IFIGS
Success Stories

Featured Insolvency

- ***Company*** **Markham General Insurance Company (MGIC)**
- ***Insurance*** **Property and Casualty (P&C)**
- ***Country*** **Canada**
- ***IGS*** **Property and Casualty Insurance Compensation Corporation**

About MGIC
Markham General Insurance Company (MGIC) was a Canadian Property and Casualty (P&C) insurance company active in three Canadian provinces. MGIC commenced operations on October 4, 1999, and was subsequently declared insolvent on July 24, 2002. The MGIC insolvency was the costliest P&C insurance company failure in Canadian history.

MGIC was licensed to sell: Accident and Sickness; Automobile; Boiler and Machinery; Fidelity; Liability; and Property insurance. Some 97% of the company's Direct Written Premium (DWP) was written in the province of Ontario, with 78% of that being in Automobile insurance – a highly competitive line of business at the time, with severe profitability issues for all market participants.

MGIC was a start-up company with an aggressive three-point business plan that proposed to:
1. Attract insurance brokers as key investors (in theory to ensure a flow of high-quality business)
2. Use computerized, internet-based underwriting and business-processing tools to achieve above-average risk selection and the lowest expense ratios in the industry
3. Focus on profit growth, rather than volume growth.

Issues became severe very rapidly and there were indications of trouble for MGIC by the end of 2001:
- Return on Equity was -162.5% – compared to 2.6% for the industry as a whole
- The combined ratio was 191.9% – compared to 111.0% for the industry
- Year-over-year growth in DWP of 326.3% was unsustainable – industry growth was just 10.6%
- Total equity decreased by 25.9% from the previous year – compared to -0.8% for the industry.

Causes of the MGIC Failure
In its short and turbulent history, MGIC was never profitable. A number of important factors contributed to the company's failure, including:
- *Inadequate pricing* – MGIC underpriced its Auto insurance products in order to attract business at a particularly bad time. It was later reported that the soaring cost of accident claims in 2001 resulted in the single-worst year ever for industry profitability
- *Deficient claims reserving* – MGIC was significantly under-reserved; loss claims increased by 607% in 2001, but reserves had only been increased by 3.6%
- *Outsourcing* – MGIC outsourced several of its key functions to third parties, including its underwriting (to its brokers), claims handling and information technology services

- *Inadequate capital* – MGIC burned through all its capital very quickly; despite setting out with $20M of capital, it was already barely in compliance with regulatory minimum capital requirements by the end of its first year of operation
- *High expenses* – Incurred expenses ($27.5M) were almost twice the level projected in MGIC's original business plan ($14.5M)
- *Poor corporate governance* – There were no independent or non-affiliated Directors on the Board
- *Business planning* – None of the company's three key objectives (noted above) were achieved.

Affected MGIC Policyholders

On June 30, 2002, MGIC had a reported shortfall of assets over liabilities of $4.9M. The quantum was later found to be much larger. MGIC was ordered to be wound-up on July 24, 2002, pursuant to Canada's *Winding-up and Restructuring Act*. **The company's liquidation affected approximately 87,000 policyholders, through a network of 90 insurance brokers**.

PACICC Assistance in the MGIC Insolvency

PACICC Member Insurers played a leading role in providing financial assistance to the policyholders affected by the MGIC insolvency. **PACICC levied general assessments totaling $22.9M (CAD) against 133 of its Member companies that were active in markets and lines of business where MGIC operated.**

Claims paid by PACICC to former MGIC policyholders totaled $21.1M. When the estate was finally closed in the Court almost 20 years later, PACICC had recovered $15.4M as the largest creditor to the MGIC insolvency. This amount included a financial settlement in favour of the estate (received in March 2009) resulting from legal action commenced against certain third parties, including MGIC's former officers, directors and actuarial advisors.

Facility Association, the non-profit association of insurers making insurance available to higher-risk drivers, funded an additional $12M of Statutory Accident Benefit claims payments to MGIC policyholders.

About PACICC

The Property and Casualty Insurance Compensation Corporation (PACICC) is the insurance guarantee and policyholder protection mechanism for Canada's P&C insurance industry. PACICC was established by Canada's private insurers in 1989, in partnership with all thirteen Provincial and Territorial regulators. PACICC's mission is to protect eligible policyholders from undue financial loss in the event that a Member Insurer becomes insolvent. PACICC works to minimize the costs of insurer insolvencies and seeks to maintain a high level of consumer and business confidence in Canada's P&C insurance industry through the financial protection that it provides to policyholders.

PACICC Members account for approximately 95% of the Canadian P&C insurance market. PACICC has participated in the winding-up and liquidation of 13 of these. There has not been a P&C insurer failure in Canada since 2003.