

From: Tracey
EXHIBIT 5
Knutson 10-05
SB 4

Principles of Inherent Risk

It is worth noting that the majority of states do not have inherent risk type legislation. The reason for this is that the common law created the inherent risk doctrine and current case law, from studied courts, perpetuates the doctrine quite nicely. As you will, or should recognize, there are four essential legal elements to establishing a cause of action for negligence. These elements include duty, breach, causation and damage. The general common law dictates that recreation providers have no duty to protect participants from the inherent risks of recreational activities, and therefore no corresponding liability to participants for injury or loss resulting from those inherent risks. If the inherent risk doctrine establishes that there is no duty present in an inherent risk type situation, a participant will not be able to make out the first element of a cause of action for negligence.

The primary assumption of risk doctrine, often referred to as the "inherent risk doctrine," provides generally that individual participants assume the inherent risks of recreational activities and all liability or responsibility for injuries resulting from those risks. Put another way, providers of recreational activities have no duty, ergo no responsibility, to protect participants from the inherent risks and dangers of recreational activities. What the principle of inherent risk specifically says is that, "[o]ne who takes part in such a sport accepts the dangers so far as they are obvious and necessary." Wright v. Mt. Mansfield Lift, Inc., 96 F. Supp. 786 791 (D. Vt. 1951). See also, Moore v. Hartley Motors, Inc., 36 P.3d 628, 633 (Alaska 2001) holding that, a risk/danger will not be considered inherent to the sport if it could be "...eliminated or mitigated through the exercise of reasonable care." Moore v. Hartley Motors, Inc., 36 P.3d at 633. In other words, the current common law relieves recreation providers from any "duty" to protect participants from the inherent risks of the associated activity, but allows participants to sue if their injuries are due to non-inherent risks created through provider negligence. As such, *critics who complain that this legislation will create a safety disincentive or that operators will not have to maintain their equipment or otherwise be safety conscious, are simply wrong. If an operator could have eliminated the risk through the exercise of reasonable care, then we are not talking about an inherent risk and this defense will not apply.*

One early case in recreational liability defined the rule as follows: "One who takes part in such a sport accepts the dangers that inhere in it so far as they are obvious and necessary." Wright v. Mt. Mansfield Lift, Inc., 96 F.Supp. 786, 791 (D. Vt. 1951). The Washington Supreme Court upheld the inherent risk defense when it wrote that "a defendant simply does not have a duty to protect a sports participant from dangers which are an inherent and normal part of a sport." Scott v. Pacific West Mountain Resort, 834 P.2d 6, 13 - 14 (Wash. 1992). *It is important to recognize that the "inherent risk" defense or theory exists under the common law because critics of the effort to codify this common law defense like to say that this is "tort reform." Codifying the inherent risk doctrine is NOT tort reform; codifying this doctrine does nothing to limit the rights of putative plaintiffs or persons who would want to sue a recreational operator and does not create anything "new" under the law.*

What is equally as important to understand or to address is the critics claim that this bill is for the

SENATE JUDICIARY
Exhibit No. 5
Date 1-10-05
Bill No. SB 4 5

commercial operators only and is designed to protect only their interests. Quite to the contrary! In the current insurance climate, having a state such as Montana refuse to recognize any of the normal defenses available to commercial recreation operators effectively creates an environment where land administrators and insurers will not allow programs to operate. Many insurers that underwrite in the outdoor recreation areas are making it clear that, in the State of Montana, where the climate is decidedly tilted towards suing plaintiffs because of a recreational operator's inability to use prerecreatioanal releases, the legislature's refusal to codify or recognize the inherent risk doctrine means that many common coverages will not be offered or underwritten or coverages will be exponentially higher than those in other states. Very few programs will stay in business without proper CGL (comprehensive general liability) coverages in place. In fact, most property owners or administrators of property will not allow or permit programs to operate on their properties without appropriate insurance in place. No insurance, no place to operate, no programs. As a recreation oriented and supported state, Montana should not stand by and watch this type of result. Beyond the negative impact on the businesses of the commercial operators, the most problematic impact is that the recreational opportunities enjoyed by all of Montana's citizens and visitors and the recreational programs which are so healthy for Montana's children will steadily be destroyed. If the courts do not hear from the legislators that, in Montana, the consideration of whether a recreational incident was caused by an inherent risk of the sport needs to be made by the courts, organizations such as little league, youth soccer or hockey, after school programs and individuals who volunteer their time as coaches could well decide that the risk of large legal fees in a state and climate where no defenses are available (remember, prerecreational releases are not allowed in Montana) are simply too significant to justify the existence of these programs. The result is that thousands of children will be deprived of the valuable opportunities afforded by recreational sports and organized sports. Once again, no insurance, no place to operate, no programs. Talk about contributing to the obesity of America's youth! ***To the critics that say this legislation is only for the benefit of the commercial operators, they are wrong!! This legislation is designed to protect the recreational opportunities of all of Montana's citizens and children.***



MONTANA STATE AUDITOR
JOHN MORRISON

COMMISSIONER OF INSURANCE
COMMISSIONER OF SECURITIES

January 10, 2005

RE: SB37

Dear Chairman Wheat and Members of the Senate Judiciary Committee:

Thank you for hearing SB 37, a bill: "REQUIRING A BANK, TRUST COMPANY OR BROKERAGE FIRM ACTING AS A CUSTODIAN OF AN INSURER'S SECURITIES TO AGREE TO INDEMNIFY THE INSURER FOR THE LOSS OF ANY OF THE INSURER'S SECURITIES WHILE IN ITS CUSTODY."

SB37 seeks only to strengthen Montana's response to the guidelines and procedures set forth in the National Association of Insurance Commissioner's Examiners' Handbook. The Examiners' Handbook includes a procedure that requires examiners to confirm during the financial examination of an insurer that an indemnification agreement is in place between the insurer and the financial institution. Attached for your reference is a copy of that standard in the Handbook.

The State Auditor's Office Financial Examination Bureau is required to be accredited by standards agreed to through Montana's affiliation with the National Association of Insurance Commissioners. The office was last examined for accreditation purposes in 2004. Addressing this issue of requiring an indemnification agreement by statute was noted in the accreditation report. The notation was not considered a deficit for accreditation purposes, but more as a suggestion for improvement. The Montana State Auditor's Office received high marks during the accreditation process; this bill will assure that our office will continue to excel during accreditation examinations.

The concept of this legislation was presented to the Interim Committee on Economic Affairs and the committee approved the concept so this bill could be drafted for the pre-introduction process.

An amendment has been requested to clarify and restrict the "any loss" in line 14 of Section 1 in the bill. A draft of that amendment is attached for your reference.

To respond to questions offered by Sen. O'Neil and Sen. Perry, section Part 1 Section (J) all of (1) and (b) and (c) of (2) describe the standards as adopted by the US banking regulator and state banking laws. The agreements themselves are regulated by either state or federal banking laws and are not addressed by SB 37. The financial institution would offer the agreement to the insurer and the

contract itself would be continue to be regulated by banking regulation, not by the Montana State Auditor's Office. The intent with this request is only to assure that the indemnification agreement be in place. It is not the intention of the office address the terms of the agreement in any way; or in any way regulate the terms of the agreement.

If you have further questions please contact me at: 444-2004.

Alicia Pichette

- g. The controlled insurer shall provide the controlling producer with its underwriting standards, rules and procedures, manuals setting forth the rates to be charged, and the conditions for the acceptance or rejection of risks. The controlling producer shall adhere to the standards, rules, procedures, rates and conditions. The standards, rules, procedures, rates and conditions shall be the same as those applicable to comparable business placed with the controlled insurer by a producer other than the controlling producer.
- h. The contract shall specify the rates and terms of the controlling producer's commissions, charges or other fees and the purposes for those charges or fees. The rates of the commissions, charges and other fees shall not be greater than those applicable to non-controlling producers for comparable business (i.e., same kinds of insurance and risks, similar policy limits, and quality of business) placed with the controlled insurer.
- i. Controlling producer compensation based on insurer profits shall not be determined or paid until at least five years after the premiums on liability insurance are earned and at least one year after the premiums are earned on any other type of insurance. Commissions shall not be paid until an independent casualty actuary or loss reserve specialist has confirmed the sufficiency of the controlled insurer's reserves on remaining claims, including incurred but not reported (IBNR).
- The contract shall specify a percentage limit of writings the controlling producer is entitled to make relative to the controlled insurer's surplus and total writings. The insurer may establish a different limit for each line or subline of business. Notification by the controlled insurer to the controlling producer is required when the established limit is approached. Once the limit has been reached, the controlled insurer is prohibited from accepting business from the controlling producer. The controlling producer shall not attempt to place business with the controlled insurer if it has been notified that the limit has been reached.
- k. The controlling producer may bind facultative reinsurance contracts pursuant to obligatory facultative agreements if the contract with the controlled insurer contains underwriting guidelines for assumed and ceded business that includes a list of reinsurers with which automatic agreements are in effect, the coverages and amounts or percentages that may be reinsured, and commission schedules. Otherwise, for business placed by the producer, the controlling producer is entitled to negotiate but is unable to bind reinsurance on behalf of the controlled insurer.

J. Custodial or Safekeeping Agreements

When conducting financial examinations, the custodial or safekeeping agreements should be considered and evaluated with this guidance.

1. An insurance company may by written agreement provide for the custody of its securities with a custodian. If permitted by the state of domicile, the custodian must either be a broker/dealer that is registered with and subject to jurisdiction of the Securities and Exchange Commission, maintains membership in the Securities Investor Protection Corporation, and has a tangible net worth equal to or greater than \$250,000,000; or a national bank, state bank, or trust company adequately capitalized and qualified to accept

securities as determined by the standards adopted by the U.S. banking regulators and regulated by state banking laws or a member of the Federal Reserve system. Custodial agreements shall be authorized by a resolution on behalf of the board of directors or an authorized committee of the insurance company. The agreement should state that certificated securities of the insurance company shall be held separate from all other securities. Those securities held indirectly by a custodian or in a clearing corporation shall be separately identified on the custodian's official records as being owned by the insurance company. Registered custodial securities shall be registered in the name of the company, in the name of a nominee of the company, in the name of the custodian or its nominee, or clearing corporation or its nominee. The securities, other than those held to meet deposit requirements, shall be held subject to the instructions of the insurance company, and shall be withdrawable upon the demand of the insurance company. Confirmation of all transfers should be provided to the insurance company in hard-copy or in electronic format.

2. Custodial or safekeeping agreements with an agent or clearing corporation meeting the requirements herein should contain satisfactory safeguards and controls, including but not limited to the provisions provided below. (For the purpose of this guidance, an agent is a national bank, state bank, trust company or broker/dealer with an account in a clearing corporation or a member of the Federal Reserve System. A clearing corporation is a corporation as defined in Article 3 of the Uniform Commercial Code that is organized for the purpose of effecting transactions in securities, by computerized book-entry, including the Treasury Reserve Automated Debt Entry Securities System (TRADES) and Treasury Direct book entry securities systems, except those securities issued under the laws of a foreign country.)
- a. The custodian is obligated to indemnify the insurance company for any insurance company's loss of securities in the custodian's custody, except that, unless domiciliary state law, regulation or administrative action otherwise require a stricter standard (Section 2.b. sets forth an example of such a stricter standard), the custodian shall not be so obligated to the extent that such loss was caused by other than the negligence or dishonesty of the custodian;
 - b. If domiciliary state law, regulation or administrative action requires a stricter standard of liability for custodians of insurance company securities than that set forth in Section 2.a., then such stricter standard shall apply. An example of a stricter standard that may be used is that the custodian is obligated to indemnify the insurance company for any loss of securities of the insurance company in the custodian's custody occasioned by the negligence or dishonesty of the custodian's officers or employees, or burglary, robbery, holdup, theft, or mysterious disappearance, including loss by damage or destruction;
 - c. In the event of a loss of the securities for which the custodian is obligated to indemnify the insurance company, the securities shall be promptly replaced or the value of the securities and the value of any loss of rights or privileges resulting from said loss of securities shall be promptly replaced;
 - d. The custodian shall not be liable for any failure to take any action required to be taken hereunder in the event and to the extent that the taking of such action is prevented or delayed by war (whether declared or not and including existing wars), revolution, insurrection, riot, civil commotion, act of God, accident, fire, explosions, stoppage of labor, strikes or other differences with employees, laws,

regulations, orders or other acts of any governmental authority, or any other cause whatever beyond its reasonable control;

- e. In the event that the custodian gains entry in a clearing corporation through an agent, there should be a written agreement between the custodian and the agent that the agent shall be subjected to the same liability for loss of securities as the custodian. If the agent is governed by laws that differ from the regulation of the custodian, the Commissioner of Insurance of the state of domicile may accept a standard of liability applicable to the agent that is different from the standard liability;
 - f. If the custodial agreement has been terminated or if 100% of the account assets in any one custody account have been withdrawn, the custodian shall provide written notification, within three business days of termination or withdrawal, to the insurer's domiciliary commissioner;
 - g. During regular business hours, and upon reasonable notice, an officer or employee of the insurance company, an independent accountant selected by the insurance company and a representative of an appropriate regulatory body shall be entitled to examine, on the premises of the custodian, its records relating to securities, if the custodian is given written instructions to that effect from an authorized officer of the insurance company;
 - h. The custodian and its agents, upon reasonable request, shall be required to send all reports which they receive from a clearing corporation, which the clearing corporation permits to be redistributed including reports prepared by the custodian's outside auditors, to the insurance company on their respective systems of internal control.
 - i. To the extent that certain information maintained by the custodian is relied upon by the insurance company in preparation of its annual statement and supporting schedules, the custodian agrees to maintain records sufficient to determine and verify such information.
 - j. The custodian shall provide, upon written request from a regulator or an authorized officer of the insurance company, the appropriate affidavits, with respect to the insurance company's securities held by the custodian;
 - k. The custodian shall secure and maintain insurance protection in an adequate amount; and
 - l. The foreign bank acting as a custodian, or a U.S. custodian's foreign agent, or a foreign clearing corporation is only holding foreign securities or securities required by the foreign country in order for the insurer to do business in that country. A U.S. custodian must hold all other securities.
3. Except as provided below, the examiner shall verify such securities by actual inspection and count, and whenever necessary ascertain whether the securities are the specific ones acquired by the company:

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SENATE BILL NO. 37
INTRODUCED BY T. SCHMIDT
BY REQUEST OF THE STATE AUDITOR

A BILL FOR AN ACT ENTITLED: "AN ACT REQUIRING A BANK, TRUST COMPANY, OR BROKERAGE FIRM ACTING AS CUSTODIAN OF AN INSURER'S SECURITIES TO AGREE TO INDEMNIFY THE INSURER FOR THE LOSS OF ANY OF THE INSURER'S SECURITIES WHILE IN ITS CUSTODY."

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF MONTANA:

NEW SECTION. **Section 1. Indemnification agreement.** An insurer may contract with any national or state bank, trust company, or securities brokerage firm to act as custodian for the insurer's securities. The contract must contain an indemnification agreement stating that the custodian is obligated to indemnify the insurer for any loss of the insurer's securities in its custody.

NEW SECTION. **Section 2. Codification instruction.** [Section 1] is intended to be codified as an integral part of Title 33, chapter 12, part 1, and the provisions of Title 33, chapter 12, part 1, apply to [section 1].

- END -

Pichette, Alicia

From: Driscoll, Pat
Sent: Thursday, January 06, 2005 5:59 PM
To: Lane, Valencia; Pichette, Alicia
Subject: Proposed Amendment SB37

Proposed Amendments
Senate Bill No. 37
Introduced Bill

1. Bill Title, Line 7, following "INSURER'S SECURITIES"

Insert: "RESULTING FROM THE INTENTIONAL OR NEGLIGENT ACT OR OMISSION OF THE CUSTODIAN WHILE THE INSURER'S SECURITIES ARE"

2. Section 1, Line 14, following "insurer's securities in its custody"

Insert: "resulting from the intentional or negligent act or omission of the custodian, or the employee, officer or agent of the custodian"

- end -

Montana Code Annotated 2003

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33-1-401. Examination of insurers. (1) The commissioner shall examine the affairs, transactions, accounts, records, and assets of each authorized insurer as often as the commissioner considers advisable. The commissioner shall examine each authorized insurer not less frequently than every 5 years.

(2) The commissioner shall in like manner examine each insurer applying for an initial certificate of authority to do business in this state.

(3) In lieu of making an examination under this part of any foreign or alien insurer licensed in this state, the commissioner may accept an examination report on the company prepared by the insurance department for the company's state of domicile or port-of-entry state until January 1, 1994. After January 1, 1994, the reports may only be accepted if:

(a) the insurance department was at the time of the examination accredited under the national association of insurance commissioners' financial regulation standards and accreditation program; or

(b) the examination is performed under the supervision of an accredited state insurance department or with the participation of one or more examiners who are employed by such an accredited state insurance department and who, after a review of the examination workpapers and report, state under oath that the examination was performed in a manner consistent with the standards and procedures required by their insurance department.

(4) For purposes of completing an examination of any company under this part, the commissioner may examine or investigate any person or the business of any person, in so far as the examination or investigation is, in the sole discretion of the commissioner, necessary or material to the examination of the company.

History: En. Sec. 32, Ch. 286, L. 1959; R.C.M. 1947, 40-2713; amd. Sec. 39, Ch. 596, L. 1993.

Provided by Montana Legislative Services

Donald A. Gatzke, Ph.D.
243 Lake Blaine Drive
Kalispell, Montana 59901-7629
(406) 755-1380
gatzkedonalda@centurytel.net

DATE: January 9, 2005
TO: Senator Brent Cromley
FROM: Donald A. Gatzke, Ph.D.
RE: SB 111, concerns

Dear Senator Cromley:

For over 20 years I have worked as a Professional Clinical Counselor, Mediator and Business Consultant. During that time I have always attempted to serve my clients in an ethical, professional and legal manner.

Recently I have been reading about a situation in the Flathead Valley that makes me realize that I have possibly, unwittingly been violating the laws of Montana as recently interpreted by a judge in her ruling against Senator O'Neil. As I read the paper I realized that the things he was charged with, I and many of my professional colleagues are also probably guilty.

Never did I feel I was "playing lawyer", rather I was "advising and counseling." In reading about O'Neil's case I saw that because he charged a rate similar to that of an attorney he was in fact giving "legal advice." Well, this being the case, I am probably doing the same thing. I use a "sliding scale", designed to charge clients according to their ability to pay. This makes the low end almost "pro bono" whereas the top end is equal to or greater than many attorneys in the area. Because of this, I am able to serve many people who could not otherwise afford assistance. However, until this issue is resolved, I will greatly restrict my professional activities.

Please give serious consideration to supporting SB 111. There are so many of us who regularly, in the process of working with our clients, currently seem to be in violation of the law "BY DISCUSSING THE LAW WITH ANY PERSON".

We in the "helping professions" need SB111. Without this bill a great many people will lose vital services.

A final question. Have you ever "discussed the law with any person?" Have you ever visited with an individual about an act they have or may take, discussing the implications of the law with them? Have you ever given your "opinion" as to what a law means in a specific situation? If so, you too need to support SB111.

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RESULTING FROM THE INTENTIONAL OR NEGLIGENT ACT OR OMISSION OF THE CUSTODIAN WHILE THE INSURER'S SECURITIES ARE IN ITS CUSTODY.

NEW SECTION. Section 1. Indemnification agreement. An insurer may contract with any national or state bank, trust company, or securities brokerage firm to act as custodian for the insurer's securities. The contract must contain an indemnification agreement stating that the custodian is obligated to indemnify the insurer for any loss of the insurer's securities in its custody.

NEW SECTION. Section 2. Codification instruction. [Section 1] is intended to be codified as an integral part of Title 33, chapter 12, part 1, and the provisions of Title 33, chapter 12, part 1, apply to [section 1].

- END -

resulting from the intentional or negligent act or omission of the custodian or the employee, officer, or agent of the custodian

Amendments to Senate Bill No. 37
1st Reading Copy

For the Senate Judiciary Committee

Prepared by Valencia Lane
January 7, 2005 (7:40am)

1. Title, line 7.

Following: "SECURITIES"

Strike: "WHILE"

Insert: "RESULTING FROM THE INTENTIONAL OR NEGLIGENT ACT OR
OMISSION OF THE CUSTODIAN WHILE THE INSURER'S SECURITIES
ARE"

2. Page 1, line 14.

Following: "custody"

Insert: "resulting from the intentional or negligent act or
omission of the custodian or the employee, officer, or agent
of the custodian"

- END -

(See over)

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