

THE UNIFORM RECEIVERSHIP LAW: WHAT IT IS AND WHAT IT ISN'T

Michael J. Dugan, Esq.
Robert F. Craig¹
(402) 397-8450

In September 1998, the members of the Interstate Insurance Receivership Commission² formally adopted the Interstate Insurance Receivership Compact's Uniform Receivership Law ("URL"), a comprehensive statutory structure for the administration of what are currently "formal delinquency proceedings," rehabilitation and liquidation as well as "conservation," the seizure and control of an insurer's business and assets on a temporary basis pending further analysis and the decision on whether to pursue either rehabilitation or liquidation.

In November 1999, the board of directors of the International Association of Insurance Receivers ("IAIR")³ adopted a formal resolution recommending adoption of a uniform law such as the URL. In the same month, the URL received the approval of the National Conference of Insurance Legislators.

The URL is the collaborative work product of the Interstate Compact Commission members and the Commission's Receivership Law Advisory Committee ("RLAC"). The RLAC, itself, consisted of a cross section of volunteers from around the U.S. who worked over the span of almost two years, meeting almost monthly. RLAC's membership included representatives of the regulatory community, life guaranty funds, property and casualty guaranty funds, receivers, reinsurers, life insurers, property and casualty insurers, and lawyers who work with these various factions in receivership proceedings.

Since its promulgation in the fall of 1998, a number of states have begun a review of the URL as either a possible new model receivership statute or as a source for new concepts and provisions to supplement their existing statutes.

Although a complete review of the URL and its approach to the receivership process is beyond the scope of this article, there are some aspects of the URL that have been misunderstood. There are many which represent significant improvements to the current system.

What the URL is Not

At least three myths have developed concerning the URL and how it works:

Myth #1: If a state adopts the URL it *must* become a member of the Interstate Insurance Receivership Compact.

There is no requirement that a state become a member of the Interstate Compact as a condition to, or as a result of, adoption of the URL.

To the contrary, although the URL has provisions designed to interface a receivership proceeding and the future development of receivership legislation with the Interstate Compact Commission, excising those provisions, which are few, has no impact on the structure or legal efficacy of the URL. As adopted by the Interstate Compact, the URL has eleven separate chapters and 107 separate sections. Fewer than ten non-substantive changes are necessary to transform the URL into stand-alone legislation.

Myth #2: All receiverships will be administered by Big Brother on Wacker Drive.

Upon entry of an order of conservation, rehabilitation or liquidation, the court is required to appoint the Commissioner/Director/Department, as case may be, as receiver. There is no discretion to do otherwise. The genesis of the Big Brother issue is a series of provisions in the enabling legislation which created the Interstate Compact itself. Under those provisions, there are configurations in a receivership by which the Compact Commission could be asked to perform certain receivership functions. Again, those provisions are not part of the URL.

Myth #3. Enactment of the URL will do away with existing statutory provisions and hard won case law.

During its deliberations and the drafting process, RLAC was sensitive to concerns that an overhaul of the system would somehow come at the expense of existing statutory and case law developments. A deliberate effort was made to preserve valuable case law through consistent statutory provisions. To that extent, the collective thought was that case law had developed in a way inconsistent with the policies inherent in the insurer receivership system and conscious decisions were made to override that case law with specific provisions of the URL.

To further allay concerns over the rewrite, to the extent possible the policies and practices, if not the identical language, of the existing Model Act and Uniform Act were retained.⁴

What the URL Is and How It Will Work

Without impairing the basic framework and substance of the existing systems, the URL differs in a number of significant respects from existing statutory schemes. The URL:

- Adds provisions to address administrative and substantive issues which neither of the existing model schemes deal with adequately.
- Provides a clearer and more complete sequencing of the events which mark the various stages of a receivership proceeding.
- Clarifies the rights of those with a stake in the outcome of the receivership to participate in its administration.
- Promotes a more streamlined administration through statutory clarity which will result in more efficiency, fewer administrative costs, quicker resolution of issues, and earlier distribution of value to policyholders and other creditors.
- Restructures existing statutory provisions to eliminate internal replication and inconsistencies.
- Provides mechanisms for the estimation of claims and classes of claims and for mandatory negotiation and arbitration of reinsurance recoveries.

The Adoption of The Essential Elements of the Existing Schemes

Under the URL only the Commissioner/Director (“Commissioner”) of Insurance may initiate a case and only the Commissioner may serve as the receiver. The basic schemes of conservation, rehabilitation, and liquidation are retained. The basic grounds for initiating a case remain as does the right of the company to contest the action. Because RLAC’s charge was to develop a more effective scheme for administering formal delinquency proceedings, the URL does not address administrative supervision and similar remedies which will continue under existing law.

Guaranty fund obligations are triggered only in those cases where the court enters an order of liquidation with a finding of insolvency, consistent with current legislation. When a liquidation is ordered, policies are terminated except for life and health policies and annuities covered by guaranty funds, which are continued as appropriate to the discharge of guaranty association duties. Rights of creditors are fixed once a liquidation order is entered.

Claims are filed and adjudicated by the receiver’s office with recourse to the court for review of the receiver’s decisions. The priority of policyholder claims over those of general creditors is preserved. Provisions for early access distributions to guaranty funds are retained. The receiver’s ability to recover preferential, fraudulent, and other inappropriate transfers is retained and clarified. Provision for ancillary proceedings and ancillary claims adjudication is retained, although the URL minimizes or eliminates the need for ancillary proceedings.

New Concepts of the URL

While maintaining the basic policies and procedures of the existing schemes, the URL adds new provisions to address issues not adequately dealt with by the Model and Uniform Acts.

The Receivership Court. The URL clarifies and strengthens the jurisdiction and authority of the receivership court by giving it exclusive jurisdiction over all receivership proceedings as well as exclusive jurisdiction over all property of the insurer, “including property located outside the territorial limits of such court.” The court also has non-exclusive jurisdiction over civil disputes arising under or related to the receivership proceedings. Through this combination of jurisdictional grants, all matters that can be adjudicated in the receivership court will be adjudicated in the receivership court. At the same time, the court’s non-exclusive jurisdiction over civil disputes enables a receiver to initiate such cases in the receivership court when appropriate but, if expedient or required because of constitutional constraints, the receiver may seek the assistance of other courts. With a limited exception for defensive counterclaims, all inbound claims against the estate must be brought in the receivership court, as is the case today.

Addressing an issue which impacts many estates and on which there is some diversity of opinion, the URL adopts a policy which expressly preserves existing arbitration rights as they relate to assets of the estate being pursued by the receiver, e.g., reinsurance collection disputes. Contractual arbitration rights of creditors making claims against the estate are eliminated unless the receiver initiates a judicial, administrative or other action against that creditor in which case the arbitration right may be enforced. Otherwise, all claims against the estate must be submitted under the claims filing and adjudication provisions of Chapter 7 of the URL which closely mirrors current practice.

Entities Subject to the Receivership Process. In some instances essential elements of an insurer’s operations have been allocated to affiliates that are not “insurers” within the normal regulatory framework. When formal delinquency proceedings become the remedy of choice for the Commissioner, difficulties can arise concerning those affiliates.

To address this problem, the URL expands the scope of those entities which may be subject to its provisions. In addition to standard, domestic “insurers,” affiliates of an insurer against which a receivership proceeding has been or is being filed under the URL may themselves be the subject of a URL receivership proceeding.⁵ Although they *may* be subject to the receivership process under the URL, the process for taking over such an affiliate is the same as that for taking over the insurer itself, and the grounds for doing so must be established by evidence or agreement. There is no automatic right to take over an affiliate merely because of its status as an affiliate of the insurer.

Uniform Receiver Powers. Although by cross-reference and otherwise, rehabilitators and liquidators under the Model and Uniform Acts are clothed with similar authority and powers, there are subtle differences which, in some cases, can give rise to unintended results.

The grant of authority to a receiver under the URL is applicable whether the receiver is functioning as a rehabilitator or as a liquidator. Beyond the grants of authority to and the responsibility of the office of the receiver, affirmative duties are imposed on third parties to expedite and assist in the collection of assets and records. Those who are in possession or control of property of the insurer “. . . shall . . .” deliver it to the receiver. Those who owe the insurer “....shall....” pay such debt to the receiver. Subject to applicable privilege, those in possession of books and records concerning the insurer’s business “....shall disclose and, on request of the rehabilitator or liquidator,....” turn them over to the receiver.

An Automatic Stay and Affirmative Obligations to Turn Over Assets and Records. As is the case under the Model Act, under the URL the initiation of a receivership proceeding gives rise to a pervasive automatic stay of all acts which may diminish the estate. Additionally, the URL expands the scope of the stay vis a vis actions against insureds and gives the receivership court the ability to extend this third party stay “for good cause shown.” Those who willfully violate the stay are subject to liability for actual damages incurred, including costs and attorney fees, and, where appropriate, punitive damages.

Addressing a split in the courts, the URL permits a creditor to assert counterclaims based on pre-petition obligations of the insurer in any judicial, administrative or other action brought by the receiver.

Beyond this stay of actions against the estate and its assets, the URL clarifies the affirmative obligations of those in possession of assets of the estate, including its books and records. Except for those without knowledge of the filing of the case and subject to limited privilege exceptions, “any person or entity in possession, custody or control” of assets to which the receiver is entitled has an affirmative obligation to turn those assets over to the receiver.

The Right to Appear and be Heard - Balancing the Interests. Entitlement to and the mechanisms available for parties with an interest in the administration and outcome of a receivership under current practice is unclear. On the whole, the URL is designed to strike a balance among the competing interests of those involved with and impacted by the receivership process. This policy of balance is clearly stated in section 304, Right to Appear and Be Heard.⁶

This section is not to be read in a vacuum. While the URL vests rights in parties in interest, with limited exceptions it will be the responsibility of those parties to take it upon themselves to follow the progress of the case. It will also be the responsibility of those parties to bear the costs of participating in the receivership proceeding beyond basic entitlements to notice.

A Document Depository. Although in most jurisdictions there is a high level of cooperation among the receiver’s office, creditors, guaranty funds, reinsurers, and others with a stake in the administration and outcome of the receivership proceeding, in some jurisdictions and some proceedings such is not the case. In order to make the process more transparent for those affected, the URL requires all receivers to establish and maintain a document depository in which copies of all material filings, etc. will be maintained. Absent a contrary receivership order, everything in the depository is public record and must be made available to those interested.

This is not to say that this depository must be a *separate* set of records, replicating that which is already maintained. If the receiver’s existing system contains all of the elements required by the statute, that existing system can qualify as a document depository.

Claims Estimation and Reinsurance Recoveries. Among the most divisive issues existing under current law and practice is the ability of a receiver to estimate claims and concomitantly accelerate reinsurance recoveries based on those estimates. The URL has created mechanisms for dealing with the difficult problems embedded in these relationships in a way which permits the estimation of claims and classes of claims so that the receivership process on the whole can move forward. To strike a balance in this process, the URL gives reinsurers alternative methods for responding to the exposure which can result from the estimation process. The reinsurer may accept the result of mandatory arbitration or may opt to establish a Reinsurance Recoverable Trust, the cost of which must be born by the reinsurer.

A Receivership Plan. To provide an early and, to the extent possible, detailed outline of the receiver’s approach for administering the receivership estate, the URL requires the receiver to develop and file a plan within one year of the order of rehabilitation or liquidation and further requires that the receiver receive court approval of that plan within eighteen months of such an order. If either of these deadlines is not met and there has been no court order entered extending them, any party in interest may file a plan for submission to the court.

A plan need be no more complex than is appropriate to the case for which it is being filed. A simple liquidating plan might say little more than the assets will be liquidated, the reinsurance recovered and claims will be paid in the order of their priority, to the extent possible. At the other end of the plan spectrum could be a restructuring with as much sophistication and financial disclosure as is appropriate.

The mandatory elements of a plan are few. The plan must:

1. except for claims classified by the court as de minimus, provide the same treatment for each claim or interest of a particular class, unless the holder of a particular claim or interest agrees to a less favorable treatment;
2. provide adequate means for the plan’s implementation;
3. to the extent possible, contain adequate information concerning the financial condition of the company and the

effect of the plan or identify sources from which that information can be obtained;

4. provide for the transfer of books, records, documents and other information relevant to the duties and obligations covered by the plan;
5. provide for the notice to parties in interest of the provisions of the plan and an opportunity to be heard; and
6. provide for the termination of the receivership proceedings and discharge of the receiver, if appropriate.

While the scope of mandatory plan elements is fairly limited, the scope of what a plan *may* provide is only limited by the fundamental rights of those affected and the imagination of the receiver. By way of example only, a plan *may*:

1. establish trusts to implement its terms,
2. provide for substitute life or health insurance products or annuities,
3. provide for early access distributions,
4. create and provide for separate classification and treatment of *di minimus* claims in order to make future administration more efficient.

If the plan otherwise meets these statutory elements and it is determined that the plan provides each class of claims not less than what they would receive if the assets were merely liquidated and their value distributed, it may be approved by the receivership court.

At least three significant benefits inure to the process through the adoption of the plan approach:

1. Upon entry of the order approving the plan, the provisions of the plan and the order approving it are binding on the insurer, policyholders, other creditors and the company's equity holders. While this may invite those so inclined to raise issues in the course of the plan approval process, this concern is more than balanced by the ability to deal with those issues in a single forum charged with balancing the interests of all parties in interest.
2. Interim distributions can be made to policyholders and others with allowable claims at the same level. Although for a number of reasons the Model Act contains provisions for early access distributions to involved guaranty funds, there is no direct counterpart for distributions to policyholders and others holding claims of the same class.
3. Small claims for which administrative costs may outweigh the benefits provided to the claim holders may be separately classified and treated, eliminating the need to carry them through the receivership process.

Interstate Relations

The interstate relations provisions of the Uniform Act are incorporated in the URL as is a new provision which allows for the filing of a foreign receivership order in a URL state. Once filed, that order is given the same effect and is enforceable as if it was an order of the URL state's own court.

Conclusion

Early in the process of developing the URL, the RLAC members agreed that they did not perceive the current system as "broken." To the contrary, much of the existing system works well in many cases, and all of the existing system works

well in some cases. The URL provides a more complete scheme that can provide reasonable participation, uniform entitlements, predictability and consistent results in all receivership proceedings.

Endnotes

1. The authors are both partners in the Omaha based law firm of Lamson, Dugan & Murray. Mr. Dugan formerly served as Director of Insurance for the State of Nebraska. Mr. Craig is president of the International Association of Insurance Receivers and served as lead reporter to the Receivership Law Advisory Committee of the Interstate Compact Commission.
2. Membership in the Commission consists of the three compacting states: Michigan, Illinois, and Nebraska.
3. Information concerning IAIR, its members, and activities can be found on the Internet at www.IAIR.org.
4. As of July 1998, the NAIC reports the following 33 jurisdictions have adopted the Model Act or similar Legislation: Alaska, Colorado, Connecticut, D.C., Georgia, Hawaii, Idaho, Indiana, Iowa, Kansas, Kentucky, Maine, Michigan, Minnesota, Mississippi, Missouri, Montana, Nebraska, Nevada, New Hampshire, New Jersey (Life Insurers), North Carolina, North Dakota, Ohio, Pennsylvania, Rhode Island, South Carolina, South Dakota, Tennessee, Utah, Vermont, Washington, and Wisconsin. The Uniform Act is reported to have been adopted in 19 jurisdictions: Alabama, Arizona, Arkansas, California, Delaware, Florida, Guam, Illinois, Louisiana, Maryland, Massachusetts, New Jersey (P/C Insurers), New Mexico, New York, Oklahoma, Puerto Rico, Virgin Islands, West Virginia and Wyoming.
5. § 401 Entities Subject to This Act, subsection E:

The receivership proceedings authorized by this Act may be initiated against any insurer and against any of the following persons, if not an insurer, including, but not limited to, the following:

agents, managing general agents, brokers, premium finance companies, insurers, insurance holding companies, and all other non-risk-bearing entities engaged in any aspect of the business of insurance, whether or not such entities are licensed to engage in the business of insurance in this state, if such person is an affiliate of the insurer against which a receivership proceeding has been or is being filed under this Act.

6. URL § 304 Right to Appear and Be Heard.
 1. A party in interest may raise and may appear and be heard on any issue in a receivership proceeding under this Act, without reimbursement of attorneys' fees or expenses unless such reimbursement is expressly authorized elsewhere by the statutes of this state. This subsection shall not affect any right of a reinsurer under a reinsurance contract to recover reasonable fees and expenses to which it is entitled in connection with the interposing of defenses to a claim against the insurer.
 2. Any guaranty association or association of guaranty associations which is or may become liable to act as a result of the entry of an order of receivership shall have standing to intervene as of right or otherwise appear and participate in a receivership proceeding under this Act. Exercise by any guaranty association or association of guaranty associations of the standing rights conferred under this subsection shall not constitute a submission to the general jurisdiction of the courts of this state.