

SUBJECT: Establishing the Insurer Receivership Act

COMMITTEE: Insurance — committee substitute recommended

VOTE: 9 ayes — Smithee, Seaman, Eiland, Isett, B. Keffer, Oliveira, Taylor, Thompson, Van Arsdale
0 nays

WITNESSES: For — None
Against — Brad Kading, Reinsurance Association of America; Brenda Nation, American Council of Life Insurers
On — Jose Montemayor, Texas Department of Insurance

BACKGROUND: Insurance Code, art. 21.28 concerns liquidation, rehabilitation, reorganization, or conservation of insurers.

DIGEST: The bill would amend Insurance Code, Title 1 by adding ch. 21 A, the Insurer Receivership Act, and repealing art. 21.28.

General provisions. The stated purpose of the Insurer Receivership Act is to protect generally the interests of the insured, claimants, creditors and the public. The bill would not limit the powers granted under other provisions of the law but would be cumulative, in addition to other laws .

Insurer receivership laws and related laws governing guaranty associations would be construed together in a consistent manner. In the event of a conflict, the bill would prevail.

The bill would include a comprehensive list of persons, corporations, associations, or entities that were subject to delinquency proceedings. It also would contain definitions for terms used in the chapter.

The section on jurisdiction and venue would provide that a delinquency proceeding — any proceeding instituted against an insurer for the purpose of liquidating, rehabilitating, or conserving the insurer — would be filed in district court in Travis County.

The bill would exempt the receiver from paying any filing, recording, transcript, or authenticating fees.

It would establish requirements for notice to interested parties and would set out procedures for hearings of matters submitted by to the receivership court for approval. It would provide that the receivership court could issue orders, including stays or injunctions, to carry out the provisions of the bill. CSHB 2157 would state that the filing of a receivership petition would serve as a stay against certain actions against the insurer and its assets.

The bill would provide for limitation periods for actions brought by the receiver.

Those acting on behalf of an insurer in receivership would have to cooperate with the receiver or commissioner of insurance and would establish penalties for a violation of orders.

The bill would address applicability of defenses to actions brought by the receiver and would maintain that the receiver would not be considered a governmental entity for the purpose of any state law permitting the award of fees against a state agency.

It would define defenses and claims that could not be asserted by affiliates, controlling or controlled persons, present or former officers, managers, directors, trustees, or shareholders.

The bill would give the receiver the right to assume or reject any executory contract or unexpired lease. It would specify the competitive bidding process and promotion of historically underutilized businesses (HUBs) in soliciting for a special deputy receiver.

The bill would extend immunity to all present and former receivers, assistants, and contractors for actions or omissions, except for intentional misconduct, and would allow for indemnification for the receiver and assistants.

The bill would create a process for approval and payment of expenses of the receivership. It would declare timeframes for filing financial reports to the receivership court and filings and formats for reports by each affected guaranty association to the liquidator.

The bill would vest the receiver with title to all books and records and would give the receiver authority to certify the records. It would exempt the records from Government Code, ch. 552, the Open Records Act.

Proceedings prior to receivership order. The receivership court could issue an *ex parte* seizure order without notice of hearing that would allow the seizure of an insurer for a limited duration.

The bill would define grounds for a petition for formal delinquency proceedings. It would provide for summary hearings by the court on receivership petitions.

The receivership court would expedite receivership hearings and would grant continuances only in extreme circumstances. It would permit discovery that would be limited to grounds alleged in the petition and would be expedited. The receivership court would have to enter a judgment within 15 days of conclusion of evidence with any appeal occurring before the fifth day after entry of the judgment.

The bill would establish confidentiality of all proceedings for a seizure order and would define conditions for making such records public. Also, it would permit sharing of information with other state insurance departments or guaranty associations where the confidentiality of those records could be maintained.

The bill would outline the grounds under which the commissioner could petition the court to conserve, rehabilitate, or liquidate a domestic insurer, an alien insurer domiciled in the state, or an unauthorized insurer. It would state that the receivership court would grant the petition and issue the order, if the commissioner established the statutory grounds.

Neither the filing of the petition nor the entry of the order of seizure, rehabilitation, or liquidation would constitute a breach of any contract or lease.

Rehabilitation. The bill would give the requirements and contents of a rehabilitation order. It would grant the rehabilitator authority to direct and manage the insurer, to hire and discharge employees, and to deal with the property and business of the insurer. Under the bill, the rehabilitator would file a rehabilitation plan with the receivership court. The bill would specify the provisions that a plan would contain.

The bill would establish conditions for terminating the rehabilitation, moving for liquidation, or restoring the insurer to possession of its property and control of its business. It would permit information sharing with guaranty associations in order to ensure an orderly transition to liquidation.

Liquidation. The bill would state the requirements and contents of a liquidation order. It would establish timeframes for continuation of insurance coverage by an insurer in liquidation. It would provide for the cancellation of certain reinsurance contracts.

The bill would authorize the receiver to sell the insurer's corporate entity or charter and its licenses, with court approval, and would describe steps for dissolution of the charter if it were not sold.

It would detail the liquidator's authority to retain assistants, appoint deputies, and take action on behalf of the insurer. It would specify how notice of the liquidation order would be given and to whom it would be given, and it would specify contents of such notice.

The bill would compel agents of the insurer to provide information in their records related to any policy issued by the insurer and would allow penalties for failure to comply.

Asset recovery. The bill sets forth procedures by which the liquidator could make demand for the insurer's funds or property and would permit costs and expenses in order to recover the insurer's funds or property.

The bill would give the liquidator the right to seek recovery of any asset transferred to or for the benefit of an affiliate if the transfer were made within five years of receivership and would permit the liquidator to recover costs and expenses including attorney's fees incurred in obtaining the asset.

The bill would invalidate certain preferential post-receivership transfers. It would define conditions under which the receiver could avoid a preference. It also would allow the receiver to avoid any transfer of an interest of the insurer made within two years before the filing of the receivership petition if fraud were involved or if the insurer received less than a reasonable equivalent value.

The bill would authorize the receiver to avoid transfers or liens upon property or incurred obligations that the insurer could have avoided. It would permit the receiver to recover the property or its value from a transferee and would state conditions under which recovery would not be allowed. The bill would provide that a claim could not be allowed if the creditor had obtained a preference, unless the preferential transfer had been surrendered. It would describe the circumstances under which setoffs could be permitted and would establish procedures for determining assessments for assessable policies.

The bill would set out procedures for treatment of reinsurance contracts. It would establish methods for collecting premiums due from insureds, agents, third-parties, or premium finance companies and would provide penalties for violations. It also would describe the treatment of collateral held to secure obligations of a policyholder under a deductible agreement by guaranty associations and the receiver.

Claims. The bill would state that the last date for filing proofs of claim would be 18 months after entry of the liquidation order, unless extended by the receivership court, and would provide exceptions for late claims. It would specify items that would be included in proofs of claim filed with the receiver, including certain provisions related to claims filed by guaranty associations.

The bill would give procedures for the review and evaluation of claims and notice to affected reinsurers. It would permit disallowance of *de minimus* claims. It would permit filing of claims under occurrence policies and would provide procedures for the allowance of contingent and unliquidated claims.

The bill would allow third-party claims against an insured and the payment of distributions upon the resolution of the claim by the third-party.

The bill would set forth procedures for disputing the receiver's action on a claim and presenting settled or allowed claims to the receivership court for approval. It would permit the filing of a claim on behalf of a person liable to a claimant, if the claimant had not filed timely a proof of claim.

The bill would include procedures to determine the value of security held by a secured creditor and to credit the secured claim.

A person could not be prohibited from exercising a contractual right to terminate, liquidate, or close out any netting agreement or qualified financial contract. The bill would establish procedure for the receiver in netting agreements.

Distributions. The bill would specify classes for determining the priority of distributions on unsecured claims. It would set forth the procedures for interim and final distributions on claims. Also, it would provide timing for early access payments to guaranty associations and would give procedures to handle any unclaimed funds after the final distribution.

Discharge. The bill would prohibit an insurer released from receivership from resuming business unless guaranty associations were repaid.

It would specify termination of liquidation proceedings and discharge of the liquidator. The bill would allow for the reopening of the liquidation for good cause, such as the discovery of additional assets. It would give procedures for destruction of unneeded records and maintenance of retained records. The bill would permit the receivership court to order audits.

Interstate relations. The bill would describe actions that the commissioner could take with respect to foreign insurers. The state would give full faith and credit to other receivership laws and orders of other state receivership courts when an insurer was placed in receivership.

The bill would expand the definition of transfer of investment or credit risk without insurance risk to include transactions involving captive insurers, deductible or self-insured policies that equal policy limits, and transactions where the insured retains a substantial portion of the risk.

It also would exclude within the definition of “covered claim” any direct or indirect return of premium under a retrospective rating plan or any other direct or indirect claim asserted by a reinsurer, insurer, insurance pool, or underwriting association.

The bill would exclude unknown or unreported claims at the bar date, except worker’s compensation claims, and would permit the guaranty association to bring an action against third parties to obtain custody of claims and related records in order to carry out obligations.

The bill would establish venue in Travis County for any action by or against the guaranty association or the commissioner.

It would define recoveries to which the guaranty association was entitled and claims excluded because of the insureds' net worth at the time of the delinquency proceeding.

It would amend Art. 21.28-C, sec. 17(a) not to toll any statute of limitations or repose during a stay by the receivership court.

The bill would take effect September 1, 2005 and would apply only to a receivership proceeding brought against an insurer that was pending on the effective date and to a receivership proceeding initiated on or after that date.

**SUPPORTERS
SAY:**

CSHB 2157 would adopt the draft of the National Association of Insurance Commissioners (NAIC) Insurer Receivership Model Act as the Insurer Receivership Act. The bill would contain procedures designed to protect the interest of policyholders, claimants, and creditors by improving efficiency of insurance receiverships. The adoption of this model would clarify the law, minimize uncertainty, and litigation and promote cooperation in multi-state receiverships. The bill also would give the commissioner of insurance additional authority to act sooner to take control of a failed insurer.

The last significant update of art. 21.28 was in 1991 when the Legislature revised the statute to authorize the appointment of special deputy receivers. The NAIC Model Act was not adopted as part of the Texas Legislature's update in 1991. As a result, Texas may not be considered a reciprocal state and other states may not enforce receivership court orders issued in Texas. This has the potential effect of giving preferences to non-Texas claimants over Texas claimants or giving preferences to parties who sue Texas insurers in another state. CSHB 2157 would make Texas receivership orders enforceable in other states adopting the NAIC model law.

**OPPONENTS
SAY:**

CSHB 2157 contains overly broad immunity and indemnification provisions for all present and former receivers, assistant receivers, and receivers' contractors. Under the bill, a receiver, the receiver's assistants, and the receiver's contractors — present and former — would be immune from suit and liability for any claim for damage or loss of property or

other civil liability caused by or resulting from any alleged act, error, or omission. Although the bill would state that the immunity would not extend to intentional or willful and wanton misconduct, intent could be difficult to prove. As written, the bill would seem to encourage negligence and acts of omission or commission in dealing with very large sums of other people's money.

CSHB 2157 would incorporate the NAIC Insurer Receivership Model Act, which has yet to be adopted, because it is still a work in progress. The Texas Legislature should follow this approach and work to further refine this receivership act more before considering its adoption.

NOTES:

The committee substitute differs from the bill as introduced, making numerous changes, including:

- competitive bids for special deputy receiver contracts;
- minimum standards for reporting and filing requirements;
- procedures for reporting of workers compensation claims;
- elimination of ancillary receiverships;
- extension of 30-day claims appeal period to 45-day period; and
- deletion of provision permitting third parties to apply for a termination order.