

CIGA 2013 Liquidation Update

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Recent liquidation activity


- ▶ Lumbermens Mutual Companies
- ▶ Ullico Casualty Company
- ▶ Each involves peculiar issues
 - ▶ Deductibles from \$250,000 to \$1 million
 - ▶ Employer funding and administration agreements
 - ▶ Professional Employer Organizations (PEOs)

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Lumbermens Mutual

- ▶ Lumbermens Mutual Companies
 - ▶ Lumbermens Mutual Cas. Co.
 - ▶ American Motorists Ins. Co.
 - ▶ American Manufacturers Mutual Ins. Co.
- ▶ Illinois Insurer
- ▶ Illinois Liquidation
- ▶ 3 separate liquidation orders
 - ▶ Entered 5/8/13
 - ▶ Effective 5/10/13

Orders in Supplemental Materials

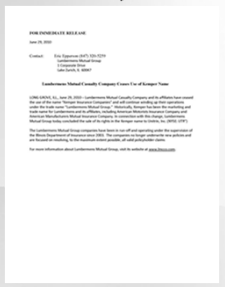


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Lumbermens Mutual

Memo in Supplemental Materials

- ▶ Lumbermens went under Kemper name until 2010
 - ▶ Kemper and Lumbermens are the same insurer



Lumbermens' mergers

Certificates of Merger in Supplemental Materials

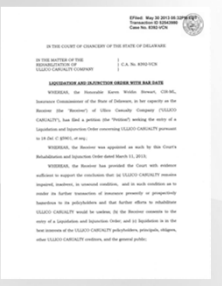
- ▶ Transfer of all rights and liabilities
- ▶ Approved mergers
 - ▶ Eagle Pacific Ins. Co.
 - ▶ Into American Protection 12/31/03
 - ▶ American Protection Ins. Co.
 - ▶ Into American Motorists 12/31/04
 - ▶ Specialty National Ins. Co.
 - ▶ Into American Motorists 12/31/04
 - ▶ Pacific Eagle Ins. Co.
 - ▶ Into American Motorists 8/31/04



ULLICO

Order in Supplemental Materials

- ▶ Ullico Casualty Co.
- ▶ Delaware Insurer
- ▶ Delaware Liquidation
- ▶ Order of Liquidation
 - ▶ Entered and effective 5/30/13



What happens at liquidation?

- ▶ Receiver/liquidator appointed
- ▶ Existing policies ordered canceled
- ▶ CIGA's statutory obligations triggered
- ▶ 45-day tolling period triggered (Ins. Code §1063.15)

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Appointment of Liquidator

- ▶ "Insolvency"
 - ▶ Inability of the insurer to meet its financial obligations when they are due (Ins. C. § 985(a)(2))
- ▶ "Liquidation"
 - ▶ Commissioner concludes it is futile to continue as conservator to rehabilitate insurer
 - ▶ May request order to liquidate and wind up business of insurer (Ins. C. § 1016)
- ▶ Order appointing liquidator issued by court of competent jurisdiction -- examples
 - ▶ Delaware - Court of Chancery (ULLICO)
 - ▶ Illinois - Circuit Court of Cook County (Lumbermens)
 - ▶ California - Superior Court (CA liquidations)

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Policy cancellation

- ▶ Existing policies canceled
 - ▶ Upon expiration date if within 30 days
 - ▶ 30 days after order of liquidation if policy period longer
- ▶ Gives employers time to obtain new insurance
- ▶ Ins. Code §1063.1(c)(1)(D)
 - ▶ To meet the threshold definition of "covered claims" the obligations must have been "incurred prior to the date coverage under the policy terminated and prior to, on, or within 30 days after the date the liquidator was appointed."
- ▶ You may have claims with post-liquidation DOIs

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CIGA's statutory duties

- ▶ Ins. Code § 1063.2
 - ▶ Pay and discharge "covered claims"
 - ▶ Directly
 - ▶ Through servicing facility (TPA)
 - ▶ Reinsurance contract/assumption of liability through member insurer
 - ▶ Contract with liquidator
 - ▶ "Covered claims"
 - ▶ Must meet definition under Ins. Code §1063.1(c)(1) – obligations of insolvent insurer, imposed by law, within the coverage of the insolvent insurer's policy etc.
 - ▶ Must not be excluded from "covered claims" by any other provision commencing with Ins. Code §1063.1(c)(3).

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45-day tolling period

- ▶ "In any workers' compensation matter the association shall have the same period of time within which to act or to exercise a right as is accorded to the insurer by the Labor Code, and those time periods shall be tolled against the association until 45 days after the appointment of a domiciliary or receiver." (Ins. C. § 1063.15)
- ▶ Applies to all periods of time to act or exercise right including
 - ▶ Benefit payment obligations
 - ▶ Petitions for reconsideration/answers
 - ▶ Petitions for writ/answers
 - ▶ Discovery demands, etc.
- ▶ Tolling periods - from appointment of liquidator
 - ▶ Lumbermens 5/10/13 to Monday 6/24/13
 - ▶ Ullico 5/30/13 to Sunday 7/14/13

Tolling period has passed but still relevant to claims of unreasonable delay.

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45-day tolling period cont'd

- ▶ No time frame: Act required on specific date within tolling period – e.g. scheduled benefit payment
 - ▶ Must be done on or before 45th day
- ▶ Time frame commences before appointment of liquidator
 - ▶ Time starts to run – stops during tolling period – balance runs after tolling stops
- ▶ Time frame commences during tolling period
 - ▶ Time starts to run following end of tolling period
- ▶ Pending orders – no effect
- ▶ Time to act or start counting days – on the 45th day
 - ▶ See CIGA litigation memorandum re: Ins. Code § 1063.15

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Insolvent's C&Rs, Stipulated Awards and F&As

- ▶ CIGA is not bound by
 - ▶ Insolvent insurer's C&R agreements to pay noncovered claims
 - ▶ Order or F&A against insolvent to pay noncovered claim
- ▶ However, CIGA follows a simple rule...
 - ▶ CIGA never places the IW in the middle of the dispute

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Insolvent's C&Rs, Stipulated Awards and F&As cont'd

- ▶ Unpaid liabilities subject to CIGA defenses
- ▶ Some examples:
 - ▶ C&R, Stips or F&A requiring insolvent insurer to pay insurer
 - ▶ C&R, Stips or F&A requiring insolvent insurer to pay liens subject to CIGA's statutory defenses
 - ▶ EDD liens
 - ▶ Liens for which "other insurance" exists
 - ▶ Liens involving unqualified assignments
 - ▶ Etc.
 - ▶ J&S award imposing liability on insolvent insurer and a solvent insurer or PST employer

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Peculiar issues

ULLICO – Policy termination

ULLICO – Cut-through agreements

ULLICO & Lumbermens – Deductible policies and "covered claims"

Lumbermens – Employer funding and administration on deductible policies

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ULLICO
**Policy Termination &
Cut-Through Agreements**

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ULLICO Policy Termination

- ▶ "Covered claims" include obligations of insolvent insurer which are, among other requirements -
 - ▶ Incurred prior to the date coverage under the policy terminated and prior to, on, or within 30 days after the date the liquidator was appointed. (Ins. Code § 1063.1(c)(1)(D))
 - ▶ 30th day was 6/29/13!
- ▶ Liquidation order effective 5/30/13
- ▶ Liquidation order terminated existing policies as of 6/30/13
- ▶ One day beyond Ins. Code § 1063.1(c)(1)(D)
- ▶ Handling DOI's on 6/30/13
- ▶ If employer did not secure new WC policy, court may impose liability on CIGA
- ▶ Did employer obtain new policy covering injuries on 6/30/13?

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ULLICO "cut-through" agreements

- ▶ ULLICO liquidation order mentions unspecified lawful and approved "cut-through" agreements and endorsement under paragraph 7
- ▶ "Cut-through" (aka "assumption endorsement")
 - ▶ Reinsurance contract or endorsement
 - ▶ Providing for reinsurer to pay loss covered by reinsurance contract
 - ▶ Directly to the claimant
- ▶ If reinsurer solvent, "other insurance"
- ▶ No specifics yet on the "cut-through" agreements

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ULLICO and
Lumbermens
Deductible Policies

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Deductible policy vs. self-insurance

- ▶ Self-insured employer must obtain a certificate of consent to self-insure (Lab. C. §3700)
 - ▶ Furnish proof of ability to self-insure and pay all compensation that may become due (Lab. C. §3700(b))
 - ▶ Submit to administrative audit (Lab. C. § 129)
 - ▶ Make substantial deposits of security (Lab. C. §3701(b))
 - ▶ Participate in the Self-Insurer's Security Fund (SISF) (Lab. C. § 3742(a))
- ▶ An insured employer without a certificate is not self-insured
- ▶ A "deductible" does not make the employer self-insured

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Deductible policy vs. specific excess policy

- ▶ "Specific excess" policies are issued to self-insured employers
 - ▶ Reimburse self-insured employers for benefits paid in excess of a "retention"
 - ▶ Generally do not require the insurer to pay benefits directly to the claimant
- ▶ Specific excess policies are not "deductible policies"

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Why we need to understand deductible policies

- ▶ We need to understand them because:
 - ▶ Many Lumbermens and Ullico deductible policies
 - ▶ Impact on insurer's liability not well-understood
 - ▶ Results in erroneous arguments by the other side
 - ▶ CIGA has heard them before – Legion & Reliance
 - ▶ CIGA's attorneys must guide WCJs and Arbitrators
 - ▶ Litigation over employer administration under Lumbermens deductible policies

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Erroneous deductible arguments

- ▶ Some of the erroneous arguments from other side:
 - ▶ CIGA can't raise its "other insurance" defense within deductible of insolvent's policy because the employer is liable
 - ▶ The insured employer under the insolvent's policy is "other insurance" within the deductible – solvent insurer claims no obligation to pay
 - ▶ "Other insurance" has no obligation to administer within the deductible of the insolvent's deductible policy because deductible is the employer's liability
 - ▶ "Other insurance" has no obligation to reimburse CIGA for benefits paid within the deductible because the employer owes the deductible

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Deductible Policies

- ▶ What is a deductible policy?
 - ▶ Employer agrees to assume some portion of the loss covered by the policy
- ▶ Greater deductible = smaller premium
- ▶ Normally see deductibles from \$250K up to \$1 million on WC policies

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All WC policies – insurer's dollar one liability

- ▶ All WC policies –
 - ▶ Insurer liable from dollar-one
- ▶ CA law –
 - ▶ Every WC policy conclusively presumed to contain certain clauses (Ins. C. § 11650)
 - ▶ One clause – that WC insurer will be directly and primarily liable to the claimant for all compensation for which the employer is liable (Ins. C. § 11651)

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Deductible policies do not alter dollar one liability

- ▶ WC deductible policies
- ▶ CA law –
 - ▶ Must contain deductible endorsement approved by Insurance Commissioner
 - ▶ Endorsement must state
 - ▶ That nonpayment of the deductible does not relieve the insurer from the payment of compensation (Ins. C. § 11735(e)(2))
 - ▶ Insurer must pay all benefits even if the employer refuses to pay the deductible!
 - ▶ That "notwithstanding the deductible, the insurer shall pay all of the obligations of the employer for workers' compensation benefits for injuries occurring during the policy period." (Ins. C. § 11735(e)(3))
- ▶ No change in insurer's dollar one liability

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Basic obligations under deductible policy

- ▶ Insurer's obligation = pay the benefits
- ▶ Employer's obligation = reimburse insurer
- ▶ We will talk about "side agreements" later

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Deductible – impact on obligations of insolvent insurer

- ▶ Do deductibles alter the insolvent insurer's obligations to pay all benefits to the claimant?

NO!

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Impact on CIGA's "covered claims" – none

- ▶ CIGA must pay and discharge "covered claims"
- ▶ CIGA's "covered claims"
 - ▶ Obligations of the insolvent insurer
 - ▶ Satisfying all requirements of 1063.1(c)(1)(A)-(G); and
 - ▶ Not excluded by any provision of (c)(3) – (c)(12) and 1063.2(h)
- ▶ Deductible does not alter CIGA's obligation to pay and discharge "covered claims"

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Impact on J&S liability of "other insurance" – none

- ▶ "Other insurance" exists where solvent insurer is jointly and severally (J&S) liable for benefits (e.g. general – special employment)
- ▶ Deductible does not affect
 - ▶ J&S liability of "other insurance" for benefits, or
 - ▶ CIGA's right to reimbursement, or
 - ▶ The amount of CIGA's reimbursement if it has paid a noncovered claim

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Deductible – impact on “other insurance”

- ▶ Does the insolvent insurer’s deductible alter the J&S liability of “other insurance?”

NO!

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Deductible Policies – overall impact

If you remember only **ONE** thing about the effect of deductibles on the insurer’s liability under the policy, remember that

Deductibles change nothing!

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Recent example of deductible “confusion”

- ▶ *Srabian* – general-special case
 - ▶ Legion insured general employer
 - ▶ Deductible policy – \$350,000
 - ▶ FFIC insured special employer
 - ▶ CIGA petitioned for reimbursement

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Recent example of deductible "confusion" cont'd

- ▶ Arbitrator (well known) found
 - ▶ FFIC only had liability if the IW exceeded the \$350K deductible
 - ▶ Error – Legion's deductible could not eliminate special's J&S liability within deductible
 - ▶ FFIC was not "other insurance" until \$350K Legion deductible exceeded – take nothing on reimbursement
 - ▶ Error – FFIC was "other insurance" due to J&S liability
 - ▶ Legion deductible policy did not cover general employer "at all" within deductible
 - ▶ Error – Arbitrator incorrectly analyzed the policy
 - ▶ Yet arbitrator ordered CIGA to administer all benefits
 - ▶ Error – not only was FFIC "other insurance" but if the Legion policy did not cover general within deductible, then claim would not be "within the coverage" of a policy of the insolvent insurer and not a "covered claim"

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Recent example of deductible "confusion" cont'd

- ▶ CIGA filed Petition for Reconsideration
- ▶ Result – Arbitrator promptly rescinded Findings and Order under Regulation § 10859

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Deductible payments and claims of "Double-Dipping"

- ▶ Relevant to reimbursement claims
- ▶ Deductible payment shows up as credit on CIGA benefit printout
- ▶ Claim that CIGA is collecting from "other insurance" and employer for the same claim
 - ▶ "Your Honor, CIGA is double-dipping!"
- ▶ CIGA is not entitled to keep and does not keep the deductible once the claim is determined to be noncovered
- ▶ CIGA does not "double-dip"

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CIGA and deductible payments

- ▶ Deductible payments
 - ▶ Managed and controlled by liquidator
- ▶ CIGA is not the liquidator!
- ▶ CIGA does not own, manage or control the deductible

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CIGA and deductible payments cont'd

- ▶ When CIGA pays a "covered claim" it becomes creditor of the estate
- ▶ CIGA may pay and later determine there was no "covered claim" (e.g. general-special employment)
- ▶ Deductible payments may be included in payments from estate to fund what were thought to be "covered claims"

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CIGA and deductible payments cont'd

- ▶ What if CIGA determines a claim is not a "covered claim" (e.g. general-special)?
 - ▶ CIGA notifies estate
 - ▶ Amount received by estate is backed-out and accounted for
 - ▶ CIGA is not entitled to keep and does not keep the value of any amount received from the estate based on payment of a noncovered claim.

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Lumbermens
**Employer Administration
and Funding Arrangements**

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**Post-liquidation employer
funding and administration**

- ▶ March 18, 2013 notice to insureds from LMG Special Deputy Receiver
 - ▶ May elect to continue self-funding and administration by agreement
- ▶ CIGA expects that many employers have opted will opt to continue funding and administration

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**Employer funding and
administration agreements**

- ▶ Under Illinois law –
 - ▶ Employers with deductible policies are permitted to contractually agree with insurer to fund and administer and pay claims within deductible
- ▶ By "side agreement"
 - ▶ Contracts separate from the policy
 - ▶ Between insurer and employer
 - ▶ Permitting employer to fund and administer within deductible

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Illinois statute – Post-liq. employer administration

- ▶ Illinois Law – 215 ILCS 5/205.1(e)
- ▶ Permits policyholders to continue funding and administering claims post-liquidation
 - ▶ Directly
 - ▶ Through a third-party administrator
- ▶ Requires liquidator to enforce agreements “where applicable” and “to the fullest extent possible”
- ▶ Funding of claims by policyholder within the deductible extinguishes liability of guaranty associations (215 ILCS 5/205.1(e))

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California parallel statute – Insurance Code § 1033.5

- ▶ Similar to Illinois statute
- ▶ Allows policyholders to continue administration and funding
 - ▶ Directly
 - ▶ Through a third-party administrator
- ▶ Not specific to WC policies
- ▶ Like Illinois statute, requires liquidator to enforce agreements “where applicable” and “to the fullest extent possible”
- ▶ Funding of claims by employer within the deductible extinguishes liability of CIGA and other guaranty associations

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So, what's not to like?

- ▶ CIGA would not have to administer claims within deductible
- ▶ Insured employer pays all the benefits within deductible
- ▶ Insured employer pays cost of administration
- ▶ CIGA's liability extinguished within deductible

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There are problems!

- ▶ CIGA's obligations controlled by CA Guarantee Act, not the IL statute
- ▶ CIGA interprets CA statute as not applying to non-CA liquidations
- ▶ CA employers who are not permissibly self-insured cannot lawfully administer
- ▶ CIGA could be required to administer non-covered claims after deductible reached

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IL statute does not control CIGA's obligations

- ▶ CA Insurance Code strictly defines the scope of CIGA's powers, duties and protections (Isaacson v. California Ins. Guarantee Assn. (1988) 44 Cal. 3d 775, 786.)
- ▶ IL statute cannot redefine CIGA's obligations
- ▶ CIGA must pay and discharge covered claims (Ins. C. § 1063.2)
 - ▶ Includes CIGA's obligation to administer "covered claims"
 - ▶ Itself
 - ▶ Through a TPA, etc.
- ▶ CIGA cannot permit insured employer to administer

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CA statute not applicable

- ▶ CA Insurance Code §1033.5
- ▶ Applicable to deductible agreement entered into between
 - ▶ Policyholder, and
 - ▶ "[A]n insurer subject to liquidation proceedings under this article [14 of the CA Ins. Code]." (Ins. C. §1033.5(a))
- ▶ CIGA interprets this statute as applying only to CA liquidations
- ▶ Lumbermens Mutual Companies are IL liquidations
- ▶ No ancillary CA liquidations

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Insured employer cannot administer claims

- ▶ Permitted "claims administrators" under CA WC law – traditional view
 - ▶ Each admitted insurer
 - ▶ Each properly self-insured employer
 - ▶ Each TPA when administering "for an insurer, a self-insured employer, a legally-uninsured employer or a joint powers authority." (Regulation § 10100.1. *Italics supplied.*)
- ▶ Insured employer cannot administer either directly or through TPA
- ▶ Both IL and CA statutes only apply where policyholder administration agreements are "applicable" and will be enforced to the "fullest extent possible"
- ▶ In CA – not "applicable" and cannot be enforced

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Administration "side-agreements" may be void

- ▶ Limitation of insurer liability only by Insurance Commissioner approved
 - ▶ Limited policy (Ins. C. § 11657) or
 - ▶ Limiting endorsement (Ins. C. § 11659)
 - ▶ Otherwise, policies are unlimited (Ins. C. § 11660)
- ▶ Lumbermens policies – no known proper limiting endorsements
 - ▶ That relieve insurer of obligation to fund and administer within deductible
- ▶ Employer administration by "side-agreement"
 - ▶ Contract between insurer and policyholder outside of approved policy documents
 - ▶ "Side-agreements" generally void, *Ceradyne v. Argonaut Ins. Co.* (2009) Fourth App. Dist. Unpublished – provided for court's reasoning

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Employer cannot raise CIGA defenses

- ▶ The employer is not CIGA
- ▶ Employer cannot raise CIGA defenses
- ▶ There will be F&As and stipulated awards that could not have been made against CIGA
- ▶ CIGA may have to administer after deductible exceeded

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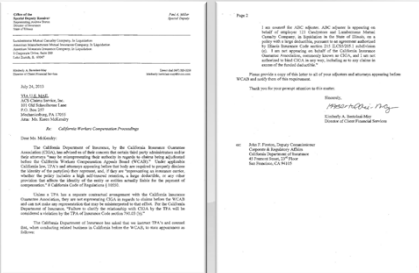
Recent activity...

- ▶ CA Dept. of Ins. has requested that IL Special Deputy Director instruct employers' attorneys to clearly state appearances at WCAB
 - ▶ As required by *Caldron v. Compuware Corp. (2002) 67 Cal. Comp. Cases 289 (WCAB en banc)*
 - ▶ Attorneys appearing are required to properly disclose the identity of the party(ies) they represent, and, if they are representing an insurance carrier, whether the policy includes a high self-insured retention, a large deductible, or any other provision that affects the identity of the entity or entities actually liable for the payment of compensation.
- ▶ Requires attorneys to state that
 - ▶ They represent the adjuster (TPA), not CIGA, under deductible agreement
 - ▶ Not appearing on behalf of CIGA
 - ▶ Not authorized to bind CIGA in any way, "including any claims in excess of the funded deductible."

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Recent activity... cont'd

In supplemental materials



- ▶ CIGA will not receive copy of the Special Deputy's letter on each employer-administered claim
- ▶ Copies of letters to each employer with administration agreement provided

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What will happen at WCAB?

- ▶ CIGA cannot predict the response to disclosure of employers' administration and funding from
 - ▶ The Board
 - ▶ May not agree with employer administration – even through TPA
 - ▶ May conclude that CIGA is necessary party
 - ▶ The IW
 - ▶ May want to join CIGA for any number of reasons
 - ▶ Other parties
- ▶ If CIGA is not joined, it will not involve itself with the claim
- ▶ But, there is a good chance someone will join CIGA

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CIGA's response to joinder

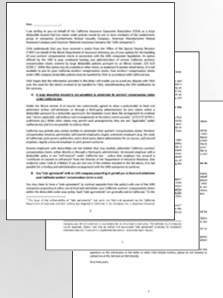
- ▶ If joined, CIGA's position
 - ▶ CIGA must administer the "covered claim" within the deductible
 - ▶ Employer must cease administration and funding
 - ▶ Employer must surrender claims file and data to CIGA
- ▶ CIGA will seek control over administration of the claim

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Gaining control of administration if joinder is pressed

In supplemental materials

- ▶ CIGA's demand
 - ▶ Form letter to employer
 - ▶ Demand that employer cease administration
 - ▶ Demand transfer of claim file to CIGA within 2 weeks



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Gaining control cont'd

- ▶ If employer ceases administration and delivers file – no further action needed
- ▶ If employer refuses or fails to respond within 2 weeks
 - ▶ CIGA to take steps to compel employer to cease administration
 - ▶ Petition for Order of Change of Administrator and to deliver claims file to CIGA
 - ▶ Template to be provided to the firms
 - ▶ File DOR with petition to request hearing
 - ▶ Litigate to conclusion

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Prejudgment interest (PJI) update

- ▶ CIGA has not stopped pursuing PJI
- ▶ *Key*, *Colamaria* and *Anson* fact patterns have not produced WCAB success or appellate review
 - ▶ Voluntary payment of benefits followed by proof of "other insurance" liability and request for reimbursement and PJI
 - ▶ *Colamaria* – Review denied (Court of Appeal and Supreme Court)
 - ▶ *Anson* – Review denied (Court of Appeal – no Supreme Court petition)
 - ▶ Both *Colamaria* and *Anson* landed in the 2nd District, Division 5 both summarily denied

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Prejudgment interest (PJI) update cont'd

- ▶ There is still potential for *Key*, *Colamaria* and *Anson* fact patterns
 - ▶ 2nd District – but other than Division 5
 - ▶ Different Appellate District altogether
- ▶ New potential fact pattern to test (preliminary thoughts)
 - ▶ CIGA compelled to pay under award
 - ▶ Issue of "other insurance" deferred
 - ▶ CIGA later prevails on "other insurance" and obtains reimbursement
 - ▶ Start looking for cases with these facts
 - ▶ Litigation memo to follow

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Questions

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