

# **LIFE-HEALTH VS. PROPERTY-LIABILITY INSURANCE GUARANTY ASSOCIATIONS<sup>1</sup>:**

## **A DIFFERENCE IN APPROACH TO INSURER INSOLVENCY**

By: Cynthia J. Borrelli<sup>2</sup>

All U.S. jurisdictions provide partial statutory protection in the event of insurer insolvency through the creation of various state insurance guaranty associations which are governed by statutes primarily based on two Model Acts promulgated by the National Association of Insurance Commissioners.<sup>3</sup> Guaranty associations are an integral part of each state's regulatory process for addressing insurer insolvency. The property-liability insurance guaranty association ("property-liability association"), however, is a different statutory creature from the life and health insurance guaranty association ("life-health association"). Simply put, the property-liability association pays claims, subject to important statutory limitations. The life-health association also pays claims, but, significantly, often it also facilitates the sale of valuable assets, *i.e.*, books of business, to solvent carriers through a variety of financing techniques, including reinsurance assumption transactions, and has certain continuing coverage obligations.<sup>4</sup> Once such a transaction has been consummated, the role of the life-health association is often substantially reduced, except with regard to the funding of enhancements to contract holders and the extended pay-out of obligations to the purchaser.<sup>5</sup> These payments are intended to satisfy the association's obligations to covered policyholders and other persons' claims under policies issued by impaired or insolvent member insurers.

A brief discussion of salient aspects of the property-liability and the life-health systems, with an integrated analysis of key differences between the two, is set forth below.

## **I. What Are Insurance Guaranty Associations?**

Through a matrix of state-specific enabling statutes, state insurance guaranty associations levy and collect assessments from member insurers, pay “covered claims” (New Jersey Property-Liability Insurance Guaranty Association) or “covered policy obligations” (New Jersey Life and Health Insurance Guaranty Association). Together with the domestic regulator of the insolvent insurer (usually the commissioner or superintendent of insurance) and the deputy liquidator (typically approved by the court presiding over the liquidation process and selected by the commissioner or superintendent of insurance as statutory liquidator), the guaranty association community (comprised of both property-liability and life-health associations located in virtually each state and their respective trade associations, the National Conference of Insurance Guaranty Funds (“NCIGF”) and the National Organization of Life and Health Guaranty Associations (“NOLHGA”), respectively)<sup>6</sup> functions as a unified system to manage, and at least partially mitigate, the impact of an insurer insolvency.

### **A. Property-Liability Insurance Guaranty Associations**

Property-liability associations have been established by law in each of the 50 states, the District of Columbia, Puerto Rico and the U.S. Virgin Islands. Most of the laws are based on the Post-Assessment Property and Liability Insurance Guaranty Association Model Act adopted by the National Association of Insurance Commissioners. (NAIC Model Regulation Service (July 1996, at 540-41, et seq.) (the “NAIC Property-Liability Model Act”)). The NAIC Property-Liability Model Act adopts a post-insolvency assessment approach to funding under which, after an insolvency has occurred and estimates of resulting claims obligations have been made, a property-liability association or its state regulator calculates assessments and the association then levies those assessments upon solvent insurers. New York is the only state

which does not use a post-assessment system. To the contrary, New York maintains a “pre-insolvency assessment” fund under which insurers are assessed a specified amount each year until total assessments collected reach a statutory maximum. These assessed contributions are held against claims from insolvencies which could arise in the future. Each insurance company writing property and casualty lines of business covered by a property-liability association is required to be a member of the guaranty association in a particular state as a condition of its authority to transact business in that state. Property-liability associations assess member insurers based upon their proportionate share of premiums written on covered lines of business in that state, *i.e.*, net direct written premiums.

**B. Life-Health Insurance Guaranty Associations**

Life-health associations have existed since at least 1941, when the State of New York formed the first Life and Health Guaranty Association. Like the property-liability associations, the life-health associations have provided financial safety nets for policyholders of insolvent insurers as a means of bolstering the public’s confidence in the insurance industry. Since 1992, when Colorado and Louisiana enacted life-health association statutes, all 50 states, the District of Columbia and Puerto Rico have in place a guaranty fund mechanism to protect resident (and, in some instances, non-resident) policyholders against the failure of life and health insurers, these life-health associations operate pursuant to state statutes which are based on one of several versions of the Life and Health Insurance Guaranty Association Model Act developed by the National Association of Insurance Commissioners (NAIC Model Regulation Service (October 1999, at 520-1, et seq.) (the “NAIC Life-Health Model Act”)). The first NAIC Life-Health Model Act was adopted in 1970 and has been periodically updated over the years.<sup>7</sup> It provides

insight to state legislatures and departments of insurance with respect to enactment of their own legislation.

Life-health associations are generally organized as unincorporated associations governed by a board of directors consisting of representatives of member insurers doing business in the state. In some states, the insurance commissioner or his designee and one or more public representatives designated by the commissioner sit on the board.<sup>8</sup> Membership in the life-health association is required as a condition of a life and health insurer's authority to transact business in the state where the association is created. Life-health guaranty associations assess their member insurers for their operating costs and the costs of providing coverage to policy and contract holders of insolvent insurers.

## **II. What Do Guaranty Associations Do?**

The purpose of the New Jersey Property-Liability Insurance Guaranty Association is to: provide a mechanism for the payment of "covered claims" under certain insurance policies; avoid excessive delay in that payment; minimize financial loss to claimants or policyholders because of the insolvency of an insurer; assist in the detection or prevention of insurer insolvencies; and to provide an organization to assess the cost of such protection among insurers doing business within the State. See N.J.S.A. 17:30A-2a.

The New Jersey Life and Health Insurance Guaranty Association is intended for a similar purpose: to protect, subject to certain statutory limitations, certain so-called "covered persons" from hardship because of the impairment or insolvency of an insurer that issued certain life and health insurance policies and annuity contracts defined as "covered contracts." See N.J.S.A. 17B:32A-2(a).

### **III. Are There Limitations On The Scope Of Protection Offered?**

#### **A. Property-Liability Guaranty Associations**

The New Jersey Property-Liability Insurance Guaranty Association Act, N.J.S.A. 17:30A-1, et seq., applies to all property and casualty lines of direct insurance (not reinsurance) authorized under New Jersey law, except workers' compensation insurance, title insurance, surety bonds, credit insurance, mortgage guaranty insurance, municipal bond coverage, fidelity insurance, investment return assurance, ocean marine and pet health insurance. There are statutory exceptions to coverage based upon whether the claim at issue constitutes a "covered claim" pursuant to statute.

##### **1. Covered Claims**

Claims which are eligible for coverage are deemed "covered claims,"<sup>9</sup> but do not include:

###### **(a) Subrogation and Reinsurance Claims:**

Any amount due any reinsurer, insurance pool, or underwriting association, as subrogation recoveries or otherwise, except that a claim for any such amount asserted against a person insured under a policy issued by an insurer which has become an insolvent insurer, which, if it were not a claim by or for the benefit of a reinsurer, insurer, insurance pool, or underwriting association, would be a "covered claim" may be filed directly with the receiver of the insolvent insurer.<sup>10</sup>

###### **(b) Interest:**

Amounts for interest on unliquidated claims;

Prejudgment interest is tantamount to an unliquidated claim and is not generally assessed against the New Jersey Property-Liability Insurance Guaranty Association.<sup>11</sup>

(c) Punitive Damages:

Punitive damages unless covered by the policy;<sup>12</sup>

(d) Attorney Fees:

Counsel fees for prosecuting suits for claims against the association;<sup>13</sup>

(e) Untimely Settlement:

Assessments or charges for failure of such insolvent insurer to have expeditiously settled claims;

(f) Pre-insolvency Expenses:

Counsel fees and other claim expenses incurred prior to the date of insolvency;

(g) Late Filed Claims:<sup>14</sup>

A claim filed with the association, liquidator or receiver of an insolvent insurer after the final date set by the court for the filing of claims against the liquidator of an insolvent insurer or, if a final date is not set by the court for the filing of claims against the liquidator or receiver of an insolvent insurer [the so-called “bar date”], two years from the date of the order of liquidation, unless the claimant demonstrates unusual hardship and the commissioner approves of treatment of the claim as a “covered claim.”

See N.J.S.A. 17:30A-5.

**2. Net Worth**

An insured’s net worth can also impact the ability to secure New Jersey Property-Liability Insurance Guaranty Association protection. Any first party claim made by an insured whose net worth exceeds \$25 million as of December 31 of the year prior to which the insurer becomes insolvent is beyond the scope of a “covered claim”. The net worth of an insured expressly includes the aggregate net worth of the insured and all of its affiliates as calculated on a consolidated basis. See N.J.S.A. 17:30A-5.

### 3. Exhaustion of Claims

Any policyholder or claimant who has an otherwise covered claim which may be recovered from more than one property-liability association or its equivalent will be required to exhaust<sup>15</sup> first his rights under the statute governing the association of the place of residence of the insured at the time of the insured event, except that if the claim is a first party claim for damaged property with a permanent location, the claimant or policyholder shall seek recovery first from the association where the property is located. Only if recovery is denied or deferred by the resident property-liability association can the person proceed to seek recovery from any other state property-liability association or its equivalent. See N.J.S.A. 17:30A-12a.<sup>16</sup>

#### **B. Life-Health Guaranty Associations**

The New Jersey Life and Health Insurance Guaranty Association also provides coverage for certain lines of life (including annuities) and health insurance, which include: direct, non-group, life, health, annuity and supplemental policies or contracts, for certificates under direct group life, health, annuity and supplemental policies and contracts, or individuals and group long-term care insurance policies and contracts, and for unallocated annuity contracts,<sup>17</sup> issued by member insurers except as otherwise limited by the New Jersey Life and Health Insurance Guaranty Association's enabling Act. See N.J.S.A. 17B:32A-3(b).

As with the New Jersey Property-Liability Insurance Guaranty Association, there are exceptions to coverage from the New Jersey Life and Health Insurance Guaranty Association as follows:

- (1) Any portion of a policy or contract not guaranteed by the insurer, or under which the risk is borne by the policy or contract holder;
- (2) Any policy or contract of reinsurance, unless assumption certificates have been issued;

- (3) Any portion of a policy or contract to the extent that the rate of interest on which it is based [exceeds a certain statutorily acknowledged threshold];
- (4) Any plan or program of an employer, association or similar entity to provide life, health or annuity benefits to its employees or members to the extent that such plan or program is self-funded or uninsured, including, but not limited to, benefits payable by an employer, association or similar entity under:
  - (a) a Multiple Employer Welfare Arrangement as defined in the Employee Retirement Income Security Act of 1974 (29 U.S.C. §1002);
  - (b) a minimum premium group insurance plan;
  - (c) a stop-loss group insurance plan; or
  - (d) an administrative services only contract.
- (5) Any portion of a policy or contract to the extent that it provides dividends or experience rating credits, or provides that any fees or allowances be paid to any person, including the holder of the policy or contract, in connection with the service to or administration of that policy or contract;
- (6) Any policy or contract issued in [the state where the guaranty association is created] by a member insurer at a time when the insurer was not licensed or did not have a certificate of authority to issue that policy or contract in that state;
- (7) Any unallocated annuity contract issued to an employee benefit plan covered by the Pension Benefit Guaranty Corporation and whose benefits will be paid under such systems;
- (8) Any portion of any unallocated annuity contract which is not issued to or in connection with a specific plan providing benefits to employees or an association of natural persons.<sup>18</sup>

Life-health associations not only provide coverage to residents, but also to nonresidents under certain statutorily specified circumstances.<sup>19</sup> This flexibility is one very important basis for the distinction between the two types of guaranty associations.

#### **IV. How The Two Types Of Guaranty Associations Differ**

The obligations of the two types of guaranty associations differ, as do the scope of their statutory authority to effect the purposes for which they are created. Moreover, funding mechanisms, while somewhat similar on the face of the two NAIC Model Acts, differ in

practice. A life-health association has the ability to implement reinsurance arrangements with solvent carriers, transfer books of business of insolvent carriers to solvent carriers, to provide guarantees under appropriate circumstances, and even to become involved in the sale of the viable portions of an insolvent company to a solvent carrier, all as a means of helping to “fund” policyholder protection. Life-health association enhancements to policyholders loosely based upon each association’s statutory obligations are intended to protect policy and contract holders, as well as to lessen the burden on the purchaser of the insolvent carrier’s business and, hence, to entice bids for the remaining profitable books of business of the insolvent carrier.

**A. Funding Mechanisms**

**1. The Life-Health Insurance Guaranty Association**

While both guaranty associations derive financial support from member company assessments, assessments differ between the two types of associations. There are two types of life-health association assessments levied upon members: Class A assessments and Class B assessments. The Class A assessment is usually a fixed amount assessed annually by the life-health association to cover its general operating expenses not allocable to a specific insolvency. On the other hand, the Class B assessment is made on an “as-needed” basis to collect funds for the life-health association to fulfill its statutory obligations to policy and contract holders in a given insolvency, as well as to fund the association’s operating expenses allocable to that insolvency. Distinct from the assessment mechanism imposed with respect to property-liability associations, assessments by life-health associations are levied against member insurers separately for each account. For purposes of administration and assessment, most life-health associations maintain two accounts: a life insurance and annuity account, which includes certain sub accounts such as the life insurance sub account, the annuity sub account and the

unallocated annuity sub account; and the second account, which is the health insurance account.<sup>20</sup> In practice, many life-health associations also assess per individual insolvency, while property-liability associations tend to assess annually to fund all of their outstanding and estimated obligations across insolvencies. Life-health associations also make inter-account borrowings in order to satisfy imminent obligations caused by a particular insurer insolvency.<sup>21</sup>

## **2. Property-Liability Insurance Guaranty Association**

In order to secure funds necessary to pay its obligations on covered claims for insolvent insurers, the expense of handling those covered claims, the costs of certain examinations of member insurers in financial distress, and other expenses authorized by the New Jersey Property-Liability Insurance Guaranty Association Act, the New Jersey Property-Liability Insurance Guaranty Association is statutorily obligated to assess each of its member insurers in the proportion that the net direct written premiums of the member insurer for the calendar year preceding the assessment bears to the net direct written premium of all member insurers for the calendar year preceding the assessment.<sup>22</sup> See N.J.S.A. 17:30A-8a(3). Additionally, the New Jersey Property-Liability Insurance Guaranty Association may borrow and separately account for funds from any source, including from certain other statutory entities whose affairs are administered by the Guaranty Association. See N.J.S.A. 17:30A-8b(2). Those inter-account borrowings are needed in certain circumstances on an interim basis to assure appropriate cash flow for the New Jersey Property-Liability Insurance Guaranty Association to satisfy its own statutory obligations. Other than periodic distributions of estate assets by liquidators of insolvent insurers, assessments and loans are the principal means of satisfying so-called “covered claims” obligations for property-liability associations.

**B. Obligations of the Guaranty Associations**

**1. Life-Health Guaranty Associations**

Life-health guaranty associations have two principal statutory obligations with respect to policyholders. First, life-health associations must provide a minimum floor of insurance claim protection. In most cases, guaranty associations limit coverage for policyholder claims to \$500,000 in life insurance death benefits, but not more than \$100,000<sup>23</sup> in net cash surrender or net cash withdrawal values for life insurance; and \$500,000 in present value annuity benefits, including net cash surrender and net cash withdrawal values, but not more than \$100,000 in net cash surrender or net cash withdrawal values for annuity benefits. In many instances, however, the life-health association is not liable to expend more than \$500,000 in the aggregate with respect to any one individual. With respect to any one allocated annuity contract, the limitation is \$2,000,000 in benefits. Finally, with respect to any one group, blanket or individual accident or health insurance or group blanket, or individual accident or health insurance policy, the New Jersey Life and Health Insurance Guaranty Association Act imposes no limitations on the benefits payable beyond any set forth in the original contract. See N.J.S.A. 17B:32A-3.d(4). Given the current economic climate and that several insurers who write long term care coverages appear to be struggling financially, unlimited health benefits will likely amount to a significant obligation for a life-health association in the event any such carrier is declared insolvent.

The other primary obligation of a life-health association, depending on the nature of the policy or contract implicated and whether the member insurer is domestic or foreign, impaired or insolvent, is the provision of continuing coverage to the policyholders.<sup>24</sup> Continuing coverage generally is not an obligation of a property-liability association. Under most

circumstances, the order of liquidation terminates property-liability policies within 30 days.<sup>25</sup> However, given the nature of life and health insurance and the difficulty which policyholders who have deteriorating health might have in obtaining replacement coverage at affordable rates, this distinction appears justified. This also accounts for the higher statutory limits on life, health and annuity claims, as opposed to property-liability claims. Property-liability coverages are more readily replaceable in the market place, as age and health do not routinely impact underwriting.

Life-health associations have a broader scope of statutory options to provide protection to the policyholders of insolvent insurers than do property-liability associations. If a member insurer is an impaired domestic insurer, the life-health association may, in its discretion and subject to certain conditions: (1) guaranty, assume or reinsure, or cause to be guaranteed, assumed or reinsured any or all policies or contracts of the impaired insurer; (2) provide such monies, pledges, notes, guarantees or other monies as are proper to satisfy contractual obligations and assure payment of contractual obligations of the impaired insurer, or (3) loan money to the impaired insurer.<sup>26</sup> On the other hand, a property-liability association merely makes payment of so-called “covered claims” subject to certain statutory caps, as more fully discussed below.

If a member insurer of a life-health association is an insolvent insurer, the association shall, in its discretion, take one of the following actions: (a) guaranty, assume or reinsure, or cause to be guaranteed, assumed or reinsured, the policies or contracts of the insolvent insurer; (b) assure payment of the contractual obligations of the insolvent insurer; (c) provide those monies, pledges, guarantees or other means, as are reasonably necessary to discharge those obligations; or (d) with respect only to life and health insurance policies, provide benefits and

coverages nearly identical to that provided under the insolvent's policy, subject to certain statutory limitations.<sup>27</sup> In essence, the life-health guaranty association can operate similarly to an insurer with respect to an insolvent insurer's business.

## **2. Property-Liability Guaranty Associations**

Property-liability associations are obligated to the extent of "covered claims" asserted against an insolvent insurer that are incurred prior to or 90 days after the determination of insolvency or before the policy expiration, if less than 90 days after that determination, or before the policyholder replaces the policy or causes its cancellation, if he does so within 90 days of the determination. The statutory cap on the New Jersey Property-Liability Insurance Guaranty Association's obligations on any covered claim is \$300,000. The \$300,000 cap applies with respect to the Guaranty Association per claim and is subject to any applicable deductible and self-insured retention contained in the policy, as well as to certain other limitations.<sup>28</sup> See, e.g., N.J.S.A. 17:30A-8. Thus, as noted above, the role of the property-liability association is to pay claims, subject to statutory limitations. There are no continuing coverage obligations beyond those for the brief period noted above. Moreover, the existing structure of most property-liability association acts may be argued to be insufficiently flexible or too narrow to permit such associations to engage in more creative measures to address insurer insolvency, such as transfers of books of business or the structuring of policies of insolvent insurers.

## **V. Conclusion**

The difference between a life-health and a property-liability association is the conceptual approach to resolution of the problem of insurer insolvency. Property-liability associations are based upon a very structured, stringent enabling statute, which essentially calls for the payment

of covered claims, subject to statutory limitations, until an insolvency proceeding is terminated and final distributions have been made to policyholders and other claimants.<sup>29</sup> Unfortunately, however, the process of liquidation can take many years, and it often does. As a primary example, consider the insolvency of Integrity Insurance Company, first placed into liquidation in the mid 1980s.<sup>30</sup>

While life and health insurer insolvencies are not always resolved quickly, for the most part, life and health insolvencies tend to be closed more expeditiously than property-liability estates. In part, this is due to the joint efforts of the liquidation estates, the various life-health associations, the associations' trade organization, NOLHGA, and solvent carriers. As noted above, the life-health association acts are far more versatile and provide the association with a number of options for fulfilling statutory obligations to assist in insurer insolvency.

While each state life-health association has sole responsibility for fulfilling its coverage obligations, there are certainly efficiencies to providing coverage jointly with other associations through NOLHGA. For examples, refer to the Executive Life,<sup>31</sup> Inter-American and Investors Equity proceedings, as well as those of Pacific Standard,<sup>32</sup> Kentucky Central Life Insurance Company,<sup>33</sup> and Confederation Life Insurance Company.<sup>34</sup> These insurer delinquency proceedings were resolved through sophisticated restructurings implicating the various life-health associations, NOLHGA, the estate receivers or liquidators, and solvent insurers.

Given the nature of the business which must be addressed by a life-health guaranty association, all of which are vital to the protection of individuals, their families and, as we have seen, to corporations who fund certain employee-benefit plans with life insurance and annuity contracts<sup>35</sup> (all of which are based, to some extent, upon health insurance underwriting), expeditious solutions are critical.

As noted above, life and health coverage is not as easily replaceable due to underwriting concerns as it is with respect to the more traditional property-liability coverages addressed by the property-liability association community. Moreover, financial market conditions fluctuate and make replacement of certain annuity contracts unfeasible or unprofitable. For this reason, coverage limits on the life-health association side tend to be more expansive than on the property-liability association side. Additionally, the statutes governing life-health associations provide for broader protections, greater flexibility, and tend to encourage joint effort and multi-party solutions.

Whether a similar approach might be successfully adopted by the property-liability association community through the NCIGF depends upon interpretation of the powers and obligations of each of the individual property-liability associations based on their enabling statutes. As noted above, many of those statutes only make general references to such things as “negotiating and becoming a party of the contracts as are necessary to carry out the purposes of this act,” and “performance of such other acts as are necessary or proper to effectuate the purposes of this act.” The property-liability association acts could be argued to lack specific authority for either the arrangements contemplated by the life-health association acts or the ability of the property-liability association to provide the types of enhancements that might be necessary in order to bridge the gap between that which an assuming carrier is willing to provide and the restricted coverage which the association’s enabling act authorizes. Only time will tell whether the property-liability association community takes the initiative and adopts an approach similar to its life-health counter-parts.

---

<sup>1</sup>This article does not undertake to inform the reader as to all aspects, or all issues, relating to the purpose, structure, or operation of state insurance guaranty associations. The enabling act, regulations, and interpretive case law of the appropriate state guaranty association should be reviewed.

<sup>2</sup> Ms. Borrelli is a shareholder with the law firm of Bressler, Amery & Ross, P.C., which has offices in Florham Park, NJ, New York, NY and Miramar, FL. The views expressed by the author are her own and not those of her law firm or its clients, the New Jersey Life and Health Insurance Guaranty Association, the New Jersey Property-Liability Insurance Guaranty Association, and the New Jersey Surplus Lines Insurance Guaranty Fund.

<sup>3</sup> For purposes of this article, the operation of the New Jersey Property-Liability Insurance Guaranty Association will be addressed and referred to as a representative prototype. It is created as a private, non-profit, unincorporated, legal entity. See N.J.S.A. 17:30A-6 et seq. (“New Jersey Property-Liability Guaranty Insurance Association Act”). While most state insurance guaranty association enactments, including New Jersey’s, incorporate features not always having their origin in the NAIC Model Act, the fact remains that the Model Act is the single most dominant thread running through almost all U.S. enactments and provides a common baseline for implementation and interpretation of their provisions. See Post-Assessment Property and Liability Insurance Guaranty Association Model Act (NAIC Model Regulation Service (July 1996 at 540-1, et seq.)). Most states also create, by separate statute, a guaranty association to respond to claims arising under life, health and annuity contracts. (See, e.g., N.J.S.A. 17B:32A-1, et seq.) The New Jersey Life and Health Insurance Guaranty Association is referred to throughout this paper for purposes of example. Additionally, New Jersey has the sole surplus lines guaranty fund in the country, the New Jersey Surplus Lines Insurance Guaranty Fund. See N.J.S.A. 17:22-6.70, et seq.

<sup>4</sup> Inter-American Life Insurance Company of Illinois provides a useful example. Inter-American was an Illinois-domiciled company licensed in 47 states and the District of Columbia. The principal lines of business which it wrote were life insurance and annuities. When it was placed into liquidation in December 1991, the Company had woefully inadequate liquid assets to pay claims. As a consequence, the implicated guaranty associations were required to assume policy administration responsibility until Inter-American’s business could be transferred to an appropriate assuming reinsurer. Those guaranty associations paid nearly \$80 million in claims during the interim period, and subsequently paid an additional \$73 million to cause Inter-American’s in-force business to be assumed by Jackson National Life Insurance Company in early 1993. See William P. O’Sullivan, “Key Developments in the Life and Health Insurance Guaranty System: 1993 to Present,” Insurer Insolvency Revisited: 1999 at 12.

<sup>5</sup> The 1991 insolvency of Executive Life Insurance is one such example where assets of an insolvent were sold to a solvent concern.

<sup>6</sup> The NCIGF is a national association of property and casualty insurance guaranty associations. The mission of the NCIGF is to: (i) build confidence and trust in the state guaranty association system; (ii) promote the efficient administration and management of the state guaranty association system on a state and national level; (iii) serve as a repository of expertise and a provider of information on the state guaranty association system and the insolvency process; and (iv) act as an agent of and in coordination with state guaranty associations in multi-state insolvencies or on issues of national significance at the request of member guaranty

---

associations. See Harris, Kevin D., “A Review of the System of Property and Casualty Guaranty Associations: Achievements and Major Developments,” *Insurer Insolvency Revisited*: 1999 at 11.

NOLHGA was formed in 1983 primarily as a mechanism for coordinating the efforts of life-health associations in multi-state insurer insolvencies. NOLHGA is a nonprofit association with tax exempt status under §501C(6) of the Internal Revenue Code and is organized as a Virginia non-profit corporation. Its members consist of each of the state life-health associations representing the 50 states, the District of Columbia and Puerto Rico.

<sup>7</sup> Amendments to the NAIC Life-Health Model Act were made in Dec. 1975, June 1977, Dec. 1985, June 1987, Dec. 1987, Sept. 1993, Dec. 1993, June 1995, Dec. 1995, June 1997, March 1998, June 1998, June 1999 and Oct. 1999.

<sup>8</sup> In New Jersey for instance, the members of the Board are selected by the member insurers subject to approval of the Commissioner of the New Jersey Department of Banking and Insurance (the “Commissioner”). While the Commissioner does not expressly serve on the Board, he or his representative are considered “ex officio members.” See N.J.S.A. 17B:32A-6(a).

<sup>9</sup> For purposes of the New Jersey Property-Liability Insurance Guaranty Association, with respect to insurer insolvencies pending as of December 2004, a so-called “covered claim” does not include a claim filed with the Association, liquidator or receiver of an insolvent insurer: (a) more than one year after December 2004; or (b) the date set by the court for the filing of claims against the liquidator or receiver of the insolvent insurer, whichever date occurs later. See N.J.S.A. 17:30A-5.

<sup>10</sup> This prohibition has long since been upheld (see Sandson’s Bakery v. Glover, 162 N.J. Super. 225, 392 A.2d 640 (Law Div. 1978). In Material Damage Adjustment Corp. v. New Jersey Prop.-Liab. Ins. Guar. Ass’n, 294 N.J. Super. 81, 682 A.2d 739 (App. Div. 1996), however, the Court held that the subrogation exclusion from the statutory definition of “covered claims” did not extend to claims by a JUA servicing carrier as a motorist’s personal automobile insurer, or against the Guaranty Association, as successor to the motorist’s employer’s insolvent automobile insurance carrier.

<sup>11</sup> See Wilton v. Cycle Trucking, Inc., 240 N.J. Super. 326, 573 A.2d. 462 (App. Div. 1984). Courts have also held that insureds whose insurer was later declared insolvent were similarly not liable for prejudgment interest on a tort award where the Guaranty Association was exempted from such responsibility. See Lehmann v. O’Brien, 240 N.J. Super. 242, 573 A.2d 171 (App. Div. 1989), and Hendricks v. A.J. Ross Co., 232 N.J. Super. 243, 556 A.2d 1267 (App. Div. 1989). Interestingly, this rationale for a ban on prejudgment interest was not extended to a medical association defending a medical malpractice action where defense counsel repeatedly represented throughout trial and settlement negotiations that it was uninsured. The Court held that the medical association was equitably estopped from asserting protection from prejudgment interest under the Guaranty Association Act because establishment of insurance status was solely within the medical association’s knowledge and control, and plaintiffs relied to their detriment on repeated assertions that there was no coverage for the claim because they were forced to go to verdict and risk that the verdict would be lesser than the settlement offer, which, indeed, it was. Delgado v. Epstein, 2005 WL 3693200 (App. Div. 2006).

---

<sup>12</sup> See ARCNET Architects, Inc. v. New Jersey Prop.-Liab. Ins. Guar. Ass'n, 377 N.J. Super. 102, 871 A.2d 728 (App. Div. 2005).

<sup>13</sup> ARCNET Architects, Inc. v. New Jersey Prop.-Liab. Ins. Guar. Ass'n, 377 N.J. Super. 102, 871 A.2d 728 (App. Div. 2005). Counsel fees incurred in connection with a professional liability action and prior to the insolvency of a liability insurer were not considered "covered claims." The insurer had retained counsel on the insured's behalf. The Court held *quantum meruit*, or unjust enrichment, did not apply to make the insured liable for the fees because the insured paid counsel through the policy premium, therefore, counsel was not in the class of entities that the Guaranty Association was designed to protect.

<sup>14</sup> A claimant may show "unusual hardship" as referenced above by filing information that demonstrates any of the following:

- (1) the claimant never received notice of the due date for filing claims, but the claimant shall be presumed to have received such notice if notice was timely mailed to the claimant's address currently on file with the insurer;
- (2) the mailing address of the claimant in the insurer's records is erroneous, and the claimant demonstrates that he or she notified the insurer or its agent of a change in address;
- (3) the claimant was incapable of responding to the notice due to an emergent and extreme medical event or similar emergent and extreme circumstances or;
- (4) the claimant is deceased, and the claimant's estate demonstrates that the death occurred within such a period that the representative of the claimant's estate did not have sufficient time to advise the insurer or its agent of such circumstances.

See N.J.S.A. 17:30A-5 and N.J.A.C. 11:1-43.21, et seq.

<sup>15</sup> Exhaustion and set-off of other solvent carriers' coverages, as well as the order of coverage where multiple policies and multiple property-liability associations are available to respond to a claim or claims, are often implicated in disputes involving environmental or toxic tort-type claims where trigger of coverage, whether coverage applies "per claim" or "per occurrence" and similar issues, can be dispositive of coverage matters. Often with environmental claims involving multiple sites and hundreds, or even thousands, of claimants, the goal of maximizing available coverage and protection to those claimants results in a litany of disputes between and among solvent insurers and, occasionally, property-liability associations.

<sup>16</sup> Additionally, other than claims for coverage for personal injury protection benefits issued pursuant to N.J.S.A. 39:6A-4 or N.J.S.A. 39:6A-3.1 ("PIP benefits"), all policyholders and claimants must first exhaust their rights under any other policy before accessing Guaranty Association coverage. See N.J.S.A. 17:30A-12b. Claims under "other insurance policies" include claims under kinds of insurance policies such as general liability, accident and health insurance, workers' compensation health benefits plan coverage, primary and excess coverage, if applicable, and all other private, group or governmental coverages except coverage for PIP benefits and those set forth at N.J.S.A. 39:6A-3.1.

<sup>17</sup> An "unallocated annuity contract" is defined to mean:

- (1) A group annuity certificate which is not issued to and owned by an individual, except to the extent of any annuity benefits guaranteed to an individual by an insurer under that contract or certificate, or
- (2) Any unallocated life insurance or health insurance funding agreement, where insurance certificates or contracts are not issued to and owned by individuals,

---

except to the extent of any life insurance or health insurance benefits guaranteed to an individual by an insurer under such funding agreement.

See, e.g., N.J.S.A. 17B:32A-4.

<sup>18</sup> This restriction on coverage for unallocated annuities being available to contract holders but not individuals is based upon the theory that there is no contractual guarantee by the insurer to specifically identified individuals under such contracts. Differences among various parties over coverage for unallocated annuities resulted in variation among the various states with respect to life-health association protection for these products. In 1991, with the insolvency of Executive Life Insurance Company, a large issuer of guaranteed investment contracts (“GICs”), many of which were held by pension plans, including those with large corporations such as Xerox, Honeywell and Unisys, the dispute with respect to coverage for unallocated annuity contracts for individuals came to a head. Executive Life’s insolvency resulted in a number of lawsuits and administrative proceedings relating to life-health association coverage for GICs. Plan sponsors instituted litigation in order to fulfill their fiduciary duties to contract holders pursuant to the Employee Retirement Income Security Act of 1974 (“ERISA”). Examples of such litigation are represented by the following cases: Board of Trustees v. Maryland Life & Health Guar. Corp., 642 A.2d 856 (Md. 1994) (utilizing liberal construction provision, Court of Appeals holds that GICs are covered annuities under guaranty association act, but remands for lower court determination as to whether annuity features of contracts are to be enforced); Unisys Corp. v. Pennsylvania Life & Health Ins. Guar. Ass’n, 6678 A.2d 1199 (Pa. Cmwlth. 1995) aff’d per curiam, 684 A.2d 546 (Pa. 1996) (GICs held covered annuities under Pennsylvania Guaranty Association Act and Association is deemed responsible to cover plan participants who are Pennsylvania residents on a pass-through basis); Bennett v. Indiana Life & Health Ins. Guar. Ass’n, 688 N.E.2d 171 (Ind. App. October 21, 1997) (No. 49AO4-9605-CV-168) (Indiana Court of Appeals finds that pension plan participants are “beneficial owners” of GICs held in trust for their benefit and that the Indiana Guaranty Association is obliged to cover GICs on a per-resident participant basis); Krahling v. First Trust Nat’l. Ass’n, 944 P.2d 914 (N.M. App., July 7, 1997), cert. denied, 942 P.2d 189 (N.M. 1997) (GICs are not annuities within the definition of the New Mexico Guaranty Association Act and, hence, there is no coverage for Executive Life GICs because the contractual obligations are owed to a Minnesota Trustee, rather than to individual plan participants); Arizona Life & Disability Ins. Guar. Fund v. Honeywell, Inc., 187 Ariz. 146, 927 P.2d 806 (Ariz. Ct. App., 1996), vacated summary judgment, aff’d, S.Ct. No. CV-96-0381-PR 1997, WL 570837 (Sept. 16, 1997) (Arizona Supreme Court vacates the Court of Appeals decision and finds that Executive Life GICs are covered annuities relying in part on provisions of the Honeywell retirement plan to find that the contracts contained life contingency); Unisys Corp. v. Olsen (Case No. 97-85841), aff’d Unisys Corp. v. Comm’r of Ins., 1999 WL595067 (Mich. App. August 3, 1999) (the court rejected the “beneficial ownership” argument and found that Executive Life GICs were unallocated annuities owned by a nonresident plan trustee and not entitled to coverage by the Michigan Guaranty Association).

<sup>19</sup> For example, the New Jersey Life and Health Insurance Guaranty Association Act provides coverage to persons who, regardless of where they reside (except for nonresident certificate holders under group policies or contracts), are the beneficiaries, assignees or payees of persons covered as owners of or certificate holders under policies or contracts, or in the case of unallocated annuity contracts, to persons who are the contract holders and who are resident or

---

nonresident but only with regard to nonresidents if the insurer which issued the policies or contracts was domiciled in the state where a life-health association exists; those insurers never held a license or certificate in the state in which the person seeking protection resides and those states have associations and coverage provisions with respect to residency similar to the association created by the New Jersey statute and those persons are not eligible for coverage by associations in their own states.

<sup>20</sup> The health insurance account also includes long term care policies.

<sup>21</sup> For instance, in June 1994, Investors Equity Life Insurance Company, a small insurer licensed only in the state of Hawaii and selling primarily deferred annuities, was placed into liquidation in December 1994. The Hawaii Guaranty Association was the only life-health association affected by the insolvency and, thus, faced substantial capacity problems in funding the approximately \$150 million in liabilities to Investors Equity policyholders. Pursuant to the terms of the Hawaii Life and Health Insurance Guaranty Association Act, the Hawaii Association was required both to pay claims when they arose and to continue coverage for the benefit of policyholders. The only sources of funding remaining available for coverage were: remaining estate assets (potentially \$50-60 million, and these assets were not necessarily liquid); assessments of members licensed to write in Hawaii; and an arrangement with Hartford Life Insurance Company, a carrier that ultimately assumed some of Investors Equity's business. Hartford agreed to credit enhancements made by the Hawaii Guaranty Association directly to policy values based on the amount, timing and application of payments of the estate assets and contributions from the Hawaii Guaranty Association which were received by Hartford. When this funding still resulted in a substantial shortfall, in particular in the annuity accounts, the Hawaii Guaranty Association borrowed from its life and disability accounts to satisfy the annuity obligations. Through this borrowing, the Hawaii Association was permitted to satisfy the deficiency in its premium assessment base in one account by borrowing capacity from another account. The borrowing was eventually repaid with interest, as the borrowing account was replenished with future assessments. See William P. O'Sullivan, "Key Developments in the Life and Health Insurance Guaranty System: 1993 to Present," Insurer Insolvency Revisited: 1999 at 12.

<sup>22</sup> Pursuant to N.J.S.A. 17:30A-16a, and subject to rules or orders of the Commissioner, member insurers are permitted to recover, over a reasonable length of time, a sum reasonably calculated to recoup assessments paid by member insurers pursuant to N.J.S.A. 17:30A-8, by way of a surcharge on premiums charged for insurance policies. Member insurers are required to recoup assessments within two years of the date they are paid. See N.J.S.A. 17:30A-16. In certain other jurisdictions, the impact of the statutory assessments upon solvent insurers is sometimes addressed in the form of rate relief or premium tax offsets.

<sup>23</sup> There is pending legislation which, if passed, will increase this limit to \$250,000, in keeping with the current NAIC Model. See New Jersey State Assembly Bill No. 3420 (or identical Senate Bill No. 2793) introduced on November 13, 2008.

<sup>24</sup> Very often, continuing coverage obligations of the life-health association are satisfied by transferring the policies of an insolvent insurer (including the policies of those who might otherwise be considered uninsurable) to a solvent insurer. In appropriate circumstances, life-health associations have continued coverage obligations and retain the policy obligations for their own account. Continuing coverage obligations of life-health associations are generally coordinated by NOLHGA.

---

<sup>25</sup> Moreover, the New Jersey Property-Liability Insurance Guaranty Association is obligated to the extent of “covered claims” incurred prior to or (at most) 90 days after the determination of insolvency. See N.J.S.A. 17:30A-8(a)(1).

<sup>26</sup> If a member insurer of the New Jersey Life and Health Insurance Guaranty Association is considered an impaired insurer, whether domestic, foreign or alien, and that insurer is not paying claims in a timely fashion, then, subject to the preconditions noted above, the Association shall, in its discretion, take one of the following actions:

- (a) take any of the actions specified with respect to an impaired domestic insurer;
- (b) provide substitute benefits in lieu of the contractual obligations of the impaired insurer solely for health insurance claims, periodic annuity payment, death benefits, supplemental benefits and cash withdrawals for policy or contract owners who petitioned therefore under claims of emergency or hardship in accordance with standards proposed by the association and approved by the Commissioner. Under certain instances, the Guaranty Association may provide more extensive coverage or guarantees if the additional coverage is a so-called essential element in allowing a rehabilitation plan to succeed as determined by the Commissioner in a competent jurisdiction.

N.J.S.A. 17B:32A-7(b)(3)(a).

<sup>27</sup> See N.J.S.A. 17B:32A-7(c)(1).

<sup>28</sup> This \$300,000 limitation does not apply to a covered claim asserted against the New Jersey Property-Liability Insurance Guaranty Association if that claim arises out of insurance coverage mandated by N.J.S.A. 39:6A-4, *i.e.*, no fault personal injury automobile insurance. As to such claims, the Commissioner may, by order, require the Association to treat all or a portion as if it were incurred prior to or after the determination of insolvency, but before the policy expiration date or the date upon which the insured replaces the policy or causes cancellation, and otherwise qualifies as a “covered claim” under the New Jersey Property-Liability Insurance Guaranty Association Act. In the case of benefits payable pursuant to N.J.S.A. 39:6A-4, the Association is liable for payment of benefits in an amount not to exceed the amount set forth at N.J.S.A. 39:6A-4.

<sup>29</sup> The broad language at N.J.S.A. 17:30A-8(b)(4) and (5) enabling the New Jersey Property-Liability Insurance Guaranty Association to negotiate and become a party to such contracts as are “necessary to carry out the purposes of the act” and “to perform such other acts as are necessary or proper to effectuate the purposes of this act” may, however, be asserted to provide the basis for such an expansive role.

<sup>30</sup> The final liquidation of Integrity Insurance Company has been over twenty years in the making, and is still pending. The Company was declared insolvent and placed in liquidation by Order dated March 24, 1987, several months after the Superior Court of New Jersey, Chancery Division, Bergen County, issued an Order on December 30, 1986 placing Integrity, a New Jersey domestic insurer, in rehabilitation. More than 17 years after the declaration of insolvency and institution of liquidation proceedings, the liquidation court formally approved a Final Dividend Plan (“FDP”) in August 2004, which granted the Liquidator’s motion for approval of the FDP and upheld the liquidation court’s opinion with respect thereto. Since 2004, the FDP and a subsequent plan, called the Liquidation Closing Plan (“LCP”), have been the subject of extensive litigation. The LCP requires that all claims be incurred and reported as of June 30, 2009 and that all proof of claims be filed by September 30, 2009. Thus, the estate is not yet wound up.

---

<sup>31</sup>Note that the insolvency of Executive Life has been the subject of complicated restructuring transactions involving the sale of books of business and guaranty association policyholder enhancements, as well as litigation almost since its inception in 1991. That estate is also not yet closed.

<sup>32</sup> Pacific Standard Life Insurance Company was domiciled in California and sold primarily life and annuity products. As a result of a speculative investment portfolio, poor asset management and strife with its parent company, the Company was placed into rehabilitation in December 1989. The life-health associations ultimately proposed an alternative rehabilitation plan to that proposed by the rehabilitator, which was ultimately approved in early 1994. Under the life-health associations' plan, a liquidation trust was established to support an assumption reinsurance transaction between Pacific Standard, the life-health associations and the Hartford Life Insurance Company. The plan uniquely provided for the estate's illiquid assets to be placed in the trust, allowing for an orderly liquidation to maximize their potential values rather than disposing of them at below market prices.

<sup>33</sup> Kentucky Central Life Insurance Company was ordered into rehabilitation on February 12, 1993. The receiver sought an order of liquidation, but without a finding of insolvency so as to avoid triggering life-health association coverages in most states. In response to the receiver's plan, NOLHGA, through a separately created task force dedicated to Kentucky Central Life, developed a supplemental benefit package designed to mitigate the burdens imposed by the policy restructurings and to comply with the statutory obligations of each of the participating guaranty associations. The benefit package was ultimately memorialized in the form of a Participation Agreement between the impacted life-health associations (those with covered persons in their state of domicile), NOLHGA, the receiver and Jefferson-Pilot Life Insurance Company with whom the receiver had contracted for the assumption of Kentucky Central's insurance policies.

<sup>34</sup> Confederation Life Insurance Company was a large Canadian insurer which became subject to receivership proceedings in Canada in 1994, along with its financing affiliate, Confederation Treasury Services, Ltd. Simultaneously, the U.S. branch of Confederation Life was placed into receivership in its port of entry in Michigan, and an affiliated insurer, Confederation Life Insurance and Annuity Co. was placed in rehabilitation in Georgia. The combined insolvencies of the Confederation Life-related companies were certainly among the largest to date. Each of the 52 state life-health associations had a significant financial stake in these proceedings and, thus, participated in a liquidation plan in 1996. The underlying structure of the plan was built on securing a new solvent insurer for each big block of policyholders, with the funding coming from estate assets, reinsurer enhancements and life-health association support of covered obligations, as well as with legal and financial protections for policyholders and associations, both as to assets and to liabilities. See William P. O'Sullivan, "Key Developments in the Life and Health Insurance Guaranty System: 1993 to Present," Insurer Insolvency Revisited: 1999 at 12.

<sup>35</sup> Executive Life Insurance Company issued multiple guaranteed investment contracts and other contracts to assist in funding employee pension plans. The plans, the plan sponsors and the employees had claims against the estate's assets.