was duly adopted and approved by the Commissioner on October 1, 1987.

Miss. Code Ann. § 83-34-29 states that, "The association is authorized to promulgate rules for the implementation of this chapter, subject to the approval of the commissioner." The resulting MWUA Manual Of Rules and Procedures was promulgated and approved by the Commissioner on October 1, 1987. The MRP, just as do the statutes and Plan of Operation, provides for the giving of credits to member companies. Specifically, the MRP provides that, "Each participating company **in order to receive such credit**, shall set up the necessary statistical procedures whereby they can accurately determine **and furnish to** the Association their voluntary writings."

The phrase, "in order to receive such credit" found in Section VIII (2)(B) of the MRP necessarily implies that if the voluntary premiums are not submitted, then credit cannot be given. In other words, credit will be denied. As to the idea that because the statute does not give a date by which voluntary credits must be reported, the MWUA cannot create one, the authorizing statutes, the Plan of Operation and the MRP all refer to credit being given **annually** [Miss. Code Ann. § 83-34-13; Plan of Operation Section I; MRP VIII (2)(B)]. The Plan of Operation and the MRP also refer to each member company's share of the costs and expenses being assessed based on the net direct premiums written by that member in either the "previous" or "prior" calendar year. *Id.* If all companies are to report their premiums and voluntary writings on an annual basis, and have their assessments based on the previous year's writings, it would be arbitrary and

capricious **not** to have a date certain by which all companies must file, particularly since the assessments are made for each company in proportion to the writings each company has to the total premium written by all member companies the prior year.

It is of interest to note that while Homesite alleges that the MWUA has no authority to set a time limit within which to file credits, it does acknowledge that, "Law and reason dictate that the statutory credit set forth in Miss. Code Ann. § 83-34-9 be given within a reasonable time period." (Brief, p. 22) Homesite then offers it's own ideas of what such a limit should be by urging the adoption of the three year general statute of limitations period.

Homesite continues with its lack of authority argument by asserting that the MWUA did not promulgate any rules regarding time frames within which to file credits, in accordance with the Mississippi Administrative Procedures Act. While the MWUA is a statutorily created entity, it is not an administrative agency and is, therefore, not subject to the Mississippi Administrative Procedures Act. All that is required is that the association submit its Plan of Operation and its Manual of Rules and Procedures to the Commissioner for approval, and this was done. Anything that needed clarification or needed to be made more specific was included in general mailings to the members, such as the information contained in the welcome packet, or the information about the true-up. As brought out during the hearing, the MWUA does not follow state rules on hiring or firing, and has never filed a rule under the Mississippi Administrative Procedures Act. (Hearing Transcript, Vol. I, p. 64)

The MWUA was not required to promulgate its rules through the Mississippi Administrative Procedure Act. Could it have done things better as far as disseminating pertinent information to its members? Probably, but the members themselves bear some responsibility in

knowing and understanding their own obligations and the rules that apply to them. Prior to Hurricane Katrina, the same process had been used to notify members of the various time restraints, filing requirements, and the like, and everyone seemed to understand the process. After Katrina and the resulting extraordinary assessments, the majority of companies still understood the process. The fact that certain companies failed to understand the process did not render the process itself invalid.

Arbitrary and Capricious

The final set of arguments presented by Homesite relate generally to the notion that the decision of the MWUA was arbitrary and capricious. Mississippi courts have defined "arbitrary and capricious" as a "[c]haracterization of a decision or action taken by an administrative agency or inferior court meaning willful and unreasonable action without consideration or in disregard of facts or law or without determining principle. *Black's Law Dictionary* 105 (6th Ed. 1990)," as cited in Miss. Real Estate Appraiser Licensing and Certification Board v. Schroeder, 2007 MSCA 2005-CC-01600-061907 (Miss. Ct. App. June 19, 2007). Further, an " 'arbitrary' act is one 'not done according to reason or judgment' but of the will alone. *Miss. State Dep't of Health v. Southwest Miss. Reg. Med. Ctr.*, 580 So. 2d 1238, 1240 (Miss. 1991)." "A 'capricious' act is one done 'in a whimsical manner, implying either a lack of understanding of or a disregard for the surrounding facts and settled controlling principles....' *Id.*" as quoted in Miss. Real Estate Appraiser Licensing and Certification Board v. Schroeder, *supra*. Finally, if a "...decision is unsupported by substantial evidence, it follows that it is arbitrary and capricious. [citations omitted]." Thomas v. PERS, 2007 MSCA 2005-CC-02184-062607 (Miss. Ct. App. June 26, 2007).

Aside from the overlap with the previously discussed issues, Homesite specifically alleges that MWUA allowed more than one "redo," despite assertions to the contrary, in that it allowed AIG to correct its numbers outside of the process set for other member companies. (Brief, p. 28)

This purported disparate treatment of AIG was previously touched upon in the order entered in Union National's second appeal. Audubon Insurance Company, a subsidiary of AIG (hereinafter, "Audubon"), was the "servicing carrier" for the MWUA, meaning that Audubon handled the administrative tasks such as printing the policies issued by MWUA, keeping up with the data processing, calculating premium taxes on the MWUA policies, keeping up with the MWUA losses by policy year, etc. Audubon did not underwrite the losses on the MWUA policies, did not accept the risk for policies written by the MWUA, and had nothing to do with the allocation of reinsurance proceeds. MWUA alone was responsible for those policies, leading ultimately to the assessments at issue. What the evidence ultimately showed was that Audubon had inadvertently included MWUA policies with its own policies when it reported its total premiums to the MWUA, resulting in an assessment to Audubon of over $33,000,000.00.

Homesite alleges that, "...unlike all the other members, AIG's percentages were reduced on January 26, 2006, before the other members numbers were due, and on January 27, MWUA paid a $31 million refund to AIG." (Brief, p. 29) Further, that the January 11, 2006 Executive Board Minutes show that "Greg Copeland was authorized [by the MWUA Board of Directors] to negotiate with AIG concerning their assessment adjustment and deferral of payments and interest charges by both MWUA and AIG to each other." (Brief, p. 29) These allegations are true, but they do not have the nefarious underpinnings as suggested by Homesite's (and other companies')

briefs.

As set forth above, Audubon did not simply fail to include all of its credits or exclusions as is the case with all the appealing companies. Audubon erroneously included MWUA premiums as their own. The "negotiations" were not for settlement or reduction of disputed amounts, but were related to figuring out the best way to correct Audubon's error while maintaining the necessary cash flow to continue to pay claims. While the complete minutes of the January 11, 2006, MWUA Executive Session can be found at Exhibit 21 to Joe Shumaker's deposition, a more complete excerpt clarifies the point:

> ...It was noted that corrections are needed due to the member companies not properly reporting and not due to MWUA miscalculating the reported premiums. Greg Copeland advised that the statutes only address how the assessment is to be calculated without any deadline for reporting the appropriate premiums. **There is concern that due to delays caused by this incorrect reporting the MWUA could experience serious cash flow problems.** Chairperson Brouse provided each member a copy of a proposed motion allowing a one time opportunity for member companies to correct any reported or unreported voluntary writings. A copy of this proposal is attached to and made a part of these minutes. Greg Copeland informed that one of the major issues in any proposed readjustment is the fact that American International Group (AIG) reported the premiums written in the MWUA and serviced by their subsidiary Audubon Insurance Company. This has generated an assessment to AIG of over $33,000,000.00 which is primarily due to MWUA premiums. Greg Copeland suggested that a correction for AIG be allowed as the courts would almost certainly rule in their favor. If AIG is allowed to adjust their report of premiums then other companies must be allowed as well and he suggest [sic] following the guidelines set forth in the attached proposal for adjusting reported premiums in Hurricane Katrina assessments. It was noted that the forms for reporting of premiums should be revised to reflect all the details needed for calculating assessments. After a brief discussion it was the consensus of the Board that AIG should have either excluded MWUA premiums or received credit for voluntary

> writings for those premiums. **Greg Copeland was authorized to negotiate with AIG concerning their assessment adjustment and deferral of payments and interest charges by both MWUA and AIG to each other.** (Emphasis added.)

When the error was discovered in late 2005, it was corrected during the true-up period, along with all the other corrections, as was offered to every other member company. As pointed out at the December 10th hearing, had it not been corrected, Audubon would have been entitled to receive credit for all the MWUA premiums at 140%, since MWUA only writes in the coastal counties, thereby increasing the other companies participation percentages. They would also have charged back to MWUA any assessments made against it, and MWUA would have had to include same in the assessments against other companies.

There is nothing in the record to indicate that Audubon was given special treatment or allowed to do anything that any other member company would not have been able to do had the same error occurred. All corrections were made within the same "true-up" period given to all member companies.

The final contention under this section is Homesite's allegation that, "The entire assessment process failed to ensure that all members properly reported their credits." (Brief, p. 30) The basic argument is that the MWUA does not audit member assessments to see if they are accurate, and that, "MWUA never noticed that Homesite was not claiming its voluntary credits."

As to the lack of auditing procedures, it is incumbent upon the member companies to "accurately determine and furnish to the Association their voluntary writings." [MRP 8(B)] Joe Shumaker testified at his September 29th deposition that the MWUA does compare the numbers submitted to it by the member companies with the numbers submitted by each company to the

Mississippi Insurance Department on its annual report; and it also does a spot check or spot audit of the bordereaus or declaration pages sent in with a company's voluntary writings. If a discrepancy is found, or a question arises, the MWUA may also contact the company and ask for additional information. Any further "audits" of the numbers submitted by member companies would still be based on what the company submitted, absent a full-blown financial examination, and would only serve to raise the costs of operation of the MWUA.

Related to MWUA's not noticing that Homesite was not claiming its voluntary credits, as stated, it is incumbent upon each company to correctly report their numbers and take whatever credits to which they may be entitled. Whether Homesite had any credits to claim was not information the MWUA would have. Also, some companies consciously choose not to report credits. As brought out at the December 10th hearing, if a company does not file credits, it pays a larger proportion of any assessment than it would if it had claimed the credits; but conversely, it would also receive a larger share of the profits in years with no hurricanes. Since there has been a profit in most years, some companies choose not to file credits. There was no way for MWUA to know if Homesite had credits or if it had voluntarily chosen not to file them.

When looking at the issue of whether the actions taken by the MWUA herein were arbitrary and capricious, the circumstances must be viewed as a whole. The situation at the time the assessments were made was different than at any other time in the MWUA's history. There were $545,000,000.00 in outstanding claims which had to be paid. While there were previous assessments made on MWUA members, there had never before been anything like Hurricane Katrina. Companies that had never worried too much about whether they had taken all the credits due them were now scrambling to find a way to reduce million, or even multi-million,

dollar assessments. Because the assessments were necessarily so large, the MWUA board looked for a way to be as fair as possible to all member companies, so it allowed all member companies to do one last "true-up" - one last submission of the correct numbers. Not everyone was happy before the true-up, and not everyone was happy after the true-up. The fact that there were operational issues in the pre-Katrina system that were not brought to light except in the wake of Hurricane Katrina, does not, therefore, mean that the original procedures used since the inception of the MWUA were arbitrary and capricious. What it means is that issues were uncovered that should be, and are being, addressed on a go-forward basis, but that should not negate all that was done in the past.

2. Group Reporting Violated MWUA's Governing Statutes

Homesite next argues that MWUA's allowing members to submit the financial data of affiliated companies on a group basis, instead of as individual companies, violated the governing statute.

From 1971 until the end of 2006, the MWUA (and its predecessor) had allowed companies to "group" (allow affiliated companies to report financial data and pay assessments on a group, as opposed to an individual, basis) their reported numbers. Prior to October, 2006, when the MWUA attorney advised the Board that they may not have the authority to allow grouping, no one had complained about the procedure, in part because the practice encouraged voluntary writings on the Coast.

It is important to note that the statute in question, Miss. Code Ann. § 83-34-9, does not specifically prohibit the grouping of premiums. That section states, in relevant part, as follows:

A member shall, in accordance with the plan of operation, annually

> receive credit for essential property insurance voluntarily written in a coast area, and its participation in the writings of the association shall be reduced in accordance with the provisions of the plan of operation. Each member's participation in the association shall be determined annually in the manner provided in the plan of operation.

Prior to October, 2006, members were given credit for voluntary writings on the coast. Nothing specifically required that credits given be from an individual company, and "each member's" participation was determined annually.

When counsel for the MWUA brought to the Board's attention in October, 2006, that he believed the Board did not have the authority to allow grouping, the Board chose to follow counsel's advice, and not allow the practice on a go-forward basis. To that end, letters were sent on November 7, 2006, advising members who had been grouping that they would need to revise their numbers on the 2006 report, and would need to report by individual company, and not on a consolidated basis.

Homesite asserts that because grouping was not specifically authorized by the statute, allowing companies to report on a consolidated basis violated Homesite's statutory rights, as well as its due process rights. The remedy sought by Homesite for the perceived wrong is not to reopen all the numbers, but only to reopen those for the years 2004 and 2005, the years in which Homesite failed to timely report its credits.

At the December 10th hearing, MWUA counsel argued: 1) the companies who filed as a group are not all represented at this hearing, and they have due process rights, too. They relied on the ability to group and defined their voluntary writing strategy relying on that fact, and to retroactively undo grouping would violate their due process rights; and 2) a residual market's

(such as MWUA) number one goal is to depopulate the plan, and grouping helped do that.

For the above reasons, the Commissioner hereby finds that the allowing of grouping for the thirty-five or so years prior to October, 2006, was not an unreasonable interpretation of the above statute, and was, therefore, not violative of Homesite's statutory rights. It is interesting to note that on March 22, 2007, the Mississippi Legislature amended Miss. Code Ann. § 83-34-9 to specifically allow grouping.[2]

3. Allocation of Reinsurance Proceeds

Reinsurance, as the name suggests, is a type of insurance that an insurance company buys to protect itself and to help offset losses that the company may sustain from paying out claims. In this case, the MWUA had purchased $175,000,000 worth of reinsurance which was used to help cover Katrina claims of $700,000,000. This meant that the MWUA only had to assess its members $545,000,000, instead of the entire $700,000,000, to cover those claims, as well as other expenses.

Pursuant to Miss. Code Ann. § 83-34-9, "All members of the association [MWUA] shall participate in its writings, expenses, profits and losses in the proportion that the net direct premiums of each such member written in this state during the preceding calendar year bears to the aggregate net direct premiums written in this state by all members of the association... Each member's participation in the association shall be determined annually in the manner provided in

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[2]Miss. Code Ann. § 83-34-9(1) states, "All assessable insurers of the association shall participate in regular assessments levied by the association based upon their percentage of participation. The association may allow affiliated insurers to combine their annual net direct premiums and other data, including data that supports any incentives that may be allowed by the association, to the extent that such grouping promotes the voluntary writing of essential property insurance in the coast area. Any provisions for credits and grouping of data shall be prescribed in the plan of operation."

the plan of operation." (Emphasis added.) Companies must report their written premiums to the MWUA on a calendar year basis, in part, because it gives a uniform time period within which all companies must report their premiums, and it allows a uniform period within which to calculate the relative percentages of participation of each company.

While the assessments made against member companies are based on premiums written during the preceding calendar year (January through December of a given year), each calendar year contains two "policy" years. Consequently, premiums written during calendar year 2004 include premiums from policies issued in both 2003 and 2004. [A policy year is the year in which a policy was issued. For example, Hurricane Katrina struck Mississippi on August 29, 2005, which means that the policies covering Katrina losses could have been issued anytime between August 30, 2004 and August 29, 2005. Those policies written in 2004 would be part of the 2004 policy year, and those written in 2005 would be part of the 2005 policy year. This includes policies issued by the MWUA.]

Because the losses sustained as a result of Hurricane Katrina covered two policy years, no one disputes the fact that the reinsurance proceeds could be allocated between the two covered policy years. What Homesite is contesting is *how* the proceeds were allocated. Homesite contends that because the greater proportion of the loss was sustained in policy year 2005, the greater proportion of the reinsurance proceeds should have been allocated to 2005. This contention is based on the arguments that: 1) because participation rates change from year to year, how the reinsurance is allocated impacts the amount of the assessment to be paid by each company; and 2) industry accounting standards dictate that reinsurance recoveries should match the underlying liabilities.

It is true that participation rates can change from year to year, but this is always true. As testified to during the Union National hearing, those changes are usually rather small. In Homesite's case, its participation percentage in the 10% assessment went from 0.071% in the August 2005 first assessment to 0.075% in the third assessment made in April 2006. Its participation in the 90% portion of the assessment went from 0.186% in August, 2005 to 0.275% in April, 2006; an increase of 0.089%. This increase had a greater impact on all companies, not just Homesite, than it normally would because of the huge losses sustained in Hurricane Katrina.

As to the second argument regarding industry accounting standards, Homesite asserted that Jim Redd had testified that the MWUA followed the PIPSO manual, and PIPSO recognizes the National Association of Insurance Commissioners (NAIC) as the authority for accounting principles. The NAIC Accounting Practices and Procedures Manual states that "reinsurance recoveries should match the underlying liabilities." The NAIC also requires that insurance companies use statutory accounting principles, thereby leading Homesite to conclude that the MWUA had done the allocation incorrectly.

The MWUA allocated the reinsurance proceeds as it did, first, because that was the precedent that had been followed throughout its history, and second, to eliminate the need for an assessment to member companies in 2004, an objective that was met.

Prior to the issue being raised by Union National in its hearing, no one had ever questioned either the allocation of reinsurance or the MWUA's accounting principles. Mr. Redd's testimony was that at the time the allocation was made, he spoke with persons from the MWUA's outside accounting firm [Harper Rains Knight & Co.], as well as representatives of PIPSO (Property Insurance Plans Service Organization) who both advised that the allocation was

acceptable. Further, the MWUA had yearly audits performed by Harper Rains Knight & Co., and has been examined by the Department of Insurance, and the allocation of the reinsurance proceeds was never questioned. After Union National filed its appeal on the reinsurance issue, the MWUA sought opinions from "accountants and others" on whether or not they had used the correct method to allocate the reinsurance, with the result that, "No one has been able to come up with a method. Everyone has told us that it is an internal decision by the board of directors." These facts were reiterated at the December 10th hearing.

The most important point in this discussion, however, is the fact that **there is nothing in any statute or regulation that mandates what type of accounting should be used by the MWUA.** Every witness who has testified on this issue, including James Collins, President of Union National; Joe Shumaker, Manager of the MWUA; Jim Redd, the former head accountant for the MWUA; and even Clem Dwyer, the expert witness proffered by Union National in its appeal, agreed that no particular type of accounting was mandated by statute or regulation.

The MWUA Board at some point made an internal decision to operate on a "modified cash basis" method of accounting. While a specific date upon which such a decision was made was not presented, the testimony was clear that the MWUA (and its predecessor) consistently used that accounting method throughout its history. Homesite, and other companies, certainly have their own opinions about how the reinsurance proceeds should have been allocated, based in part upon accounting procedures utilized by insurance companies. The problem with this opinion is twofold. First, the MWUA is not an insurance company, but a residual market - an insurer of last resort. Second, Homesite is not entitled to substitute its judgment for that of the MWUA simply because it disagrees with the MWUA position, or because there might have been

a different allocation methodology. The MWUA operated under the same accounting procedures since its inception, and it allocated the reinsurance proceeds as it had always done.

MWUA's allocation of reinsurance proceeds for policy years 2004 and 2005 was not arbitrary or capricious, was reasonable under the circumstances, and was well within the prerogative of the MWUA.

4. Misreporting of Mobile Home Premiums

Homesite's next argument relates to the misreporting by some companies of mobile home premiums as automobile insurance rather than homeowners insurance, which they allege caused "an understatement of their participation and further miscalculation of 2004 and 2005 assessments." This argument was made by Union National and was evidently raised in response to Bulletin 2006-6 sent out by the Mississippi Insurance Department on May 16, 2006, clarifying that premiums for mobile homes at fixed locations should be reported on the "Homeowners Multiple-Peril" line and not on the "Auto Physical Damage" line on statutory financial statements, and that if any company had failed to properly report such premiums, they should submit amended annual financial statements for the years 2004 and 2005.

This issue came up during Union National's first appeal, and at that time the parties were advised that this was not actually an MWUA issue, but it was something being looked into by the MID. During the hearing on Union National's second appeal, because MID's handling of the matter had not yet been concluded, there was no real testimony presented on the misreporting issue. It was, however, Union National's position that until it knew how much money was involved, and the percentage of total premiums that amount might represent, it could not really state what the overall impact would be. It could decrease the participation rates for companies

who reported correctly, or it could increase participation rates for those companies. Homesite's position is that all member companies who improperly reported their mobile home premiums should have to resubmit the correct numbers and the 2004 and 2005 assessments should be recalculated using the correct information. MWUA's position was, and is, that since the MID was handling this matter, any monies recovered would be used to pay Hurricane Katrina losses over $700,000,000, or if the losses were less than $700,000,000, any funds recovered would be included in the amount of money to be reimbursed to MWUA's member companies on a pro rata basis. In either event, there would not be a need to reopen the assessments in order to adequately deal with any recovery.

The issue of the purported misreporting of mobile home premiums is still under review by MID, and has not been concluded. While significant progress has been made by MID, it is the opinion of the Commissioner that this issue is not ripe for review.

5. Privilege Tax

In previous briefings, Homesite has argued that the MWUA assessment was actually a privilege tax and should be addressed utilizing the statutes related to such taxes. That argument did not appear in the final briefing, but to the extent that it remains an issue, the Department already ruled in the Union National case (second appeal) that:

> This issue was raised in Union National's first appeal, and the Commissioner found that "the assessments charged to member companies are a cost of doing business" and "do not constitute a 'privilege [tax]'," as same are "not assessed by virtue of the issuance of a privilege tax license and are not imposed for the 'privilege of engaging or continuing in the business' set forth in the statute, (See Miss Code Ann. § 27-15-11.)" Further, as required by the above statute, as well as by Miss. Code Ann. § 27-73-1, cited by Union National, said assessment was not paid to either the

> "Auditor of Public Accounts", the "State Tax Commission", or the "Commissioner of Insurance", rendering those code sections inapplicable. The Commissioner therefore reiterates the finding that the assessment imposed by the MWUA on Union National , and other member companies, was not a privilege tax.

The Department, therefore, reiterates that position herein.

One final observation. Homesite began its argument stating that, "With all these arguments swirling and the contentions back and forth and the positions of all the parties, I think the one thing that is unquestionably true, no matter what position you take in this case, the one thing that is unquestionably true, the assessments by the MWUA are wrong." (Hearing Transcript, Vol. I, p. 11) This position was also adopted by RLI in Hearing Transcript, Vol. II, p.15. The Department does not agree with this position. The calculations performed by MWUA were done correctly, utilizing the numbers submitted by each company to MWUA. As stated by counsel for MWUA, what the parties are actually saying is that, "...if you take this late filed information and you accept it, then they [the calculations] are inconsistent with the late filed information." (Hearing Transcript, Vol. II, p.66) That is one of the main issues presented in these appeals - should the MWUA have accepted the late filed information and recalculated the participation percentages using said information. It does not, however, follow that the calculations performed were performed incorrectly.

OneBeacon Insurance Group (hereinafter "OneBeacon")

As stated in both its Brief and by counsel at the December 10, 2008 hearing, OneBeacon has only one issue on appeal: That it was not given its exclusion for farm property as mandated by the statute, and the only reason that it did not get said exclusion was because the procedures

by which those credits were attained were not properly made available to member companies.

Mr. Andy Borst, the Chief Financial Officer, Specialty Lines, testified on behalf of OneBeacon, that he first became involved in this matter after receipt of the second Hurricane Katrina assessment in December of 2005. The first assessment made in August 2005, was for $87,980.00. The second assessment was made in December, 2005, for an additional $2,507,430.00. Because of the large amount of the assessment, and because he was the product manager for the agricultural business of OneBeacon and the assessment would affect his spreadsheet, Mr. Borst was contacted, even though he is not typically the person in the company who handles Windpool matters.

Mr. Borst was, at that time, located in Lenexa, Kansas. He got in touch with the company controller who was located in Boston, Massachusetts. He testified that he read the MWUA statutes and the Plan of Operation and found that there was an exclusion for farm property, but he did not know how farm property was defined or how one went about claiming the exclusion. He ultimately decided to call the Windpool directly, which he did on December 29, 2005. He spoke with Albert Parks, the then-manager of MWUA, who transferred him to Jim Redd, the Chief Accountant for the Windpool. Borst told Redd that he was trying to understand what the exclusion for farm property was. Redd told him the definition of "farm property." Borst responded that, "It sounds like we have some of that. What do we do?" Jim Redd purportedly looked at the statement OneBeacon had filed and told Borst that OneBeacon had filed it [the 2004 Insurer's Report] correctly.

Even after he spoke with Jim Redd, he still was not convinced that OneBeacon had gotten credit (actually an exclusion) for farm property, so he contacted Natalie Greene in OneBeacon's

legal department in Boston. As shown by e-mails submitted as part of the hearing record, Ms. Greene contacted Cecil Pearce, Counsel for the American Insurance Association (AIA), who, in turn, contacted Greg Copeland, counsel for MWUA, concerning the definition of farm property. On January 30, 2006, Copeland responded to Pearce by e-mail, providing the definition requested. According to the testimony of Mr. Borst, he does not know if that information was shared with Natalie Greene, and he did not hear back from her on the subject.

In March, 2006, he was contacted by the controller who said they had missed the deadline to resubmit premiums. Borst again called the Windpool and arranged to meet with Jim Redd and Albert Parks in person on April 20, 2006, along with Natalie Greene. At this meeting, he was given a Statement of Participation, which clearly showed that OneBeacon's farm property premiums were not being excluded, as well as a copy of the welcome letter, which defines farm property, gives the filing dates, and the like. This was the first time that Borst had seen either of these documents. He testified that if he had had these back in December, 2005, the proper filings would have been made in order to obtain the exclusions.

There was a good bit of testimony related to Mr. Borst's conversation with Jim Redd in December of 2005, wherein Mr. Redd told Borst that, "You filed the statement correctly." (Hearing Transcript, Vol. I, p. 79) However, even Mr. Borst agreed that the form he and Mr. Redd were discussing on the phone does not specifically address reduction for farm property, and that Mr. Redd's assessment that the form they were discussing had been filled out correctly, was accurate. (*Id.* at 98)

As mentioned earlier, this is one of the cases in which certain operational issues of the company were also brought to light in the aftermath of Hurricane Katrina. As was elicited on

cross-examination, at the relevant times herein, Mr. Borst was working in the Lenexa, Kansas office, while the controller and the Company's legal counsel were in Boston. All correspondence from the MWUA to OneBeacon went to the Boston office, and Borst testified that he was not the one who received same, and he was not the one who dealt with such correspondence on a day-to-day basis. (*Id.* at 97, 103) (There was no testimony as to by whom such correspondence would have been received.) Mr. Borst further testified that he was not the person who prepared the annual Insurer's Report (*Id.* at 116), and he did not know if the years prior to the 2006 Statement of Participation also showed zero farm property premiums. (*Id.* at 105) He stated that when he saw the zero on the 2006 Statement it immediately caught his attention, and if it had shown zero in the prior years it should have come to someone's attention, if that person was aware of how much farm premium was written. (*Id.* at 107) There was a good bit of effort put into finding out how to properly file for the farm property exclusion, but it was not a concerted effort, and there was certainly no urgency to the process until after the company discovered that the deadline within which to correct its previous filings had passed. While there is nothing inherently wrong with the system that OneBeacon had in place, it highlights, once again, the fact that prior to Hurricane Katrina, companies were not as interested in the credits or exclusions to which they were entitled as they were after Hurricane Katrina struck.

OneBeacon argues that since premiums on farm property are expressly excluded from the definition of "net direct premiums," the numbers on which assessments are based, then MWUA is mandated to exclude such premiums and has no authority to deviate from the statute. What this argument ignores is that fact that no definition of "farm property" is provided in the statute, and no method is provided by which same should be calculated and reported in order to

effectuate the exclusion. Even Mr. Borst agreed with MWUA counsel on cross-examination that in order to give a reduction in premium for farm property, there has to be a definition of farm property, and that it was appropriate for the MWUA Board to create such a definition. (Hearing Transcript, Vol. I, p. 102)

Along with the definition, the Board also created the process by which such exclusion could be obtained including the submission of policy pages and a deadline for filing, which was 60 days after the end of each quarter. This definition and process were set out in the welcome packet sent to all companies when they joined the MWUA, as well as being set out in Bulletin 88-4, which is the method used by MWUA to notify members of various information. (Hearing Transcript, Vol. I, pp. 102, 124) Stipulation of Fact # 36 between MWUA and OneBeacon states, "In order for farm property writings to be credited against net direct premiums, MWUA's practice was to require the submission of copies of the policies for all farm property writings that cover the perils of windstorm and hail in the entire state of Mississippi. MWUA's practice was that copies of farm property writings were required to be submitted to MWUA's office on a quarterly basis within 60 days of the end of each quarter."

In order to be able to take the exclusions set out in the statute, there must be a process detailing how the exclusions may be claimed. OneBeacon would have us adopt the position that there need not be procedures or time frames for claiming the farm property exclusion - if a company has farm property premiums, they may exclude those from net direct premium at any time and in any manner. However, the MWUA, under its authority to take the actions necessary to effectuate the purposes of the governing statues, adopted the aforementioned procedures. Prior to Hurricane Katrina, the same process had been used to notify members of the various time

restraints, filing requirements, and the like, and everyone seemed to understand the process. After Katrina and the resulting extraordinary assessments, the majority of companies still understood the process. The fact that certain companies failed to understand the process did not make the process itself invalid.

Finally, OneBeacon admits that prior to May 4, 2006, when it made its corrected filing for the farm property exclusion, it had not complied with the established procedures and requirements to obtain such exclusion. Since documentation of farm property writings must be submitted no later than 60 days after the end of each quarter, the deadline for 2004 writings was no later than March 1, 2005. However, as per the January 17, 2006 and February 1, 2006 letters related to the "true-up" period, OneBeacon could have corrected those numbers anytime before March 1, 2006. While OneBeacon claims the March 1, 2006 deadline only applied to changes in the reporting of net direct premiums and not to farm property exclusions, since farm property premiums are, by definition, a reduction of net direct premiums, the March 1, 2006 deadline by which to correct premiums did apply to OneBeacon. OneBeacon did not file corrected numbers until May 4, 2006, and was, therefore, denied the exclusion.

MWUA had the authority to create the processes and deadlines related to the reporting of farm property premiums, and since OneBeacon did not comply with same, MWUA was justified in denying the exclusion.

RLI Insurance Company (hereinafter "RLI")

To the extent that RLI addresses issues such as not being able to file corrected numbers after the March 1, 2006 true-up deadline, or that MWUA had no authority to impose the thirty

day March 1, 2006 deadline in the first place, those issues are addressed elsewhere in these findings, and the Department adopts those findings here, as well.

The two main issues raised by RLI relate to due process concerns: 1) that RLI should have been allowed to submit its corrected numbers because a valid appeal by RLI was pending before MWUA; and 2) RLI was never afforded a hearing before the MWUA Board, as requested.

On December 2, 2005, MWUA made the second round of assessments for Hurricane Katrina losses of $285,000,000.00. RLI was assessed $959,880.00, as its share of those losses. In response, RLI sent a letter to MWUA on December 16, 2005. The subject line of said letter read, "Appeal of Windstorm Assessment." It is at this point that the process became a bit less clear.

First, RLI alleges that once it filed its December 16, 2005 appeal, the MWUA took no action on that appeal. However, MWUA alleges that a careful reading of RLI's December 16th letter reads more like a request for information and/or clarification than an actual "appeal." Consequently, in response thereto, Albert Parks, the then-manager of the MWUA, called RLI, answered its questions, and thought the matter had been resolved; so much so that he never informed legal counsel of the "appeal." The first time counsel knew of the December 16th appeal was during the discovery process sometime in 2008. Also, as a result of Mr. Park's conversation with RLI, on January 3, 2006, RLI paid the $959,880.00 second assessment to the MWUA. [Deposition of Joe Shumaker, Ex. 16(A-2)]

Second, RLI stated in paragraph 3 of its Notice of Appeal to the Commissioner of Insurance, filed on July 14, 2008, "While the appeal of its assessment remained pending, RLI submitted additional information that was relevant to its appeal." At the December 11, 2008

hearing, counsel for RLI stated that after the December 16, 2005 "appeal" was filed, "They [RLI] continue filing documents," and "...they continue to file the forms as they are required." (Hearing Transcript, Vol.II, p. 8)

In the meantime, the MWUA Board voted to authorize the "true-up" and letters were sent to all MWUA members on January 17, 2006 and February 1, 2006, giving members until March 1, 2006 to submit corrected and/or supplemental information related to their 2004 premiums.

As testified to by Chris Randall, Vice President of Actuarial Services for RLI, RLI received the January and February letters. In response to the January 17th letter, Brad Bernier, the person at RLI who routinely handled Windpool matters, reviewed RLI's credits and made "a slight, small change to the credits...So he briefly filled that out and felt he was done." (Hearing Transcript, Vol. II, pp. 52-53) He sent the form back within the true-up period: "Mr. Bernier [and therefore, RLI] was aware of the window and he did take advantage of it to the best of his abilities and knowledge." (*Id.* p. 53)

After the period within which to submit corrections and/or supplemental materials had expired, the MWUA recalculated the companies' participation percentages and new assessments were issued on April 1, 2006, based on losses of $545,000,000.00. RLI's total assessment at this point was $2,349,986.00, less the $993,560.00 already paid, for an additional total due of $1,356,426,00. It was at this point that Chris Randall became involved in the process, and according to Randall's testimony, RLI "started looking at the net direct premium form." (Hearing Transcript, Vol. II, p. 28) He prepared the PowerPoint presentation presented at the hearing to show, in part, "...what we feel was a mistake made in filing the form, and how we tried to correct it." (*Id.* p. 30) He agreed that the original submission needed to be corrected. *(Id.* p. 38)

On May 16, 2006, RLI appealed the third assessment by filing its "Appeal of Windstorm Assessment" with the MWUA. This "second" appeal referenced the December 16, 2005 appeal.

In light of the above, and as will be discussed further, the Department finds that the "appeal" filed by RLI on December 16, 2005, was not "pending" such that RLI's responsibility to meet the terms of the January 17, 2006 and February 1, 2006 letters was alleviated. Assuming that the December 16th letter was a bona fide appeal of the second assessment, it was first addressed by Albert Parks telephonically. Indeed, a careful reading of that letter, while styled as an "appeal" and stating that RLI "hereby appeals this assessment," primarily deals with questions of how the assessment was calculated, why the assessment was so high, and how credits were obtained and applied - all questions easily answered in a telephone conversation. RLI did not allege that the numbers it had previously reported were wrong. The Board then went on to pass the January 11, 2006 "Motion Concerning Hurricane Katrina Assessments," which was attached to the January 17th letter. Both the motion and the January 17th letter acknowledged that there were errors made by some companies in reporting, and, therefore, possibly errors in the assessments, and that the companies could submit corrected and/or supplemental information to MWUA **by March 1, 2006**. At that point, new calculations would be made, and corrected assessments issued, where necessary. In fact, RLI took advantage of this period to correct its own numbers and made changes to the credits reported. RLI got its questions answered and steps were taken by the MWUA to correct any errors. RLI's concerns were, in fact, heard and addressed by the MWUA.

The filing of an appeal does not stay all actions of the Windpool with respect to RLI. Even if RLI had concerns remaining after the conversation with Albert Parks, the January 17th

and February 1st letters should have put RLI on notice that any appeal it had was mooted by the imposition of the true-up. Both letters clearly state that any corrected and/or supplemental information must be submitted no later than March 1, 2006, and that new calculations would be performed by April 1, 2006, and new assessments made thereafter.

RLI alleges that after the December 16, 2005 letter was sent to MWUA, they continued to make filings and ask for help (Hearing Transcript, Vol. II, p. 23); however there is nothing in the record to indicate that between December 16, 2005 and April 2006, RLI did anything to further its appeal. RLI did send corrected information to the Windpool by facsimile on May 3, 2006. [Deposition of Joe Shumaker, Exhibit 15(A)] The facts indicate RLI behaved in a manner contrary to the existence of a pending appeal: it allegedly made continued filings with the Department; it paid the assessment owing after the conversation with Albert Parks; and it participated in the true-up by making corrections to its filed credits. RLI's merely referencing the December 16, 2005 appeal in its May 16, 2006 appeal does not change the fact that the subject matter of the December appeal had already been addressed.

RLI next points to the fact that it was never given a hearing on its May 16, 2006 appeal. After the time within which to file corrected and/or additional information had passed, participation percentages were recalculated, and the third set of assessments went out on April 1, 2006. RLI filed its appeal with the MWUA by letter dated May 16, 2006. Said letter included additional and corrected information and calculations not previously presented to MWUA. No hearing was specifically requested; RLI simply requested that, based upon the additional information submitted, that its second and third assessments should be reduced accordingly. RLI also included a check for the amount it felt was the correct amount of assessment still owing;

specifically, $178,254.00 instead of the $1,356,426.00 MWUA said was due.

Section VIII (1) of the MWUA Plan of Operation dealing with "Appeals" states that, "The Board or an Appeals Committee designated by the Board shall hear and determine such appeal [appeals filed by an affected insurer] within fifteen days after same is filed." Similar language is found in Section IX (1) of the MWUA Manual of Rules and Procedures. The term "hearing" is not defined anywhere in the governing statutes, the Plan of Operation, or the Manual of Rules and Procedures. The Windpool readily admits that it did not meet the fifteen day requirement, "Not even close," due in part to the massive number of claims that were coming in. The MWUA Board chose to deal with the immediate needs of policyholders and getting claims paid over holding hearings on appeals. Given the almost total chaos that Hurricane Katrina wreaked in the lives of those on the coast, this was not an unreasonable position for the MWUA to have taken. RLI has not alleged any specific prejudice suffered by its not having had a hearing within the fifteen day period and we find that issue to be without merit.

As to the issue of holding a hearing at all, counsel for MWUA stated at the December 11, 2008 hearing that, "The Board did stop holding, you know, presentation hearings...They took it on the written record...they had the written record in front of them. Had they had anymore [sic] questions, they would have submitted them." (Hearing Transcript, Vol. II, p. 19) In its Brief, MWUA stated that, "...all appeals were considered by MWUA and decisions were reached on each after submission of materials and information," (p. 21) and, "There is no basis in the Plan of Operation for a trial or even a 'hearing' as apparently contemplated by some of the appealing companies. The Plan requires only that the MWUA Board 'hear and determine' the various appeals...The issues presented by the companies regarding their appeal were presented to the

MWUA Board. After consideration of these issues, the MWUA Board denied the appeals." (p. 22) As stated earlier, all that is required to satisfy due process in these type matters is notice and a opportunity to be heard, which was afforded to RLI, albeit perhaps not in as formal a manner as RLI would have preferred.

As testified to by Chris Randall for RLI, "The third assessment was significant enough that it brought attention to other people within the company, and they started looking at the net direct premium form." (Hearing Transcript, Vol. II, p. 28) He did not begin looking at the numbers until April, 2006, after the third assessment was made. This is exactly the same fact pattern that both the MWUA and the Department addressed in the Union National case. In Union National, the company admitted receiving the January 17th and February 1st letters concerning the opportunity to submit corrected and/or additional information. The person at the company who dealt with those letters thought the information submitted was sufficient, but when the third assessment came, the matter was sent to someone higher up in the company who, after further investigation, discovered that errors had been made. Corrections were submitted after the March 1, 2006 deadline. MWUA has consistently ruled that information related to 2004 premiums submitted after the March 1, 2006 deadline would not be considered.

Finally, the MWUA Board actually ruled on RLI's May 16, 2006 appeal at the June 2, 2006 Board meeting, denying same (see Shumaker Deposition, Ex. 22), but this fact was not communicated to RLI until June 13, 2008. Despite the fact that this should have been communicated by MWUA to RLI promptly, there has been no specific allegation of prejudice caused by the delay in communication, and we hereby find that none exists, particularly in light of the fact that from May 16, 2006 to mid-2008, RLI did nothing to check on the status of their

appeal (Hearing Transcript, Vol. II, p. 62), and did nothing to advance the prosecution of same.

Zurich American Insurance Company (hereinafter "Zurich")

There are three issues raised by Zurich that will be addressed herein: 1) recusal of Lee Harrell as the Hearing Officer; 2) the MWUA had no authority to order the original "true-up" or submission of corrected and/or additional information; and 3) even if the MWUA was authorized to reopen the reporting period, the process was arbitrary and unfair.

Recusal of Lee Harrell

Preliminary to its argument at the December 11, 2008 hearing, Zurich moved that Deputy Commissioner Lee Harrell recuse himself as the Hearing Officer herein, on the basis that he was in attendance at the January 11, 2006 MWUA Board meeting, and present during Executive Session, wherein the Board voted to authorize the "true-up" as well as the "so-called data modification" for AIG. Further, that he, "...apparently spoke in favor of the motion to allow...the true-up [which] raises an appearance of perhaps a lack of independence." (Hearing Transcript, Vol. II, p. 75) MWUA counsel responded that the only statement attributed to Mr. Harrell in the minutes was that, "Lee Harrell advised he believes there are several companies other than those represented at this meeting that have reported incorrectly and if given the opportunity would submit corrected premiums." (*Id.* p. 75; and Shumaker Deposition Ex. 21)

Mr. Harrell responded that he had no recollection of being at the January 11, 2006 meeting, but if he was there, he was at the MWUA Board meeting as an *ex officio* member, representing the Department of Insurance, and not as a voting member. He went on to say that, "We believe it is in the best interest for the resolution of these matters that we proceed today.

And I believe I can be fair and unbiased in the matter before us today. So I'm going to deny your motion." (Hearing Transcript, Vol. II, p. 79)

Indeed, there is nothing in the record to suggest that Mr. Harrell was anything other than fair and unbiased during these proceedings. Further, Mr. Harrell resigned as Deputy Commissioner, effective December 31, 2008, prior to the time these findings were drafted. His role in the matter was to guide the hearings and not to render ultimate conclusions. These findings have been made as a result of an extensive review of the pleadings, exhibits, and testimony presented herein, and are not based on opinion alone. Consequently, the Department finds no error in Mr. Harrell's serving as the Hearing Officer herein.

The True-Up Process Exceeded MWUA's Authority

Zurich was the only appealing company that argued that the MWUA Board did not have the authority to order the resubmission, or true-up, of the various numbers in the first place. Zurich alleges that since the statutes, Plan of Operation, and Manual of Rules and Procedures do not provide for the filing of motions for rehearing by parties, or the initiation of same by the Board, absent a timely appeal, then the only remedy would have been for an aggrieved insurer to have appealed the participation percentages within fifteen days, which none did.

We have previously discussed the authority of the MWUA to take the actions it did, and we adopt our previous findings herein; however, we need to go a bit further. Miss. Code Ann. § 83-34-13 provides that, "Within forty-five (45) days after the passage of this chapter, the directors of the association shall submit to the Commissioner for review and approval a proposed plan of operation. Such proposed plan shall...grant proper credit annually to each member of the association for essential property insurance voluntarily written in the coast area; and **shall**

provide for the efficient, economical, fair and nondiscriminatory administration of the association...." (Emphasis added.) The foregoing highlighted portion is the primary mandate of the Windpool. Consequently, under the facts in existence at the time of the ordering of the true-up, namely that the filing error made by Audubon would require a recalculation of participation percentages, the only "fair and nondiscriminatory" action to take was to allow everyone the opportunity to submit corrected or additional information.

The True-Up Process Was Arbitrary and Unfair

Zurich alleges that the reason that the true-up period was arbitrary and unfair was because of the "secret deal with AIG." Zurich states that AIG was allowed to submit an amended report on January 25, 2006, and that it was issued a new "Estimated Statement of Participation for 2005" on January 26, 2006, showing a reduced participation percentage. MWUA made almost immediate arrangements to refund over $31,000,000.00 to AIG. None of these facts were made known to other MWUA members when the true-up letters were sent.

A fairly extensive discussion of the AIG issue was included in the Homesite section above, and is incorporated herein, as well; however, a few additions should be made in response to Zurich's assertions. First, AIG was given a new statement of participation on January 26, 2006, and overpaid monies were immediately refunded to AIG. This was done because at that point, AIG was footing the bill for all claims made against the Windpool: "AIG advanced the $545,000,000. The claims that were paid was [sic] advanced by AIG. We were writing checks like crazy for adjusters and claims that we knew needed to be paid, and all of that would come to a screeching hault [sic]." (Hearing Transcript, Vol. I, p.46) Second, as discussed above, the error AIG (Audubon) made was not simply a matter of forgetting to take credits, as was the case with

the other companies. Audubon reported premiums that were not theirs. If the error had not been corrected, not only would the ability to pay claims have been in jeopardy, but AIG would have claimed credits for those writings, and billed MWUA for the assessments, thereby raising everyone else's participation percentages.

Zurich is quick to point to the January 26, 2006 Estimated Statement of Participation issued to AIG, wherein, once the erroneous MWUA premiums are removed, a decreased percentage of participation for AIG is shown. (Zurich Ex. 13, p. 1813) It fails to mention the April 1, 2006 "Recalculated Statement of Participation" issued to AIG, along with all other member companies once the true-up numbers were in and calculated, wherein AIG's participation percentage in the gain/loss (the 90% share) goes from 0.268% up to 0.354%, and its total assessment goes from $740,659 in January to $1,789,606 in April. (Zurich Ex. 13, p.1832)

The fact that the Board did not formally tell the other MWUA members what had transpired with AIG is not particularly significant. All members were offered the opportunity to submit additional and/or corrected information by March 1, 2006. A company either had credits that it wanted to take or it didn't. Once the March 1st deadline passed, all companies' participation percentages were recalculated and new assessments were made.

Farmers Insurance Group of Companies (hereinafter "Farmers")

Farmers raises the following issues on appeal: 1) the MWUA exceeded its statutory authority in setting an arbitrary deadline for the resubmission of premium information; 2) the process set up by MWUA for the resubmission of premium information was arbitrary and capricious and did not result in a fair and equitable allocation of the assessments; 3) the MWUA

violated Farmers' right to due process by not having a hearing on Farmers' appeal; 4) the handling of AIG's assessment resulted in the unfair and discriminatory treatment of Farmers and other member companies; 5) mobile home premiums have not been properly accounted for; 6) reinsurance proceeds were not properly allocated; and 7) Farmers should have been allowed to file as a group with its subsidiary, Foremost Insurance Group.

The first six issues have already been discussed elsewhere in these findings, and the previous determinations are incorporated herein. Even though the grouping issue was addressed in the Homesite section above, Farmers takes the opposite view of Homesite, alleging that it should have been allowed to group with its subsidiary Foremost Insurance Group, and there are some aspects of the Farmers argument that have yet to be discussed.

Farmers has adopted the position first held by the Department in the Union National case, that the MWUA did not exceed its authority in allowing grouping because: 1) the authorizing statute did not specifically prohibit grouping; 2) grouping had been permitted every year since the inception of the Windpool except 2006; 3) grouping encourages voluntary writings on the coast; and 4) the revised MWUA statutes specifically allow grouping.

Farmers seeks to group its reported premiums with Foremost, and thereby benefit from the use of Foremost's unused credits. Unfortunately, that idea did not occur to Farmers until after the third assessment was issued. Another twist to the issue is that Farmers has actually reported on a group basis for years, not with Foremost, but with Truck Insurance Exchange. When asked by the Hearing Officer why Farmers did not initially group with Foremost, counsel for Farmers responded that it was a timing issue - one company was in California and the other in Michigan, and 30 days was not long enough to get it done. (Hearing Transcript, Vol. II, p. 105) As pointed

out by counsel for MWUA, this was the first time any company had claimed that the thirty day true-up period was not long enough. (*Id.* at 102)

This is another example of the imperfections in company systems being brought to light in the aftermath of Hurricane Katrina. MWUA counsel asked why Farmers had not group reported during the original time period and the response was, "...we haven't understood the effect of grouping in loss years until '04 and '05." (*Id.* at 106) That answer is further clarified by Farmers' counsel's earlier statement, "...some of these are routine procedures filling out these forms. But when it gets to be the really big numbers, that's when closer scrutiny comes in. It's just - just like I said. With the losses and procedures, we didn't know how the calculations and procedures worked in loss years until we actually had a loss to apply it to." (*Id.* at 102) Farmers was aware, and had been for years, that it could report its premiums on a group basis, and in fact, did file on a group basis, with Truck Insurance Exchange. They filed their grouped numbers in a timely fashion. It was not until after the third assessment - the big numbers - that Farmers thought to look at grouping with Foremost, but by that time it was too late. The true-up period had ended.

Just as with the other companies that seek to go back and obtain credits for voluntary writings, Farmers seeks a second bite of the apple - to do what it could have done any time before March 1, 2006 if it had taken the time to run the numbers. The fact that it did not take advantage of the opportunity in a timely manner does not make the MWUA's denial of the credits arbitrary or capricious. In fact, it is just the opposite since the MWUA has consistently held all companies to the March 1, 2006 deadline.

Aegis Security Insurance Company (hereinafter "Aegis")

Aegis has been a licensed insurance carrier in Mississippi since 1985, and writes insurance for mobile homes and extended coverage dwellings. Aegis has been a member of the MWUA since its inception in 1987, and has paid storm assessments to, and received distributions of excess funds from, the Windpool.

On August 31, 2005, Aegis received its first Hurricane Katrina assessment in the amount of $232,070.00. On December 2, 2005, it received its second assessment in the amount of $6,613,995.00. On February 26, 2006, Aegis timely submitted its amended 2004 premium information pursuant to the true-up authorized by the MWUA Board. On April 17, 2006, Aegis was assessed a third time in the amount of $9,036,668.00, for a total assessment of $15,882,733,00. On May 17, 2006, Aegis appealed its Hurricane Katrina assessment to the MWUA. The two issues raised by Aegis in its appeal relate to grouping (allowing affiliated companies to report financial data and pay assessments on a group basis) and reporting of mobile home premiums.

The grouping issue has been addressed in both the Homesite and Farmers sections of these findings, and those previous discussions are incorporated herein; however, Aegis also alleges that, "The MWUA's failure to consider the impact of grouping before allowing it is an alarming fact given the dramatic and harmful affects [sic] grouping has had on Aegis and other MWUA partners in the Hurricane Katrina assessment process." (Aegis Brief, p. 13) It further alleges that there is no proof in the record to suggest that grouping actually accomplished the goal of encouraging voluntary writings in the coastal counties.

First, there is no proof in the record suggesting that grouping actually accomplishes the

goal of encouraging voluntary writings in the coastal counties because no one questioned the fact that it does encourage such writing; when the MWUA statutes were revised in 2007, grouping was specifically permitted for that very reason.

As to MWUA's failure to consider the impact of grouping before allowing it, grouping was a practice that had been in existence since before the MWUA was formed, almost thirty-five years. No one, including Aegis, who has been a member of MWUA since its inception ever questioned the grouping practice until after the Hurricane Katrina assessments. As with many of the other situations brought to light by Katrina, it was just never an issue until the resulting extraordinary assessments were made.

Clearly, in retrospect, the practice of grouping did have a profound negative impact on Aegis, but that does not mean that the practice itself was arbitrary, capricious, or ill-conceived. As stated by Aegis on page 14 of its Brief, the financial results of grouping were enormous **"in the context of the Katrina assessments."** As with many of the issues raised in these appeals, this is another example of imperfections in the system being brought into focus in the aftermath of Hurricane Katrina, but it does not mean that the procedure, at its inception, was flawed.

As to the improper reporting of mobile home premiums, Aegis's position is that all member companies who illegally reported their mobile home premiums should have to resubmit the correct numbers and the 2004 and 2005 assessments should be recalculated using the correct information. MWUA's position was, and is, that, since the MID was handling this matter, any monies recovered would be used to pay Hurricane Katrina losses over $700,000,000, or if the losses were less than $700,000,000, any funds recovered would be included in the amount of money to be reimbursed to MWUA's member companies on a pro rata basis. In either event,

there would not be a need to reopen the assessments in order to adequately deal with any recovery.

The issue of the purported misreporting of mobile home premiums is still under review by MID, and has not been concluded. While significant progress has been made by MID, it is the opinion of the Commissioner that this issue is not ripe for review.

Conclusion

A reading of the MWUA authorizing statutes, the Plan of Operation, and the Manual of Rules and Procedures clearly reveal and establish that in order to claim credits or exclusions, there must be some procedure prescribed for doing so. This procedure was provided to member companies in the form of the welcome packet and Bulletin 88-4. The six companies herein, along with all other member companies, were also given two notices of the opportunity to submit corrected and/or additional information to the MWUA before a final Hurricane Katrina assessment was made. These notices made it clear that any such submissions would have to be received by March 1, 2006, or same would not be considered. All six companies had actual, or at least constructive, notice of the applicable deadlines, and failed to respond by the stated deadline.

The opportunity to furnish corrected and/or additional information was provided in an attempt to fairly and equitably make the necessary assessments to cover the losses sustained by Hurricane Katrina. The plan devised, while not perfect, fell within the statutory and regulatory powers of the MWUA Board.

In keeping with the standards of review herein, the Commissioner hereby finds that the decisions of the MWUA Board to deny the appeals of the six companies herein were not arbitrary

or capricious, were not beyond the power of the Board to make, and were not violative of any statutory or constitutional rights of said companies, and the decisions of the MWUA in each of these appeals should be affirmed.

IT IS, THEREFORE, ORDERED AS FOLLOWS:

1. The decision of the MWUA to deny the relief requested by Homesite Insurance Company is hereby affirmed.

2. The decision of the MWUA to deny the relief requested by OneBeacon Insurance Group is hereby affirmed.

3. The decision of the MWUA to deny the relief requested by RLI Insurance Company is hereby affirmed.

4. The decision of the MWUA to deny the relief requested by Zurich American Insurance Company is hereby affirmed.

5. The decision of the MWUA to deny the relief requested by Farmers Insurance Group of Companies is hereby affirmed.

6. The decision of the MWUA to deny the relief requested by Aegis Security Insurance Company is hereby affirmed.

7. It is suggested that the MWUA provide to the assessable insurers on a yearly basis a copy of all definitions and procedures necessary to obtain credits and/or exclusions, such as those contained in the welcome packet discussed herein. Said information may be sent with the annual reporting forms, or by other means as determined by the Board. The same information should also be posted on the MWUA website.

8. At a minimum, the MWUA should annually compare the premiums reported to MWUA with those reported to the Mississippi Department of Insurance on each assessable insurer's Annual Report, and the MWUA should develop such other procedures as may be necessary to identify filing irregularities by assessable insurers.

9. Homesite Insurance Company, OneBeacon Insurance Group, RLI Insurance Company, Zurich American Insurance Company, Farmers Insurance Group of Companies, and Aegis Security Insurance Company may appeal this decision as provided by law.

SO ORDERED, this the 11th day of February, 2009.

MIKE CHANEY
COMMISSIONER OF INSURANCE
STATE OF MISSISSIPPI

MIKE CHANEY

Certificate of Service

I hereby certify that a true and correct copy of the foregoing Consolidated Findings, Conclusions, and Order, has been sent via e-mail to the following:

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This the 11th day of February, 2009.

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