Received 4/22/2019 10:45:23 PM Commonwealth Court of Pennsylvania

IN THE COMMONWEALTH COURT OF PENNSYLVANIA

In Re: Penn Treaty Network America Insurance Company in Liquidation	No. 1 PEN 2009
AND	
In Re: American Network Insurance Company in Liquidation	No. 1 ANI 2009

RESPONSE OF THE INTERVENOR HEALTH INSURERS TO THE LIQUIDATOR'S APPLICATION FOR DECLARATION REGARDING POLICYHOLDER CLAIMS FOR NON-GA POLICY BENEFITS

TABLE OF CONTENTS

Page

TABLE OF CONTENTS
(continued)

Page

TABLE OF AUTHORITIES

Page(s)

Cases

TABLE OF AUTHORITES
(continued)

Page(s)

Statutes

TABLE OF AUTHORITES
(continued)

Page(s)

TABLE OF AUTHORITES
(continued)

Page(s)

INTRODUCTION

Pursuant to the Court's Order of March 22, 2019, Intervenors Aetna Life Insurance Company, Anthem, Inc., Cigna Corporation, HM Life Insurance Company, Horizon Healthcare Services, Inc. d/b/a Horizon Blue Cross Blue Shield of New Jersey, QCC Insurance Company, United Concordia Life and Health Insurance Company, United Concordia Insurance Company and UnitedHealthcare Insurance Company (collectively, the "Health Insurers"), through their undersigned counsel, hereby submit this response to the Application for Declaration Regarding Policyholder Claims for Non-GA Policy Benefits (the "Application") filed by Jessica K. Altman, Insurance Commissioner of the Commonwealth of Pennsylvania, in her capacity as Statutory Liquidator (the "Liquidator") of Penn Treaty Network America Insurance Company ("PTNA") and American Network Insurance Company ("ANIC" and, together with PTNA, the "Companies").

In 2014, the Pennsylvania Supreme Court decided *Warrantech Consumer Products Services, Inc. v. Reliance Insurance Company, in Liquidation*, 96 A.3d 346 (Pa. 2014) "*Warrantech*"), which held that under Sections 520 and 521 of Article V of the Insurance Department Act of 1921 (the "Receivership Act") policies of a company in liquidation terminate by operation of law no later than the thirtieth day after entry of the liquidation order. *Warrantech*, 96 A.3d at 356-57.

The Court held that termination barred claims for coverage based on events occurring after the thirtieth day following the liquidation order (hereafter referred to as a "Termination Date").[1] *Id.* at 357. The ruling followed prior Pennsylvania decisions, and was in fact the result sought by the Pennsylvania Insurance Department in the case. *See, e.g., Foster v. Colonial Assurance Co.*, 668 A.2d 174, 184 (Pa. Commw. Ct. 1995), *aff'd sub. nom., Kaiser v. Colonial Assurance Co.*, 673 A.2d 922 (Pa. 1996) (affirming liquidator's zero dollar valuation for loss that arose after policy termination by operation of Sections 520 and 521).

This Court, in this case, reached the same conclusion as the Supreme Court in *Warrantech* two years before that case was decided. *See Penn Treaty Network Am.*, 63 A.3d at 378 ("In a liquidation, all policyholders will have their policies cancelled in 30 days. At that point the guaranty fund in the state where a particular policyholder resides will offer some kind of replacement coverage."); *see also id.* at n.7 ("Of course, policyholder claims against an insolvent insurer estate may be filed after the insurer is liquidated. However, the claim must be one for a loss that occurred while the policy was in existence, *i.e.,* before the liquidation."); *see also id.* at 378, 446 n.51 (noting that the Pennsylvania Insurance Department has consistently taken the position that claims against the estate that arise more than

[1] The Liquidator observes that she did not ask the Court to enter an order terminating the policies. Application ¶ 16. But this misses the point. The policies terminate by operation of law without the need for an order. 40 P.S. §§ 221.20 and 221.21; *see also Consendine v. Penn Treaty Network Am. Ins. Co.*, 63 A.3d 368, 378 (Pa. Commw. Ct. 2013) ("In liquidation, all policyholders will have their policies cancelled in 30 days.").

thirty days after liquidation are barred, and citing the *Colonial Assurance Company* and *Legion Insurance Company* cases as examples).

The clear consequence of *Warrantech* is that a liquidator may not administer an estate by setting aside a fund to pay policyholders for claims under policies as they arise after a Termination Date. Yet the Liquidator in this case seeks to do exactly that by disguising it as a supposed transfer to an unfunded captive insurance company. The Liquidator devises two paths around the express provisions of the Receivership Act and *Warrantech.* First, the Liquidator contends that the policies did not terminate because they were transferred to a solvent assuming insurer prior to their Termination Date. As discussed below, no such transfer occurred. Second, the Liquidator contends that if the policies did terminate, claims for breach of contract by each policyholder may be allowed as class (b) priority claims under Section 544 of the Receivership Act. This contention is belied by the facts of the proposed distribution. It is also contrary to the distribution scheme created under Pennsylvania law.

In an effort to avoid the Receivership Act and *Warrantech*, the Liquidator also disregards the fundamentals of the guaranty association system. That system replaced an outdated receivership model under which the best a receiver could do was distribute assets to policyholders based on reserves. That system did not give policyholders the benefit of their bargain, which was coverage in return for the payment of premium. The guaranty association system does. The fundamental bargain of the guaranty association system is that the associations provide ongoing subsidized coverage for a premium. In return, they get the assets that the policyholders would have received under the old system.

The Liquidator's attempt to engineer around the application of Sections 520 and 521 of the Receivership Act through the use of an unfunded captive insurance company must fail. Policyholders who have claims arising more than thirty days after the Companies' liquidation orders will have coverage through their guaranty associations. The guaranty associations will collectively provide approximately $2.6 billion in continued coverage for the Companies' policyholders. The modern statutory regime requires that the Companies' remaining assets be used to help fund that coverage.

ARGUMENT

I. THE LIQUIDATOR'S PROPOSED TREATMENT OF EXTRA-GA POLICY BENEFITS VIOLATES PENNSYLVANIA LAW.

The Liquidator proposes to distribute a substantial portion of the Companies' assets for the purpose of paying benefits under policies once guaranty association coverage is exhausted ("Extra-GA Benefits"). Of necessity, Extra-GA Benefits accrue based on events that occur after the Termination Date. The use of estate assets to pay Extra-GA Benefits accruing after the Termination Date directly contravenes Pennsylvania law.

Under Pennsylvania receivership law, policyholders are only entitled to receive assets from the estate if they have a claim. *See* 40 P.S. §§ 221.44 and 221.46 (providing for distribution of assets to holders of claims and the order of distribution to claims in liquidation). Extra-GA Benefits are not claims that may be asserted against the Companies' estate under Pennsylvania law.

A. Under Sections 520 and 521, Policyholders Cannot Recover Benefits That Accrue More Than 30 Days After Entry of the Liquidation Orders.

Section 520(d) of the Receivership Act provides that upon the issuance of a liquidation order for an insurance company, "the rights and liabilities of any such insurer and of its creditors, policyholders, shareholders, members and all other persons interested in its estate **shall become fixed** as of the date of filing of the petition for liquidation, except as provided in sections 521 and 539." 40 P.S. § 221.20(d) (emphasis added). Under Section 520(d), policies remain in force only for thirty days after the date the liquidation order is entered, and claims for benefits that accrue during that 30-day period are allowed. Claims accruing after the 30-day period are not.

The Pennsylvania Supreme Court confirmed the meaning of Sections 520 and 521 in *Warrantech*, a controlling decision that is directly on point. In that case, a policyholder (Warrantech) bought insurance from an insurer (Reliance) to cover claims made under Warrantech's warranty and service contracts for vehicles, homes, and consumer products. *Warrantech*, 96 A.3d at 348. Reliance was placed into liquidation by an order dated October 3, 2001. *Id.* at 349. As of that date, Reliance was obligated to provide insurance payments to Warrantech for all consumer claims made against Warrantech arising under service contracts that were in effect in 1999 or 2000, no matter when those future claims might be made. *Id.* The issue in the case was whether Warrantech would be entitled to make claims against Reliance in its liquidation proceeding for service contract claims that were made against Warrantech on dates after November 2, 2001—i.e., after expiration of the 30th day after the entry of the liquidation order. *Id.* at 349-50. The Pennsylvania Supreme Court squarely held that such claims were barred by Section 521 of the Receivership Act, and hence were properly determined by the liquidator to be valueless. *Id.* at 354-58.

The Court held that "[b]ut for Section [521] providing policyholders of insurers entering liquidation a thirty-day window to acquire replacement insurance, Section [521(d)] would cut off coverage to every policyholder whose insurer enters liquidation as of the date the petition is filed, without notice and an opportunity to seek replacement coverage." *Id.* at 356. The impact of Section 521 was simply to extend the cut-off thirty days after the liquidation order. This cut off of coverage applied to any claim that had not accrued under the terms of the policy prior to the Termination Date. *Id.* at 357. The Court rejected Warrantech's argument that its claims were triggered prior to the cut-off because the "trigger" occurred when Warrantech issued the underlying service contracts. *Id.* at 356-57. The Court held that "the triggering event is a claim made after a product breakdown under one of Warrantech's service contracts . . . . " *Id.* at 357.

In this case, Extra-GA Benefits – claims that would exceed the guaranty association limits (generally $300,000 per policyholder) – would necessarily accrue long after the Termination Date, which was March 31, 2017 (thirty days after the Companies' liquidation orders were entered). Those claims would be directly barred by the plain text of Sections 520 and 521 and the clear holding of the Pennsylvania Supreme Court's controlling decision in *Warrantech*.

As noted above, this Court previously reached the same conclusion in this case, relying on Pennsylvania precedent that preceded *Warrantech*. *See Penn Treaty Network Am. Ins. Co.*, 63 A.3d at 378, 445-46 (citing *Foster v. Colonial Assurance Co.*, 668 A.2d 174, 184 (Pa. Commw. Ct. 1995), *aff'd sub. nom.*, *Kaiser v. Colonial Assurance Co.*, 673 A.2d 922 (Pa. 1996)). This Court noted that the Pennsylvania Insurance Department has continued to take this same position in other insurance company estates, including, for example, the Legion Insurance Company liquidation. *Id.* at 378, 446 n.51. The Insurance Department again took this position in *Warrantech* and the Supreme Court agreed.

B. The Liquidator Cannot Evade Sections 520 and 521 by Forming an Unfunded Captive Insurance Company.

The Liquidator attempts to work around Pennsylvania law's disallowance of claims for Extra-GA Benefits by transferring a portion of the estate's assets to a captive insurer under the terms of a Partial Assumption Reinsurance Agreement, and having the captive pay the Extra-GA Benefits. Application ¶¶ 22-23.

The Liquidator argues that this device circumvents Sections 520 and 521 because it transfers policy obligations to a solvent assuming insurer. This would prevent termination of the policies, and under the Liquidator's theory, permit the transfer of assets from the estate to the Captive. *Id.* at ¶¶ 82-87. Alternatively, the Liquidator proposes to allow claims for breach of the policies by virtue of their termination as of the Termination Date. The Liquidator argues further that the resulting claim is entitled to priority as a class (b) claim under Section 544, and therefore a portion of the assets can be transferred to the Captive. *Id.* at ¶¶ 88-97. Neither of these theories supports the use of assets to pay the Extra-GA Benefits.

II. THE LIQUIDATOR DID NOT "TRANSFER" POLICY OBLIGATIONS AS CONTEMPLATED BY SECTIONS 521 AND 523.

The Liquidator asserts that a transfer of a portion of the Companies' obligations under the policies was made to a "solvent assuming insurer" (the Captive) within thirty days of the liquidation orders pursuant to Section 523 of the Receivership Act. Application at ¶ 84. This transfer, the Liquidator argues, avoids termination of the policies by operation of Sections 520 and 521. *Id.* at ¶ 86. But this supposed transfer fails to meet the express requirements of Section 523(8): first, it must be made to a "solvent assuming insurer"; second, it must be made within thirty days of the order of liquidation; and third, it must not prejudice the priorities under Section 544. 40 P.S. § 221.23(8). In addition, while Section 523(8) does not specifically require court approval, a transaction of this type, which is well outside of the ordinary course of receivership operation, requires court approval. Putting aside these fundamental deficiencies, the Liquidator also ignores the fact that there is no authority in Section 523(8) for the transfer of only a portion of an insolvent insurer's policies to a solvent assuming insurer. Finally, based on the documents submitted with the Application and Washington, D.C., law, it does not appear that the Liquidator's captive insurer has the authority to insure the long-term care policy obligations that were purportedly transferred to it.

A. The Purported "Transfer" Was Not Made to a Solvent Assuming Insurer Within Thirty Days of the Liquidation Orders.

The Liquidator's purported transfer fails to meet the first two, and most fundamental, requirements of Sections 521 and 523: a transfer (i) to a "solvent assuming insurer" and (ii) within thirty days of the order of liquidation. The documents attached to the Application demonstrate that the Liquidator's "transfer" cannot possibly meet both of these requirements.

The Partial Assumption Reinsurance Agreement between the Companies and Penn Treaty Plus, Inc. (the "Captive"), attached as Exhibit C to the Application (the "Reinsurance Agreement"), purports to be effective as of the day after the entry of the liquidation orders. Reinsurance Agreement at Section 2.01. However, the Reinsurance Agreement also states that "the Reinsurer's obligations are conditioned on the transfer to it of the XS Benefits Assets." *Id.* at Section 2.05. Those assets have not been transferred and cannot be transferred without an order of this Court. *See* 40 P.S. § 221.20(c) ("An order to liquidate the business of a domestic insurer…shall direct the liquidator forthwith to take possession of the assets of the insurer and to administer them under the orders of the court."). For purposes of Section 523(8), this leads to one of two inexorable conclusions: as of the Termination Date, either (1) the Captive had not assumed the Extra-GA Benefits liabilities and therefore was solvent, or (2) the Captive had assumed the Extra-GA Benefits liabilities and was therefore insolvent. In either case, there cannot have been a transfer to a "solvent assuming insurer" as of the Termination Date.

The Liquidator attempts to overcome these deficiencies by conditioning the Captive's obligations under the Reinsurance Agreement on the transfer of assets. Reinsurance Agreement at Section 2.05. But this circular provision will not save the "transfer" for purposes of Section 523(8). If the Captive's obligations are conditioned on the transfer of assets, which transfer still has not occurred, then the XS Benefits Liabilities (as that term is defined in the Reinsurance Agreement) were not transferred to or assumed by the Captive within thirty days of the liquidation orders. Indeed, under the terms of the Reinsurance Agreement, no assumption has occurred even today.[2] Alternatively, if there was an effective assumption of liabilities within thirty days, as asserted by the Liquidator (Application ¶ 22), then the Captive, which has no assets to back the XS Benefits Liabilities, was insolvent at the Termination Date (and remains so today).

In addition, the "transfer" of liabilities has not been approved by this Court. In fact, the Liquidator sought authorization from the Court and was denied. In the Liquidator's Proposed Form of Liquidation Order attached to each of the Verified Petitions to Convert Rehabilitation to Liquidation, the Liquidator requested authorization to make "arrangements with state guaranty associations **and/or another insurer** for the transfer and guarantee of policy obligations, including the continued payment of claims and coverage arising under [PTNA's/ANIC's] policies." Verified Petition to Convert Rehabilitation to Liquidation, 1 PEN 2009 (July 27, 2016) (emphasis added); Verified Petition to Convert Rehabilitation to Liquidation, 1 ANI 2009 (July 27, 2016) (emphasis added). The Court declined to

[2] The Reinsurance Agreement also provides for notification of the insureds that an assumption has occurred. Reinsurance Agreement at Section 3.01. The Liquidator has not provided any evidence that this has occurred, thereby further confirming that no assumption has occurred to date.

provide such authorization. Instead, the liquidation orders provide for the "transfer [of] policy obligations, including the continued payment of claims and continued coverage arising under [PTNA's/ANIC's] policies, **to state guaranty funds**." Order of Liquidation, 1 PEN 2009, at ¶ 10 (March 1, 2017) (emphasis added); Order of Liquidation, 1 ANI 2009, at ¶ 10 (March 1, 2017) (emphasis added). The Liquidator's attempt to complete this transaction without notice or the Court's approval highlights the fact that it is nothing more than a blatant attempt to paper over the circumvention of Sections 520 and 521, the Supreme Court's ruling in *Warrantech* and possibly this Court's prior Orders.

B. The Liquidator's Requested Distribution of Estate Assets to the Captive Violates the Priorities Mandated by the Receivership Act.

Even if the Liquidator's "transfer" can overcome these fundamental deficiencies (which it cannot), it still does not comply with Section 523(8). The transfer is designed to prejudice the interests of the guaranty associations as class (b) creditors by using assets to pay claims that otherwise would not exist. Section 523(8) permits a transfer to a solvent assuming insurer only if that transfer can be arranged "without prejudice to applicable priorities under Section 544." 40 P.S. § 221.23(8). Here, the entire purpose is to pay claims that would be disallowed under Sections 520 and 521 and the Supreme Court's decision in *Warrantech*. *See* Sections III. B. and C., *infra*. The legislature cannot have intended to have this narrow provision topple major pillars of the receivership scheme such as priority and allowance of claims.

The Liquidator's purported transfer violates both the letter and the intent of the statute. The transfer would take assets that should go to the guaranty associations, and use them to make payments of Extra-GA Benefits even though the policyholders would not have a claim against either the estate or the guaranty association for such benefits. This violates the requirement that any such transfer be accomplished without prejudice to the priorities under Section 544. It is also at odds with any reasonable interpretation of the statute. The Liquidator should not be permitted to disregard the statutory scheme in favor of the Liquidator's own free floating views of equity. *See* Op., *Pratter v. Reliance Ins. Co.*, No. 269 M.D. 2001, at 5 (Pa. Commw. Ct. Sep. 27, 2010) ("[W]here, as here, there is a pure question of law regarding the application of the Insurance Department Act to the policies, such deference is not appropriate.") (citing *Koken v. Legion Ins. Co.*, 831 A.2d 1196, 1232 (Pa. Commw. Ct. 2003), *aff'd*, 878 A.2d 51 (Pa. 2005)).

C. The Liquidator Cannot Transfer Only Part of a Policyholder Obligation.

There is no authority in Section 523(8) for the transfer of only a portion of an insolvent insurer's policies to a solvent assuming insurer. Section 523(8) was intended to permit the transfer of business to an operating insurer so that policies or contracts could be assumed and the policyholder relationship could resume its ordinary course. To be sure, this provision can be used to transfer certain blocks of policies of the insolvent insurer, but there is no authority under Section 523(8) to sever still undefined *portions* of individual policies (i.e., Extra-GA Benefits) and transfer them to a third party.[3] The Liquidator does not even identify the Extra-GA Benefits the Captive will pay. Instead, the Liquidator seeks authorization for the Captive to pay "an equitable portion" of the Extra-GA Benefits. Application ¶ 23. This is not the type of transfer contemplated by Section 523(8).

D. The Liquidator Has Not Demonstrated That The Captive Can Insure the Extra-GA Benefits Under Applicable Insurance Laws.

The Liquidator's purported transfer faces significant legal infirmities, as described above. But even assuming it clears the hurdles described in the previous sections, the Liquidator has failed to demonstrate that the Captive has the legal authority to insure long-term care insurance obligations under Washington, D.C. law, and the laws of the various states in which the policyholders reside.

Based on the Reinsurance Agreement and a review of public records in Washington, D.C., it appears that the Captive was formed under the laws of Washington, D.C., D.C. Code §§ 31-3931.01 *et seq*. Assuming that is correct, it would not have had authority to assume long-term care insurance obligations to

[3] Curiously, the Liquidator spends a significant amount of time in the Application taking the Health Insurers to task for proposing a "bifurcation" of the policies. Application ¶¶ 64-70. The Health Insurers have proposed no such bifurcation, but rather seek only to ensure compliance with the relevant provisions of the Receivership Act. The Liquidator, on the other hand, appears to have "bifurcated" the policies and attempted to transfer one portion – without authorization from this Court – to a captive insurance company with no assets.

individuals. D.C. Code § 31-3931.02(b) severely limits the types of obligations that a captive can undertake.[4] Essentially, coverage is limited to risks of entities that have some relationship with the captive sponsor. Individual policyholders are not even arguably within that class.

Even if the Captive's charter permitted it to provide coverage to an individual long-term care insured, it could not do so under the laws of the various states where those individuals reside unless it has a license or certificate of authority. For example, Florida law requires a certificate of authority to transact any insurance, and the failure to have a certificate of authority is a felony. Fla. Stat. §§ 624.401(1) and (4). The Application is devoid of any indication that the Liquidator has complied with this and other state laws necessary to assume coverage to individual long-term care insurance policyholders.

---

[4] That section provides in relevant part as follows:

> (b) Notwithstanding subsection (a) of this section, a captive insurer shall not…
>
> > (3) Insure any risks other than those of its parent and affiliated companies if it is a pure captive insurer;
> >
> > (4) Insure any risks other than those of the member organizations of its association and the affiliated companies of the member organizations if it is an association captive insurer;
> >
> > (5) Insure any risks other than those of the policies that are placed by or through the insurance agency or brokerage that owns the captive insurer if it is an agency captive insurer;
> >
> > (6) Insure any risks other than those of the policyholders or associations that have entered into agreements with the rental captive insurer for the insurance of those risks if it is a rental captive insurer, and shall use a form approved by the Commissioner for these agreements….

D.C. Code § 31-3931.02(b).

III. THE LIQUIDATOR LACKS AUTHORITY TO TRANSFER ESTATE ASSETS TO THE CAPTIVE BASED ON POLICYHOLDER BREACH OF CONTRACT CLAIMS.

The Liquidator asserts that the proposed asset transfer to the Captive for the purpose of paying Extra-GA Benefits is based on the premise that policyholders have claims for breach of their policies and that such claims are entitled to class (b) priority. Application ¶¶ 88 to 97.

This argument fails for two reasons. First, the Liquidator's plan does not actually provide for the allowance of policyholder claims for breach of the policy. Second, regardless of what the plan says, those claims are not entitled to class (b) priority.

A. The Liquidator's Proposal Does Not Allow Claims for Breach of Contract.

The Liquidator contends that she is allowing claims for breach of contract by each policyholder as a class (b) priority under Section 544 of the Receivership Act. That is clearly not what the proposal provides. If it were, then the distributions on those claims would be paid to the policyholders that have the claims. Instead, the Liquidator intends to pay the distributions to the Captive, so it can pay policyholders on Extra-GA Benefit claims. *Id.* at ¶¶ 22-25, 88, 93.

The Liquidator plans to seize the distributions of some policyholders and redistribute them to others, but does not cite any provision of Pennsylvania law that would permit such redistribution. A policyholder with a substantial breach of contract claim will not receive anything from the Captive if the policyholder never goes on claim. By the same token, a policyholder with only a small breach of contract claim may receive substantial benefits. The Court should not allow the Liquidator to distort the claims allowance process to achieve a result demonstrably at odds with the statute and controlling precedent.

B. Policyholder Claims for Breach of Contract are Not Entitled to Class (b) Priority.

Regardless, the allowed claims are not entitled to class (b) treatment under Section 544. The breach of contract claims posited by the Liquidator would seek damages for the termination of the policy rather than for benefits under the terms of the policy. As such, they would be general creditor claims entitled to class (e) priority rather than the class (b) priority accorded to "claims under policies for losses" as contemplated by the Receivership Act's priority scheme. *See Penn Treaty Network Am. Ins. Co.*, 63 A.3d at 446 ("Here, losses that occur more than 30 days after the liquidation would be covered by the replacement guaranty fund coverage; they would not be losses *under* a PTNA or ANIC policy.") (emphasis in original).

The breach of contract claims the Liquidator conceives are not "claims under policies for losses wherever incurred." 40 P.S. § 221.44. This provision refers to claims for which insurance is provided by the policy. The losses incurred under long-term care insurance policies are losses arising out of the insured's inability to perform certain acts of daily living. The insurer's failure to perform due to insolvency is not one of the "losses wherever incurred" referred to in the statute.

It is not the case, as the Liquidator suggests, that a claim by a policyholder is entitled to priority just because it is asserted by a policyholder. Application ¶ 91. For example, while Section 544 gives priority to "[a]ll claims under policies for losses wherever incurred, including third party claims," in the same sentence, it says "all claims against the insurer for liability for bodily injury or for injury to or destruction of tangible property which are not under policies, shall have the next priority." 40 P.S. § 221.44(b). Thus, claims not under policies, even if asserted by policyholders, are not class (b) claims. Section 544 assigns to class (e) "[c]laims under nonassessable policies for unearned premium or other premium refunds . . . . " 40 P.S. § 221.44(e). Claims for unearned premium and premium refunds clearly are claims by policyholders, and are not entitled to class (b) treatment. Thus, contrary to the Liquidator's position, a claim is not entitled to class (b) priority just because it is held by a policyholder.

The Liquidator argues that the Court in *Warrantech* established that policyholder claims for breach of contract were entitled to class (b) priority. Application ¶¶ 63-64. This entirely mischaracterizes the Supreme Court's decision in *Warrantech*. The question presented to the Supreme Court in that case was "[w]hether the Commonwealth Court misinterpreted contractual liability insurance policies and a section of the Pennsylvania Insurance statute…in overruling Warrantech's objections to Notices of Determination…, which allocated no value to consumer claims if they were made after November 2, 2001." Brief of Appellant Warrantech, *Warrantech Consumer Prods. Srvs., Inc. v. Reliance Ins. Co. in Liquidation*, No. 82 MAP 2013, 2013 WL 8351275, *4-5 (Pa. Dec. 10, 2013). The priority level of claims arising after the Termination Date was not presented to the Supreme Court, and the Court did not reach the issue since it held that such claims were properly assigned a zero value by the Commonwealth Court. *Warrantech*, 96 A.3d at 358.

The Commonwealth Court, in an earlier decision involving Warrantech, did address the priority level of Warrantech's post-Termination Date claims, but the issue was much different than the issue in this case. The issue before the Commonwealth Court was whether claims for loss under Reliance's policies should be treated as reinsurance, entitled to class (e) priority under Section 544, or claims under insurance policies, entitled to class (b) priority. Op., *Reliance Ins. Co.*, No. 269 M.D. 2001 at 4. In the proceeding before a referee assigned by the Commonwealth Court to hear and make recommendations on Warrantech's objections, the parties agreed that the issue was "whether there should be a distinction drawn between the priority of claims of those involving fortuitous risks as opposed to those contracts providing reimbursement for contractual liabilities voluntarily undertaken as part of [Warrantech's] business." *Id.* at 4-5. Neither the referee nor the Commonwealth Court considered whether a claim for breach of the policy (as distinguished from a claim for loss under the policy) was entitled to class (b) priority because the claimant (Warrantech) did not make the argument. *See Warrantech*, 96 A.3d at 359 (Saylor, J., concurring) ("Notwithstanding the above, in the present appeal Warrantech has taken an all-or-nothing approach, opting to argue that its insurance coverage as such remained in effect after the thirty-day window because the policies under which that coverage came into being had been cancelled well before the date of the liquidation order."). Thus, the issue of whether a breach of contract claim would be entitled to priority was never addressed by either the Commonwealth Court or the Supreme Court, and the Liquidator's reliance on *Warrentech* for the "priority" argument is wrong.

C. Guaranty Association Claims are Entitled to Class (b) Priority.

Guaranty associations' claims against the estate are entitled to class (b) priority under Section 544. *Ala. Ins. Guar. Ass'n v. Reliance Ins. Co.*, 100 A.3d 702, 725 (Pa. Commw. Ct. 2014) (Leavitt, J., dissenting) (citing *Gen. Reins. Corp. v. American Bankers Ins. Co. of Florida*, 996 A.2d 26, 34 (Pa. Commw. Ct. 2010)). While Section 544 does not specifically mention the guaranty associations, other provisions of the Receivership Act as well as provisions of the guaranty association statutes make it clear that the guaranty associations are to be paid immediately after expenses of administration, which under the Receivership Act places guaranty association claims in class (b).

Section 536 is titled "Liquidator's proposal to distribute assets," and provides in relevant part as follows:

> Within one hundred twenty days of a final determination that an insurer is insolvent or in such condition that its further transaction of business will be hazardous to its policyholders, or to its creditors, or the public by a court of competent jurisdiction of this Commonwealth, **<u>the liquidator shall make application</u>** to the Commonwealth Court for approval of a proposal **<u>to disburse assets out of such company's marshalled assets</u>**, from time to time as such assets become available, **<u>to any guaranty association</u>** in the Commonwealth or in any other states having substantially the same provision of law. The liquidator need not make application, as required above, in instances where it is reasonable to conclude that the assets of the insolvent insurer will not exceed the amounts necessary to pay the costs of liquidation and the **<u>payment of claims of creditors either secured or with a priority higher than policyholders</u>**. A guaranty association shall have the right to petition the Commonwealth Court to review an order of the liquidator concluding the assets will not exceed such costs.

40 P.S. § 221.36(a) (emphasis added). This statute makes clear that, other than paying the costs of liquidation and claims "with a priority higher than policyholders," the assets of the estate are to be sent to the guaranty associations that assume the insurance coverage of the liquidated company. The guaranty associations are entitled to those assets. Subsection (b) of Section 536 makes clear that this disbursement of assets is mandatory, as it provides that "[t]he proposal **shall** at least include provisions for . . . . (2) Disbursement of assets marshalled to date and subsequent disbursement of assets as they become available" and "shall"

also include "(3) Equitable allocation of disbursements to each of the associations **entitled** thereto." 40 P.S. § 221.36(b).[5] Thus, the Liquidator does not have discretion to disburse the assets of the estate in any way the Liquidator thinks is equitable. Rather, the law requires those assets be used to pay the costs of liquidation, the creditor claims that have a higher priority than policyholders (such as secured claims), and then to be disbursed to the guaranty associations for them to use in providing continued insurance coverage under their respective statutes. *See also* 40 P.S. § 221.36(b)(4) (requiring a plan for distributing assets to guaranty associations and requiring agreements from guaranty associations to return disbursements made pursuant to Section 536 to satisfy claims of a higher priority than that of policyholders).

The guaranty association statutes likewise confirm that the guaranty associations are entitled to receive the assets of the liquidated insurance company's estate to pay the costs of the continued coverage provided for in the guaranty association statutes. For example, the Pennsylvania guaranty association statute has the following provision:

---

[5] Section 536 provides that the liquidator's proposal should also include an agreement with guaranty associations to return any assets that they receive that should have been kept to pay liquidation costs or creditor claims of a priority higher than those of policyholders, or to pay other creditors who have a priority that is the same as policyholders "in the event that the association may have received a disbursement of assets in excess of that available to pay all creditors of the insolvent insurer in the same class of priority as policyholders." 40 P.S. § 221.36(b)(4). These provisions protect the claims of creditors, but in no way can be read to allow the Liquidator to avoid having to disburse those assets to the guaranty associations as required by the statute in order to pay Extra-GA Benefits.

> For the purpose of carrying out its obligations under this article, the association shall be deemed to be a creditor of the impaired or insolvent insurer to the extent of assets attributable to covered policies reduced by any amounts to which the association is entitled as subrogee pursuant to section 1706. Assets of the impaired or insolvent insurer attributable to covered policies **shall be used to continue all covered policies and pay all contractual obligations of the impaired or insolvent insurer as required by this article**. Assets attributable to covered policies, as used in this subsection, are that proportion of the assets which the reserves that should have been established for such policies bear to the reserves that should have been established for all policies of insurance written by the impaired or insolvent insurer.

40 P.S. § 991.1712(c) (emphasis added). This section tracks the language found in Section 14.C of the National Association of Insurance Commissioners Life and Health Insurance Guaranty Association Model Act (the "NAIC Model Act"), and has been adopted in various forms in all but one state. This section provides a clear statement that the guaranty associations are intended to have that portion of the estate assets that policyholders were intended to have prior to the creation of the guaranty association system.[6] *See* Section IV, *infra*.

A close reading of Section 1712 demonstrates why guaranty associations are entitled to class (b) priority under Section 544. The second sentence of Section 1712 indicates that the guaranty association is entitled to a share of the assets, which are to be used to continue covered policies. If the guaranty association were

[6] The Comments to the NAIC Model Act make the intent of Section 14.C even clearer: "Since this Act imposes the obligation upon the Association to continue coverage for policyholders of insolvent insurers, the assets of the insolvent insurer ought to be used, to the extent available, for the purpose of continuing such coverage. Subsections C and D are designed to accomplish this purpose." NAIC Model Act, Comments to Section 14.

relegated to a junior creditor priority level, it would not wind up with the assets of the insurer, and would likely have to give back the assets it received through the early access provisions in Section 536 discussed above. There would have been no point to the early access in the first place. This could not have been intended by the legislature.

The third sentence of Section 1712 provides that the guaranty association is entitled to a share of the assets that represents its proportional share of the entire reserve that should have been established for a covered policy. The allocation of assets according to the reserves is the methodology that was used by the courts under prior law to deal with an insolvent disability insurer's estate. *See, e.g.*, *Caminetti v. Pac. Mut. Life Ins. Co.*, 142 P.2d 741, 749 (Cal. 1943); *Comm'r of Ins. v. Mass. Accident Ins. Co.*, 50 N.E.2d 801, 808-09 (Mass. 1943); *see also* Section IV, *infra*. Under the guaranty association statute, the reserve assets are provided to the guaranty association, rather than the policyholder, because the guaranty association is providing ongoing coverage.

Finally, the first sentence of Section 1712 provides two important features that clinch the interpretation. The sentence states that the guaranty associations "shall be deemed a creditor . . . to the extent of assets attributable to covered policies." 40 P.S. § 991.1712(c). This demonstrates that the drafters of the statute expected that the guaranty association's access to the estate assets would be through a senior position in the priority scheme. Without that senior position, it would not receive a significant share of the assets and would have to give back assets received under early access provisions to pay other creditors. It would make very little sense for the guaranty association to receive assets, only to have to give them back to other creditors. It would substantially complicate accounting and make assessments to guaranty association member insurers nearly impossible to calculate with any certainty.

The other important feature of the first sentence of Section 1712 is that it (and its equivalent in the other states) gives a claim to the guaranty association equal to "assets attributable to covered policies **reduced by any amounts to which the association is entitled to as subrogree pursuant to section 1706**." 40 P.S. § 991.1712(c) (emphasis added). This provision recognizes that the association is entitled to a claim that goes beyond its entitlement to a subrogation claim. (In fact, it suggests that the subrogation piece of the claim would be small compared to the reserve claim, since it is subtracted from the claim based on reserves.) The fact that the reserve claim and the subrogation claim are treated in the same sentence is important. It suggests that the drafters intended them to be treated the same. Even the Liquidator concedes that the subrogation claim is entitled to class (b) priority to the extent that it arose prior to the Termination

Date.[7] Application ¶ 75. Treating the reserve portion of the guaranty association's claim as a general creditor (class (e)) claim would defeat the overall purpose of the section, which is to ensure that the associations have access to the estate's assets to continue coverage for policyholders. The only way to accomplish this under the Receivership Act is to recognize that the guaranty association claim has the same priority level as the pre-Termination Date subrogation claim, which is entitled to class (b) priority.

Pennsylvania's well developed rules of statutory construction also require this interpretation. The goal of statutory interpretation is always to determine legislative intent. 1 Pa.C.S. § 1921. Where possible, statutes should be read in *pari materia.* 1 Pa.C.S. § 1921(b). As discussed above, the guaranty association statutes can (and should) be read together with the Receivership Act to conclude that the guaranty association's reserve claim is entitled to class (b) priority. However, if the Court determines that the provisions of Section 1712 conflict with the provisions of Section 544(b) of the Receivership Act, then the Pennsylvania rules of statutory construction dictate that the provisions of Section 1712 should prevail. 1 Pa.C.S. § 1933 provides:

> Whenever a general provision in a statute shall be in conflict with a special provision in the same or another statute, the two shall be

[7] In any liquidation, there will be a "backlog" of claims that includes both those claims that were incurred but not reported prior to the Termination Date, and those that were incurred and reported prior to the Termination Date but not yet paid.

> construed, if possible, so that effect may be given to both. If the conflict between the two provisions is irreconcilable, the special provisions shall prevail and shall be construed as an exception to the general provision, unless the general provision shall be enacted later and it shall be the manifest intention of the General Assembly that such general provision shall prevail.

1 Pa.C.S. § 1933. Section 544 of the Receivership Act deals generally with claims against the receivership estate. Section 1712 deals specifically with the rights of the life and health insurance guaranty association. Because Section 1712 is the more specific provision, it should prevail and be construed as an exception to Section 544(b).

Section 1712 is also the later-enacted legislation. The current version of Section 544(b) was enacted in 1977 (Act 1977-280), whereas the life and health guaranty association act was created in 1978 (Act 1978-280) and repealed and replaced in 1992. (Act No. 1992-178) Each of these laws has subsequent amendments, but those amendments do not deal with the subjects at issue here.[8]

The subsequent enactment of the guaranty association statute also provides a separate basis for its primacy here. 1 Pa.C.S. § 1933 provides that "[w]henever the provisions of two or more statutes enacted finally by different General Assemblies

---

[8] In 1996, the priority statute was amended to elevate the priority of policyholder claims over claims of employees and the federal government, but no change was made to the text of what is now Section 544(b). This reordering was directly in response to the U.S. Supreme Court's decision in *U.S. Dep't Treasury v. Fabe,* 508 U.S. 491 (1993). In 2007, the legislature modified the Life and Health Guaranty Association statute in connection with the formation of the Long Term Care Partnership. Among other things, the coverage and limits section of the act were modified, but no substantive change to Section 1712 was made. (Act No. 2007-40).

are irreconcilable, the statute latest in date of final enactment shall prevail." 1 Pa.C.S. § 1933. Under this section, the priority provisions of the guaranty association statute would provide the relevant rule for distribution of the estate.

The Liquidator maintains that the guaranty associations could only have class (b) priority claims if the policyholders have priority claims. Application ¶¶ 66, 73-74. This position is based on two faulty propositions. First, the Liquidator posits that the guaranty associations have assumed the policies and are paying claims under them. *Id.* at ¶¶ 18, 24. Second, the Liquidator posits that the rights of the guaranty associations are limited to the rights of the policyholders.

The guaranty associations' obligations do not depend on the status of the policies. They are statutory obligations and exist independent of the policies. *See, e.g.*, 40 P.S. § 991.1706(c) (providing that the guaranty association *shall* guarantee, assume or reinsure the policies or contracts of an insolvent insurer); *see also*, 40 P.S. § 991.1706(d)(2) (providing that the guaranty association may reissue terminated coverage or issue an alternative policy in place thereof). As discussed above, the guaranty associations also have rights against the estate that are independent of the policies. The Liquidator correctly observes that the guaranty associations subrogate to the rights of policyholders, but these are not the only rights that the guaranty associations are provided. The Receivership Act expressly provides for the assets of the liquidated insurance company's estate to be used by the guaranty associations to pay for the continued coverage the guaranty associations are required to provide under their respective statutes. *See* 40 P.S. § 221.36; *see also, e.g.*, 40 P.S. § 991.1712 (of which there are corresponding provisions under each state's guaranty association statute).

These statutes demonstrate the interlocking nature of the statutory framework, and confirm that the system functions very simply and sensibly: policyholders who have claims arising more than thirty days after the liquidation must look to their guaranty associations for payment of their claims, not the liquidated company. Those policyholders have continued coverage solely from the guaranty associations, and subject to the guaranty association limits; the guaranty associations use the assets of the estate to pay those continuing policyholder claims, and then assess their member companies to make up the difference between their obligations and the estate assets.

D. The Termination of the Companies' Policies Pursuant to Sections 520 and 521 Does Not Affect the Obligations of the Guaranty Associations.

The Liquidator argues that if the policies terminate as a result of the Companies' liquidation orders, then the guaranty associations would have no obligation to pay policyholders. Application ¶ 74. According to the Liquidator, this result follows because the guaranty associations obligations are "wholly derivative" of the Companies'. *Id.* This argument is misplaced. The guaranty associations' obligations are *statutory* not contractual. The Pennsylvania Life and Health Insurance Guaranty Association's statute, for example, provides that the guaranty association shall "guarantee, assume or reinsure or cause to be guaranteed assumed or reinsured the policies or contracts of the insolvent insurer[.]" 40 P.S. § 991.1706(c)(1). A "guaranty" clearly does not require that the policy continue in effect. The purpose of the guaranty is that the guarantor continues performance even after the principal has been excused by insolvency. *See, e.g.*, *Janes v. Scott*, 59 Pa. 178, 182 (1869) ("[W]hen the principal debtor is insolvent at the maturity of the debt, no such proceeding (as judgment and execution), is necessary as a foundation to an action on the guaranty. Nor is it necessary in such a case to show even a demand on the principal debtor and notice of non-payment given to the guarantor.") (Citations and quotation marks omitted). The obligation of the guarantor is measured by the contract in effect *prior* to the insolvency, regardless of what happens to the contract as a result of the insolvency. If insolvency could discharge the guarantor's obligation in the same way it discharges the principal's, guaranties would be worthless.

While the obligations of the guaranty associations are measured by the contracts as they existed prior to the insolvency, those obligations do not depend on the contracts. The source of a guaranty association's obligations is the guaranty association's statute, not a transfer effectuated by the Liquidator. This result is further illustrated by the provision of the guaranty association statutes that allows a guaranty association to "reissue the terminated coverage or to issue an alternative policy" to satisfy its coverage obligations. 40 P.S. § 991.1706(d)(2)(i). Indeed, the California Life and Health Insurance Guarantee Association, which has the largest coverage obligation of any guaranty association in this case (over $400 million), chose to issue alternative policies to satisfy its contractual obligations. Neither the Health Insurers nor any other party have suggested that the association has been relieved of its coverage obligations as a result of the termination of the Companies' policies.

Following these same lines, the Liquidator also rehashes the tired argument that the position advanced by the Health Insurers (and the Supreme Court in *Warrantech*) could mean the "insolvent insurer will suddenly be solvent again, and the owners, shareholders, and other creditors will see a windfall at the expense of policyholders." Application ¶ 75. This Court has already explained why that result could never happen under the Receivership Act: "there can be no windfall to the stockholders here because in a liquidation the Companies' policyholders would be transferred to guaranty funds after their policies terminated. By statute, those guaranty funds then become creditors against the estate of the Companies." *Penn Treaty Network Am. Ins. Co.*, 63 A.3d at 445. In this case, the guaranty associations will pay out benefits that exceed the assets of the Companies by approximately $2 billion. Thus, there will be no "windfall" for equity. Even in a hypothetical case in which an impaired or insolvent insurer had significant assets, the result advanced by the Liquidator would not occur. If the insurer had assets to repay the guaranty associations in full, with excess available to pay lower priority creditors, it would not make sense to invoke the guaranty associations at all. Instead, there would be a rehabilitation to restructure the policies, providing more value to policyholders than they would receive in a liquidation and preserving the going concern value of the company.

IV. THE GUARANTY ASSOCIATION SYSTEM DISPLACED THE PRIOR RECEIVERSHIP PRACTICE.

The Liquidator cites a group of cases for the proposition that policyholders have a right to receive a portion of the estate assets based on the share of the reserves attributable to their policies. Application ¶ 95. All of those cases save for two pre-date both modern insurer insolvency statutory regimes and the guaranty association system. *In re Exec. Life. Ins. Co.*, 38 Cal. Rptr. 2d 453 (Cal. App. 1995), was a rehabilitation case and is therefore not relevant to the issues concerning policy termination in liquidation. The only other case cited by the Liquidator that was decided after the enactment of insurer insolvency statutes and the guaranty association system, *In re Liquidation of Integrity Ins. Co.*, 685 A.2d 1286 (N.J. 1996), dealt with a breach of contract claim resulting from the termination of a surety bond. As this Court noted in discussing the *Integrity* case, surety bonds are expressly excluded from coverage under New Jersey's guaranty association act. *See Penn Treaty Network Am. Ins. Co.*, 63 A.3d at 443-44. (citing N.J. Stat. §§ 17:30A-2(b) and 17:22-6.71). Thus, the *Integrity* Court, much like the courts in the cases dating from the 1800s and 1940s, had to fashion some remedy for the surety bondholders otherwise they would have been left with no claim.[9] Here, all policyholders have coverage provided by a guaranty association.

As this Court has observed, reliance on precedent pre-dating modern insurer insolvency statutes and the enactment of the guaranty association system is problematic when addressing issues under the Receivership Act.

> There are several problems with the Rehabilitator's reliance on this above-reviewed line of precedent. Except for *Integrity Insurance*, they are ancient. They pre-date any insurer insolvency statute, or at least the modern version developed by the NAIC Model Act, which Pennsylvania has adopted. All concerned policyholders without guaranty fund protection, either because they were exempt from guaranty funds, as in the case of surety bond holders, or because guaranty funds had not yet been invented. The precedent relied upon by the Rehabilitator establishes that where there is no guaranty fund protection, it is inequitable to limit a policyholder's claim against an insolvent insurer's estate to a refund of premium.

Id at 445. This Court's reluctance to rely on cases pre-dating the insurer insolvency statutes and guaranty association system cases is well-founded. Those cases dealt with a very different set of circumstances than those facing modern

[9] It is worth noting that while the Liquidator endorses the *Integrity* case, the court in that case valued the claims based on the cost of replacement coverage. As discussed in Section V, *infra*, with little support the Liquidator proposes to value Extra-GA Benefits (to the extent they exist and should not be valued as zero) based on the Companies' reserves.

liquidators and policyholders. Prior to the enactment of the guaranty association statutes, the liquidator had a mass of assets to distribute with few good alternatives. One alternative would be to keep paying benefits at some percentage for an indefinite period until all policyholders could no longer have claims. This would leave estates open indefinitely and at great expense. It ran contrary to the fundamental receivership principle that receivership terminates contracts.[10] It also provided coverage to policyholders that were no longer paying premium. Receivers uniformly rejected this alternative and instead distributed estates based on reserves. This alternative also had shortcomings. It resulted in policyholders getting cash rather than coverage; policyholders that would never have losses received payments; and policyholders that had substantial losses received too little in payments. But it allowed estates to close and policyholders to receive some recovery.

The guaranty association system solved this problem by providing coverage to policyholders on an ongoing basis. Policyholders paid premium and received full payment of their claims as and when they occurred (subject to guaranty

[10] Cases holding that policies terminated upon the entry of a liquidation order were legion. *State v. Surety Corp. of Am.*, 162 A. 852, 856 (Del. 1932); *Boston & A.R. Co. v. Mercantile Tr. & Deposit Co. of Balt.*, 34 A. 778, 784 (Md. 1896); *Doane v. Millville Mut. Marine & Fire Ins. Co.*, 11 A. 739, 743 (N.J. Ch. 1887); *Commw. v. Mass. Mut. Fire Ins. Co.*, 119 Mass. 45, 51 (1875); *In re Commercial Ins. Co.*, 36 A. 930, 930–31 (R.I. 1897); and *Reliance Lumber Co. v. Brown*, 30 N.E. 625, 627 (Ind. App. 1892). The Pennsylvania Supreme Court's decision is *Warrantech* was just one more in a long parade.

association maximums specified by statute). This system was paid for by the taxpayers and insureds of the various states through a system of assessments of solvent member insurers and premium tax offsets and policy surcharges. In order to ensure that the burden on the taxpayers and other policyholders was kept to a minimum, the associations receive early access to the assets of the estate. They also receive assets of the estate based on the reserves carried by the company – much as the policyholders had under the old system.

The Liquidator maintains that even though the guaranty association system provides ongoing coverage to policyholders in return for ongoing premium, the policyholders still get a share of the assets based on reserves, as if the pre-guaranty association system still existed. This makes no sense. It maintains the feature of the pre-guaranty association system that was the most problematic – allocating assets in a way that does not reflect policyholders' actual losses. And it does so at the expense of the taxpayers and member insurer policyholders that are paying the massive cost of the new system.

Perhaps the most convincing indictment of this position is that the Liquidator does not intend to implement it. In fact, the Liquidator's plan is to fund the newly formed (and still unfunded) Captive to pay some portion of policyholder benefits as policyholders' claims occur. The Liquidator's contention that policyholders have a priority claim for damages based on reserves is not for the purpose of paying them their share of the reserves, but only for the purpose of funding the Captive. The Liquidator is actually using these purported claims (without policyholder consent) to fund a mini-guaranty association that collects no premium, provides uncertain benefits, and imposes further burden on the taxpayers and policyholders of solvent companies. When legislatures around the country enacted the statutes that created the guaranty association system, they could not have intended this result.

The Liquidator advances the argument that her view of the system is the only way that a policyholder that had no guaranty association coverage could recover anything in an insurance company failure. But this fails to recognize that the guaranty associations provide comprehensive coverage and go to great lengths to provide coverage even in doubtful cases. This case is a perfect example. In this case, there were approximately 400-500 policyholders who resided in New York at the time the liquidation orders were entered. Neither PTNA nor ANIC was ever licensed in New York or held a certificate of authority in New York. The Pennsylvania Life and Health Insurance Guaranty Association Act provides that it will cover the claims of non-Pennsylvania residents (under so-called "orphan policy" provisions) if all of the following conditions are met: (A) the insurer that issued the policy is domiciled in Pennsylvania; (B) the insurer never held a license or certificate of authority in the states in which such persons reside; (C) these states have associations similar to the association created by this article; and (D) these persons are not eligible for coverage by those associations. 40 P.S. § 991.1703(a)(2)(ii). New York does not have a guaranty association that covers long-term care insurance for its residents. Thus, the requirement under Section 1703(a)(2)(ii)(C) that the state has an association "similar to the association created by this article" was not met, and therefore coverage for New York residents should have been excluded. Nevertheless, the Pennsylvania guaranty association, at the urging of the Liquidator, voted to cover the New York residents.

It is theoretically possible that there could be policyholders who would not receive coverage from any guaranty association. In practice, it is a black swan event, and the Health Insurers are prepared to introduce evidence to that effect.[11] A theoretical possibility should not dictate the Court's construction of the guaranty association and receivership statutes and system. In practice, as this case demonstrates with respect to the New York policyholders, the guaranty associations find a way to provide coverage. If they do not, a receiver should be

[11] In the property and casualty context, there are many examples of non-resident insureds being denied coverage by the local guaranty association. *See e.g.*, *Owens Corning v. Miss. Ins. Guar. Ass'n*, 947 So.2d 944, 948 (Miss. 2007) (upholding guaranty association's denial of non-resident insured's claim despite insured's effort to use the underlying tort claimant's residence to satisfy residency requirement); *Flipps Nine, Inc. v. Mo. Prop. & Cas. Ins. Guar. Ass'n*, 941 S.W.2d 564, 568 (Mo. Ct. App. 1997) (upholding guaranty association's denial of non-resident insureds' claim despite insureds' use of resident purchasing groups to acquire P&C policies). However, the Health Insurers' research did not yield a single case in which an individual policyholder was left uncovered by a life and health insurance guaranty association as a result of his or her residency.

able find a way on an exceptional basis to accommodate a small number of policyholders to achieve a fair result.

V. THE VALUATION OF CLAIMS FOR EXTRA-GA BENEFITS, IF THEY EXIST, SHOULD BE THE SUBJECT OF A SEPARATE APPLICATION.

The Liquidator requests an order authorizing the valuation and payment of Extra-GA Benefits based on the Companies' gross premium reserves. Application ¶¶ 98-105. As authority for this request, the Liquidator cites the NAIC Receiver's Handbook for the proposition that liquidators may rely on the records of the insolvent insurer for valuing claims. *Id.* at ¶ 100. The Liquidator also cites the NAIC Handbook for the proposition that liquidators should rely on liquidation cases from the early 1800s through the 1940s in valuing "immature" claims. *Id.* at ¶ 103. These cases all pre-date the implementation of modern insurer insolvency statutes. As discussed in Section IV, *supra*, reliance on this precedent is problematic. *Penn Treaty Network Am. Ins. Co.*, 63 A.3d at 445.

If the Court determines that policyholders can maintain claims for Extra-GA Benefits against the estate – and such claims should not be valued at zero – there should be additional briefing and an evidentiary hearing on the method of valuation of such claims. The appropriate valuation methodology may differ depending on the basis for paying Extra-GA Benefits (i.e., as a continuation of the policy or as a breach of contract claim). For example, under a breach of contract theory, should the damages factor in replacement cost? In short, other than relying on cases that pre-date modern insurer insolvency practice, the Liquidator has not demonstrated why gross premium reserve is the proper methodology. Other valuations may be more appropriate. The Health Insurers therefore respectfully request that the Court defer this determination until after adequate briefing and an evidentiary hearing.

CONCLUSION

For the reasons set forth above, the Health Insurers respectfully request that the Court enter an order denying the Liquidator's Application.

Respectfully submitted,

MORGAN, LEWIS & BOCKIUS LLP

Dated: April 22, 2019

By:______________________________

Harold S. Horwich *(admitted PHV)*
Benjamin J. Cordiano (*admitted PHV)*
MORGAN, LEWIS & BOCKIUS LLP
One State Street
Hartford, Connecticut 06103-3178
Telephone: 860.240.2700
Facsimile: 860.240.2800

John P. Lavelle, Jr. (PA I.D. 54279)
MORGAN, LEWIS & BOCKIUS LLP
1701 Market Street
Philadelphia, PA 19103

Telephone: 215.963.4824
Facsimile: 215.963.5001

Attorneys for Aetna Life Insurance Company; Anthem, Inc.; Cigna Corporation; HM Life Insurance Company; Horizon Healthcare Services, Inc. d/b/a Horizon Blue Cross Blue Shield of New Jersey; QCC Insurance Company; United Concordia Life and Health Insurance Company; United Concordia Insurance Company; and UnitedHealthcare Insurance Company

CERTIFICATE OF CONFIDENTIALITY COMPLIANCE

I certify that this filing complies with the provisions of the *Public Access Policy of the Unified Judicial System of Pennsylvania: Case Records of the Appellate and Trial Courts* that require filing confidential information and documents differently that non-confidential information and documents.

Dated: April 22, 2019

s/ John P. Lavelle, Jr.
John P. Lavelle, Jr.

CERTIFICATE OF SERVICE

I certify that on April 22, 2019, I caused courtesy copies of the foregoing Response of the Intervenor Health Insurers to the Liquidator's Application for Declaration Regarding Policyholder Claims for Non-GA Policy Benefits to be served via E-mail on the counsel listed below.

Counsel for Jessica K. Altman, Insurance Commissioner of Pennsylvania, in her capacity as Statutory Liquidator of PTNA and ANIC

James R. Potts
Michael J. Broadbent
COZEN O'CONNOR
One Liberty Place
1650 Market Street, Suite 2800
Philadelphia, PA 19103

Leslie Miller Greenspan
Carl E. Singley
Kevin L. Golden
TUCKER LAW GROUP, LLC
Ten Penn Center
1801 Market Street, Suite 2500
Philadelphia, PA 19103

Counsel for NOLHGA

Caryn M. Glawe
Jane D. Wilson
FAEGRE BAKER DANIELS
300 N. Meridian Street, Suite 2700
Indianapolis, IN 46204

Mark D. Bradshaw
STEVENS & LEE
17 North Second Street, 16th Floor
Harrisburg, PA 17101

Dated: April 22, 2019

s/ John P. Lavelle, Jr.
John P. Lavelle, Jr.