International Association of Insurance Receivers

Volume 5, Number 2 — The Newsletter — Summer 1996

In This Issue

Features

Departments

Mark Your Calendar

IAIR Anchorage Round Table
September 28, 1996
See page 5 for topics and details!

IAIR/NCIG Seminar
November 7-8, 1996
At the Hyatt West-Shore Hotel in Tampa Florida. Registration information is to be mailed shortly.

INSOL International '97
March 23-26, 1997
New Orleans, Louisiana, USA
Information has been mailed!

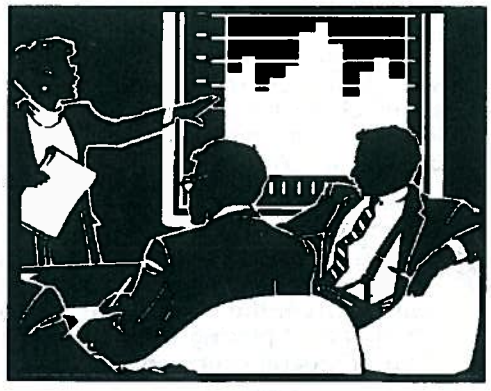
President's Message

By Dick Darling, Chief Operating Officer, Illinois Department of Insurance

Somebody called this morning, and advised me of the deadline for the President's Message to be printed in this newsletter. Needless to say, I was shocked, where had the time gone. It's summer in Chicago, and I suspect where you are also. It's ninety seven degrees, the humidity is higher than I care to count, and I am watching my electrical meter spin off the wall (this should be an interesting billing period). I hope all of you are continuing to pursue your insolvency related practices with the vigor and excitement this topic engenders.

The June 1996 roundtable in New York was once again a success. The Board thanks Michael Miron, Meetings Chair, and host, and A. Marc Pelligrino for all of their hard work in putting together a lively and interesting agenda. We would also like to thank all of the IAIR members who, once again, graciously donated their time to assist in the various presentations.

The agenda and planning for the second joint IAIR/NCIGF Seminar, "Moving Forward Together: Addressing Today's Concerns—Reinsurance Issues," is well on its way to completion. The objective of these seminars between the Receiver members and the guaranty fund members of the NCIGF is to further enhance personal relationships developed through business dealings and to develop knowledge,



professionalism and understanding of each others needs and concerns related to important issues in the world of insurance insolvency. This year, we will focus on reinsurance issues, including the impact of the Lloyd's reorganization, restructuring, early estate closures, and the role of reinsurance. Please mark your calendars for November 7-8, 1996 for the IAIR/NCIGF Seminar to be presented in Tampa, Florida at the Hyatt West-Shore Hotel. Registration and information concerning this seminar will be mailed during the fall of this year and may be available at the Anchorage, Alaska NAIC.

Speaking of Anchorage, we are scheduling our fall roundtable to be held in conjunction with the NAIC on Saturday, September 28, 1996. The fall roundtable will be hosted by Joyce Wainscott, (907) 277-9222, and Michael Miron, (201) 907-0824. Any members with suggestions or ideas for topics to be covered at the next roundtable should feel free to contact either Joyce or Mike.

It was good to see many members at the joint IAIR/NCIGF cocktail reception in New York. The Board would once again like to thank the NCIGF for co-hosting this event. We look forward to future joint June receptions.

IAIR is planning a cocktail reception in Anchorage for Monday, September 30, 1996. We are still accepting patron sponsors for this event and if anyone is interested in being a patron sponsor, they are urged to contact Frank Bistrom at association headquarters, (913) 262-2749.

As promised in the Spring 1996 Newsletter, the Accreditation Committee has been actively working on the standardization of our designation and application forms. I am pleased to inform you that I saw a final copy of the necessary forms come across my desk yesterday and upon approval of the Board, we would be actively soliciting members to apply for the AIR and CIR

continued on page 10

COMMENTARY

Quackenbush v. Allstate Ins. Co., 64 U.S.L.W. 4379

By Karl L. Rubinstein,
Rubinstein & Perry, A Professional Corporation

Editor's Note: *Many of you will note that we have presented two articles on the Quackenbush v. Allstate decision issued on June 3, 1996. Be assured that this is not a point/counter-point type of presentation. That is, neither author has previously seen the other's comments and, although the two articles take very different perspectives on the decision, neither author is addressing or rebutting the other's comments. At least, not yet. We hope that providing both comments will give our readers a more balanced view of the decision than may be available elsewhere.*

Efforts by the several California Insurance Commissioners to marshal the assets of the Mission Insurance Companies, particularly the reinsurance recoverables, have resulted in recoveries exceeding $1.3 Billion. The process has involved a substantial amount of litigation and one suit, seeking a turnover of several million dollars from Allstate Insurance Company, was removed by Allstate to federal court. On the Commissioner's motion, the federal district court dismissed and remanded the case. Although the Commissioner had relied upon both Colorado River and *Burford* abstention doctrines[1] the federal court abstained only on *Burford*. Allstate appealed to the Ninth Circuit Court of Appeals. The Ninth held that it had the jurisdiction to review the remand order by appeal (not merely by mandamus) and reversed the district court on the narrow grounds that a federal court could never abstain under *Burford* unless the underlying suit was "in equity."

Substantial conflict existed among various circuit courts of appeals on both of these issues and Commissioner sought a writ of certiorari from the U.S. Supreme Court. That writ was granted in *Quackenbush v. Allstate Ins. Co.*, 64 U.S.L.W. 4379, on the issues of:

1) whether a remand order which decides nothing but the fact of remand is "final" and, therefore, appealable, and

2) whether the Ninth Circuit is correct in its *per se* rule that a federal court can never abstain unless the underlying case is purely a case "in equity."

The Supreme Court agreed with the Ninth Circuit that the remand order was appealable, and agreed that the district court should not have dismissed the case outright; however, the Court also *rejected* the Ninth Circuit's *per se* rule and held that a stay of the federal action rather than an outright dismissal might have been appropriate. *Quackenbush* transcends the procedural details of that individual case and provides important abstention principles which are beneficial to insurance regulators.

The Commissioner did not have a strong interest in the outcome of the appealability issue, but recognized that the Supreme Court would probably want to resolve the conflict in the Circuits. To resolve the conflict regarding appealability, the Supreme Court had to move away from its earlier opinion in *Thermtron Products, Inc. v. Hermansdorfer*, 423 U.S. 336 (1976), where it explicitly stated that a remand order was not appealable and could only be reviewed by mandamus. In *Quackenbush*, the Supreme Court stated:

> To the extent *Thermtron* would require us to ignore the implications of our later holding in *Moses H. Cone*, however, we disavow it. (Slip Op. p. 7)

In *Quackenbush*, the Supreme Court held that since the effect of the remand order was to remove the federal court entirely from the case, it had the effect of placing the parties "out of federal court" and therefore met the "finality" requirements as set out in the "collateral order doctrine"[2] recognized in *Cohen v. Beneficial Industrial Loan Corporation*, 387 U.S. 541 (1949).

The abstention issue was quite important to the Commissioner and we are pleased that the Supreme Court rejected the *per se* rule adopted by the Ninth Circuit and ruled that a district court may stay a federal action on abstention-type principles even in a suit which seeks only damages.

In particular, the Supreme Court disapproved the Ninth Circuit's position that a federal court could only abstain in equity cases and that federal courts could never abstain in damages cases. The Supreme Court held that:

> The *per se* rule described by the Ninth Circuit is, however, more rigid than our precedents require. We have not strictly limited abstention to 'equitable cases'...but rather have extended the doctrine to all cases in which a federal court is asked to provide some form of discretionary relief....Moreover, as demonstrated by our decision in *Thibodaux* ... we have not held that abstention principles are completely inapplicable in damages actions. (Slip Op. p. 24)

Significantly, the Supreme Court specifically stated that federal courts may abstain in declaratory judgment cases because such relief is "generally committed to the courts' discretion." (Slip Op. p. 11) In order to focus sharply on the issues in this case, the Commissioner conceded for the purposes of the writ that the underlying suit was a damages action. In fact, the underlying suit also included a declaratory judgment action and *Quackenbush* will permit federal courts to abstain in declaratory judgment actions, assuming that the principles of the abstention doctrines are met.

While the foregoing aspects of the

opinion are quite significant, the case also establishes that perhaps an even more important principle is that a district court may, on abstention-type principles, stay even damage suits. This *"Quackenbush* abstention" principle was explained as follows:

> For example, given the situation the District Court faced in this case, a stay order might have been appropriate: The setoff issue was being decided by the state courts at the time the District Court ruled...and in the interest of avoiding inconsistent adjudications on that point, the District Court might have been justified in entering a stay to await the outcome of the state court litigation. (Slip Op. p. 24)

After *Quackenbush,* the only distinction between a damage suit and other actions is that damage actions may not be dismissed outright; however, they may be stayed. When a stay is issued and the case proceeds to judgment in the state court, the result is binding on the parties. Accordingly, to a litigator there is not likely to be any practical difference between a stay and a dismissal. Under federal jurisdictional philosophy, as illuminated in *Quackenbush,* however, there *is* a significant difference between a stay and a dismissal in that it is generally the rule that federal courts must exercise their jurisdiction if they have jurisdiction. While the abstention doctrines permit certain exceptions to this rule, the Supreme Court has often held that these doctrines should be used only in "exceptional circumstances."[3] Thus, to the Supreme Court there was a crucial difference between dismissing the suit (in which event the federal court declines all jurisdiction) and in staying the suit in federal court and permitting it to proceed in state court. In the latter circumstance, the federal court retains its jurisdiction, although it delays its exercise. The Supreme Court determined in *Quackenbush* that a stay is permissible under abstention doctrines in *all* types of cases, including damage cases and that outright dismissal is proper where the underlying suit is either in equity or otherwise involves the discretionary jurisdiction of the court. Thus, the Supreme Court drew a bright line as to outright dismissal where the underlying suit is purely in damages, but it would permit a *Quackenbush*-type stay based on abstention principles even where the underlying case is solely in damages.

> "Significantly, the Supreme Court specifically stated that federal courts may abstain in declaratory judgment cases because such relief is 'generally committed to the courts' discretion.'"

This result is very satisfactory and workable and it provides a much needed clarification of the law in this area. This clarification will transcend this case and will benefit all similar receivership cases. My own practice in similar cases has been to file an abstention type motion seeking dismissal, or alternatively, a stay. Some federal district courts have dismissed the action, such as was done by the federal court in this case, and others have stayed the federal action pending resolution in state court. The practical effect of these two approaches is functionally the same as far as the regulator is concerned and I have never had a case that returned to federal court after a stay was issued in deference to the underlying state receivership court litigation. In all such cases the matter was fully resolved in the state court.

Quackenbush also reaffirms *Burford* and the power to *dismiss* a case:

> [I]f it presents 'difficult questions of state law bearing on policy problems of substantial public import whose importance transcends the result in the case then at bar,' or if its adjudication in a federal forum 'would be disruptive of state efforts to establish a coherent policy with respect to a matter of substantial public concern.' (Slip Op. p. 20)

The Court also holds that the exercise of the power to dismiss must also reflect the "principles of federalism and comity."

> Ultimately, what is at stake is a federal court's decision, based on a careful consideration of the federal interests in retaining jurisdiction over the dispute and the competing interests for the "independence of state action," ... that the State's interests are paramount and that a dispute would best be adjudicated in a state forum...whether adjudication in federal court would 'unduly intrude into the processes of state government or undermine the State's ability to maintain desired uniformity." (Slip Op. p. 21)

The Court reaffirmed that dismissal on abstention principles should be the exception, not the rule, and, turning from general principles to the situation presented in this particular case, the Court noted that "at first blush" this case involved only a "run-of-the-mill" contract dispute, but also acknowledged that there may be deeper issues involved:

> What differentiates this case from other diversity actions seeking damages for breach of contract, if anything, is the impact federal adjudication of the dispute might have on the ongoing liquidation proceedings in state court. (Slip Op. p 22)

The Court expressly noted that a "hotly contested" offset issue had been pending at the time of the dismissal and remand in this case and that a stay of the federal proceeding to permit the state courts to resolve this issue might have been appropriate. It is clear that the Supreme Court would have approved the federal court's action in this case had it stayed the matter, as opposed to dismissing it. Indeed, although the original offset issue was resolved by the California Supreme Court, there is a new and equally "hotly contested" offset issue which has arisen in this case subsequently to the Ninth Circuit opinion. This, and other circumstances, would justify a

continued on page 4

Commentary (Continued from page 3)

stay under *Quackenbush*.

The recognition by the Court that a dismissal could occur in declaratory judgment actions is particularly significant to insurance insolvency practitioners because it permits abstention and dismissal where one seeks a declaratory judgment which will resolve unsettled issues of state law. The litigation my firm has handled for regulators in various cases, such as that arising out of the Baldwin-United life insurance subsidiaries insolvency, that of Executive Life Insurance Company and the Mission Insurance Companies, among others, has frequently involved unsettled issues of state law. A declaratory judgment action filed in state court seeking a resolution of such unsettled issues, would, under *Quackenbush*, be subject to dismissal and remand if removed to federal court or if filed directly in federal court. Such actions would also be subject to a stay to permit the case to proceed in state court. In either case, the important interest of having state law issues resolved in state court would be preserved. It is also important that the Supreme Court added that:

> We have no occasion to resolve what additional authority to abstain might be provided under our decision in *Fair Assessment*....Nor do we find it necessary to inquire fully as to whether this case presents the sort of "exceptional circumstance" in which *Burford* abstention or other grounds for yielding federal jurisdiction might be appropriate. (Slip Op. p. 24)

The importance of this statement lies in the fact that the Court was well-aware that we conceded, for the purpose of the argument and the crisp presentation of the issues, that the underlying case was a damages case. Thus, the case was designed to present the issue in its broadest terms and to include the point at which the Court might draw the line to clarify the conflict among the courts of appeals. The Court, however, was careful to include the phrase "at first blush," in describing this action and it also deliberately did not rule out the potential that the case may involve other issues that might still permit traditional *Burford* abstention.

The Court was careful to decide only what it needed to decide and to not "inquire fully into whether this case presents the sort of 'exceptional circumstance' in which *Burford* abstention or other grounds for yielding federal jurisdiction might be appropriate." It is pertinent, however, that the Court cited the 1935 decision in *Pennsylvania v. Williams*, 294 U.S. 176 as support for the proposition that federal courts may abstain in cases which would be duplicative of a pending state proceeding. I read *Pennsylvania v. Williams* and its companion case *Penn Gen. Casualty Co. v. Pennsylvania*, 294 U.S. 189 (1935) as recognizing, even prior to the decision in *Railroad Comm'n Of Texas v. Pullman Co.*, 312 U.S. 496 (1941) an abstention doctrine applicable to insurance insolvencies.

It is also noteworthy that in *Quackenbush* the court quotes extensively from *Pullman* in order to explain the principle underlying abstention doctrines. Significantly, the passage selected by the Court included the following:

> Few public interests have a higher claim upon the discretion of a federal chancellor than the avoidance of needless friction with state policies [including] the administration of a specialized scheme for liquidating embarrassed business enterprises, or the final authority of a state court to interpret doubtful regulatory laws of the state. (Slip Op. p.10)

A complete analysis of the nature of insurance insolvency proceedings, in this context, must await another day, but *Quackenbush* not only provides current benefits and guidance, it also sets the stage for a reaffirmation of the special nature of insurance insolvency proceedings.

The United States Supreme Court paints on a broad canvas and establishes rules for all cases. It chose this case, not only to resolve the conflicts among the circuits, but also to clarify confusion over the state of the abstention doctrines. Beyond the issues discussed above, there had been scholarly and judicial speculation that in *New Orleans Public Service, Inc. V. Council of City of New Orleans* 491 U.S. 350 (1989) ("NOPSI") the Court was narrowing abstention doctrines and was moving away from *Colorado River* and *Burford*. This opinion makes it very plain that both types of abstention are alive and well.

In summary, this case was selected by the Supreme Court to resolve conflicts among the courts of appeals. The conflicts are now largely resolved in a manner beneficial to those of us who litigate on behalf of insurance regulators. The specter of multiple litigations in multiple courts with the attendant waste of precious assets and risk of inconsistent results is very real. By enunciating a rule that plainly permits federal courts to stay even purely damage actions in favor of state court proceedings and clearly extending abstention doctrines beyond cases "in equity" to permit even an outright dismissal of appropriate declaratory judgment actions and other actions which seek discretionary relief will serve to protect the principles of federalism and comity so important to our judicial system.

---

[1]Colorado River Water Conservation District v. United States 424 U.S. 800 (1976); Burford v. Sun Oil Co., 319 U.S. 315 (1943).

[2]The essence of the "collateral order doctrine" is that some orders which would normally not be viewed as "final" do constitute a final disposition of a matter collateral to the merits of the case, which matter is too important to await appellate review at the end of the case. The issue here was whether a remand order which decides no issue other than the fact of remand can fall within the doctrine. The Supreme Court held that it could. This resolved the conflicts among the circuit courts as well as the conflict between the plain language of *Thermtron* and that of *Moses H. Cone*. Still unresolved is the

"The recognition by the Court that a dismissal could occur...is particularly significant to insurance insolvency practitioners... ."

apparent anomaly between the intent of the Congress as expressed in 28 U.S.C. Sec. 1447 (d) ("An order remanding a case to the State court from which it was removed is not reviewable on appeal or otherwise.") and the Supreme Court's view that this statuary bar to appellate review applies only to those remand orders based on the grounds set out in 28 U.S. Sec. 1447 (c) (See, e.g. *Things Remembered, Inc., v. Petrarca*, 516 U.S.___ (1995)). This leaves some remand orders absolutely not appealable and others subject to appeal. It seems that the resolution of this problem, if it is a problem, lies with the Congress.

[3]It is interesting that both Justices Kennedy and Scalia wrote concurring opinions. Justice Kennedy stated that the Court should not rule out the possibility that there could be situation in which outright dismissal might be appropriate even in damages actions "where a serious affront to the interests of federalism could be averted in no other way. We need not reach that question here." Justice Scalia stated that he did not believe such a serious affront could occur as a practical matter. Justice Scalia also made the point that, while the court did not, in this opinion, inquire fully as to whether the "exceptional circumstances" for abstention were present, there "were certainly grounds for such an inquiry if we thought it relevant." He noted that in addition to the unsettled offset issue the district court had relied upon the State's "overriding interest in regulating insurance insolvencies and liquidation in a uniform and orderly manner." See page 24 Slip Opinion.

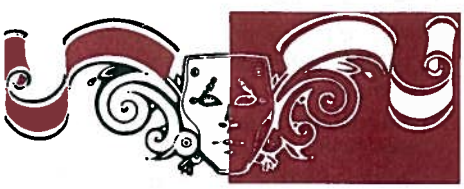
INSOL '97

As you know from previous items which have appeared in *the Newsletter*, IAIR is collaborating in the production of a one day program in New Orleans in conjunction with the Quadrennial meeting of INSOL International, INSOI '97. INSOL International is International Insolvency Practitioners Organization.

This is the one program you cannot afford to miss and you should ensure that **March 23-26, 1997** is put into your diary now.

This program will form part of IAIR's 1997 educational program and you are encouraged to attend and to bring your friends, colleagues and staff as well. Info has been mailed!

INSOL '97—Don't Miss It!



Fall 1996 • IAIR Roundtable

Date: Saturday, Sept. 28, 1996

Time: 1:00 - 5:00 p.m.

Place: Katmai &Dillingham Rooms

Hilton Hotel, Anchorage, Alaska

A wide range of current topics are expected to be covered at our Fall Roundtable which will be held on Saturday afternoon, September 28, in connection with the NAIC meeting.

The Roundtable will be chaired by Joyce Wainscott, Deputy Receiver Pacific Marine Insurance Company of Alaska

We hope to see all of your who are at this NAIC session at the IAIR Roundtable.

This will be an open discussion roundtable, like the old days. Please bring any topic you want to discuss or questions you need addressed by your fellow receivers and other experts in this field.

Lead Topics For Discussion:

1. **Liability based restructuring by insurance companies.**
2. **Voiding of preferences - statute of limitations.**
3. **Disputes between liquidators.**
4. **Estimation of losses for reinsurance collection.**
5. **Presentation of evidence to prove grounds for liquidation.**

Letter to the Editor

To the Editor:

Nelson Burnett's Pari Passu column in the Spring edition of the IAIR Newsletter fails to mention the many advantages to the receiver associated with the concept of co-management of assets. Co-management, for example, depoliticizes the asset management process, and enables the receiver to counter the defenses of regulator fault and imputation. Through co-management, cost benefits are achieved, such as decreasing the probability of the estate having to pay for multiple sets of pro-fessional advisors to the various constituencies.

The receiver does not "lose power" with the co-management approach. He may retain the right to remove for cause any manager appointed by others. In addition, the receivership court would retain control over estate functions, such as plan implementation and litigation.

The co-management approach is consistent with NOLHGA's commitment to asset recovery and has worked well in the Executive Life Insurance Company and Mutual Benefit Life Insurance Company cases. The method is also being employed in the National Heritage Life Insurance Company insolvency and will be a part of the plan for Confederation Life Insurance Company. A more complete examination of co-management appeared in the Winter, 1995 edition of the NOLHGA Journal and we would be pleased to send copies to those who wish to learn more about the subject.

Sincerely,

Lisa M. Meyer
Manager,
Industry Communications

Pari Passu

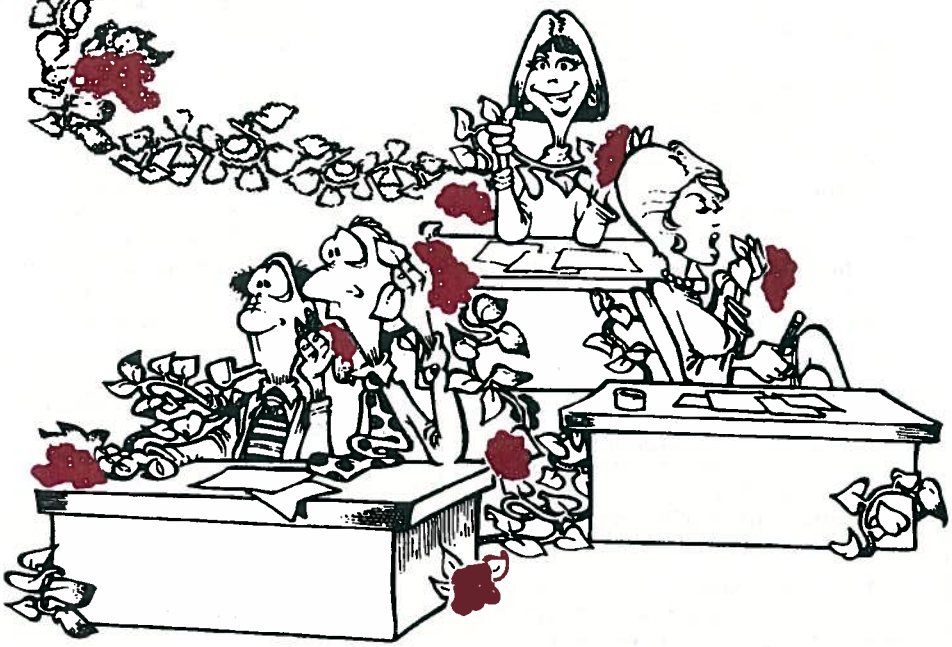
by Nelson Burnett, State of Alabama, Department of Insurance, Receivership Division

How much can Alaska take? Earthquakes, volcanic ash pollution, sawing asunder by the billion dollar pipeline, Valdez-Prince Edward Sound pollution, chronic environmental depredations and depravity exceeded perhaps only in Russia, then, as this is written, incalculable destruction from the mother of all forest fires, two at once, and the coming invasion by NAIC types in September!

The Locaquious Liquidator tells me he has found his cause, not a niche, it's great, global! He says he has always been "green." But, too much effort and emphasis is being placed upon animals, seals and snail darters when we have to go beyond to the basics, forests, and specifically trees, any tree. He suggested that the best people column I could do would be on trees. After hearing him out I made the connection and thought it worthy of sharing with you. So here 'tis.

Himself had explained that we are making some progress, we no longer call natural catastrophes, usually man-generated ones, Acts of God. I agreed that my God doesn't act that way. Trees do need better press albeit, Himself has me siding with the trees against the spotted owl, except there are ways to protect both, right? Trees are beautiful, most wonderful Acts of God.

How often whole nations, worlds, forget that trees are the purifiers, actually the greatest proof of God's plan for perpetuity. Trees take the deadly dirty carbon dioxide humans and animals emit and turn it into oxygen. Oxygen is a basic requirement for life. Trees set benignly and beautifully blessing animals of all orders with life. (I am over simplifying, but generally this is positively true.) You know about oxygen deprivation and brain damage or terminal effect therefrom. You know the sun triggers green leaf chloro-processing of oxygen, assuring all creatures breathing rights. Without trees our oxygen supply would run out and without oxygen to merge with the God-supplied hydrogen, we would face global water depletion and ultimately the uninhabited Atlantic and Pacific deserts!



To get specific, we all learned Joyce Kilmer's classic poem "Trees." It thrilled and chilled many generations including ours and part of it goes,

I think that I shall never see
A poem as lovely as a tree...
Poems are made by fools like me,
but only God can make a tree.

Remember the teacher would always tell you how Kilmer was killed in action in World War I and buried with thousands of American servicemen in a foreign field *with no trees.* This has been remedied, there are trees about Kilmer's grave now.

Our generation had Ogden Nash's treatment of these verses:

I think that I shall never see
a billboard lovely as a tree
Indeed, unless the billboards fall,
I'll never see a tree at all!

Grace Noll Crowell said it better:

God wrote his loveliest poem on the day
He made the first tall silver poplar tree.

O'Henry wrote about "tall arrowy white pines." Coleredge told us that friendship is a sheltering tree. And Wadsworth wrote of a brotherhood of venerable trees.

Steven Vincent Benet, my favorite "action poet" wrote:

Broad-streeted Richmond...the trees in the streets
are old trees used to living with people. Family trees
that remember your grandfather's name.

As only he could, Thoreau put nature and tree appreciation into these beautiful words:

For many years I was self-appointed inspector of snow-storms
and rainstorms, and did my duty faithfully, though I
never received one cent for it. I

frequently tramped
eight or ten miles through the
deepest snow to keep an
appointment with a beech tree,
or a yellow birch, or an
old acquaintance among the
pines.

Willa Cather knew whereof she spoke writing:

I like trees because they seem
more resigned
to the way they have to live
than other things do.

George Bernard Shaw had it right when he wrote, "Except during the nine months before he draws his first breath, no man manages his affairs as well as a tree does."

In any direction, easy walking distance from where you are reading this, there's a valiant tree or trees growing out of a rocky outcrop of impossible soil or no soil at all, just a rock that is cracked or pavement that it lifted up. It's not difficult at all to find many of these venerable centenarians just "making it", not only for themselves but for God, country and all other living things.

Nostalgia is what El Loquacio and I do best. When I go back home, Eastern Kentucky, I always try to walk a familiar ridge and observe the working trees on Johns Creek, it's one way I really return to my raisin'.

A couple of years back at a ridge overlook, I saw a sourwood tree that I had never noticed before. It was bowed over at roughly 45 degrees and half of it, the topside of its large trunk, was carved out by harm and decay. It was very much like an Indian dugout canoe or morbidly a burial vessel, a pretty coffin. I had hiked several miles, mostly through rough terrain and underbrush and I was tired. I could not resist the temptation. I just fitted right back into the declivity in that tree trunk and at that angle of repose I had a good view of the forest, the rocks and ridges off to infinity and far below small cars were moving on a highway made straight by cutting down many siblings of my host. I stayed there too long, but it was a revealing and refreshing pause. When I finally got back to my Aunt Shirley's, something was said about my being out hugging a tree and I could truthfully say, "YES, and one hugged me!"

Since this summer effort has become totally ex parte, self-centered and selective I thought some of you folks would be interested in the fact that I found occasion to before one of my supervising judges utilize the Receiver's credo caution as recorded in the scriptures, Matthew 24:28, NIV, Jesus said, "Wherever there is a carcass, there the vultures will gather." Ben Franklin put it: "Where carcasses are, eagles will gather, and where good laws are, much people flock thither."

Still on personal war stories and such. Many of you know my background in insurance claims and law. I got into receivership work in 1985 and found my life's calling too close to the end thereof. What fascinates me the most about insolvency practice is the opportunity for creativity. Maybe I should say the necessity for it if one is to do it successfully. Now there are those among us who would stifle that creativity and it may be good, certain general guidelines are necessary but that will eventually come with compacts, nationalization, and countrywide adoption and utilization of the model acts. May my Tree Creating God help us if we ever reach the regimented state described by Rabbi Harold Kushner. In his book, "When All You've Ever Wanted Isn't Enough" he retells the story of the medieval Spanish monk writing in his journal, "I am confident that, after my death, I will go to heaven because I have never made a decision on my own. I have always followed the orders of my superiors, and if I ever erred, the sin is theirs, not mine." Responsibility, initiative, creativity, are all parts of our receivershipping endeavor, if we do it, as it has to, should be, done.

Heard any good consultant jokes lately? That was provoked today by the receipt of the excellent new IAIR Directory. Splendid work, Frank, Publications, all contributing thereunto. We left out a category though, I'll just save it for my personal use after retirement. That's George Bernard Shaw styling himself, "General Consultant to Mankind." I like the generality of that self-appellation but it may bring on specifics such as Oscar Wilde's later remark about Shaw, "An excellent man, he has not an enemy in the world, and none of his friends like him."

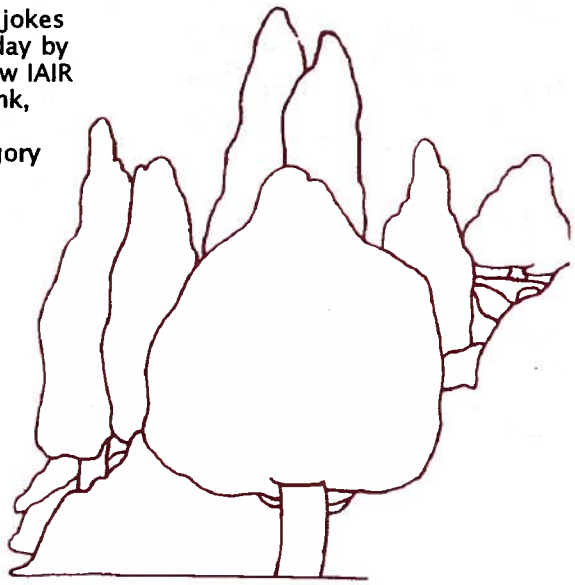
Most of you are familiar with the changes in Alabama impacting yours truly more so than I desire but I am surviving so far. It didn't help to recently note a popular wall plaque, "Just because you are paranoid, doesn't mean they are not out to get you!" Then I read Michael Palmer, his 1994 novel *Flashback* wherein he recites, "The chances that a man is in the right increase geometrically by the vigor with which others are trying to prove him wrong." Next comes Ben Franklin's ancient adage, "Distrust and caution are the parents of security."

Here are some thoughts on preventive paranoia. (It is an interesting environment down here.) I probably don't have any, but it's good advice as expressed by John F. Kennedy, "Forgive your enemies, but never forget their names." And I go back to Oscar Wilde again, he said, "A man can't be too careful in the choice of his enemies." And Ben Franklin's, "There is no little enemy.

Of course I'm hooked on controlled paranoia. Early in his writings Shakespeare cautioned, "Love all, trust a few." Later in the Rape of Lucrece he warns, "Extreme fear can neither fight nor fly." That's a way of saying don't get ulcers, give 'em. My, one of many shortcomings, is that I refuse to sin by silence. Arthur Whaley described that thusly, "What is hard today is to censor one's own thoughts—to sit by and see the blind man on the sightless horse riding into the bottomless abyss."

Think trees...

Carefully, Pari Passu.



Meet Your Colleagues

Frederich J. Bingham

Rick Bingham is Director of Claims Operations with the Illinois Office of the Special Deputy Receiver where his responsibilities include overseeing the claims, reinsurance claim services and special projects departments.

Prior to this, Mr. Bingham had over 18 years experience working with three major multi-line insurance companies and a major international insurance consulting firm.

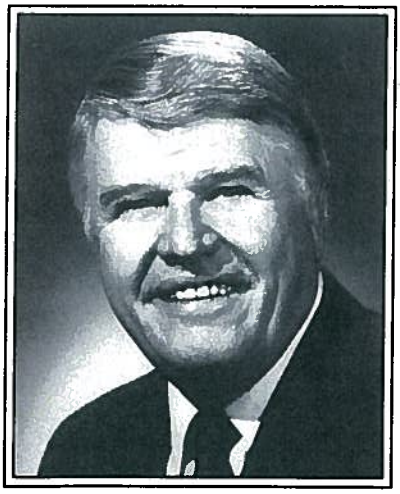
Mr. Bingham received his B.A. in history at Centre College in Danville, Kentucky. He subsequently completed numerous industry-related courses, including the American Education Institute's "Law for the Claimsman."

As a partner at a major international insurance consulting firm, Rick worked on a number of projects related to overseeing the work of financially distresses insurance companies. In one project, Mr. Bingham oversaw the final runoff of all pending claims for an estate in liquidation, including integration of reinsurance and guaranty fund information.

Rick has led a number of engagements which required the estimation of asbestos, environmental, toxic tort and other class action long-tail claims. These projects involved the organization of large volumes of records, coding of claim files, estimation of claim liabilities and the allocation of damages between multiple defendants and carriers.

A contributing member of the International Association of Insurance Receivers, Rick has made presentations at its educational and professional programs. Most recently, in Albuquerque in January, 1996, Rick discussed the implications for estates of estimating long-tail liabilities.

Rick is a former Marine, and when he is not straightening out estates, he enjoys showing Rhodesian Ridgebacks at dog shows all across the country.



Richard C. Cecil, CLU

Dick Cecil is Deputy Receiver for the Rehabilitation and Liquidation Bureau of the State of Delaware, Department of Insurance. He serves as the receiver for twelve Delaware domicillary and ancillary receiverships. Dick is a graduate of the University of Delaware and holds a Masters Degree in Business from Cornell University.

Dick's insurance career began in 1964 when he became a life insurance agent for Home Life of New York. He later became assistant general agent for Massachusetts Mutual for about seven years.

In 1978, Dick was appointed Deputy Insurance Commissioner for the Delaware Department of Insurance where he served for three years. He was appointed the Deputy Receiver in January 1993 by Insurance Commissioner Donna Lee. H. Williams.

In addition to IAIR membership, Dick is the Delaware Insurance Department's representative to the Insolvency (EX5) Subcommittee of the NAIC. He also is the Regulatory Coordinator for Chapter 1 Takeover and Administration and Chapter 6 Guaranty Funds for the NAIC Receiver's Handbook.

Beyond his professional duties and activities, Dick also has a family and personal interests. He and his wife Lynn have two sons, Rob who is a French teacher at the high school level in Delaware, and Ryan who is a Captain and pilot in the United States Air Force and father to Dick and Lynn's two grandchildren, Roxanne and Eric.

When not involved with work or family, Dick serves as a County Councilman for New Castle County and represents the Delaware Association of Counties on the National Association of Counties Board of Directors where he was recently elected Second Vice President.

He also serves on the Board of Trustees of Trustees of the Delaware Symphony and is the Chairman of the Board of the Greater Wilmington Convention and Visitors Bureau.

MELISSA S. KOOISTRA

Melissa S. Kooistra is a shareholder of Rubinstein & Perry, A Professional Corporation in the Los Angeles office. Melissa is an experienced litigator in the insurance insolvency, reinsurance and regulatory areas, having acted as outside counsel to the California Insurance Commissioner for the past ten years. Her practice has been centered on the nationally prominent Mission Insurance Companies and Executive Life Insurance Company insolvencies and has encompassed all aspects of insolvency matters and litigation.

Melissa has particularly focused on reinsurance commutation, being the attorney principally responsible for the negotiation and documentation of more than 500 commutation and settlement agreements representing hundreds of millions of dollars in recoveries to the Mission estates.

Melissa's practice has also included extensive responsibility for the Final Liquidation Dividend Plan for the Mission estates, the California Proposition 103 rate rollback liability hearings, and has further included general civil litigation, particularly reinsurance collection litigation, numerous issues regarding letters of credit, detail work on set off, and the successful enforcement of judgments abroad.

She has also participated in the rehabilitation trial of *ELIC*, supervised outside law firms on the handling of litigation, and handled numerous appeals in both *ELIC* and *Mission*, including the recent litigation before the United States Supreme Court in *Quackenbush v. Allstate Insurance Company*, United States Supreme Court Case No. 95-244.

Melissa is a graduate of UCLA with a B.A. in Political Science in 1982 and obtained her J.D. from Pepperdine University School of Law in 1985. She has recently spoken at the January 1996 IAIR/NAIC Insolvency Workshop on long-tail claims estimation and at the IAIR Roundtable at the Summer NAIC Conference in New York.

RICHARD L. WHITE

Dick presently is the Deputy Liquidator of Integrity Insurance Company in Parmus, New Jersey and has an extensive background in the financial and insurance communities.

He served with the U.S. Marines in the early 1960s, thereafter completing the MBA program at Columbia University and the Professional Accounting Program at Northwestern University Kellogg School of Management.

Prior to military service, Dick received a Bachelor of Science in English from Seton Hall University.

He is a Certified Public Accountant and has been an adjunct faculty member for both graduate and undergraduate programs at PACE, Seton Hall, Fairleigh Dickinson and Rutgers Universities.

He has served as Chief Financial Officer and Senior Vice President with Skandia America, Senior Vice President of Crum and Forster, Senior Vice President of The Resolution Group and was in public practice with both Arthur Young & Company and Wailoo & White.

His responsibilities over this period have included finance, accounting, insurance, reinsurance billing and collection, arbitrations, forensic accounting and administration.

Dick is an avid enthusiast of outdoor activities, especially touring the country on his Harley.

PLEASE NOTE: *If you have someone that you would like to see profiled, sent in your recomendation to:*

Profile Editor
IAIR Newsletter
5818 Reeds Road
Mission, Kansas 66202-2740

President's Message

continued from front cover

designations shortly. The principle guiding factors of our professional organization dictate that we establish both a meaningful and attainable accreditation standard. We feel that the future credibility of our organization is grounded in both the professionalism and experimental backgrounds of our membership as exhibited by the accreditation standards.

By now, all of you should have received the new 1996 IAIR Membership Directory. Our thanks to Frank Bistrom and the association staff for a job well done. If any member has not yet received a copy of the directory, please contact association headquarters, and they will be happy to send one to you.

IAIR has a new logo, shown on the front cover of this newsletter. Our thanks to Kristine Bean and her staff as well as association staff for the design and implementation. We feel the new logo is more representative of the international status of our association.

December will be here before any of us realize where the year has gone. Currently, we have four directorships expiring in December. Any qualified members interested in serving on the Board of Directors of the International Association of Insurance Receivers, should contact Tom Wrigley, Nominations Chair, (515) 226-0514, for more information.

The Board would like to extend its appreciation to former Amicus Chair Jim Stinson for his time and continued assistance to the association. Jim has decided to devote more time to making a living and has relinquished the Chair position to Ellen Robinson of Robinson, Curley and Clayton, Chicago, Illinois.

Members interested in exploring the assistance of IAIR as Amicus should contact Ms. Robinson, (312) 663-3100.

In closing, I wish all of you a productive and healthy summer, and hope to meet with as many of you as possible in Anchorage.

AIR Newsletter

The IAIR Newsletter is intended to provide readers with information on and provide a forum for opinion and discussion on insurance insolvency topics. The views expressed by the authors in the IAIR newsletter are their own and not necessarily those of the IAIR Board, Publications Committee or IAIR Executive Director. No article or other feature should be considered as legal advice.

The Newsletter is published quarterly by the International Association of Insurance Receivers, 5818 Reeds Road, Mission, Kansas 66202-2740 (913) 262-2749 FAX: (913) 262-0174. Frank Bistrom, CAE, Executive Director; Jane Male, CAE, Associate Executive Director. **Editorial Board:** Doug Hartz, Publications Committee Chair; Morty Mann, Managing Editor; Nelson Burnett, Michael Cass, Jim Stinson, and Mary Veed, Assistant Editors. **IAIR Officers:** Richard Darling, President; Doug Hartz, Vice President; Mike Marchman, Treasurer; Robert Deck, Secretary. **Directors:** Thomas Wrigley, Philip Singer, Betty Cordial, Michael Surguine, Robert Craig & Nelson Burnett.

Highlights of IAIR's June Roundtable

By Michael Miron, Meetings Subcommittee Chair

Current topics on the cutting edge of liquidation developments, presented by active participants, were featured in New York City at our June Roundtable—which coincided with the NAIC meeting. The meeting was attended by about 80 IAIR members.

Recent actions aimed at improving the liquidation process in New York's Liquidation Bureau—by far the largest liquidation unit in the United States—were outlined by Marc Pellegrino, a new IAIR member who heads that Bureau. Richard Karpin, another new IAIR member, pointed out several of the unique situations that confront the NYLB and how these matters are addressed, including remedial legislation now pending. Mark Keenan Esq., counsel for the NYLB gave an insight into New York's complex Union Indemnity litigations, a lawsuit which has had ripple effects nationwide.

A panel discussion addressed the issue of accelerated closing of those insolvent insurance estates having material long tail liabilities. Melissa Kooistra, Esq. explained Mission's approach which was then pending before a California appellate court. Richard White, Deputy Liquidator of Integrity, outlined concepts which proved timely in view of Integrity's filing a few weeks later of a plan to conclude that liquidation. Richard Darling, of Illinois' Office of Special Deputy, added their experience on the Pine Top liquidation. Updates on a potpourri of other subjects were discussed including the Interstate Compacts, the Fabe case, the Charter Re lawsuit, Equitas and the pending study of the liquidation process by a group from within the American Bar Association.

In addition to the top notch presentations, the question and answer sessions involving the audience contributed significantly to making this Roundtable especially worthwhile.

Ann Duffy speaks on

Dick Darling speaks on

R. Karpin and Michael Miron

Pay As Paid - House of Lords Decision

"The Final Say on Pay As Paid"–Charter Re -v- Fagan

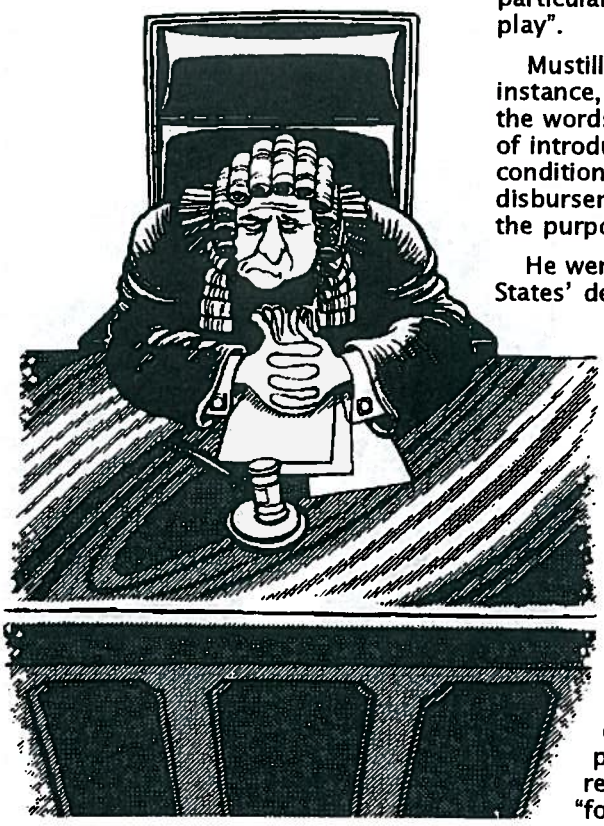
Nigel Montgomery and Philip Singer

The English House of Lords have dismissed the appeal by the Feltrim Syndicates against the decision of the Court of Appeal and the first instance decision of Mr. Justice Mance on the Pay as Paid issue.

The House of Lords Judgement

Their Lordships have finally and conclusively determined what the words—"sum actually paid"—mean in whole account excess of loss reinsurance contracts. The question to be determined was (in Lord Mustill's words) whether "the words prescribe that no sum will be paid by reinsurer to reinsured in respect of a loss... until the reinsured has paid out a sum of money to the person whose claim against him has brought the reinsurance in to play".

Lord Mustill conceded that "at first sight" he had thought that the meaning of the words was quite clear and that "the complexities and mysteries of the specialist reinsurance market had hidden the obvious solution and had led the Courts below to abjure the simple and right answer". Having reflected carefully however he concluded that the words "actually paid" were not included in order to create a condition precedent. In a phrase which is destined to become familiar to those who need to consider how the meaning of words in documents are to be interpreted, he said that "the words must be set in the landscape of the instrument as a whole". He analysed the provisions of the standard form of Ultimate Net Loss clause in wide usage throughout the Excess of Loss Market and concluded that there were only two conditions to be satisfied before an indemnity fell due. Those conditions were:



"First, that an insured event shall have occurred within the period of the policy, and second that the event shall have produced a loss to Charter of a degree sufficient, when ultimately worked out, to bring the particular layer of reinsurance in to play".

Mustill followed the Judge at first instance, J. Mance in agreeing that the words "did not have the purpose of introducing a temporal precondition to recovery in the form of disbursement", but were there "for the purpose of measurement".

He went on to analyse the United States' decisions and concluded that there was nothing in the available history of those cases or clauses in use in the UK which suggested that the words "actually paid" were included in order to create a condition precedent of prior payment by the reinsured.

Lord Hoffmann delivered a supporting Judgment. He said that the effect of the words used could only appear from the context from which the phrase was used. He then reviewed the history of both "follow the settlement" and "pay as paid" clauses concluding that the Ultimate Net Loss (UNL) clause was, throughout history, shown to be concerned with ensuring that the reinsurer cannot be called upon to pay more than the reinsured has been required to pay. He recognised that the London Excess of Loss Market operated on the assumption that a reinsurance program would relieve the insurer of the burden of having to pay claims covered by the reinsured layers. He also recognised that the regulators of insurers in this country use a test of solvency which treats reinsurance cover as a proper deduction from the insurer's liabilities. "None of this would make any sense if the insurer had first to satisfy the claim out of his own resources before he could call upon his reinsurers to pay". He concluded that:

> *"Considerations of history, language and commercial background therefore lead me to the conclusion that the word "actually" in a UNL clause is used to emphasise that the loss for which the reinsurer is to be liable is to be net and that the clause does not restrict liability to the amount by which the liability of the reinsured for the loss has been discharged".*

He finally paid tribute to the Judgment of Mr. Justice Mance at first instance with which he fully agreed.

The other Judges, Lord Goff, Lord Griffiths and Lord Browne-Wilkinson were in agreement with Lord Mustill and Lord Hoffman.

The Effect of the Decision

First of all, certainty has been restored. This will bring relief to creditors of the 30 or so insolvencies in the London Insurance Market. Reinsurance recoveries are the principal assets of these insolvent companies and the flow of these recoveries will now increase, leading to greater dividends and, possibly, earlier payments.

What is now clear is that in most circumstances a reinsurer cannot

hold his reinsured to ransom, by using the Pay as Paid defence, perhaps (cynically) in the knowledge that in doing so he might push his reinsured into insolvency.

Lloyd's have indicated that the decision will not affect Equitas as the Syndicate reserves calculated for the purposes of Equitas had already been calculated on the basis that the Judgment would be upheld.

Subject to the Regulatory Authority's view on insolvency clauses, the Judgment does leave reinsurers the option of making prior payment a condition precedent. There are good reasons for doing so in certain areas, notably the context of what is effectively mutual reinsurance. However, very clear words must be used and the authors suggest the actual use of the words "condition precedent" for such a condition to be created. Lord Mustill expressly recognised this when he said that in his mind it would "be strange if a term changing so fundamentally the financial structure of the relationship were to be buried in a provision such as clause 2, concerned essentially with the measure of indemnity, rather than being given a prominent position on its own".

One cloud on the horizon for those collecting reinsurance recoveries, particularly in insolvencies, is the situation at Lloyd's. A number of informed commentators have suggested that there will be a considerable backlog of paperwork and processing to be cleared before Syndicates' net liabilities or recoveries can be assessed. Some have suggested that this process might take several years to complete, although as yet the Lloyd's Claims Office has not made any formal statement on this point.

The effect of the decision on cashflow in the market is harder to assess. Original estimates of its impact revealed that, in gross terms, perhaps some £3billion was affected by the Pay as Paid dispute. The net position will, of course be very different. In most insolvent reinsurance companies, a large proportion of creditors are also debtors in their capacity as retrocessionaires. By virtue of set off, they will effectively receive 100p in the pound for the amount they are owed by the insolvent company, up to the total of their debt to it.

> **"The long term effects for the insurance industry can only be good and it is noticeable that the majority of the market have welcomed this decision—even those who may be more reinsurer that reinsured."**

The long term effects for the insurance industry can only be good and it is noticeable that the majority of the market have welcomed this decision—even those who may be more reinsurer that reinsured.

The case is destined to become a leading authority not only for the reinsurance market on the meaning of a standard wording in wide usage throughout the market, but also on the manner in which words and phrases are to be construed and interpreted in commercial documents.

Not only did those of us fighting the case have confidence from the outset that the Pay as Paid defence was not valid but many throughout the industry made their agreement with that view clear to us. We are very grateful for their support and encouragement in helping us to bring this case and to obtain a rapid conclusion to it - from first to final Judgment has taken almost exactly one year.

What Will the Regulatory Authority Do?

The DTI will surely breathe a sign of relief as the decision means that the large number of insurance companies who would potentially have faced hardship, if not insolvency, had the decision gone the other way, can take credit for their reinsurance programmes in the knowledge that they will respond without - as the Syndicates suggested in argument - their having to borrow or use some other device to pay claims first again. It has, however, been suggested that the DTI will still require the use of a U.S. style insolvency clause to prevent any moves by reinsurers to use revised wordings that might make payment by the reinsured a precondition to their own liability.

What Would Have Happened Had the Case Been Lost?

One of two things would have happened.

It is clear that "actual" payment does not require a physical payment in cash. The insurance market for example frequently effects payment of premiums and claims on the basis of net accounting. Set-off then, can provide an effective discharge of a debt.

Many insolvent reinsurance companies, and Charter Re is a prime example, have creditors on inwards business who are also debtors on outwards business. At its simplest, after set-off, part or all of some creditors' claims would have been discharged. Following that discharge claims would have been made upon reinsurers and the subsequent collections distributed to creditors in the form of a dividend. That partial discharge of liabilities would have led to further partial recoveries from reinsurers, leading to further distributions to creditors, further partial collections and so on ad infinitum.

The practical consequences do not bear imagining and perhaps demonstrate graphically the illogicality of the "actual payment" argument.

Brokers and reinsurers would have had to process the collection of the same claim, perhaps 10, 20 or more times and the closing of insolvent estates would have been delayed by many years, whilst the cost of administering those estates would have sky rocketed.

The alternative, and much more

continued on page 14

Pay As Paid

continued from page 13

likely consequence, and for which insolvency practitioners had already carried out some contingency planning, would have been for current and future schemes to have mechanisms incorporated into them to provide for the effective discharge of creditors' claims in a way which did not require actual physical payment. Collections would then have continued to be made in full, from reinsurers, thus avoiding the lunatic scenario outlined above.

> **"What is now clear is that in most circumstances a reinsurer cannot hold his reinsured to ransom... ."**

Nevertheless significant costs would have been incurred in varying the twenty or more current schemes, as well as those in the pipeline, which would have been borne by creditors (principally the insurance industry).

Had the case been lost, the real winners would have been the insolvency practitioners and their lawyers as a result of the increased fees arising from the additional work which they would have had to do. The losers would have been the insurance market.

Philip Singer is a partner in the National Insolvency Practice of Coopers & Lybrand and is one of the Joint Provisional Liquidators of Charter Re.

Nigel Montgomery is a partner of Davies Arnold Cooper and head of the London-based law firm's corporate insurance and insurance insolvency department.

DAC act for the Joint Provisional Liquidators and were responsible for bringing the case to and through the Courts.

This Article is based upon one which was published in Insurance Day on 28 May 1986.

Insolvency (EX5) Subcommittee

by Michael Surguine

The duties of this subcommittee shall be administrative and substantive as they relate to issues concerning insurer insolvencies and insolvency guarantees. Such duties include, without limitation, monitoring the effectiveness and performance of state administration of receiverships and the state guaranty fund system; coordinating cooperation and communication among regulators, receivers and guaranty funds; monitoring ongoing receiverships and reporting on such receiverships to NAIC members; developing and providing educational and training programs in the area of insurer insolvencies and insolvency guarantees to regulators, professionals and consumers; developing and monitoring relevant model laws, guidelines and products; and providing resources for regulators and professionals to promote efficient operations of receiverships and guaranty funds.

1. Continue development, testing and implementation of uniform data standards for both property/casualty and life/health insolvencies to facilitate exchange and use of information concerning receivership administration between receivers, guaranty funds and other interested parties.

2. Produce annual supplement to the *Receivers Handbook for Insurance Company Insolvencies.*

3. Review the protection currently available to subscribers, enrollees and policyholders in the event of the insolvency of non-profit hospital and medical service organizations, health maintenance organizations, and other health care delivery entities that do not participate in state guaranty associations, determine the adequacy of insolvency protection available, and, if appropriate, determine whether these entities should be incorporated into the existing guaranty system or whether one or more separate guaranty mechanisms should be created to provide insolvency protection to subscribers, enrollees and policyholders of such entities. Make report by Summer National Meeting.

4. Consider whether the Life and Health Insurance Guaranty Association Model Act should be amended to address certain unique business written by hospital and medical service organizations and other health care mechanisms provided by insurers that participate in state guaranty associations. Make recommendations by Summer National Meeting.

5. Monitor guaranty association assessments in relation to system capacity.

6. Monitor and discuss issues arising with respect to receiverships of "nationally significant" multistate insurers and guaranty association activities involved with these receiverships.

7. Monitor activities concerning the Interstate Insurance Receivership Compact and other interstate compact proposals relating to insurer insolvencies.

8. Recommend appropriate amendments to the Insurers Rehabilitation and Liquidation Model Act related to an insolvent insurer's participation in swaps and derivative agreements, sources of funds to defray the expense of the administration of low or no asset estates, and the need to bring delinquency proceedings to closure.

9. Study desirable amendments to the Life and Health Insurance Guaranty Association Model Act and recommend amendments for adoption as appropriate by Fall National Meeting.

10. Continue the study of desirable amendments to the Post-Assessment Property and Liability Insurance Guaranty Association Model and recommend amendments as appropriate by Fall National Meeting.

11. Identify and report issues related to claims of the federal government in insurer insolvencies, other insolvency related issues concerning asserted federal supremacy, and other matters requiring interaction between receivers and the federal government. Make report by Fall National Meeting.

12. Consider and make recommendations whether reinsurance recoverables associated with intercompany pooling arrangements are, in substance, policyholder claims and should be treated as such in a liquidation. Make recommendations by Fall National Meeting.

SSO Staff Support: Michael Surguine

RECEIVERS' ACHIEVEMENT REPORT

Jim Dickinson, Chair

Reporters: Northeastern Zone, William Taylor (PA); Midwestern Zone, Ellen Fickinger (IL), Brian Shuff (IN); Southeastern Zone, Roger Hahn (FL), James Guillot (LA); Western Zone, Mark Tharp (AZ), Jo Ann Howard (TX); International, Philip Singer (England), John Milligan-Whyte (Bermuda)

Our IAIR achievement news received from United States' reporters covering the fourth quarter 1995 is as follows:

RECEIVERS' ACHIEVEMENTS by STATE

Hawaii (Linda C. Takayama, State Contact Person)

Estates Closed	Year Action Commenced	Insurance Category	Dividend Percentage
Receivership			
Investors Equity Life Insurance Co.	1994	Life	N/A

Illinois (Mike Rauwolf, State Contact Person)

Disbursements for the Fourth Quarter 1995

Receiverships		*Amount*
American Mutual Reinsurance Company		$1,000,489
Centaur Insurance Company		113,421
Equity General Insurance Company		80,716
MedCare HMO, Inc.		845,681
Merit Casualty Company		241,669
Millers National Insurance Company		262,556
Multicare, Inc.		400,000
Pine Top Insurance Company		220,794
Prestige Casualty Company		1,949,273
Security Casualty Company		120,208
	Sub-total	$5,234,807
Plus seven (7) additional estates where disbursements for each estate were below $15,000		(23,364)
	Total	$5,211,443

Summary by Disbursement Category:

Payments to various guaranty funds/associations (including administrative expenses)	$3,476,864
Payments to policyholders/contractholders (including loss adjustment expenses)	734,090
Payments to ceding companies	1,000,489
Total	$5,211,443

Kansas (Don Gaskill, State Contact Person)

Disbursements made to various guaranty associations during Fourth Quarter, 1995

Receivership	*Amount*
National Colonial Insurance Co	$ 1,198,260 Class 1 - Administration Claims
	11,238,038 Class 3 - Policyholders

continued on page 16

Missouri (Robert Deck, State Contact Person)

Estates Closed	Year Action Commenced	Insurance Category	Dividend Percentage
American Independence Life Ins Co	1990	Life/Annuities	3.0%

Disbursements made to Guaranty Associations and other Creditors (1st Quarter 1996)

Receivership	*Amount*
American Independence Life Ins. Co.	$407,643 Guaranty Association
	3,350 All other creditors

Pennsylvania (William Taylor, State Contact Person)

Estates Closed	Year Action Commenced	Insurance Category	Dividend Percentage
Amherst Insurance Company	1982	P&C	100.0% Class B 44.5% Class C (Policyholder)
Keystone Small Business Association	1991	A&H	100.0% Class B 1.9% Class C (Policyholder)
PARCare, Inc.	1989	A&H	54.0% Class B 10.0% Class C (Policyholder)*
Penn State Mutual Insurance Company	1977	P&C	100.0% Class A 100.0% Class B 100.0% Class C (Policyholder) 97.0% Class D

**Partial disbursement made in December 1995*

Early Access Disbursements Made to Various State Guaranty Funds/Associations during Fourth Quarter 1995

Receivership	*Amount*
Summit National Life Insurance Company	$ 21,000,000
Rockwood Insurance Company	11,500,000
Paxton National Insurance Company	3,390,126 (correction from Third Qtr. 1995)

Other Developments

Bill Taylor (PA) updated an earlier report covering the **Fidelity Mutual Life Insurance Company ("FML")** rehabilitation and advised that in March of 1995, the court approved the formation of a Policyholder's Committee. The Committee subsequently engaged a law firm and accounting firm to represent them. During the Summer of 1995, their experts conducted the due diligence necessary to become familiar with FML and the provisions of the Amended Rehabilitation Plan filed on January 12, 1995. By the Fall of 1995, it was apparent that the financial condition of FML had improved to the point where the terms of the Stock Purchase Agreement did not accurately capture the true value of the company, to the possible detriment of the policyholders and creditors. Consequently, the Rehabilitator decided to ask the three finalists in the 1994 investor selection process to submit improved proposals for the purchase of a minority interest in the company. It is expected that these improved proposals will be submitted by the end of April, 1996. No guaranty association assessments are expected in connection with the rehabilitation plan.

Policyholder death benefits and annuity payments are being paid 100%. On March 4, 1996, the Rehabilitator filed a petition to ease the moratorium restrictions currently in place by allowing policyholders to exercise previously denied policy options, such as choosing to purchase a reduced paid-up policy or an extended term policy with their cash values. The petition also asks for authority to allow access to 10% of cash values under policy provisions, with only applicable contractual charges.

If approved, the petition will also permit an increase of 50 basis points in crediting rates, with another increase possible later in the year. Policyholders who purchased retirement policies or are retiring (or totally disabled) under the provisions of a qualified plan will also be able to receive a lump sum payment under certain conditions.

Bill Taylor also advised as to developments in the rehabilitation of the **Mutual Fire, Marine & Inland Insurance Company** that adjusted claims of policyholders were paid 100% (Class 4 claims). A petition was filed by the Rehabilitator on January 18, 1996 seeking the Court's approval to set aside funds (a reserve) for remaining unsettled Class 4 claims and all Class 5 claims (surety bond claimants) and make an initial distribution to Class 6 claimants (general creditors including cedents of Mutual Fire). This motion is pending the Pennsylvania Commonwealth Court's approval.

On November 29, 1994, Mutual Fire's Rehabilitator filed a Petition seeking Court approval of their record and bar dates for the cedents (Class 6) claims. Argument on objections to the Petition were held November 28, 1995. On December 15, 1995, the Pennsylvania Commonwealth Court entered an Order fixing the record date for claims of cedents at December 31, 1995 and a bar date for claims of cedents to file a fully completed proof of claim by March 31, 1996. The Court additionally ordered that claims shall be allowed only with respect to losses and loss adjustment expenses actually paid by the record date and that no case loss reserves or incurred but not reported ("IBNR") losses shall be submitted.

Linda Chu Takayama (HI) advised that on February 5, 1996, the policies of **Investors Equity Life Insurance Company ("IEL")** were restructured and assumed by Hartford Life Insurance Co. As part of the agreement, IEL contributed $18 million to the state guaranty association, which was used to partially fund the policyholders' accounts. The total IEL and guaranty association contribution was $65 million. Total liabilities assumed by Hartford approximated $140 million.

Sara Begley (AZ) by letter provided the following achievement news for developments in Arizona:

1. **AMS Life Insurance Company**- announcement of a $14.95 million early access distribution.
2. **Mission Insurance Company** (ancillary)- Completed distribution of $8.9 million to California domiciliary receiver after satisfying the claim of the Arizona State Compensation Fund involving special workers' compensation deposit.
3. **Employers Casualty Company** (ancillary) - Distributed $2.5 million to Texas domiciliary receiver after satisfying the claim of the Arizona State Compensation Fund involving special workers' compensation deposit.

Jim Gordon (MD) in updating happenings in the **Trans-Pacific Insurance Company** estate advised that one defendant in a criminal action, Martin Bramson, had been arrested by the Liechtenstein State Police in January, 1995. Mr. Bramson had in his possession at the time of his arrest in excess of $3.0 million in gold and various currencies. The U.S. Justice Department has filed a formal extradition request. The Liechtenstein Government submitted an extradition letter to the United States which contained terms that were not in the Treaty between the countries. As a result, the U.S. officials have formally rejected the extradition letter. Mr. Bramson continues to oppose extradition.

Civil actions have been filed against a number of former directors, stockholders, officers and other control persons. Judgments in excess of $35 million, respectively, have been rendered against four of the defendants.

LAUGH 'TIL IT HURTS

"No, you aren't here to liquidate our insurance company."

NOMINATING COMMITTEE REQUEST

By Thomas G. Wrigley
Nominating Committee Chair

Principal Members, on December 31, 1996 the term of the following named Board of Directors will expire:

Richard Darling
Douglas Hartz
Thomas G. Wrighley
Philip Singer

The members of the Nominating Committee for 1996 are:

Thomas G. Wrigley, Chair
Betty Cordial
Michael E. Surguine

We would like to solicit your assistance by submitting to the Chair of the Nominating Committee your suggested candidate(s) to be considered for nomination for election to the Board of Directors. Please include, along with the candidates name, their signature indicating a willingness to serve, if nominated and elected. It would be appreciated if you would forward your suggestion as soon as possible, but prior to **October 7, 1996.**

NAIC New York Meeting Recap

By Mary Cannon Veed

The 1996 Summer National Meeting of the NAIC was held in New York, which put on its best face for the occasion. A festival atmosphere generated by the Tony Awards being presented down the street combined with the sort of summer weather every Chamber of Commerce loves to claim to create a relaxed and pleasant setting. In spite of which, most of the participants spent the weekend wandering interior hallways and windowless meeting rooms, as the business of the NAIC ground on.

There has been an identifiable shift in the NAIC's center of gravity, with attention diverted away from the mechanics of liquidation and towards the operation of "live" insurers, whose business is rapidly changing. When everyone is fascinated by new business innovations and opening vistas of profitability, liquidators are about as welcome as ants at a picnic—but some of those new ideas are bound to be bad ones, and it's worthwhile keeping an eye on them.

Three things seem to preoccupy the Commissioners, and they all have code names: re-engineering, dumping, and the federal government. Re-engineering refers to a move to de-regulate the insurance of large risks placed by supposedly sophisticated consumers. When neither the insurers or the insureds really want to be regulated, and where regulations fashioned for more fungible risks arguably do more harm than good when applied to the coverage of packages of multistate and multiline exposures, it makes sense to consider less meddlesome approaches. But there are complications. Chief among them are how to insulate regulated business from that deregulated—to keep people who do not qualify as "sophisticated risks" from being sold unregulated insurance (apparently cheaper and more flexible insurance) by operators skilled in finding loopholes, and to keep companies which become overcommitted to the novel marketplace from dragging down their regulated affiliates. There's also the problem of the camel's nose: if deregulation becomes fashionable, there will be intense pressure on those charged with supervising conventional insurance to extend similar liberties to their charges - which may or may not be a good or a bad idea, but will cause turmoil either way. Maybe what attracts the most pointed attention, though, is the effect that changes like these would have on the specialists whose business it now is to find ways around the Byzantine tangle that passes for the surplus lines business, and who could find themselves quite suddenly obsolete. Dick Bouhan had the look, at the public hearing on this subject, of a dentist energetically, but ambivalently, promoting flouride.

The public hearing on the subject was a large affair, and everyone stuck to their scripts. Unless I missed something, the chief significance of it was who came (every trade that ever claimed competance in alternative risk financing), rather than what they said. It will be a while before any NAIC-level conclusions are reached, but several states have already launched deregulation schemes for large risks, and if they are successful, other states will probably follow suit.

Am I the only one who has noticed that the approach they use is identical to the recently adopted Insurance Directives of the European Communities?

It has to be symptomatic of this stage of the insurance cycle that the "liability dumping" argument is being driven, not by the policyholders whose claims are being dumped, but by the competitors of the dumpers. The combatants are engaged in an elaborate minuet, going through the motions of establishing advisory groups and writing outlines for a white paper. This time they produced an outline of subject matter, and spent some time rearranging it. No clear indication yet, though, what the final steps will look like.

Two issues active at the moment implicate the relationship between insurance regulators and the federal government. The first is the aftermath of the Gallagher case, which opened up the possibility that banks might have the opportunity to engage in various insurance activities without benefit of state regulation. The impression subsists that the Comptroller of the Currency harbors territorial ambitions which would spur it to argue that the Gallagher case's approval of the use of the small-town agency rules to launch big-time insurance operations must also exempt those agencies from operational regulation by the states. The NAIC's response was an oblique reminder, to those of short

memory, that frustrating state regulation of financial services, without establishing a replacement authority on the federal side, and committing the resources to make it effective, is a recipe for trouble. A resolution passed by the Executive committee urged Congress and the Administration to reaffirm the primacy of state regulators over agency activities of national banks, and challenged any states which might use the confusion as an excuse for abdicating their responsibilities in this regard to resist the temptation.

A streak of isolationism runs not too far below the surface of most Americans, insurance regulators no less than the rest of us. A textbook example of thoughtless jingoism turned up in the purpose clause of the proposed Model Act on Credit for Reinsurance, in the form of a reference to the "insuperable obstacle" to collection of reinsurance balances posed by the need to pursue collection outside the United States. One wonders why regulators would countenance overseas placement of reinsurance at all, if they are so convinced it is uncollectible, but the fact is that, within the circle of developed nations, collection of reinsurance presents no more insuperable obstacle than the cost of plane fare—a cost which did not bother the people who originally signed the treaty. The preamble amounted to a completely gratuitous slap in the face to residents of nations which work just as hard to make their business and judicial systems fair and effective as we do, and the committee was persuaded to remove it.

But the streak persists, witness the same committee's reaction to the current tizzy over the possibility that a 304 order might eliminate the protection of reinsurance and surplus lines trust funds for American policyholders. The Committee is about to write itself out of business, but it was suggested that it recommend to the Executive committee that something be done to limit the effect of 304 orders on trust funds, although that would clearly require some action by Congress. This controversy is a curious one, because it is driven, not by liquidators or even disgruntled creditors, but by the US reinsurance industry, which is enjoying the opportunity to equate both "foreign" and "federal" with "dubious"—and scratch that jingoistic itch.

Those of the liquidation community who have travelled it know that the road to London and beyond is a two-way street. In honoring the authority of foreign liquidators over their own bankrupt citizens, our courts make it possible for US liquidators to move with similar liberty on foreign soil. Living day to day with the convention that the domiciliary state takes the lead role in multistate liquidations, it is not a great leap to conclude that a foreign liquidator of a foreign company can fill the same role if he chooses to accept the same burden. And a couple of disastrous efforts have convinced many that a "beggar thy neighbor" approach to collecting assets of a bankrupt estate is more likely to impoverish the isolationist than anyone else.

Section 304 has developed an impressive jurisprudence, which elaborates on the statute's express command that the Court consider the rights of American creditors before granting its order. While it is theoretically possible for a bankruptcy court to order a US Trust fund turned over to a foreign liquidator without restricting its use, in practice it does not happen, and is not likely to. This is not to say 304 is perfect - it's not - but the bogeyman described by the proponents of the current change is largely imaginary. It remains worrisome that the Committee seemed prepared to react to the "horror story" proposed to it without any inquiry to the liquidation community, or even a close reading of the statute. Receivers should closely watch this issue and demand to be involved in any changes: there is much to be lost to inexpert tinkering in this complex area.

Routine prevailed for our usual subjects. The Handbook threatens to reach the printer this month; first drafts of the 1997 revisions are due about now, with exposure in Anchorage. The Guaranty Fund Issues group heard more presentations form NOLHGA (out in full force) on proposed revisions to the life act, but it seemed clear that unless the organization can articulate reasons why it should receive most of the advantages and none of the burdens of a liquidator, the revisions were headed nowhere. [R&L model?] A note of reason was struck in the Alien Requirements working group, which received an elegantly revised version of the Standard Form Trust Agreement assembled and meticulously annotated by Jim Morris of CNA. The logic is clearer, the grammar is better - why didn't we do this a long time ago?

My favorite irony of the meeting was the vehement objection of NAPSLO to the new Nonadmitted Model Act's provisions on a broker's liability when a nonadmitted insurer neglects to pay claims. They thought this opened new vistas of broker liability, but, as Ellen Wilcox pointed out in a thorough survey of existing law, they already operate under an equal or greater burden, which they apparently have not noticed before.

I am told that the IAIR Roundtable was well attended and especially well presented, and the gremlins which haunted the committee meetings and other activities in Detroit seem to have stayed there. Alaska is one of the few states in the Union I haven't been to. If the weather holds up, it should be one of the real fringe benefits of riding this circuit. See you all there!

WANTED

Your Articles for *the Newsletter*

If you have an article you would like to submit for publication in *the Newsletter*, please submit it in MS Word 6.0, or Wordperfect 5.0 or 5.1 on an IBM formatted 3.5" floppy disc. Mail it to IAIR Headquarters, attention Heather.

Article(s) must be received by the first of the month, one month prior to publication date. All submissions become property of IAIR and may or may not be chosen for publication.

If you wish to have your diskette returned please enclose a 6"x9" SASE.

Quackenbush v. Allstate: The Supreme Court Clarifies Abstention

By Peter R. Chaffetz and Steven C. Schwartz[1]

On June 3, 1996, the U.S. Supreme Court issued its long-awaited decision in *Quackenbush v. Allstate Ins. Co.*, 1996 U.S. LEXIS 3609 (1996). In *Quackenbush*, the latest decision to arise out of the liquidation of Mission Insurance Company ("Mission"), the Court explored the limits of the *Burford* abstention doctrine, a tool that has been used by insurance company liquidators to keep actions in state liquidation courts.

Ruling in favor of a reinsurer that had removed the liquidator's reinsurance collection action to federal court, the Supreme Court held that the district court erred in applying *Burford* abstention to remand the case to the liquidation court. However, the Court rejected the *per se* rule urged by the reinsurer—and adopted by the Ninth Circuit—that Burford abstention applies only in actions seeking equitable relief. Instead, the court opined that, where the plaintiff seeks purely legal relief (i.e. monetary damages), Burford abstention may justify a stay, though not an outright remand or dismissal.

As shown in this article, *Quackenbush* continues a trend narrowing the *Burford* abstention doctrine. While the Court did not eliminate the doctrine from the liquidator's arsenal, the opinion contains language that may lead courts to refuse to abstain in many circumstances. In particular, federal courts may be less likely to abstain from deciding ordinary contract disputes where the only ground for abstention is that one of the parties is an insolvent insurance company.

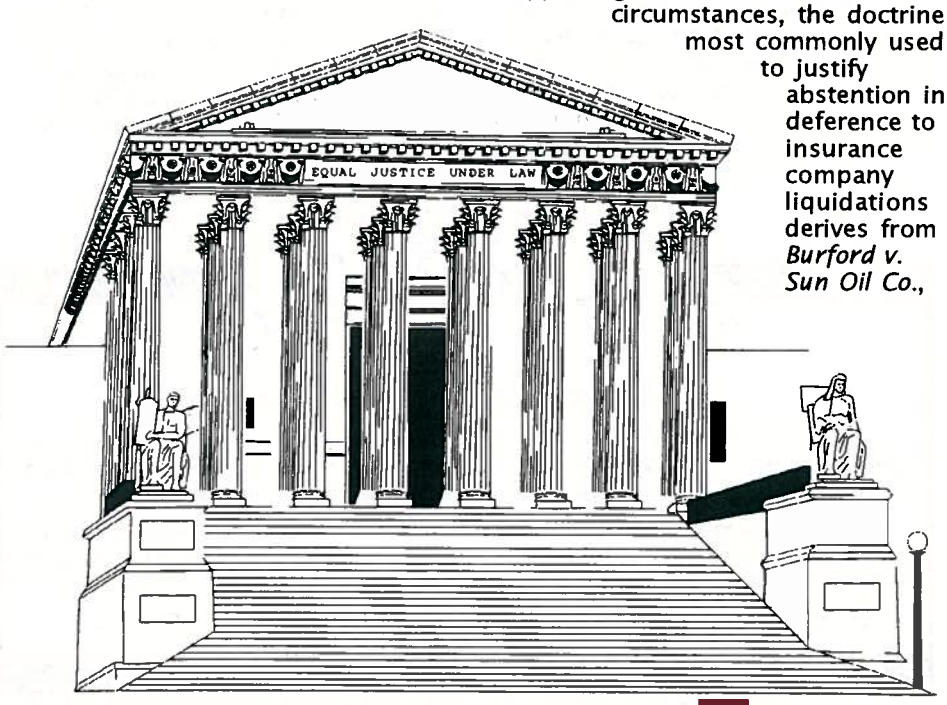
I. Abstention in Insurance Company Insolvencies

When a federal court abstains, it declines to exercise jurisdiction over a case that otherwise satisfies the legal requirements for federal jurisdiction. Where it is permissible, abstention is "an extraordinary and narrow exception to the duty of a District Court to adjudicate a controversy properly before it." *County of Allegheny v. Frank Mashuda Co.*, 360 U.S. 185, 188 (1959).

Although federal courts have developed several distinct theories supporting abstention in various circumstances, the doctrine most commonly used to justify abstention in deference to insurance company liquidations derives from *Burford v. Sun Oil Co.*, 319 U.S. 315 (1943). In a pre-*Quackenbush* case, the Supreme Court described the *Burford* doctrine as follows:

> Where timely and adequate state-court review is available, a federal court sitting in equity must decline to interfere with the proceedings or orders of state administrative agencies:
>
> (1) when there are "difficult questions of state law bearing on policy problems of substantial public import whose importance transcends the result in the case then at bar"; or
>
> (2) where the "exercise of federal review of the question in a case and in similar cases would be disruptive of state efforts to establish a coherent policy with respect to a matter of substantial public concern." *New Orleans Public Service, Inc. v. Council of City of New Orleans*, 491 U.S. 350, 361 (1989)("*NOPSI*").

Some insurance company liquidators have argued that federal courts should abstain from deciding any case related to insurance liquidations on the ground that federal court involvement will "be disruptive" of the state liquidation scheme. For example, in *Corcoran v. Ardra Ins. Co., Ltd.*, 842 F.2d 31 (2d Cir. 1988), the liquidator of an insolvent insurance company commenced an action in state court to collect amounts owed the estate by a reinsurer. After the reinsurer removed to federal court, the district court remanded to the state court based on the *Burford* abstention. The Second Circuit affirmed, noting that "New York's '"complex administrative and judicial system for regulating and liquidating domestic insurance companies"' is the type of regulatory scheme that warrants serious consideration of abstention when the question before the court is a novel one." 842 F.2d at 37. Explaining that the collection of reinsurance proceeds was important to the liquidation scheme, the court opined that "the district court's decision to abstain appears to fit



particularly well within the *Burford* goal of avoiding interference with specialized state regulatory schemes." See also *Lac D'Amiante du Quebec, Ltee, v. American Home Assur. Co.*, 864 F.2d 1033, 1045 (3d Cir. 1988) ("the regulation of insurance companies unable to meet their obligations entails the type of strong state interest in which application of *Burford* abstention is appropriate').

However, in *NOPSI*, *supra*, the Supreme Court cautioned against over-reliance on *Burford* abstention. The Court noted that "[w]hile *Burford* is concerned with protecting complex state administrative processes from undue federal interference, it does not require abstention whenever there exists such a process, or even in all cases where there is a 'potential for conflict' with state regulatory law or policy." 491 U.S. at 362.

Thus, following *NOPSI*, courts grew more reluctant to abstain in cases relating to insurance company liquidations. For example, in *Melahn v. Pennock Ins., Inc.*, 965 F.2d 1497 (8th Cir. 1992), the liquidator of Transit Casualty Company sought remand on abstention grounds of a collection action against a former agent. The Eighth Circuit reversed the district court's remand order, holding that the action in federal court would not unduly interfere with state liquidation proceedings. See generally *Michael A. Knoerzer, Flagging the Obligation: Federal Courts' Abstention In Favor of State Rehabilitation and Liquidation Proceedings*, 28 Tort & Ins. L.J. 837 (1993).

II. The Quackenbush Case

The *Quackenbush* case grew primarily out of a question raised by *NOPSI*. The *NOPSI* Court had described the *Burford* doctrine as applicable to "a federal court sitting in equity . . ." 491 U.S. 350. Opponents of abstention argued that this and other authority showed that abstention was available only in a case involving a federal court's equitable powers. After lower courts divided on the issue, the Supreme Court agreed to resolve it in *Quackenbush.*[2]

The distinction between law and equity has roots in English common law. Although the distinction has largely faded, it remains important to the kinds of relief a court may grant. Equitable remedies are generally non-monetary, and include injunctions, specific performance and the like. Legal remedies, on the other hand, are forms of monetary damages. Historically, courts have been allowed far more discretion in awarding equitable remedies than legal ones.

In *Quackenbush*, the district court invoked *Burford* abstention to remand a case in which the Mission liquidator sought a purely legal remedy—collection of reinsurance proceeds. The Ninth Circuit reversed on the grounds that abstention is simply unavailable in such a case.

The Supreme Court undertook an historical analysis of abstention, and concluded that abstention has been upheld in both legal and equitable cases. However, the Court found, the doctrine has supported outright dismissal or remand only in cases at equity. Where the claim is legal, the Court concluded, the trial courts may abstain only to the extent of staying the case temporarily. Therefore, the Court affirmed the result reached by the Ninth Circuit, because it agreed the case should not have been remanded. However, it rejected the Ninth Circuit's *per se* prohibition of abstention in cases at law, noting that "Burford might support a federal court's decision to postpone adjudication of a damages action pending the resolution by the state courts of a disputed question of state law." 1996 U.S. LEXIS 3609 *45.

In addition to discussing the arcane distinction between law and equity, the Supreme Court offered views on the application of *Burford* abstention that were not strictly necessary to its decision. Allstate had removed the liquidator's action to federal court in order to move to compel arbitration under the Federal Arbitration Act. The liquidator's primary dispute with Allstate was over Allstate's right to setoff. The liquidator argued that the setoff issue raised an important question of state law that should be resolved in the liquidation court.

Citing *NOPSI*, the Court stated that:

> *Burford* allows a federal court to dismiss a case only if it presents 'difficult questions of state law bearing on policy

continued on page 22

Quackenbush v. Allstate

continued from page 21

> problems of substantial public import whose importance transcends the result in the case then at bar,' or if its adjudication in a federal forum 'would be disruptive of state efforts to establish a coherent policy with respect to a matter of substantial public concern.'

1996 U.S. LEXIS 3609 *38-39. Here, the Court observed, the "federal interests...are pronounced, as Allstate's motion to compel arbitration under the Federal Arbitration Act implicates a substantial federal concern for the enforcement of arbitration agreements." 1996 U.S. LEXIS 3609 *42. The state law concerns, on the other hand, seemed insubstantial because "the case appears at first blush to present nothing more than a run-of-the-mill contract dispute." *Id.*

However, the Court acknowledged the liquidator's concern that federal adjudication of the setoff question could have an impact on the state liquidation proceeding. Although the court did not decide whether this concern would have justified abstention, it suggested that it might have supported an abstention-based stay:

> given the situation the District Court faced in this case, a stay order might have been appropriate: The setoff issue was being decided by the state courts at the time the District Court ruled...and in the interest of avoiding inconsistent adjudications on that point, the District Court might have been justified in entering a stay to await the outcome of the state court litigation.

1996 U.S. Dist. LEXIS 3609 *45-46. Thus, the Court has left room for liquidators to seek abstention in certain cases, including those in which unsettled questions of state insolvency law are at issue.

III. Implications for Insurance Company Liquidations

Even though *Quackenbush* rejected the Ninth Circuit's *per se* rule against *Burford* abstention in actions at law, it effectively eliminates this procedural device for preventing federal courts from adjudicating actions seeking solely monetary damages. Now, the federal courts can, at most, defer adjudicating such claims pending the outcome of parallel state court litigation. Presumably, if no such action is pending in the state court, then even a stay would be unavailable.

Moreover, *dictum* in *Quackenbush* reinforces the narrow view of *Burford* abstention adopted in *NOPSI*. Under this view, the mere pendency of liquidation proceedings is not sufficient to justify abstention. Rather, courts must assess the particular state and federal interests involved to determine whether abstention is warranted.

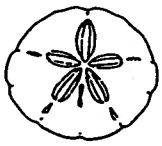
The *Quackenbush* case is also significant for what it did not decide. Because the Supreme Court ruled on narrow federal procedural grounds, the case does not address an important underlying issue in both the particular case before the Court and in insurance insolvencies generally: whether arbitration clauses remain enforceable after liquidation. Indeed, all that Allstate was asking the federal court to do in the *Quackenbush* case was to compel arbitration, not to resolve the setoff question. Thus, the Supreme Court's suggestion that the federal court might have stayed the action pending the state courts' resolution of the setoff issue seems odd. The Court apparently assumed that once the issue was decided by the state courts, the federal court could have proceeded to resolve the reinsurance contract dispute in accordance with the resulting rule of state law. But if the federal court granted the petition to compel arbitration, the arbitration panel may not have been required to decide the matter in accordance with any state court rulings.* Thus, while there may be situations where a stay makes sense, the actual case before the *Quackenbush* Court does not appear to have been one of them.

In short, the decision to affirm the result in the Ninth Circuit but reject that court's *per se* approach virtually ensures that there will be further litigation over the scope of *Burford* abstention. It does appear, however, that successful abstention claims will now be rarer in insurance insolvencies.

***The reported cases are split on whether setoff disputes involving liquidators are arbitrable, or whether the liquidator can insist that the liquidation court rule on the setoff issue.**

[1]Peter R. Chaffetz is a partner in the New York and Los Angeles offices and Steven C. Schwartz is counsel in the New York Office of Chadbourne & Parke LLP.

[2]The *Quackenbush* Court also resolved a question regarding the appealability of absention-based remand orders, holding that they are appealable.



ORMOND INSURANCE AND REINSURANCE MANAGEMENT SERVICES, INC.

SERVICES OFFERED

- ❑ **Administration of MGA, Primary or Reinsurance Books of Business**
  data processing, accounting, underwriting claims, regulatory filing, rehabilitation strategies. . .
- ❑ **Arbitration and Litigation Support**
  expert testimony, discovery work, case management, depositions, litigation assistance, reconstruction of records, arbitration panel member. . .
- ❑ **Audits and Inspection of Records**
  pre-quotation, contract compliance, aggregate exhaustion, reserve adequacy. . .
- ❑ **Commutation Negotiations**
  reserve determination, present value calculation. . .
- ❑ **Contract Analysis**
  analysis of reinsurance contracts, analysis of primary or excess coverage, contract drafting. . .
- ❑ **Reinsurance Recoverable Administration**
  reporting, collections, letter of credit control, security review. . .
- ❑ **Special Projects for Rehabilitators, Liquidators, and Insurance Company Management**
  reconstruction of premium and loss history, loss development analysis, reserve determination. . .
- ❑ **Statutory Accounting**
  annual and quarterly statement preparation, diskette filing, premium tax returns. . .
- ❑ **Client Representative**
  settlement conferences, attend informational meetings, monitor activities of defense counsel. . .
- ❑ **Reinsurance Data Systems**
  main frame and PC systems in place for processing of underwriting, claims and accounting for assumed, ceded or retrocessional business

ORMOND INSURANCE AND
REINSURANCE MANAGEMENT SERVICES INC.

140 South Atlantic Avenue, Suite 400
Ormond Beach, Florida 32176

Telephone: (904) 677-4453
Telefax: (904) 673-1630

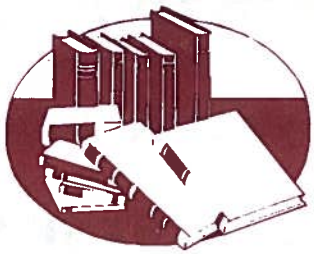
John B. "Jay" Deiner
Executive Vice President
Secretary & General Counsel

A.L. "Tony" DiPardo
Senior Vice President

William T. "Bill" Long
Senior Vice President

Other News & Notes

By Douglas A. Hartz,
Missouri Receivership Supervisor



First, it is with much regret that I must inform all that Michael Miron has retired from the Board of Director's of IAIR. Mike was one of the founding members of IAIR (or SIR as it used to be known) and served as its second President. From personal knowledge I can safely say that we would not have IAIR today if not for the leadership and dedication of Mr. Miron. Moreover, there are some receiverships that would not be nearly as far along as they are if not for his contributions and his qualities. His insights, incites to act and mastery of the art of delegation will be very personally missed on the Board although I am sure he will still be active in IAIR.

Second, Jacqueline Reese, the Michigan Director of the Receivership division, has moved out of the receivership world taking a job promising fresh challenges in a completely unrelated area of state government. Her participation in working groups and round-tables and her Northern perspective will be very much missed. I suppose that all of the receivership issues in Michigan have landed now on top of Patrick McGuire who may possibly miss Jackie more than anyone.

Third, in what I believe is an unrelated item to the above, I have been informed that Michigan has become the fifth state to join the Interstate Insurance Receivership Compact. I have also read the version of the compact bill in Wisconsin, subject to a partial veto by Governor Tommy G. Thompson, and would have to comment that it appears Wisconsin has not quite joined the Compact. In short, anything to do with two "f-words", funding and finance, was excised.

As noted in the last newsletter, we have changed the schedule for the Newsletter so that it will be produced after, instead of immediately before, the NAIC meetings in the first week of April, July, October (not August as last indicated) and January. We will also send out a shorter Meetings Bulletin about two weeks prior to each upcoming meeting. Every member should have received this bulletin prior to the New York meeting. If you did not please contact Frank Bistrom, CAE. Further on publications matters, it has been suggested that the directory should have a cross reference by state, which we plan to implement in the next Directory. Which, by the way, is a much improved Directory in which everyone should consider placing an advertisement of their services and capabilities.

Hopefully you have all followed the EMLICO developments. In line with the last issues' brain straining comment, let me ask a few more questions. If there is guaranty fund coverage of the claims in EMLICO, then are the guaranty funds going to get their claims paid at the same priority as all creditors? Suppose there are $200 in claims paid by the GF's, $100 in non-GF-covered (NGG claimants) policyholder level claims, $200 in reinsurance claims, and $200 in assets in EMLICO. Under the model act then, don't the GF's get a liquidation dividend of $133.34? Following on, the NGC claimants get $66.66 and the reinsureds get nothing under the model act, correct? In Bermuda though, don't the GF's get $80, the NGC claimants get $40 and the reinsureds get $80? Can anyone explain why the reinsureds are trying to pull this back into a model act state? Or is it only EMLICO's reinsurers that want it back in the good old U.S.? Is it that the reinsureds are not some of the same entities as the reinsurers (ala Mission) such that there would be a different issue due to the potential restriction of offsets in a model act state? Is it that there is one very large policyholder level claimant that can have its way with a scheme of arrangement more so than it could in a model act state? Is it that the normal balance of interests in an estate are turned around here? That is, normally there are a very few reinsurers with large interest in the estate versus many insureds each with relatively smaller interests, and in EMLICO the opposite of the norm, very few insureds with really big interest, happens to be the case?

By my count five states are now involved in experiments in accelerated estimation of long-tail claims and recovery of related reinsurance balances. They are California, Illinois, Missouri, New Jersey and Utah. Three (IL, MO and UT) have statutes that expressly authorized this procedure. Since our last newsletter, the Mission plan was held to exceed the express statutory provisions and the Deputy Commissioner/Liquidator, Karl Rubinstein, has amended that plan. It has be reported that interim distributions among the affiliates will range from 55% to 70%, but that the timing on the remaining 30% or more (yes, that's right Mission may cover the policyholders in full) depends on estimation and possibly on the statues expressly authorizing the procedure. Perhaps we should all be looking to amend our statues to allow for this procedure that could significantly shorten P&C liquidations. Albeit, let us not all run to our respective legislatures to obtain just this one correction when there is so much more to be corrected and such opportunities to do so in concert or, at least, greater unison.

We are at a crossroads of opportunity to increase the consistency of our various state rehabilitation and liquidation laws from two sources.

First, is fact that the IIRC folks are beginning the process of determining what rules will be applied in the compacting states. Which means there will be consistency among five states, at least, but that consistency may (will) be very inconsistent with the other forty-five. Since the other forty-five are not all that consistent I suppose these five will logically have to be inconsistent with about all of them. I suggest that whatever is adopted by the IIRC as its model Rehabilitation and Liquidation Rules should also be adopted, or at least considered, by the NAIC through the Model Acts Working Group of the Insolvency Subcommittee, and visa versa.

That is, I would hope that the IIRC will build its Rules from the current NAIC Model Act with improvements in 1) the accelerated estimation of long-tail claims and recovery of related reinsurance balances, 2) the differentiation between rehabilitations and liquidations, 3) the ground for liquidation of not transacting the business of insurance for one year changed to not issuing, renewing or servicing policies for one year; to heed lessons from the FABE related decisions, 4) the contract disaffirmance provisions, 5) the interstate (inter-compact?) relations provision, and 6) the differentiation between L&H and P&C type proceedings.

Which brings us to the second opportunity to obtain greater consistency among our state laws. That being, the NAIC is hopefully on the verge of adopting an updated and much improved Life and Health Insurance Guaranty Association Model Act that is likely to be aggressively pushed in the next couple of years of state legislation and deserves the support of the various insurance departments.

This expected push opens another window of opportunity to get the closely related Rehabilitation and Liquidation Model Act adopted. If we can obtain a greater consistency it should lower costs, speed the process, and perhaps forestall such nasty alternatives as an accreditation requirement (imposed compaction?) or some form of federal legislation.