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INSURANCE DEPARTMENT ISSUES ADVICE ON CANCELLATION OF MUNICIPAL BOND INSURANCE POLICIES

The New York Insurance Department (the “Insurance Department”) has issued a circular letter advising financial guaranty insurers (“FGIs”) that in light of the recent and potential downgrades in the ratings of FGIs, the Insurance Department will not object to the cancellation or termination of in-force bond insurance policies on the basis that such termination or cancellation conflicts with non-cancellation provisions in these filed policies.

The Insurance Department issued Circular Letter No. 12 (2008) in response to recent developments wherein municipal bond issuers have sought to cancel or terminate in-force bond insurance policies as a result of concerns spurred by the recent downgrades (or potential downgrades) of the credit ratings of FGIs. The Insurance Department’s guidance was issued in an effort to avoid the adverse consequences that the Department explains could directly result from such downgrades (including the loss of liquidity facilities for the repurchase of a municipality’s outstanding bonds), as well as consequential effects (such as a depression of auction-rate municipal bonds, failures of interest rate setting auctions, and imposition of higher interest rates for municipalities).

The Insurance Department has specifically advised that notwithstanding the presence of any “non-cancellation” provisions of a bond insurance policy, the Insurance Department will not object to the cancellation or termination of such policies provided that the municipality, the FGI, and bondholders all consent to the cancellation or termination. In addition, the Insurance Department suggests that such cancellation or termination be done in a prudent manner, providing all parties with an opportunity to evaluate the merits of the proposed cancellation or termination, and that a FGI’s determination to consent to cancel or terminate policies be done in accordance with a non-discriminatory set of criteria. Furthermore, the Insurance Department provided a reminder that any modifications made to existing policy forms must be filed with the Insurance Department.

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Circular Letter No. 12 demonstrates the Insurance Department's forward thinking approach to handling issues of significant importance to the New York and national insurance markets. The Insurance Department has played a significant role in addressing the recent troubles befalling bond insurers, and its willingness to act outside the box to find a workable solution to allow the market to move forward is the most recent demonstration of the Insurance Department's current results-oriented approach.

If you would like more information on this or any other insurance, reinsurance or insolvency regulatory actions, please feel free to contact Francine L. Semaya, Esq., Chair, Insurance Corporate and Regulatory Practice Group, (212.908.1270, fsemaya@cozen.com) or Laurance D. Shapiro, Esq. (212.908.1363, lshapiro@cozen.com).

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