



*Losing California Certificate of Authority...*

## Applied Underwriters' California Ins Company More Controversial Acts

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Amidst charges of unapproved and uncollateralized loans to affiliates, unapproved property transfers, the California Department of Insurance's Conservation and Liquidation Office says it is drafting a unilateral "rehabilitation" plan for California Insurance Company (CIC). The plan will transfer its policies to another carrier and resolve the numerous filed lawsuits pending between Applied Underwriters / CIC and their former insureds. The plan will also force the carrier to surrender its California certificate of authority.

The Conservation office says it is preparing the rehabilitation plan on its own after Applied / CIC management unilaterally stopped negotiating in May over a deal to lift the conservation order. It's pretty clear to observers the CDI and Liquidation office has had enough.

But Applied / CIC argues in a court filing last week that the Department is getting ahead of itself and that a rehabilitation plan may not be necessary. It notes that it has filed to vacate the conservation order, and there is a hearing on that motion scheduled for next month. *Workers' Comp Executive* could find no instance where a seized carrier got a conservation order vacated.

California Insurance Company was seized by CDI and has been operating under the oversight of a court-appointed conservator since last November. Applied Underwriters is continuing to file lawsuits against insureds for promissory notes under the RPA. But the seizure does not allow the insureds to file cross complaints concerning the illegal RPA.

Insurance Commissioner Ricardo Lara sought and received the conservation order to prevent a merger from being finalized without the Department's consent. Applied's founder, Steve Menzies, attempted to merge CIC with a newly formed entity in New Mexico to complete his purchase of the company from Berkshire Hathaway (for extensive past coverage, see our Applied Underwriters Investigations section by [clicking here](#)).

"Attempting to merge without the Commissioner's permission is among the specified grounds in the Insurance Code for conserving an insurer," the CLO notes in its first status report to the court. The report and other court filings review Applied Underwriters' long history of acting outside the law and highlight new evidence of its scofflaw nature.

CLO says it expects the ultimate rehabilitation plan to be a "complex financial and legal" document that will set the terms for

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*"In addition, the transaction violated applicable provisions of the Insurance Code," – CDI Conservator*

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CIC to complete its merger into the New Mexico company and surrender its California certificate of authority.

“The plan will provide for determination of the carrier assuming the CIC policies, will address the necessary financial arrangements for it to assume the CIC policies, will provide means for orderly resolution of the [reinsurance participation agreement] litigation, and will address the regulatory issues that presently cloud the estate,” the Conservator noted in the status report.

## Flouting Regulatory Processes

The CLO points to Applied Underwriters' extensive history of “flouting California regulatory processes” through an unfiled reinsurance participation agreement (RPA) that was a required part of its EquityComp program. The RPA, which modified the pricing of the CIC guaranteed cost policy, was deemed illegal by the Commissioner and two appellate courts.

Despite these legal losses, the CLO notes that Applied is still attempting to enforce the terms of the RPA and hold policyholders financially responsible for charges it claims arose under the illegal RPA. Numerous lawsuits have ensued.

“The Conservator has reviewed these attempts by CIC and its affiliates to collect from policyholders, together with other suits brought by policyholders seeking to recover amounts collected in excess of the guaranteed cost, and yet others challenging CIC's calculations under the filed and unfiled rates, which represent a substantial body of pending litigation materially affecting California policyholders,” the Conservator notes in a status report.

These cases have been stayed under the conservation order. “This broad injunction is intended to maintain the status quo, preserve CIC's assets, and allow the Conservator to resolve the conservation of CIC without the distraction of participating in multiple forums.”

Attorney Nick Roxborough, a partner in Roxborough Pomerance Nye & Adreani, whose firm is handling a few of the many cases against Applied says the Department is looking at including several settlement options for resolving the RPA litigation.

The options will likely include allowing employers the choice of not settling and taking their claim to court. He says it is also likely that there will be some set formulas that will enable employers to resolve the question of what is owed and to whom without the need for expensive litigation. “The Department has fought hard for employers' rights vis-à-vis Applied Underwriters, and I appreciate the effort,” he tells *Workers' Comp Executive*.

One outstanding question is whether or not the CDI agreement will set forth a formula and reserves to protect all employers similarly situate and not just those presently in litigation.

Other lawyers handling most of the cases refused to comment citing confidentiality issues.

## Illegal Money Transfers

In addition to the on-going court efforts to enforce portions of the RPA, the CLO report also details new transgressions by Applied Underwriters.

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*“The Conservator has reviewed these attempts by CIC and its affiliates to collect from policyholders ... to recover amounts collected in excess of the guaranteed cost,” – Court Filing*

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“Over four months after service of the Conservation Order, and without notice to the Conservator, on March 31, 2020, CIC made a loan of \$20 million issued to Applied Underwriters, Inc.,” the CLO says, noting that the uncollateralized loan was never brought to the attention of nor approved by the Conservator as required by the conservation order. “In addition, the transaction violated applicable provisions of the Insurance Code.”

The filing also notes that back in October, when Menzies was seeking to evade CDI’s oversight, CIC entered several purchase agreements with Applied Underwriters, whereby it bought several properties for \$157 million.

The next day CIC also lent another \$15 million to Applied.

“The Department of Insurance Financial Analysis Division has informed the Conservator that these transactions may not have been entered in compliance with California laws regulating admitted insurers’ financial transactions generally and transaction with affiliates,” the CLO writes in the report. It says it is preparing a response to this action.

## Wrapping Up

CLO says it intends to have the rehabilitation plan ready for court review before August 31, 2020. Under its proposed timeline, policyholders, other creditors, and the public would then have the opportunity to review and submit written comments on the proposed plan through the fall.

The conservation office proposes giving CIC’s pre-conservation management until October 15, 2020, to file its response to the rehabilitation plan. Non-parties would have until November 16, 2020, to submit their support or opposition to the rehabilitation plan. CLO projects having all written submissions and responses filed with the court by December 7, 2020.

The conservation office asks the San Mateo Superior Court for a hearing on July 30 to review and approve this proposed timeline. As of deadline, the court had not acted upon the Department’s request for a hearing and order.

CIC’s attorneys have made several requests with the court this spring to have a hearing on its proposal to have the conservation order vacated. It’s latest attempt occurred last week seeking an August 6 hearing. To date, however, the court has not taken up the hearing requests.

