



Portfolio Media, Inc. | 860 Broadway, 6th Floor | New York, NY 10003 | www.law360.com
Phone: +1 646 783 7100 | Fax: +1 646 783 7161 | customerservice@law360.com

Health Republic's Curious Liquidation: Part 1

Law360, New York (June 21, 2016, 11:59 AM ET) -- Health Republic Insurance of New York, New York's only Affordable Care Act nonprofit health insurer, has finally been placed in liquidation. Health Republic's liquidation definitely could use a policyholders' committee and a health providers' committee to sort out how this failed insurer will be wound up, particularly given the liquidation's chaotic and belated commencement.

Health Republic's failure took up a substantial part of the New York Senate Insurance Committee's June 8 confirmation hearing for then-Acting Department of Financial Services Superintendent of Insurance Maria T. Vullo^[1] and certainly got a lot of attention when it failed. For those familiar with Health Republic's demise, skip to: "Health Republic's Liquidation." For those who are not familiar with the Health Republic story, a little background is in order.



James Veach

Nonprofit Obamacare Co-Ops

The 2010 Affordable Care Act included a Consumer Operated and Oriented Plan Program to create nonprofit insurance companies or Co-Ops. Congress intended for these Co-Ops to compete against larger (and increasingly fewer) for-profit health insurers like Anthem, UnitedHealthcare and Aetna.

Under the ACA, the federal government's Department of Health and Human Services and its Centers for Medicare & Medicaid Services were to provide capital for the Co-Op program.^[2] Congress, however, did not preempt state regulatory oversight over the Co-Ops themselves.^[3] As a result, even though federal tax dollars funded the Co-Ops, state insurance regulators remained responsible for Co-Ops operating in their states. In New York's case, that meant that NY's DFS had to approve Health Republic's rates and policy forms and assure that the Health Republic stayed solvent.^[4]

Twenty-three Affordable Care Act Co-Ops were ultimately established in 26 states. For a comprehensive, albeit arguably partisan, review of the Co-Op program and the poor job done by the federal government overseeing the Co-Op program, see *Failure of the Affordable Care Act Health Insurance Co-Ops*, Majority Staff Report of the Permanent Subcommittee on Investigations for the Committee on Homeland Security and Governmental Affairs (March 10, 2016) (Portman report).^[5]

Freelancers' Union Applies to the Co-Op Program

In February 2012, the CMS approved the Freelancers Union's application to participate in the Co-Op program. The Freelancers Union is a nonprofit, New York-based organization that advocates for and makes health insurance available to its more than 300,000 members, most of whom work as consultants, independent contractors, temps and part-timers and more than half of whom live in New York State.

When CMS approved Freelancers' application to participate in the Co-Op program, CMS also approved two loans: (1) a \$23.7 million startup loan and (2) a \$151 million solvency loan. The solvency loan covered capital reserves and other solvency requirements imposed by the DFS.

In July 2013, the DFS licensed Freelancers to write health service indemnity coverage. In October 2014, Freelancers had changed the name of its Co-Op to Health Republic of New York. The DFS approved Health Republic's proposed rates, rates that were far lower than any of its competitors.

In September 2014, the CMS approved an additional \$90 million loan to Health Republic in order to satisfy reserve requirements set by the DFS. This brought the total solvency funding to about \$241 million. (Health Republic later sought an *additional* \$70 million loan, but by then HHS had exhausted its Co-Op loan authority and Congress had refused to provide further funding.)^[6]

The DFS required that Health Republic, now a licensed NY health insurer, submit annual and quarterly financial statements to the superintendent. Health Republic was also subject to examination by the DFS at any time. Health Republic opened offices located at 30 Broad Street in Manhattan, literally around the corner from DFS' offices.

Health Republic's Short, Unhappy Life

Health Republic began writing on Jan. 1, 2014. Within hours, 30,000 people signed up, including five new enrollees who were admitted to Memorial Sloan Kettering Cancer Center for expensive treatment. For a comprehensive take on how and why Health Republic failed, see M. Waldholz, The short and chaotic life of an Obamacare darling, Crain's New York Business.[7]

The Crain's article describes many missteps, including management's decision to set rates below those recommended by its actuaries at Milliman Inc. and the then superintendent approving those too-low rates, then refusing to allow the new Health Republic CEO to increase Health Republic's rates.

The Crain's article also addresses what Waldholz characterizes as the DFS's failure to monitor Health Republic. Although Health Republic lost more than \$77 million in its first year of operation, the DFS waited until early 2015 to demand monthly, as opposed to quarterly or annual, financial statements and allowed Health Republic to continue to issue policies until Oct. 31, 2015. By that time, Health Republic had lost \$544 million in 2015 alone.

In January, joint New York State Senate Committees on Health and Insurance conducted a hearing in Albany concerning Health Republic's collapse.[8] During the hearing, Insurance Committee Chairman James L. Seward asked, but was not answered, why the acting superintendent of insurance had not already petitioned to place Health Republic in receivership.

Liquidating a Failed NY Insurer

New York-domiciled insurers that fail are placed in liquidation under New York Insurance Law Article 74.[9] Since 1909, the New York Liquidation Bureau (NYLB), a non-New York state agency that operates outside the DFS (and its Division of Insurance), has overseen the rehabilitation or liquidation of troubled/failed New York insurers.[10] Under Article 74, New York insurance company liquidation proceedings are subject to the exclusive jurisdiction of a New York Supreme Court Justice.[11]

Article 74 calls for the superintendent, in her/his role as liquidator to prepare a plan to liquidate the insurer.[12] Within 180 days after the order of liquidation has been entered, the superintendent should apply to the court with a proposal to disburse the failed insurer's assets.[13]

Claimants, be they policyholders, general creditors or others, are to submit their claims against the estate within four months of the entry of the liquidation order pursuant to a claims procedure devised by the superintendent, although this four-month claim submission deadline is often extended.[14] Claims are then divided into nine classes and, under the court's supervision, every claim in each class is paid in full before the members of the next class receive any payment.[15]

Health Republic's Liquidation

The receivership process for Health Republic is off to a slow start.

About half of the original 23 ACA Co-Ops had failed by early 2016.[16] Nevertheless, New York was one of the last states with a troubled Co-Op to place its Co-Op under supervision or in rehabilitation or liquidation.

State insurance regulators in Iowa, Nebraska, Louisiana, Nevada, Kentucky, West Virginia, Tennessee, Colorado and Oregon obtained orders of supervision, rehabilitation or liquidation for failed Co-Ops in late 2014, throughout 2015, or by the latest January 2016. [17]

The DFS directed that Health Republic cease writing new policies on Sept. 25, 2015, but did not cancel Health Republic's existing policies. Nevertheless, based on a subsequent DFS and CMS review of the company's finances, the DFS and CMS announced on Oct. 30, 2015 that it would be "in the best interest of consumers to end all Health Republic policies ... on Nov. 30, 2015." [18]

Even though Health Republic had at that point lost more than half a billion dollars and would receive no additional HHS funding and even though Health Republic's board had consented in October 2015 to have the company placed in liquidation, the DFS waited until April 22, 2016 to petition for an order liquidating Health Republic and placing it under court supervision.

In almost all instances, the NYLB works in conjunction with state guaranty insurance funds that pay, up to a statutory limit, approved policyholder claims. Although New York has several different guaranty funds for policies written by insolvent insurers writing property-casualty, life, workers' compensation and automobile insurance, New York does not have a guaranty fund for a failed health insurer, including an ACA Co-Op. While policyholders in Co-Ops in Colorado, South Carolina and Iowa have access to guaranty funds, Health Republic's policyholders have no guaranty fund capable of paying some or all of their allowed unpaid medical claims.

The Liquidation Begins

In New York, the liquidation process usually begins with an application from the New York attorney general for an order to show cause (OTSC) why the insurer should not be placed in liquidation. In the case of a domestic insurer, notice of the OTSC must be given to the insurer's president with constructive notice usually provided to its policyholders through publication in newspapers or by other means as required by the court issuing the OTSC.[19]

The Health Republic OTSC required service on only one person: Ronald J. Vance Jr. Vance, however, is not Health Republic's president. Vance is the Chief Restructuring Officer of Health Republic and an employee of Alvarez & Marsal, a financial advisory firm that is assisting with Health Republic's runoff.[20]

Although the OTSC did not direct that notice be mailed to Health Republic's policyholders and health providers, on May 10 about five dozen Health Care members/policyholders, as well as a few health providers represented by counsel, crowded into Justice Carol Edmead's courtroom on the fourth floor of 60 Centre Street.

The court quickly discovered that many Health Republic policyholders attending the hearing spoke only Spanish. The court directed that a Spanish interpreter translate the proceedings. After an assistant attorney general completed his presentation urging that a liquidation order be entered, the court determined that no objections to the liquidation itself had been filed and granted that part of the application.[21]

Interestingly, counsel that had been representing Health Republic after the DFS directed that Health Republic cease writing business or paying claims, but before the liquidation, Weil Gotshal & Manges LLP, then addressed the court as counsel for Acting Superintendent Vullo.

Although no party opposed the liquidation itself, an objection had been filed concerning the scope of an injunction within the proposed liquidation order. This provision would enjoin not only the commencement or prosecution of any action against Health Republic, the NYLB or the acting superintendent in her role as liquidator, but would also bar any action on her claim against the DFS and would thus enjoin the pro se objector's previously commenced suit against the DFS.

The court denied the motion to modify the injunction, but you can find on another website a copy of the papers objecting to the scope of the injunction. This website is maintained by the Garden City Group, which describes itself on its website as an organization that handles "complex class action settlements, bankruptcy reorganizations, mass tort administrations and legal notice programs like no one else."

No NYLB Involvement

Ordinarily, the NYLB marshals a failed insurer's assets, collects all records, establishes a claims procedure, processes policyholder claims, collects reinsurance and otherwise winds up the company. Although Acting Superintendent Vullo has designated two persons at the NYLB and one former NYLB employee who now works at the DFS, as her agents with respect to Health Republic, at this point it, appears that the NYLB's role with respect to NY's failed Co-Op is confined to posting court orders on its website.

With respect to their claims, Health Republic's policyholders are, at this point, being directed to the website maintained by the Garden City Group. This website advises that Health Republic's policyholders should "submit their claims for out-of-network services by March 31, 2016 in accordance with the procedures and deadlines set forth in their insurance policies" and that they will receive an "Explanation of Benefits statement ... as soon as available."

Brokers and vendors, however, are told not to bother filing claims in that "it is highly unlikely that Health Republic will have sufficient funds to pay any claims," other than administrative expenses, i.e., the expenses presumably already incurred and being incurred by vendors such as Alvarez & Marsal, the Garden City Group and Weil Gotshal.

Health Republic's last quarterly financial statement covered the period ending on June 30, 2015. At this point, it remains unclear how much of Health Republic assets remains or when the liquidator will establish an Article 74 claims procedure.

Nothing has been posted on the NYLB or the Garden City websites with respect to Health Republic's assets and liabilities. Under these circumstances, committees of policyholders and health providers would assist greatly in opening up and expediting Health Republic's liquidation. This will be examined more closely in the second part of the article.

—By James Veach, Mound Cotton Wollan & Greengrass LLP

James Veach is a partner in Mound Cotton's New York office.

The opinions expressed are those of the author(s) and do not necessarily reflect the views of the firm, its clients, or Portfolio Media Inc., or any of its or their respective affiliates. This article is for general information purposes and is not intended to be and should not be taken as legal advice.

[1] Acting Superintendent Maria T. Vullo's testimony during her June 8, 2016 confirmation hearing. The NY State Senate confirmed Gov. Andrew Cuomo's appointment of Vullo on June 15, 2016.

[2] The Affordable Care Act also provided certain "risk sharing" mechanisms to shift funding among the Co-Ops and provide certain excess reinsurance in order to help these new insurers deal with policyholders, many of whom were previously uninsured. See generally, Durkin & Taylor, *Emerging Disputes Over Risk Sharing Under The ACA*.

[3] Under the McCarran-Ferguson Act, 15 U.S.C.A. §§ 1011 et seq. (2016), Congress left the business and regulation of insurance to the states unless a federal statute "specifically relates to the business of insurance." See *United States v. Fabe*, 508 U.S. 491, 493, 498 (1993).

[4] See generally, *Obamacare's Co-Ops: The "Charter Schools" of Health Care*, 17 *Quinnipiac Health Law Journal* 105 (2013-2014).

[5] Sen. Portman left Congress in 2005 to serve as the United States Trade Representative and then served as the Director of the Office of Management and Budget under President George W. Bush.

[6] Portman Report, p. 43, n. 257.

[7] Crain's commissioned this article, supported in part by a CUNY Journalism School Grant. Waldholz is a Pulitzer-winning former editor and journalist at the Wall Street Journal and Bloomberg News.

[8] You can view a video of the hearing here.

[9] See generally, *NEW APPLEMAN NEW YORK INSURANCE LAW* (2d. Ed.) Vol. 3, Ch. 45 (2015) (APPLEMAN).

[10] *Dinallo v. DiNapoli*, 9 N.Y.3d 94, 103 (2007) ("The Bureau is not part of the Insurance Department's budget, operates without the benefit of state funds, maintains its own errors and omissions coverage and is represented by its own private counsel, not the Attorney General, as is normally the case when a state agency is sued.") For a comprehensive critique of the Bureau and how it might be improved and restructured, see P. Bickford, *New York's Liquidation Bureau: a Critical Analysis, Parts I and II*, *Insurance Advocate*, No. 10 (May 18, 2009) at 18 and No 11 (June 1, 2009) at 24.

[11] *Knickerbocker Agency Inc. v. Holz*, 4 N.Y.2d 245, 252 (1958 quoting *Motlow v. Southern Holding & Securities Corp.*, 95 F.2d 721, 725-26 (8th Cir. 1938) ("[I]t is essential that the title, custody, and control of the [insolvent insurer's] assets be entrusted to a single management under the supervision of one court.")

[12] *In re Lawyers Title & Guar. Co.*, 254 App. Div. 491, 495, 5 N.Y.S.2d 484, 487 (1st Dept. 1938), reh'g denied, 255 A.D. 1032, 9. N.Y.S. 2d 126 (1st Dept. 1938) ("The Superintendent may not be compelled to surrender his trust created by statute. * * * He may ask the help of the Court in solving the problems which arise from time to time but all propositions for the liquidation of the corporation must be approved by him." * * * There is nothing to prevent the Superintendent himself from negotiating with parties interested for the formulation of an appropriate plan of liquidation, and, when he has decided upon such plan, it may be submitted for the approval or disapproval of the court.")

[13] NYIL § 7405 (f)(1).

[14] NYIL § 7432(b).

[15] NYIL § 7434.

[16] C. Borrelli, What The Demise of Insurance Co-Ops Says About the ACA, www.law360.com/articles/748140.What-the-demise. (January 22, 2016).

[17] Portman Report, pp. 10-15.

[18] NYDFS, NYSOH, CMS Announce Additional Actions Regarding Health Republic Insurance of New York. The New York Department of Health then oversaw an emergency effort to enroll Health Republic policyholders with 15 other NY health insurers.

[19] NYIL § 7418 (a)(1).

[20] Crain's Article at 11/19 ("The insurer's office in downtown Manhattan shut down in November and its assets, if any, are being managed by the restructuring firm Alvarez & Marsal, which didn't return calls for comment.")

[21] The Court also directed that a copy of a transcript of the May 10 proceeding, including a Spanish translation, be posted on the NYLB website.

All Content © 2003-2016, Portfolio Media, Inc.