INTERNATIONAL ASSOCIATION OF INSURANCE RECEIVERS
PROMOTING PROFESSIONALISM AND ETHICS

THE INSURANCE RECEIVER

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PRESIDENT'S MESSAGE

Donna Wilson –CIR-MIL

Autumn…Harvest….Football……Fall has arrived in Oklahoma. A season of change – leaves, temperature, daylight, time and IAIR Directorship. And with that change, my time as IAIR President will soon end. It has been an honor and pleasure to serve and as I reflect, I realize we have accomplished much. However, as my term ends, there is still much to do.

We continue to work towards a new designation process. Documentation has been fully developed and exposed to members and changes made to the grandfathering provision after considering the comments received. The next step is to seek funding support from parties that will benefit from qualified receivers and their staff.

Work continues towards a webinar/podcast series on receivership basics. An outline has been developed and now it is time to start scripting each session and move toward production.

Soon we hope to develop an on-line presence where members can share our successes, concerns, passions, joys and sorrows. I hope this will be a supportive and responsive resource to all our members and those we serve.

Communications/relations with the International Committee have been re-established and we look forward to assisting this vital part of our organization as they move forward with providing events and assistance for our non-US members.

We have worked to develop, revise and implement many operational procedures. However, with each step we identify other areas to be considered.

I am very thankful for the support and efforts of my fellow directors, committee chairs, general counsel, sponsors, and the membership. And I would be remiss if not to mention Bart Boles as Immediate Past President. I hope I can be as much of a resource and support for my successor as Bart has been to me.

I started my first message as President with IAIR's mission statement that has served us well for years. However as the Board considered IAIR's future, we realized it stated more what IAIR does than why. I shall conclude this, my last message as President, with the mission statement being considered by the membership at the upcoming annual meeting in Honolulu.

"To serve as a resource and promote best practices for the resolution of troubled insurance companies and enhance expertise among the community."

With great fondness ~~ Donna

WHAT DOES BREXIT MEAN TO THE INSURANCE INDUSTRY? A REPORT FROM THE UK

By Vivien Tyrell, Partner Reynolds Porter Chamberlain LLP

Participants in the global insurance industry will be looking at events in Europe with great interest. Many will want to know how it affects their own business either in terms of investment or if they are purchasers of reinsurance from the UK or other members of the EU.

This note gives an update on the contingency planning being undertaken by regulators and firms in order to smooth the effects of the UK's withdrawal from the EU.

Time line

On 23 June last year the referendum in the UK on whether the UK should leave the EU was held resulting in a very significant majority voting to leave.

On 29 March of this year the UK served notice under Article 50 of the Treaty on the European Union triggering the UK's departure from the EU automatically on 29 March 2019 unless an extension is agreed between the UK and all 27 remaining EU Member States.

Effects on the insurance and wider financial services industries

You will be aware that the UK 's membership of the EU bloc has allowed financial services providers in the UK and other EU States to reap big benefits from the mutual system of "passporting". Passporting allows those firms to sell those services throughout the bloc as well as in Iceland, Liechtenstein and Norway which together comprise the European Economic Area (EEA). Under this system, there is mutual recognition of each Member State's regulatory standards allowing e.g. insurers and banks to market their services throughout the EU while only needing to be regulated by their home state regulator. In the UK the regulators in question are the Prudential Regulation Authority (PRA) (whose focus is not only on protecting the end user but also on maintaining a robust financial industry in a fully working financial services market) and the Financial Conduct Authority (FCA) (which, as its name implies, is focussed on fair conduct and protection of the end user).

The passporting regime is found in a number of EU Directives and Regulations which have been implemented in the form of legislation in each Member State over some 45 years. That legislation is enforced by the courts in each Member State subject ultimately to rulings by the European Court of Justice in Luxembourg.

Outside the perimeter of the bloc insurers and banks in "third countries" such as the US have to be authorised in one of the EU States in order to operate in that State and that authorisation process is facilitated when third country regulation and resilience in the industry in question (e.g. insurance or banking) has "equivalence" with that of Member States of the EU. This seems to have worked well historically between the US and the EU with US branches gaining authorisation in order to sell their services in any given EU State. Also, by establishing an authorised subsidiary in one EU State, a US insurance group can gain access to this single market.

The UK's withdrawal from the EU without an EU wide agreement on the continuation of passporting would mean a viable alternative having to be put in place instead. Detailed analysis is being undertaken in the UK and in EU counterpart countries about the effects of withdrawal on both UK authorised firms and those authorised in different home States. It is in each side's commercial interests for passporting to continue or for a viable alternative to be agreed.

What practical steps are being taken at the moment?

Cleary insurers and banks cannot await the outcome of negotiations between the UK's Department for Exiting the EU and Michel Barnier on behalf of the remaining 27. While a lot of press coverage has been spent claiming very little progress is being made, there has been a lot of activity at business operational level both driven by commercial imperatives and as a result of regulator requirements.

Market sources indicate that some UK based firms are actively "de-branchifying" i.e. setting up subsidiaries in other EU States to replace their branches, seeking approvals from local regulators in those other States. In some cases those subsidiaries are earmarked as group companies controlling activities with the aim of outsourcing the operational work to the UK as a third country. In this way it is hoped access to the single market will be maintained. Similarly, firms which are regulated in another EU State are seeking authorisation to provide services in the UK. It is a two way street whose traffic must continue to flow.

On 7 April this year Sam Woods, the Deputy Governor and CEO of the PRA sent a letter to CEOs of regulated entities (banks, insurers and designated investment firms) which undertake cross-border activities between the UK and the rest of the EU. The letter stated the PRA's expectation was that all such firms would undertake "appropriate contingency planning" for the UK's withdrawal from the bloc. The aim of the Government is cited as being a new trade relationship with the EU coupled with an implementation period i.e. after the 29 March 2019. The letter acknowledged that there would be a wide range of outcomes so that firms were expected to plan for a variety of potential scenarios. The letter expected firms to make plans assuming one outcome would be no agreement having been reached with the 27 by 29 March 2019 and no implementation period. Contingency plans have got to be made and firms stand ready to execute them in order to maintain safety and soundness of their UK operation mitigating the risk of any adverse stability impacts on the UK economy as a whole. Responses from the firms confirming what contingencies are being implemented were required by 14 July.

The PRA received 401 responses to Sam Woods' letter, 254 of them were from insurance companies. They included all UK firms and material branches of EEA firms who had received his letter. The information is being analysed and the Bank of England's Financial Policy Committee together with the Prudential Regulation Committee are to consider this information and reach a view on it imminently. Interim points which have been made by Mr Woods to the Treasury Committee overseeing progress in a letter of 2 August mention the complexity of some of the contingency arrangements and the increased workload to be borne by the PRA and FCA as a result of EU firms having to be regulated in the UK. On 26 September he revealed to Reuters that there will be at least 130 EU financial services firms applying for authorisation in the UK. There is strong support for there to be an implementation period.

What is going to happen?

In the field of Insurance Run-off, the PRA has itself been responding to the increased activity including in the area of insurance business transfers. There has been a reorganising of personnel with a view to streamlining certain processes which have been slow to date. The UK run-off industry welcomes these moves which will be essential in ensuring that cross-border business transfers in particular are dealt with in a timely manner prior to the date of withdrawal.

It is impossible to judge at this point what the timings will be and whether an agreement can be reached which would facilitate the continuation of passporting to some degree. The whole question of the UK's withdrawal is political and the outcome in terms of business continuity and how that takes place in the regulated world of insurance is balanced on political decisions. In a sense however, the politics must be driven by the exigencies of the commercial world in which we live and firms are lobbying for a sensible solution which will protect the financial and operational stability of the industry both in the UK and in the remaining 27 States. Our colleagues in the US will no doubt share our desire for such an outcome.

For further information concerning the current developments in Brexit please contact the author at vivien.tyrell@rpc.co.uk

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THE PERFECT RECEIVER: THE LAW

Salus Populi Suprema Lex [1]

If we desire respect for the law, we must first make the law respectable.

-Louis D. Brandeis.

INTRODUCTION

Recent weeks have seen much of my attention focused on the review of certain "model" laws, ostensibly to make them better suited for our evolving insurance insolvency world. In this endeavor, I am one of a large number among whom there are several I consider friends. And yet no unanimity of view is assured (nor much acrimony prevented) by that amity. So then, I am compelled to wonder, how can society assure itself of the best possible laws? Broad as this topic might be, it is singularly important to receivers, especially those active in IAIR and the NAIC, given that we are as a group so pitifully incapable of resisting the temptation to change the rules much more frequently than our own behavior. In this installment, I mount my soap box for the ambitious purpose of suggesting how good laws should be made. I do so knowing that many of our readers (that is to say, two of the currently three individuals who could find nothing better to do with their time than to expose themselves to my drivel) are likely to be involved in drafting legislation.

As a starting point, one should recognize that virtually all legislation involves balancing conflicting interests among two or more competing constituencies. Typically, advantages are conferred on one group only at the expense of others. It is a rare law that does not require some to pay for any benefit gained by others. Legislation of any complexity may involve balancing different interests among multiple constituencies in conflicting ways for separate sections. The constituency you strive to help in one section may be affected adversely by your position in another section and vice versa.

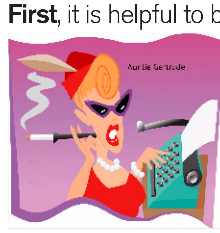
There are romantics who proclaim that their interest lies in creating a "good law" and not in benefitting any constituency. "Poppycock!!" say I. Once truth serum is digested, the authors of that absurd assertion will soon confess that, well disguised as it may be behind glorious principles, the aim of their effort was nonetheless laser-focused on bettering one or more constituencies at the expense of others. At best, we delude ourselves and ascribe undeserved nobility to our effort by lauding the merits of the constituency we seek to benefit while pointing out how undeserving is the constituency at whose expense the objects of our benevolence will make their gains.

With my customary audacity, I will offer here what I hope are some practical suggestions to drafting legislation. I confess that I have allowed some normative observations to creep into my comments.

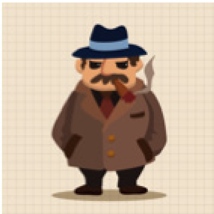
HOW TO MAKE LAWS

Handed down through generations, wrapped in an oil cloth to protect the parchment, and all enclosed hermetically in a locked glass case, the secret and fool-proof formula for good legislation has for centuries rested safely in a secure, climate controlled, room in an important European university library. Unfortunately, the only guy with the combination to the box's lock was last seen heading for coffee in Pompeii, remarking as he went "Who cares about a few ashes?" So, it is that the rest of humanity has been left to its own devices in the law-drafting business. Thankfully, several millennia of experience with varied results have yielded some valuable lessons. Here then are a dozen ingredients of good lawmaking [2].

First, it is helpful to begin the drafting process by understanding which group's interests are paramount on our agenda. We need to understand who we want to help and at whose expense that is likely to come. Often those are easy determinations. When we impose special fees and restrictions on Gentlemen's Clubs, we know that we will be helping the school children who will benefit from those fees and Aunt Gertrude. We know also that it will come at the expense of Uncle Roy who will now have to spend even more time with Aunt Gertrude. At other times, identifying the constituencies benefitted and those disadvantaged by particular legislation may require more analysis. Thus, a bill authorizing a petroleum pipeline may easily be predicted to help the pipeline builders and the petroleum industry at the expense of those who are affected by its environmental consequences. Less obvious though may be the unintended harm to oil tanker loaders and drivers and unintended benefit for the endangered species that will thrive under the pipeline's shelter. In short, it is worthwhile to take the time to learn who will benefit and who will hurt if proposed legislation is enacted.



Second, understand who is likely to oppose the legislation you propose and why. Tailor your negotiation or discussions to what is important to them. The cost of support may be materially lower once you understand the true nature of objections.



Third, recognize that many parties will act with insufficient information. Thus, intended beneficiaries may not immediately realize how the proposed legislation will help them. Educational efforts may result in useful allies and supporters. Conversely, those who may be affected adversely by legislation you support may be unaware of its pendency or its likely consequences. Avoid informing them inadvertently.

Fourth, calibrate your eyes to your stomach. It is tempting to strive to address several issues in one piece of legislation. The more disparate the matters addressed the more likely is the legislation to draw opposition and the more challenging it will be to draft persuasively and in a manner that makes implementation manageable. Accommodating one constituency may erode the intended benefit to another.

Fifth, Keep It Simple St_pid. Convoluted legislation will draw unnecessary opposition from those who simply don't want to take the time to understand it. It is far more likely to create unintended consequences. And it is less likely to accomplish its intended purpose in a predictable manner. Separate distinct issues into distinct legislative provisions.

Sixth, don't reinvent the wheel. Strive to avoid using new terms unnecessarily and instead bootstrap on existing definitions and statutory provisions. The less new stuff the better! After all, how much can you really expect us to learn? Moreover, modernization becomes simpler when statutes interrelate and use common terms.

Seventh, articulate your goals clearly from day one and attempt to identify potential objectors before you begin drafting. You may be able to negotiate objections away by explaining your purpose in advance and you may be able to avoid some altogether with minor adjustments to your proposal before it sees the light of day. There is value in avoiding even the fights you can win.

Eighth, "It's not personal; it's business!" In debating legislation, it is important to strive to keep egos and emotion out of the mix and to narrow the debate to the actual legislation. Far too often it is personal animus, rather than the merits, that impedes the progress of legislation.

Ninth, choose your battles wisely. Unless you are the people I always end up fighting, you have limited political capital. You have to deploy it astutely to accomplish any of your goals. Too many fights or too many opponents will kill your agenda. Make a list of your key priorities and focus on them without being distracted by inferior concerns.

Tenth, there is no shame in compromise. Giving a little may avoid a larger fight and get you closer to your goal sat lower cost.

Eleventh, always preserve an exit ramp and a retreat path. You can't win all your fights. Preserve enough respect and friendships to survive for the next battle.

Twelfth, (placed at the end for emphasis, not because I just thought of it), remember who depends on you! The debate that produces legislation, at least in the mind of the author, is best served if its participants are unambiguous about the constituency(ies) they strive to protect. Equally important is that the particular interest sought to be advanced (or harm sought to be avoided) be articulated clearly. Armed with this information, the parties, when acting in good faith, will often find ways of accomplishing one party's goals with lessened burden on competing constituencies. In my world, roles are assigned with some care. Insurers are tasked with collecting premium and paying only such claims as will not lead institutional investors to think less of management. To the policyholders falls the burden of paying those premiums and taking their chances. Plaintiff's lawyers have the solemn geological responsibility of transforming all mole hills into tall mountains. Actuaries are the wizards that will tell you how many people will die in each of the next ten years [3].

But what of receivers and insurance regulators? To them the higher power hath assigned the responsibility of protecting policyholders and insureds. When we abandon that solemn mission in favor of better-heeled corporate interests we mortgage our souls. It serves us well to remember each morning (after brushing our teeth) that WE are the ones who protect the little guy. If we step off that wall, the little guy is well and truly screwed!

I hope that these twelve suggestions will prove valuable. I leave you with this:

If a man sets out to study all the laws, he will have no time left to transgress them.

- Johann Wolfgang von Goethe

"The Maxims and Reflections of Goethe"

Patrick Cantilo is the Managing Partner of Cantilo & Bennett, LLP.

[1] Let the welfare of the people be the supreme law.

[2] It is rumored that the ancient formula had 42 ingredients! I just don't know that many words. Indeed, as you see, I am having to use many of my words several times.

[3] The really good ones will tell you who they are.

FSOC'S AIG DE-DESIGNATION AND THE ROAD AHEAD

By Patrick Hughes, Faegre Baker Daniels LLP

During the presidential campaign, candidate Donald Trump said there weren't many Obama-era policies he would maintain. So, when President Trump's administration endorsed the Obama administration's Covered Agreement initiative, the playbook on where the President was taking us on insurance regulation got a bit murky.

On September 29, 2017, the rudder snapped back closer to candidate Trump's direction when the Financial Stability Oversight Council rescinded the determination that financial distress at AIG could pose a threat to US financial stability, effectively de-designating AIG as a systemically important financial institution. The action was pursuant to the regular annual review of the designation mandated by Dodd-Frank, which created the systemic designation process in the first place.

FSOC's analysis focused on two predominant themes: (1) AIG got smaller and exited certain lines of business, which changed the risks that an AIG failure presented, and (2) additional analysis indicated that the prospect of policyholder surrenders did not present significant risk of systemic impact. Along the way FSOC discussed resolution issues, indicating certain concerns (e.g., "significant obstacles to its orderly resolution") but ultimately not concluding that those concerns created systemic risk.

The AIG decision represents the biggest tangible new direction for federal insurance policy since President Trump's inauguration, so it merits study for those in the insurance regulatory and public policy arena. Because the analysis behind FSOC's action discusses resolution issues, that is doubly so for those with an interest in resolution policy.

Risk Transmission Channels: FSOC's Core Analysis in a Nutshell

Systemic risk is discussed along three risk transmission channels – exposure, asset liquidation, and critical function or service. Additional regulatory considerations are the complexity and resolvability of the entity, and existing regulatory scrutiny. All those considerations show up in FSOC's September decision.

The discussion of the "Exposure Channel" asks the question of whether creditors, counterparties, investors, or others have significant enough exposure to the entity to materially impair them and create a systemic threat. FSOC's discussion of the exposure channel focused on AIG's significant reductions in debt and assets, as well as certain activities that have drawn specific attention in systemic analysis – securities lending and derivatives among others. While not concluding there was systemic risk identified, this analysis discussed the significance of funding needs of the guaranty system as well as the potential for impact on the rest of the insurance industry through guaranty system assessments. However, the FSOC analysis acknowledged that statutory caps and premium tax offsets mitigated the impact on and from guaranty assessments.

The "Asset Liquidation" channel analyzes whether the rapid liquidation of an entity's assets can create systemic risk. The plain reality is that AIG has gotten smaller, which obviously reduces any alleged risk from a "fire sale" of assets. Additionally, the AIG analysis acknowledged that historical evidence indicated that there is not a significant systemic risk from policyholder surrender.

The "Critical Function or Service" channel addresses whether the failure of an entity would create the loss of a critical function for which there are not ready substitutes. FSOC's assessment that AIG reduced its size again was the key to this part of the analysis.

Complexity and Resolvability, and the Regulatory Structure

As part of FSOC's analysis, the "Complexity and Resolvability" of the entity was also considered, and again the reduction in size was noted. Nevertheless, FSOC discussed AIG's "extensive and complex footprint," spread out throughout the country and world, with over 700 offices worldwide.

FSOC's analysis relied on the analysis of risk transmission channels to conclude that the "difficulty to resolve AIG and the potential for the company's disorderly resolution do not lead to a conclusion that AIG's material financial distress could pose a threat to U.S. financial stability." FSOC noted the importance of new systemic risk management tools like crisis management groups. Despite development of systemic regulatory tools, the council also noted that no global regulatory framework exists for cross-border resolution.

What's Next and What to Watch For

- Since Prudential remains a designated systematically important financial institution, additional analysis and discussion may lie ahead.
- FSOC's discussion of resolution questions such as cross border cooperation means that resolution issues remain a focus for regulators.
- It's not immediately clear how AIG's de-designation meshes with its ongoing status as a Globally Systemically Important Insurer by the Financial Stability Board. Regulatory analysis of systemic risk has other avenues than FSOC, and that conversation will continue.

The fact of and analysis behind the AIG de-designation share 2017 headline (to date) status with the final negotiation of the Covered Agreement. This tangible step is a new direction, but it wouldn't be a 2017 development if the new direction didn't come with additional uncertainty about what's next.

RESOLUTION OF FDIC CLAIMS IN BANCINSURE OKLAHOMA RECEIVERSHIP

By Ryan Leonard & Robert Edinger, Counsel for the Receiver

BancInsure, Inc. ("BancInsure") was an Oklahoma domestic insurer incorporated in 1985 that originally sold various insurance products, including fidelity bonds and director/officer liability policies, to community banks around the country. At its zenith, BancInsure was licensed to sell insurance in 49 states. Following the economic downtown in 2008-2009, a number of the banks insured by BancInsure failed, causing BancInsure to diversify by expanding its offering of workers' compensation policies. As the net loss ratios rose dramatically under its bank and worker's compensation policies, BancInsure sought additional capitalization in late 2012. In February 2013, BancInsure was sold to an investment group from New York, FJIC, LLC (a subsidiary of Foster Jennings, Inc.), which promised to inject new capital, and its name was changed to Red Rock Insurance Company, Inc. ("Red Rock") in November 2013. Red Rock was ultimately placed into statutory receivership by the Oklahoma County District Court in August 2014 (the "Oklahoma Receivership"). The court ordered Red Rock to be liquidated by John Doak, the Oklahoma Insurance Commissioner, who was appointed as Receiver for the company (the "Receiver"). The authors of this article and their law firm were subsequently retained as counsel for the Receiver.

In accordance with the statutory liquidation proceeding for Oklahoma insurance companies, creditors and policyholders of Red Rock submitted proofs of claim. The total proofs of claim exceeded $275 million, of which approximately half, or $135 million, was submitted by the Federal Deposit Insurance Company ("FDIC") as the receiver for various failed banks. The FDIC asserted that it was entitled to coverage under director/officer liability policies (labeled as "D&O" policies or "Professional Liability (PLI)" policies) issued by BancInsure. When a bank failed and the FDIC took over as receiver, the FDIC would typically file lawsuits against the directors and officers, alleging that their negligence and breach of fiduciary duty caused substantial losses in the bank's loan portfolio. The directors/officers would, in turn, make claims for coverage as the intended beneficiaries of BancInsure's policies issued to the banks. Frequently, the directors and officers would settle the litigation with the FDIC through agreed judgments or similar settlements and assign their coverage rights under BancInsure's policies to the FDIC. The FDIC then pursued coverage against BancInsure.

By August 2014, when BancInsure was placed into receivership proceedings, it had already denied coverage to the FDIC as receiver for the failed banks based on an exclusion in the BancInsure policies, often called the "insured v. insured" exclusion. While the D&O policy and PLI policies varied in material ways, both policies explicitly excluded coverage for claims made "by any successor, trustee or receiver" of the insured (the "Successor Clause"). Notwithstanding the evident intent of the exclusion (i.e., barring claims by successors of an insured bank such as a "receiver"), the FDIC pressed their loan loss liability claims against directors and officers of banks insured by BancInsure with the objective of recovering under the policies. In each case, BancInsure denied coverage of the claims based on the Successor Clause. The FDIC responded by instituting coverage actions against BancInsure in multiple federal district courts across the country, arguing that the Successor Clause was ambiguous and did not apply to the FDIC when it assumed control over a bank under federal law.

By August 2014, when BancInsure was placed into receivership proceedings, it had already denied coverage to the FDIC as receiver for the failed banks based on an exclusion in the BancInsure policies, often called the "insured v. insured" exclusion.

On the date BancInsure/Red Rock was placed into receivership in August 2014, six federal lawsuits had been filed by the FDIC against BancInsure in federal district courts in California, Nevada, Washington, Kansas and Georgia. Decisions had been reached in three of those cases, with two federal district courts having ruled in favor of BancInsure (the County Bank case filed in California and the Columbian Bank case filed in Kansas), and one court having ruled in favor of the FDIC (the Security Pacific Bank case in California). Two of these cases (County Bank and Security Pacific Bank) were on appeal (or soon to be appealed) to the 9th Circuit Court of Appeals, and the third case (Columbian Bank) was pending before the 10th Circuit Court of Appeals. Three other cases (the Washington First Int'l Bank case in Washington, the Carson River Bank case in Nevada and the Bank of Effingham case in Georgia) were pending in federal district courts in various stages of litigation, but no final orders had been entered in those cases. All of these cases involved claims by the FDIC seeking coverage under BancInsure's D&O and/or PLI policies, bringing into dispute the meaning and application of the "insured v. insured" exclusion.

In the County Bank case, the federal court for the Eastern District of California ruled in favor of BancInsure holding that the Successor Clause exclusion applied to all receivers, including the FDIC. The court applied the reasonable expectations test applied in coverage disputes and the principle that a policy designed for and issued to a bank is to be construed as a whole. The federal district court in Kansas reached the same conclusion in the Columbian Bank case, ruling that the Successor Clause in BancInsure's D&O policy barred a recovery by the FDIC acting as a receiver. In the Security Pacific Bank case, however, the federal district court for the Central District of California reached a different conclusion, ruling in favor of the FDIC. The Security Pacific Bank court construed the identical exclusion and applied the same reasonable expectations test as the federal district court in the County Bank case. However, relying on an exception retaining coverage for shareholder derivative suits found within the D&O policy, the Security Pacific Bank court deemed the policy to be ambiguous. The court held that claims for breach of fiduciary duty brought by the FDIC directly on behalf of the failed bank were so closely analogous to derivative suits brought by shareholders that there was an ambiguity as to whether the term "receiver" applied to the FDIC. In accordance with California state law, the court construed the ambiguity against BancInsure as the insurer.

At the outset of the receivership, therefore, the BancInsure Receiver was faced with approximately $135 million in claims submitted by the FDIC, conflicting decisions by federal district courts on the issue of coverage, three cases already on (or poised for) appeal and three other cases pending in federal district court with no decision.

At the outset of the receivership, therefore, the BancInsure Receiver was faced with approximately $135 million in claims submitted by the FDIC, conflicting decisions by federal district courts on the issue of coverage, three cases already on (or poised for) appeal and three other cases pending in federal district court with no decision. Contained within the order placing BancInsure into liquidation was an injunction by the Oklahoma County District Court issued pursuant to the Oklahoma Uniform Insurers Liquidation Act, 36 O.S. §1901 et seq. ("OUILA"). The injunction prohibited any party from prosecuting litigation against the defunct BancInsure outside of the Oklahoma District Court liquidation proceedings. On its face, the injunction applied to all FDIC litigation pending in the federal courts against BancInsure. However, there was arguably an exception for any pending case where a state guaranty association was obligated to defend the lawsuit after assuming coverage of the claim. In that situation, the BancInsure Receiver was statutorily obligated to "defer to that obligation." 36 O.S. § 1922 (3)(d). This occurred in the Columbian Bank case at the 10th Circuit in which the Kansas Insurance Guaranty Association had stepped into the shoes of the BancInsure Receiver and was both assuming coverage and prosecuting the same legal position that BancInsure would have prosecuted on its own behalf. Accordingly, there was no enforcement of the injunction in the Columbian Bank appeal at the 10th Circuit.

With one strategic exception, the FDIC strongly resisted enforcement of the Oklahoma Receivership Court's injunction against outside federal litigation being pursued by the FDIC against BancInsure. The legal basis for this resistance was a 2005 ruling by the 9th Circuit Court of Appeals in Hawthorne Savings F.S.B. v. Reliance Ins. Co. of Illinois, 421 F.3d 835 (9th Cir. 2005). In Hawthorne, the 9th Circuit concluded that an injunction issued in a state court insurance receivership proceeding, while precluding enforcement or collection of a judgment against the receivership estate, did not bar a federal court action to obtain a judgment outside the receivership. Because the pending federal actions (except Bank of Effingham in Georgia) were located in states within the 9th Circuit's jurisdiction (i.e., California, Nevada and Washington), the FDIC believed it would be successful in preventing enforcement of the injunction as to the litigation involving Security Pacific Bank, County Bank, Washington First Int'l Bank, and Carson River Bank. Conversely, because Georgia was located in a different federal appellate jurisdiction (where the injunction was more likely to be enforced) and because the Bank of Effingham lawsuit was in its infancy, the FDIC and the BancInsure Receiver agreed to place an administrative hold on the Bank of Effingham lawsuit in Georgia.

Although the BancInsure Receiver had good legal arguments to distinguish the Hawthorne opinion, there were strategic and cost considerations that favored allowing the 9th Circuit to proceed to final appellate rulings in Security Pacific Bank and County Bank. The cost of litigating the injunctions in multiple legal forums would potentially deplete the assets of the receivership whereas the cost of appellate briefing before the 9th Circuit was economically reasonable. Also, any interpretation of the Successor Clause by the 9th Circuit could be considered by (though would not be binding upon) the federal district courts in Washington and Nevada as well as the Oklahoma Receivership Court. Accordingly, the BancInsure Receiver requested that the Oklahoma Receivership Court lift the injunction for the sole purpose of allowing the Security Pacific Bank and County Bank appeals to proceed on the basis that it would conserve Receivership resources and that any final decisions by those courts could be useful guidance to the Oklahoma Receivership Court in resolving the FDIC's claims. On February 13, 2015, the Oklahoma Receivership Court agreed and lifted the injunctions only as to the pending appeals at the 9th Circuit.

Meanwhile, the BancInsure Receiver sought to enforce the injunction to prevent the federal district courts in Washington and Nevada from proceeding. Despite the FDIC's stiff resistance, the federal district court in the Washington First International Bank case relied upon principles of comity and the reciprocal provisions of the Uniform Insurer's Liquidation Act (UILA) adopted by both Washington and Oklahoma to stay the federal proceedings. FDIC v. BancInsure, Inc., 2015 U.S.

Dist. LEXIS 97823 (W.D. Washington, July 24, 2015). The Court acknowledged that its stay would allow the Oklahoma Receivership Court to resolve the FDIC's claims. Id. However, approximately one (1) month later, the federal district court in Nevada in the Carson River Bank case opted to ignore the Oklahoma Receivership Court's injunction and allow the litigation to continue outside of the receivership proceeding. BancInsure, Inc. v. Jacobs, 2015 WL 5092845 (D. Nevada, Aug. 26, 2015). The Nevada federal court relied in part on the rationale of the Hawthorne decision to conclude that a district court's resolution of an insurance coverage issue does not cause federal interference with the state insurance company liquidation procedures. As a result of this ruling, the BancInsure Receiver began litigating the Carson River lawsuit through the motion for summary judgment procedures.

During the late spring of 2015, the FDIC sought to delay the Oklahoma Receivership proceedings so that the FDIC could submit discovery to the Oklahoma Receiver concerning the status of BancInsure's financial health and its reinsurance treaties. The Oklahoma Receiver objected to this discovery, arguing that the statutory receivership procedures were "summary" in nature and not intended to allow discovery of the Receiver, which could potentially cause the receivership estate to be depleted through expensive and time consuming depositions and discovery disputes. On June 2, 2015, following briefing and a hearing, the Oklahoma Receivership Court agreed with the Receiver, ruling that the summary nature of the proceedings did not allow the FDIC to engage in discovery with the Receiver. The Court's decision saved the receivership estate tens of thousands of dollars in legal expenses that would have otherwise been incurred, and established the important precedent that creditors are not entitled to obtain "discovery" from the Receiver under the statutory liquidation of a domestic insurance company.

In August 2015, one year after BancInsure was ordered into liquidation and receivership, the 10th Circuit Court of Appeals in the Columbian Bank case ruled in favor of BancInsure and against the FDIC, denying the availability of coverage to the FDIC under BancInsure's policy. In January 2017, the 9th Circuit Court of Appeals in the Security Pacific Bank case reached the same conclusion (reversing a lower court judgment in favor of the FDIC), ruling that BancInsure's D&O policy unambiguously excludes coverage of the FDIC's claims against Security Pacific's former directors and officers. Finally, in March 2017, the 9th Circuit affirmed judgment in favor of BancInsure and against the FDIC in the County Bank case. Following the three appellate court decisions, the remaining actions pending in federal district court were dismissed, and the FDIC ultimately withdrew its proof of claims seeking coverage under the failed banks' D&O and PLI policies in the BancInsure receivership.

Through the strategic decision to litigate the 9th Circuit appellate cases to conclusion, the BancInsure Receiver obtained favorable rulings denying coverage, and resolved conflicting federal district decisions on the issue of coverage that were entered pre-receivership. The appellate decisions also served to provide further guidance to the Oklahoma Receivership Court on the issue of coverage on substantial claims totaling approximately $135 million. This course, including the Receiver's resistance to allowing creditor-driven discovery, resulted in significant savings to the receivership estate, and ultimately will inure to the substantial benefit of approved claimants and creditors of the BancInsure estate.

Ryan Leonard is lead counsel for the Red Rock Insurance Company/BancInsure Receiver and is a partner in the firm of Edinger, Leonard & Blakley, PLLC. Robert Edinger is a partner in the firm of Edinger, Leonard & Blakley, PLLC

UPCOMING NAIC MEETINGS

NAIC FALL 2017 NATIONAL MEETING

DECEMBER 2-4, 2017

HILTON HAWAIIAN VILLAGE & HAWAII CONVENTION CENTER | HONOLULU, HI

HONOLULU

2018 NATIONAL MEETINGS

SPRING 18 MILWAUKEE WISCONSIN MIL

SUMMER 18 BOSTON MASSACHUSSETTS BOS

FALL 18 SAN FRANCISCO CALIFORNIA SF

COMMITTEE REPORTS

On August 7, IAIR held a Members Meeting to update membership on the undertakings of our committees since the December 2016 annual meeting . Following is a summary of those reports.

Audit Committee

Chair:
Evan Bennett, Evan D Bennett LLC

The committee was charged with two major items to complete since August of 2016:

1. To develop a Records Retention Policy for IAIR

2. To develop an RFP for obtaining an Audit Firm to review IAIR's records and prepare the IAIR Form 990 each year

The committee has completed both charges.

- The records retention policy was adopted by the Board on December 12, 2016
- The RFP selection was made and Cunningham,Porter and Phillips were selected in September 2017

Education Committee

Co-Chairs:
Kathleen McCain, Michelman & Robinson, LLP
James Kennedy, Texas Department of Insurance

The Resolution Workshop was held in Austin in February 2017 and had a great group of speakers. The Workshop had a turnout of about 160, one of IAIR's best attended workshops.

Bill Goddard invited a group of IAIR members to participate in a UConn class on insurance receiverships again this year. IAIR appreciated the opportunity to be part of the program.

Issues Forums were held at each NAIC National Meeting. The Committee thanks everyone for their attendance and support. The Committee plans to continue to have Issues Forums 3 times a year.

Future activities for the Committee included putting a "basic receivership 101" webinar together and plans to create a webinar working group. Plans are proceeding for the 2018 resolution workshop.

Ethics Committee

Chair:
Wayne Johnson, Risk & Regulatory Consulting, LLC

During the first part of 2017 the Ethics Committee has been working primarily on two projects; the proposed designation program revisions, and updating the continuing education reporting and monitoring.

The Committee has some work remaining to incorporate all the elements of the proposed designation program revisions into the various documents associated with the project. That process should be complete before the Fall NAIC meeting.

The Committee will also be sending out a letter to members clarifying the reporting and tracking of continuing eucation credits, and member responsibilities.

The Committee continues to accept and process applications from members for both AIR and CIR designations and encourage qualifying members to submit those applications. The requirements for those professional designations can be found at www.IAIR.org under the Education tab.

Finance Committee

Chair:
Lowell Miller, North Carolina Life & Health Insurance Guaranty Association

The Finance Committee met in person in conjunction with each NAIC/IAIR meeting. The Committee reviewed the financial statements and reports generated by Accolade each month and followed up with any questions. Reports were sent to the board for each board meeting. The Treasurer also reported to the board at each meeting and addressed questions or concerns raised by board members.

IAIR had a very successful Resolution Workshop in February which provides a positive cash flow for the year. Membership renewals were less than expected so revenues from dues were less than projected in the budget.

Governance Committee

Chair:
Jonathan Bing, Jackson Lewis PC

The Governance Committee has been busy with a number of issues. The Committee reviewed and analyzed a questionnaire of issues regarding the operations of the IAIR Board and will be reporting on the results of the questionnaire to the Board. The Committee is reviewing the IAIR Mission Statement, tidying it up and making it more reflective of where IAIR is today.

IAIR lost its General Counsel Bill Latza this year due to a change in his employment. The Committee reviewed responses from potential candidates and recommended that Rich Fidei of Greenberg Traurig be selected. Mr. Fidei was selected by the Board and provides guidance to the Board on a Pro Bono basis.

Membership and Promotions Committee

Chair:
Bruce Gilbert, Nevada Insurance Guaranty Association

This year IAIR remained relatively steady in its membership, approximately 200 members. There were 11 new members year to date in 2017. There are a few members that have not paid their dues for 2017. The Committee asked if anyone had not paid his or her dues please make sure they get paid.

The Committee has also working on a retiree status to allow retirees to continue as members and expected the retiree membership application and affidavit would be published after the NAIC meeting. The retiree membership application incorporates the comments received regarding the initial draft of the application and affidavit.

Newsletter Committee

Chair:
Jenny Jeffers, Jennan Enterprises

There have been three newsletters since The Insurance Receiver resumed publications. The Committee appreciates the people who have written and submitted articles. The Committee is also working on designing a blog, which was not complete at the time of the meeting.

Nominations & Elections Committee

Chair:
Jonathan Bing, Jackson Lewis PC

The Committee has taken a careful look at the elections process with Mr. Fidei. The elections process last year was somewhat unusual in that there were 5 persons coming off the board and 5 individuals that were running for those vacancies. There are 5 individuals coming off the Board again this year and nominations are due by September 15, 2017.

Receivers and Guaranty Funds Relation Committee

Co-Chairs:
Lynda Loomis, Principal of Lynda G. Loomis
Wayne Wilson, California Insurance Guarantee Association

The Receivers & Guaranty Fund Relations Committee (R&GF) holds three meetings a year in conjunction with the NAIC meetings. The R&GF Committee:

- Focuses on current topics impacting receivers and guaranty funds
- Provides open forum for discussions of new issues receivers and guaranty funds encounter
- Engages the wide-ranging receivership and guaranty fund community

In 2017, the R&GF held a meeting on April 8, 2017 during the NAIC 2017 Spring National Meeting/IAIR Committee Meetings in Denver, Colorado. The topics included (1) a discussion of developments regarding the CastlePoint National Insurance Company receivership, and (2) updates regarding in health insurance receiverships. David Wilson and Joe Holloway from the California Conservation & Liquidation Office presented CastlePoint. Joe Holloway talked about how CastlePoint was initially put into rehabilitation and how the process worked moving to liquidation with an emphasis on data collection and transmission to guaranty associations during the rehabilitation process due to the large amount of electronic data and document images that needed to be in the hands of the guaranty associations for them to do their job. Comments were made by various R&GF Committee members. Then, Frank O'Loughlin of Lewis Roca Rothgerber Christie discussed numerous developments in the health insurance receiverships involving Co-Ops formed under the Affordable Care Act.

The R&GF held a meeting on August 6, 2017 during the NAIC 2017 Summer National/IAIR Committee Meetings in Philadelphia, Pennsylvania. The topics included a roundtable discussion regarding federal government claim priority in health insurer receiverships following a survey of the receivership community. R&GF reached out to the receivers of the other state CO-OP insolvencies not already discussed to seek their input and participation in the ongoing conversation. The R&GF also held an open forum on topics for future discussions at the R&GF committee meetings. Based upon the discussion at the August 6th meeting, the R&GF Committee has agreed to provide a forum for our community to develop a document (1) outlining issues in current and future receiverships and (2) suggesting solutions. The document may cover issues such as readiness, regionalization, preservation of institutional knowledge, preparation for technology innovations, and regulatory involvement.

The R&GF appreciates the significant participation and collaboration of our receivership and guaranty fund community.

Interested in becoming involved?

Join an IAIR Committee today! Click here to join.

THE RECEIVERSHIP LEGAL REVIEW

By C. Philip Curley and Robert L. Margolis, partners, Robinson Curley P.C.

The Receivership Legal Review is presented by C. Philip Curley and Robert L. Margolis, partners in Robinson Curley P.C. It contains general information about receivership-related legal issues and case law, does not constitute legal advice, and should not be relied upon or treated as such.

Notwithstanding that many insurance companies are part of an insurance holding company system, directors of a wholly-owned insurer owe fiduciary duties to the insurance company and its policyholders.

Justice Felix Frankfurter once wrote: "to say that a man is a fiduciary only begins the analysis; it gives direction to further inquiry. To whom is he a fiduciary?" SEC v. Chenery Corp., 318 U.S. 80, 85-86 (1943). As a general rule, a corporate director owes fiduciary duties of care and loyalty to the corporation's shareholders, which in the case of a wholly-owned subsidiary is the parent holding company. Courts agree, however, that directors of a wholly-owned subsidiary owe fiduciary obligations to the subsidiary as well. See, e.g., In re Sw. Supermarkets, LLC, 376 B.R. 281, 283 (Bankr. D. Ariz. 2007) ("[i]t would be a startling and dramatic departure from settled law to conclude that officers and directors do not owe any fiduciary duty to the corporation they serve"); First American Corp. v. Al-Nahyan, 17 F. Supp. 2d 10, 26 (D.D.C. 1998) ("the directors of a wholly-owned subsidiary owe the corporation fiduciary duties, just as they would any other corporation").

In the context of the insurance industry in particular, a director has fiduciary duties to the insurer and its policyholders, even if it is a wholly-owned subsidiary and part of an insurance holding company system. These obligations arise from the fact that "the business of insurance so far affects the public welfare as to invoke and require governmental regulation." German Alliance Ins. Co. v. Lewis, 233 U.S. 389, 412 (1914). Most state insurance codes specifically note that "the business of insurance is affected with the public interest." E.g., Rev. Code of Washington, 48.01.030.

The in pari delicto defense remains unavailable in receivership cases.

In Wooley v. Lucksinger, 61 So.2d 507 (La. 2011), the Louisiana Supreme Court (applying Texas law) reversed the dismissal of breach of fiduciary duty claims against directors of wholly-owned HMOs arising out of their role in a change-in-control transaction. In obtaining regulatory approval, the directors made certain representations to regulators about the assets of the HMOs post-sale but then structured the transaction so that the HMOs' parent was able to take more assets out of the HMOs, leaving them in a financially precarious position. The directors contended they only owed duties to the parent company, but the court held otherwise:

Whatever the scope of the fiduciary duty owed by the HMOs' directors/officers to the subsidiary corporations under Texas law, we hold it would be broad enough to encompass the duty to refrain from involvement in a conspiracy or scheme to mislead regulators in connection with a sale of the subsidiary HMOs which would strip them of assets reserved to pay future health care costs and which would leave the HMOs unable to meet the statutory and regulatory requirements in order for them to continue to do business in their respective states. 61 So.3d at 592.

Thus, directors of a wholly-owned insurer have an obligation to operate the insurer in such a way that it can meet its statutory and regulatory requirements, including the obligation to pay policyholder claims. In the next installment of The Receivership Legal Review, the obligations of a parent company director to a wholly-owned insurer and its policyholders will be explained.

Most jurisdictions recognize the defense of in pari delicto, which holds that a plaintiff may not pursue a claim if he or she participated in the underlying misconduct. Courts, however, typically will not apply the in pari delicto defense to claims brought by a receiver, even if the now-insolvent company or its officers, employees, or agents was a party to the misconduct. A thorough discussion of the in pari delicto defense in an insurance receivership context can be found in McRaith v. BDO Seidman, LLP, 909 N.E. 2d 310 (Ill. App. 2009).

Two very recent decisions have upheld the continued inapplicability of in pari delicto when claims are brought by a receiver. In Nicholson v. Shapiro & Associates, LLC, 2017 IL App (1st) 162551, a case involving claims brought by a court-appointed SEC receiver, the Illinois Appellate Court reaffirmed the holding of McRaith that in pari delicto does not apply to a court-appointed receiver. And in Jo Ann Howard and Associates, P.C. v. Cassity, 868 F.3d 637 (8th Cir. 2017), because consumers and funeral homes were also beneficiaries of the preneed trusts, the court did not apply in pari delicto even though a wrongdoer was also a beneficiary.

IAIR AT THE MIDWEST GUARANTY ASSOCIATION ADMINISTRATORS MEETING

A regional meeting of the Midwest Guaranty Association Administrators was held in Oklahoma City October 4-6, 2017. IAIR provided a panel discussing issues a Receiver has to consider and deal with prior to the entry of a receivership order and in the early days of an estate.

Thank you to the Oklahoma Life & Health Insurance Guaranty Association and Oklahoma Property & Casualty Insurance Guaranty Association for the opportunity for this presentation.

Also, thank you to the following for their participation in the planning and presentation:

- Chris Fuller, Fuller Law Group
- JoAnn Howard, JoAnn Howard & Associates PC
- Jenny Jeffers, Jennan Enterprises
- James Kennedy, Texas Department of Insurance
- Kathleen McCain, Michelman & Robinson LLP
- Donna Wilson, Oklahoma Receivership Office Inc

If you have an event that you would like IAIR to make a presentation on this or any other receivership topic, please contact Nancy Margolis (nancy@iair.org).

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