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Date: February 1, 2005
Time: 10:16 a.m.
Room: LOB, Room 102

The Senate Committee on Banks and Insurance held a hearing on the following:

SB 74 making certain technical changes in the insurance laws.

Members of Committee present: Senator Flanders
Senator Roberge
Senator Barnes
Senator Odell
Senator Foster
Senator Gottesman

The Chair, Senator Robert B. Flanders, opened the hearing on SB 74.

Senator Robert B. Flanders, D. 7: I am the prime sponsor of SB 74 and I put this in on behalf of the Insurance Commission, who asked me to sponsor this bill for technical changes. With that, I'm going to recognize the Insurance Department to explain their bill. I'm sorry, Representative Hunt is here. I'm sorry. I didn't see you. Co-sponsor Representative Hunt. I will open the hearing with Representative Hunt.

Representative John Hunt: Thank you, Mr. Chairman. Greetings to the Committee. Thank you for the opportunity to introduce this legislation.

SB 74 is making technical corrections. Obviously, we don't like to call these legislations housekeeping because sometimes housekeeping can be very dirty business. In this case, there is an issue that has come up and all I can say to the Committee is that this actually was a little bit of news to me, involving re-insurance on the converting market. Seeing we don't want to be disruptive to the market place, I think it is an opportunity for us to sit down with the parties and try to sort through it.

The most important piece that I would like the Committee to know is that obviously The Home Insurance has been an ongoing issue for this state. As a matter of fact, when I first got on the Commerce Committee eighteen years ago, The Home Insurance situation was just being created. So, it has been around seemingly for my entire political career relative to insurance and it seems like it might be around here for another eighteen years.

What I want you to know is that we need to take a much more global view to the situation and not be focused on just this one company and this one instance. We need to be careful and think about other companies that might be in the same business. We want to make sure that we don't disrupt the market place and that whatever we do has the foresight to do what is best for New Hampshire and our constituents.

Senator Robert B. Flanders, D. 7: Any questions of the witness? If not, thank you for your testimony. I don't know how many saw the paper this morning, but Travelers has now been bought by Met Life. I don't know how many saw that this morning. I thought that was an interesting development, Travelers being one of the bigger and better companies in the past. Deb O'Loughlin from the Department.

Deborah O'Loughlin: Good morning, Senators. My name is Deb O'Loughlin. I am the legal coordinator for the Insurance Department and I think what I am going to do is walk you through the different sections of the bill to tell you what we intended. But, what I am going to do, because of testimony and issues, I am going to leave section five for the end of the discussion because that is probably the section of the bill that has the greater majority of issues associated with this.

Section number one of the bill is only correcting an incorrect cite. If you go into the Board of Medicine statute, RSA 329, they reference an insurance statute, RSA 420-J and they reference paragraph seven. When you go into the language, you realize that you are reading the incorrect cite. So, we are changing it so that the cite is correct. It should be paragraph eight and that is the intent of that particular section of the bill.

Section two of the bill talks to electronic fund transfers. The State likes it when the different departments have the funds sent to the State through electronic fund transfers. It is much easier for the State of New Hampshire to collect the revenue. This is specific to the premium tax. We came in a few years ago and said, "Okay, we didn't have electronic fund transfers. We want to have them now." We set it up so that the insureds, if they have premium debt to the State of New Hampshire of over $100,000 or more, would make it through electronic fund transfers. Other states in New England are starting

to drop that from the $100,000 down to $40,000 and so on. What we are trying to do is create a gradual step down so that, by the year 2006, any premium tax that comes due, that would be $40,000 or more, would be done through electronic transfers. What we didn't want to do is have it happen instantaneously because we want to give companies, particularly the small companies that we might have as New Hampshire domestics, the chance to get on line for electronic fund transfers. All of our larger companies today are doing it through electronic fund transfers. It is easier for the State; it is easier for them. So, that's what section two is in reference to.

Section three talks about premium refunds, particularly more towards property and casualty than anything else, but what it is trying to do is clarify the provisions under premiums and refunds that, when they are due, that the insurer refunds to the individual in different instances that are delineated under the law. We are saying now to the insurer that, if you have a refund due that is $15 or less, you're not necessarily required to make that refund; however, you must notify the individual to which that $15 is part of their refund, to let them know. If that individual wants their $15 paid to them, that the insurer must make that payment. But, I think it is just trying to clean up language that was a little bit ambiguous about how premium refunds are intended to be made and the party shall be credited, either on their account or they can receive a check or whichever way the consumer intends to receive their premium refund.

Section four and Mr. Roussos and I were having a conversation about this section earlier. Section four is a provision in our liquidation and rehabilitation law that was intended to allow what they call pass through or cut throughs on reinsurance contracts. Mr. Roussos and I do have some gentlemen here with me who can talk to this better than I can. We have realized that there may be a change we need to make to the language, so I would like the opportunity to work with Mr. Roussos to come to some agreed upon language for section four and come back to the Committee with an amendment that will address that particular issue.

I am going to skip over section five and I am going to take you to section six, which deals with the producer licensing law. The producer licensing law was put in place numerous years ago now and we followed the NAIC model and we varied in one instance and we varied in 402-J:17, II where it said that we have put in fifteen days for pre-trial hearing date that a producer has to report any criminal prosecution, whatever. The great majority of the other states are adopting the model with the thirty day provision, which is in fact what is in the NAIC model. So, we want to align ourselves with the model and change the fifteen days to thirty days so that we are in line with the other states and also with the model.

Section seven, you're going to see, I believe Senator Flanders has SB 78 that will be coming up at a later date. I believe it comes up next week. It talks to prompt payment and such from insurers. What we are trying to do in this particular section. Excuse me. This is the one. I'm messing up my sections here. Section seven is dealing with grace periods. We have had this conversation, I think, numerous times over the years as to a grace period being allowed an insured to pay to an insurer and we have had instances where a grace period has been granted by the insurer to an insured and ultimately the insured does not pay. Then you find that employees go to file a claim and they are not getting their claims paid. What we're trying to do here is say that there is a thirty-one day grace period and, after that, the insurer has to make the determination whether to continue down the line and, if they do, the insurer is on the hook for any claims that come in in that time period so that the consumer or the individual employee receives payment of their claim. I'm sure there will be further discussion of that item within this group.

Section eight is the one that addresses the overdue payment. This is the one that is talking of prompt pay, which I believe is also going to be addressed in SB 78. The only item that the Department is taking on in this particular section is the topic of interest on a late payment from an insurer. We just wanted to make it clear that, when a claim is due or payment is due, it is due and interest stops on the point when the payment is due. So, there is no question as to should an insurer be paying interest on a claim and when does that time period start. So, all we're trying to do is just clarify that section of the law.

Sections nine, eleven and twelve deal with grievance procedures under managed care. We brought this before the Legislature last year or the year before, somewhat unsuccessfully. What we're trying to do is require that when a grievance procedure and the appeals process is, when an individual is going through the appeals process, that the practitioner or the doctor, whoever, that is looking at the appeal has some expertise in the field to which the appeal is being made. It is my understanding that the NCQA, which is an accreditation team that accredits the insurers, requires that a professional in a particular type of treatment or health problem is required by NCQA in the grievance processes. So, what we're trying to do is put into the law in the three separate sections the fact that, if you are bringing an appeal, the person looking at the appeal has to have some type of similar credentials to the condition or the health problem that is being brought in the appeal.

Section ten is correcting a typographical error in our title insurance code. When we were changing the law under the rating laws a couple of years ago,

we noticed that the term of this section was still left in the law and it has absolutely nothing to do. This section, by itself, stopping there, refers itself back to previous provisions under the law. So, we're just having the cap.

Section thirteen adds a new paragraph to the rating law which would enable the Commissioner to obtain information from an insurer for purposes of monitoring and maintaining a competitive property and casualty market. As you may remember, a few years ago, we put in a brand new rating law that is to try to open up competition in the market. What it does is, instead of sending in rates, the insurers are able to file rates in certain instances where they can begin to use them. We are checking the rates for viability in the market and the competitiveness in the market. One of the things that was missing from the bill is the tools we need to make that assessment as to whether there is still a competitive market. What this is intending to do is to say that the Commissioner can ask the insurers to provide him with documentation so that the Department is able to make an assessment as to whether a competitive market is being maintained and whether or not we need to look at anything going on in the market or do a more in depth study if particular rates are being filed by the insurer.

David Withers is also here today, so if you want to ask particular questions about the rating and how it applies, he is the Department's property and casualty actuary and he can answer a lot more of those questions than I can.

Section fourteen is also something that Mr. Withers can address for you to a degree. It is talking to workers comp and requiring that insurers writing workers comp in a voluntary market file opting not to use the rates that were filed by the NCCI filed with the Commissioner their rating information for approval. Mr. Withers can go into that more if the Committee would like to discuss that.

Section fifteen also addresses workers comp and basically says that, if an insurer is offering coverage at a rate higher than that proposed in the assigned risk plan, they need to make a notification to that insured. We have had instances where an employer would choose to stay with a company that is rating at a higher rate than what is in the assigned risk plan because they feel that the benefits to them are greater. But, we just want them to be aware that they do have the option of going into the assigned risk plan at a lower rate than what is being offered by the insurer.

Sections sixteen and twenty talk to the purchasing alliance law that was passed in 2000. The purchasing alliance law would enable small employers to band together to purchase small group insurance. To date, we have not really had anybody approach the Department saying they want to form a

purchasing alliance until very recently. There has been some talk about this. What happens, however, is when the purchasing alliance law was put into legislation; it was also put in with a sunset provision that would make the purchasing alliance expire January 1, 2006. What we are hoping to do, because of all the items that are going on now with regard to small group and large group health insurance, is to enable the purchasing alliance law to stay on the books beyond January 1, 2006 so that if, as we proceed forward on the issues of SB 110 and all the other things associated, there is this option that is left out there.

Section seventeen and I think Senator Flanders is aware of this particular issue. It deals with administrative rulemaking. When the Department goes before Administrative Rules we have a lot of rules that are given to us by the NAIC as a companion piece to a law that may have been passed. A few years ago, we approached the Legislature to give us an exemption from the drafting provisions of administrative rulemaking. We have that exemption in place. Over the last year or so, we have found, as we bring these rules in to the Administrative Rules process, there are instances where, while we are trying to meet a national standard, we are running afoul of some of the provisions of the administrative rules laws. Representative Patten, as Chairman of the Administrative Rules Committee, over the last couple of years had asked us to put together some legislation that would give us an exemption for when we are using an NAIC model only so that we will not continue to run afoul of the administrative process. We are not asking for an exemption from going through the administrative rules process and I want to make that very clear. We intend to go through Administrative Rules; we hold our public hearings and so on. This would be an exemption from certain provisions in the drafting of the rules that are currently running us afoul and I think Senator Flanders can attest to how many times we have come across this. It is only when we are using an NAIC model and not if we are bringing in a rule that the Department has written of its own.

Section eighteen is intended to close the loophole in the insurance laws that enable certain insurers to secure health insurance outside the traditional market. We have a section in the law that is called, deals with purchasing insurance basically in the surplus lines market and an industrial insured is primarily the insured that would be going to purchase coverage in the surplus lines market or an untraditional market. What we have found is that up until this point, that law, I think or we all interpreted the law, to mean that it would deal with special coverages. That if you have a plant that has a special need requirement and you need to get specific insurance just for that, you have the ability to go out and purchase these surplus lines and it is not an illegal purchase of insurance. What we are doing is putting in an amendment in the law that excludes access to health insurance. The law

currently excludes access to life coverages and we have found that as the market tightens up and the issues surrounding SB 110 that employers are looking to this industrial insured access and are now looking to purchase health insurance outside of the traditional market. The Department feels that that is probably not something that we want to allow because, as employers will cross over to purchase outside the traditional market, they are weakening the pool in the large employer pool. So, we want to exempt, along with life insurance that is already exempted, to add that health insurance is also exempt from that type of a purchase, that we need the numbers in the pool to continue to make it work.

The last section repeals the guarantee issue provisions for individual health insurance policies when a party is eligible for group coverage. It is kind of a redundant item in the statutes right now and individuals have access to group coverage so that the guaranteed issue does not need to be there or they have access to other types of policies.

That's primarily it. I will go back to section five, which is the issue under the rehabilitation and liquidation statute and what it is intended to do is to clarify payments to claimants in a lower priority class that assists or results in the collection or recovery of assets or property for the benefit of claimants in a higher priority class as administrative cost. I think probably the greater majority of your discussion will be on that issue today. But, I would like to address any other questions you might have surrounding other sections of the bill first and then we can get into that portion of the bill, if that is okay with the Chairman.

Please see Deb O'Loughlin's "Amendments to Senate Bill 74", attached hereto and referred to as Attachment #1.

Senator Robert B. Flanders, D. 7: Senator Barnes?

Senator John S. Barnes, Jr., D. 17: Thank you, Mr. Chairman. I have two questions. Did I hear you say section nine was something that was brought in front of the Legislature last year?

Ms. O'Loughlin: Yes. I don't know if it was last year. It could have been the year before, Senator Barnes. Sections nine, eleven and twelve of this particular bill are repeat provisions that we thought were good for the consumer in the last session and all those provisions did not make it through the Legislature and we are bringing them back.

Senator John S. Barnes, Jr., D. 17: Have they been changed since the last time you brought them?

Ms. O'Loughlin: The provisions have not been changed. The language is roughly the same as what we had in the prior legislation.

Senator John S. Barnes, Jr., D. 17: Okay. Second question, if I may, Mr. Chairman.

Senator Robert B. Flanders, D. 7: Follow up.

Senator John S. Barnes, Jr., D. 17: Section fifteen. Did I hear you mention that that was not going to have any impact on maybe what comes up with SB 110 and the changes that might be made with SB 110?

Ms. O'Loughlin: Section fifteen is actually addressing workers comp and what it does is state, and I don't know if that is the section you wanted. I think you might mean the purchasing alliance section, sections sixteen and twenty.

Senator John S. Barnes, Jr., D. 17: Sixteen. I stand corrected.

Ms. O'Loughlin: The purchasing alliance law was put on the books in 2000 and what it was intended to do at that time was enable small employer groups to band together to purchase coverage. We have not had, up until very recently, there was a lot of talk at the beginning and then it kind of died down and recently we have had some talk that there are a few groups that are interested in forming purchasing alliances. Unfortunately, when the purchasing alliance law was passed, it was passed with a sunset provision. All we're really requesting is that that sunset provision be removed so that the opportunity is there for small employers to band together and the purchasing alliance to move forward.

Senator John S. Barnes, Jr., D. 17: Thank you very much.

Senator Robert B. Flanders, D. 7: We have SB 66, which hasn't been scheduled yet, which is establishing a committee to study creation of a northern New England purchasing alliance. That hasn't been scheduled. So, that is in the works.

Senator Gottesman?

Senator Joseph A. Foster, D. 13: I just have a follow-up question. Representative Dickinson has a bill on purchasing alliances. Are you familiar with that? Does this impact that in any way?

Ms. O'Loughlin: No. We thought originally that it was the same thing, but in actuality, Representative Dickinson's bill is talking to associated health plans, I believe, which is something that the Insurance Department and the State have not put their arms around because it takes away some of the protections that the state laws have for the individuals that are part of that group. We have not had a discussion with Representative Dickinson, but it sounds like it is the same thing, but it is not the same thing.

Senator Joseph A. Foster, D. 13: Thank you.

Senator Robert B. Flanders, D. 7: Senator Gottesman?

Senator David M. Gottesman, D. 12: Thank you, Mr. Chairman. I have many questions, mostly out of ignorance, so if you would just bear with me. My first one is on number three where you said something about not giving a refund if the premium is $15 or less, but you would be willing to notify them that they can get their money back. I would assume that to notify them to get their money back, why not just give them their money back?

Ms. O'Loughlin: That's a very good point. This came from our property and casualty filing division and I don't know if it has been a problem. I don't know that it is assumed that this money would be applied against other monies that were owed or whatever. I would like to go back and ask that question myself, Senator Gottesman. I have David Withers who can possibly answer that, so why don't you sit here and help me with that one, Mr. Withers. Mr. Withers is our property and casualty actuary from the Department. Go ahead.

David Withers: It is quite standard nationally to have a larger waiver of premium for return and additional premiums when changes are made to policies. New Hampshire's rule right now on return premium is a dollar and in nearly every other state or many states are ...(inaudible)... The insurance industry, insurance companies, tend to program their systems to automatically return premium amounts larger than a dollar. We are enforcing that. We are requiring companies to change their systems to put in a difference for New Hampshire to make it a dollar. That creates extra expense on the insurance companies, which is an extra expense. I guess our opinion is that, when the new declarations, the adjustment is made, the insured is notified anyway. So, that is not an extra expense that is being added to the company. The policyholder gets the amendment and there will be a notice in there that says your premium, you are entitled to X dollars in refund. Just call us or send in something and we will send it to you. But, there is a cost differential and that extra expense. So that is the reason. $15 is a fairly common practice. It becomes particularly problematic on

commercial lines policies where the premium sizes are in the tens of thousands of dollars and we are requiring a refund of $1.22 if it comes out that way or something like that.

Senator Robert B. Flanders, D. 7: Follow up?

Senator David M. Gottesman, D. 12: If you could just go back up to 3-I, where it says in bold the original policy to be cancelled, should there be an "or" after that?

Ms. O'Loughlin: Yes.

Senator David M. Gottesman, D. 12: So, you either get the policy back or these other things. Right?

Ms. O'Loughlin: Yes.

Senator David M. Gottesman, D. 12: On number three again, under paragraph three, it talks about for any refund that is given and then, in the second line, it talks about giving interest to people at the legal rate. Do you know what the legal rate is defined as anywhere in the State of New Hampshire?

Mr. Withers: We can get back to you on that. I believe it is in the statute somewhere. I think it somehow changes every year.

Senator David M. Gottesman, D. 12: I just didn't know. Under paragraph six, you're changing the fifteen to thirty days. If a person has committed a crime in another jurisdiction, wouldn't we want the notice to be as short as possible so that our consumers would be protected instead of going to what the standard is of thirty days?

Ms. O'Loughlin: We do. But, what I think, what's happening is that we are basically saying that it is thirty days of the initial pre-trial hearing date. I think what they are saying in this is that, if an action is brought against you in another state, you have to notify us within thirty days. That doesn't mean that the final action has been taken. We just need to know that an action has been begun so that we are put on notice that there is something that we should be looking at or following. So, I think that is what...

Senator David M. Gottesman, D. 12: Follow up?

Senator Robert B. Flanders, D. 7: Yes.

Senator David M. Gottesman, D. 12: In the paragraph before that, it is talking about another administrative action against the individual in another state and you are changing that from fifteen to thirty days as well.

Ms. O'Loughlin: Correct. I think, though, when you're talking administrative action, you're talking a non-criminal action. It would be a state taking an action against an individual. So, I think it was to enable the individual to produce documents and get them to us. We have, and I think probably something that we have available to us is the NAIC, the clearing house at this point in time for producers and we have a check and balance system that kind of goes on between these partners. Everything that the Department does goes up to the NAIC relative to producers or whatever. So, we are getting information on actions other states may be taking at any given point in time.

Senator David M. Gottesman, D. 12: Follow up, Mr. Chairman?

Senator Robert B. Flanders, D. 7: Yes.

Senator David M. Gottesman, D. 12: On paragraph eight, doesn't this take away the notice provision to the insurer by striking out the language that we're talking about here?

Ms. O'Loughlin: I think this is the section of prompt pay. Section eight?

Senator David M. Gottesman, D. 12: Yes.

Ms. O'Loughlin: I believe what we were trying to do is take away a delay, I guess, in paying a premium when it is overdue. If the health care provider wants to make a notification in writing to the insured that the claim is overdue, they may. But, we're taking away the requirement that they have to notify the insured because I think, up to this point, what has been happening is the insurer says, "Well, I don't have to pay that until I get a notice from the provider". I think what we're trying to say, is, "Whether or not they notify you and that claim is due, you need to make the payment".

Senator David M. Gottesman, D. 12: Follow up, Mr. Chairman?

Senator Robert B. Flanders, D. 7: Go ahead.

Senator David M. Gottesman, D. 12: On nine, eleven and twelve you changed the definition of the person who is going to review to essentially a practitioner who typically and currently treats that condition or health problem or a person with similar credentials and licensure. Is there supposed

to be a difference in the two, say, between nine and eleven? In eleven, the credentials aren't in there. Credentials and licensure. I guess, as a follow up, a doctor who has a license to practice medicine and who typically treats a particular condition. Is that person qualified just because they are not board certified as perhaps another doctor would be who is board certified?

Ms. O'Loughlin: I believe that when we're talking about these issues, you're talking to the industry that has to meet the NCAQ standards and they have certain individuals or whatever that they have to qualify to their plan. So, I would say that you're talking to kind of like a specific group of physicians that would be dealing with the issues. I think what happens today is I make an appeal on the first level of the appeal, a physician that not necessarily is qualified to treat the condition or that normally would treat the condition or the health problem is sometimes used by the carrier to take a look at the appeal. All we're trying to do is say in those instances, on the first level grievance appeal, you should be using physicians that, if it is a gynecological issue, we don't want to see a podiatrist doing the appeal and that kind of thing. I have checked with our consumer people and we have instances where we have had one, two, three, four, five, six, seven issues of appeal and only one insurer is currently using somebody that has the same medical expertise as the appeal that is being brought to review. Others are using a wider variety.

So, I think that is all we're trying to do for the consumer, to give them some kind of security that a physician that normally would treat this is sitting on that appeals board taking a look at the appeal.

Senator David M. Gottesman, D. 12: Follow up, Mr. Chairman?

Senator Robert B. Flanders, D. 7: Yes.

Senator David M. Gottesman, D. 12: Under paragraph thirteen, it says that you are to be given what you ask for. Do you have subpoena power under your present rules? If you don't, would you like it?

Ms. O'Loughlin: I believe we have it in general. I would have to go back and check the statute. It might be under the 400-A section if we were to bring somebody in. I think what we intended, and Mr. Withers can address this more because this talks to the rating law, which was to be able to obtain material information that lets us monitor the competition the way we need to. I don't know if you want to add. The rating law, we didn't necessarily say, "while you're at it, please provide this, this and so on." So, we can't make a complete judgment as to whether the competition and the market place is operating the way it should. I don't know in this instance whether

we would need subpoena power, but I will go back and check that and let you know.

Senator David M. Gottesman, D. 12: Okay. One more follow up?

Senator Robert B. Flanders, D. 7: Okay.

Senator David M. Gottesman, D. 12: Under number fourteen, the definition for what is appropriate insurance is changing from what is just and reasonable and adequate for the risk to adequate, not excessive, and not unfairly discriminatory. Can you please address that for me? The phrase adequate, not excessive, and not unfairly discriminatory are the three requirements that exist for all the other lines of business within the rating RSA 412, the standard terminology or the standards to which premiums are judged to be found acceptable by the Insurance Department, by the Commissioner. The words just, reasonable and adequate are the existing language just for workers comp. When we redid 412, we kind of left the workers comp section alone and this is an example of those phrasings. They are saying the same thing. They should have been lined up just the same as unfairly discriminatory. Reasonable is the same as not excessive and adequate is adequate.

Thank you, Mr. Chairman, for your indulgence.

Senator Robert B. Flanders, D. 7: Any other questions? If not, thank you.

Ms. O'Loughlin: Now, what I would like to do is to have section five addressed, I think, in a little more in depth look and I'm going to ask Eric Smith, who is with the firm of Rackemann & Sawyer from Boston and he is that Department's outside counsel for The Home Insurance. I would ask that he join me and give you testimony relative to section five so that it is clearly understood.

Senator Robert B. Flanders, D. 7: State your name for the record please.

Attorney Eric Smith: Eric Smith from the law firm of Rackemann, Sawyer & Brewster, counsel for the Commissioner of Insurance as a liquidator of The Home Insurance Company. The Department has asked me to speak here today.

Section five of the bill does two things. First, it just mentions, cross references Chapter 404-H, which is just a new recent section that had the guaranty association. So, that is just a cross reference.

Then the reason that the Department asked me to speak today concerning the additional sentence at the end in bold, which is intended to amend section C:44, which is the section that specifies the priorities that are applicable to the distribution of assets from the insolvent insurance company. If the insurance company is insolvent, there's not going to be enough assets to pay all creditors in full and the statute specifies a series of priorities. The amendment here actually is meant to clarify that payments that a liquidator may make to collect assets are not barred because those payments are made to lower priority creditors. This would assist in collecting assets for the benefit of the estate and that benefits, as indicated in the tag ending of the language, that is for the benefit of higher priority creditors.

The Department's view of the Insurers Reutilization and Liquidation Act in general is to see, to further the interests of policyholders, creditors, and the public generally and that is achieved through the priorities statute by giving the priority to claims of policyholders and this statute will enable to clarify whether to bring in assets to be distributed in accordance with the priority scheme and thus will benefit the higher priority creditors. This will not only benefit policyholders, it will also benefit associations which are paid many claims against insolvent insurance companies and thus, indirectly, will also benefit the insurers who are members of the guarantee associations and to pay the assessments designed to fund those associations to the extent there is a shortfall from the insolvent insurer.

The provision here, in our view, is neutral with respect to reinsurers. Debtors generally, but reinsurers in particular, as the matter arose in context of all liquidations and it avoids a windfall to them by essentially requiring and assisting the liquidator to make payments that will make him pursue assets and collect amounts that would have been paid if the insolvent's insurance company had not gone into a liquidation proceeding in the first place. So, it does not, it is neutral to the debtors and avoids a windfall to them.

It should also be stressed that this is a clarification in the existing law, the liquidator's view which has been sustained so far by the Superior Court, that this is what the law currently is, that these payments may be made consistent with the priorities scheme. This change does not, for that reason, this change does not somehow make New Hampshire an outlier, but it is consistent with the positions that have been taken by the National Association of Insurance Commissioners. In the amicus brief, they dealt with The Home proceeding so that this evidence is a consistent regulatory view across the nation. It is simply a clarification of existing law.

With that, I will close my remarks.

Senator Robert B. Flanders, D. 7: Senator Foster?

Senator Joseph A. Foster, D. 13: So this would have, in effect, retroactive application or prospective? What was the intention?

Attorney Smith: It would apply to payments made after its effective date and thus go to pending and any future litigation.

Senator Joseph A. Foster, D. 13: Follow up?

Senator Robert B. Flanders, D. 7: Follow up.

Senator Joseph A. Foster, D. 13: What I am trying to understand is. I do bankruptcy work and the liquidation type of issue, priorities in Chapter 11 and Chapter 7 cases. We have administrative costs and those tend to be costs incurred by professionals that obviously haven't been paid. They can't pay every priority holder's money at the end, court approval and so forth. So, what here are we talking about? Can you give us some concrete examples of what it is that we are saying? Normally, you wouldn't begin paying lower priorities first; you might pay professionals who are higher and not lower priority as court administrative costs. I'm trying to figure out how lower priorities could be administrative costs.

Attorney Smith: Okay. Well, it is not the lower priority as such. The payment to a creditor, to a lower priority claimant that happens to bring assets into the estate. One could have, for instance, contingent payments that are made, for instance, to lawyers and pursuing assets of the estate might get a percentage of the assets for insurance for collecting it. Real estate brokers who sell assets of the estate receive a percentage of fees. So, this kind of contingent payment is nothing unusual. It just so happens that you may have a case where a payment is made to someone who happens to be a lower priority creditor. The fact that they are a lower priority creditor should not disable them from receiving that payment.

Tape turned.

They have essentially no reason to spend client resources to file or prove their claims in the proceeding and they do not do so. Then the liquidator will not be able to seek reinsurance for those claims and bring in reinsurance to the estate. So, there would be effectively a low priority creditor who would not otherwise receive anything, not file a claim and thus, the liquidator is then able to pursue the reinsurance assets which would not become insolvent. The company would pursue it and would collect the monies for the estate. So,

here we have a situation where you have a substantial amount of money which could be brought into the estate to be paid to priority creditors, but would not be brought into the estate absent these payments.

Senator Joseph A. Foster, D. 13: Follow up?

Senator Robert B. Flanders, D. 7: Follow up.

Senator Joseph A. Foster, D. 13: I'm not sure I understood that. You're saying that the reinsurer. Explain, maybe some concrete ... It sounds like you are reordering things. Maybe that's what the common law is, I don't know, but for whatever reason, we are putting it in the statute so it is obviously not crystal clear (inaudible)... something else to people. I just don't understand.

Attorney Smith: Okay. Let me just explain the situation. The Home reinsured a group of insurance companies and, in turn, reinsured its exposure for those companies with another reinsurer. So, you have claims against The Home and filing based on claims that come in against the Home. If the claims are not made against The Home, they may not get paid.

Senator Joseph A. Foster, D. 13: They don't get paid?

Attorney Smith: Not in this particular instance because, if they were allowed in a liquidation estate, that would trigger the ability of The Home's liquidator to pursue reinsurance on these claims. So, there is the situation where, if the claim is not made into the estate and prosecuted at the point where they are allowed, the liquidator would not be able to pursue the reinsurance and bring in millions of dollars of reinsurance which should then be added to the estate and distributed to the priority creditors. So, it is the reinsurers, the persons whose claims we're talking about, are low priority and so are not subject to those claims.

Senator Joseph A. Foster, D. 13: One more follow up.

Senator Robert B. Flanders, D. 7: Follow up.

Senator Joseph A. Foster, D. 13: So, are we paying the administrative claimants under the reinsurers who are bringing the prosecuting claims or are we paying the reinsurance clients?

Attorney Smith: We are not paying claims; we would be making distribution of a certain percentage on the amount of reinsurance that is recovered with respect to those claims. In other words, it is a contingent payment, to the

extent that these claims, if allowed, permit the liquidator to actually collect monies from the reinsurer, The Home reinsurer, then a percentage of those monies collected would be paid to the claimants.

Senator Joseph A. Foster, D. 13: What percentage is that?

Attorney Smith: In this particular case, it is rather complicated, but roughly speaking, it is about 15%.

Senator Joseph A. Foster, D. 13: Is that by contract?

Attorney Smith: That is an agreement that is subject to review by the Superior Court and that litigation is ongoing.

Senator Joseph A. Foster, D. 13: So, it is a contingency kind of arrangement?

Attorney Smith: That's correct.

Senator Joseph A. Foster, D. 13: Thank you.

Senator Robert B. Flanders, D. 7: Any other questions? Yes?

Senator David M. Gottesman, D. 12: Mr. Chairman, thank you. If New Hampshire were to adopt this language, how many states would be in alignment with this direction?

Attorney Smith: Well, in our view, the states... That's two questions. The first is, do other states have this particular language in their statutes and the answer is no they do not. But, in our view, the other states, and it is supported by the National Association of Insurance Commissioners, which is the association of the chief regulators across the country who have filed an amicus brief in The Home case taking the position that The Home liquidators are taking and that is clarified by the statute. It is indeed what the existing law means. So, New Hampshire has not been outlined by adoption, but rather, just to clarify the position that the insurance commissioners nationwide have already taken.

Senator David M. Gottesman, D. 12: Follow up?

Senator Robert B. Flanders, D. 7: Yes.

Senator David M. Gottesman, D. 12: To just boil that down, New Hampshire would be the only state in the country that would have this position.

Attorney Smith: Correct. This particular clarifying language. That is correct.

Senator David M. Gottesman, D. 12: Just one more follow up, Mr. Chairman?

Senator Robert B. Flanders, D. 7: Yes.

Senator David M. Gottesman, D. 12: Isn't this, for lack of a better term, a gimmick to pay costs as administrative costs to force a reinsurance situation by people who are trying to avoid paying those claims?

Attorney Smith: It is a means of clarifying that the liquidator has the ability to collect from a reinsurer of The Home, who otherwise would get a potential windfall from The Home liquidation if The Home had not gone into liquidation.

Senator David M. Gottesman, D. 12: Thank you.

Senator Robert B. Flanders, D. 7: Any other questions? If not, thank you for your testimony. Obviously, I misjudged this. We had a little hearing yesterday on being a good chairman and I guess I failed. What I would like to do is recess this until after we hear the other two bills because we have a long way to go. I don't want to shorten anybody's testimony because I think there is a lot we need to know about this. So, with permission, I will recess SB 74 and get the people in from the hall and we will go to SB 111. Then, as soon as we get done these two bills, which I hope will be rather short, we will go back to 74. Thank you for your...

Hearing recessed at 11:03 a.m.

Chairman Senator Flanders reopened the hearing at 11:35 a.m.

Senator Robert B. Flanders, D. 7: The next speaker would be Paula Rogers, who is not present at this time, so I am going to go to George Roussos.

Senator John S. Barnes, Jr., D. 17: Mr. Chairman, for the record, I have a 1:00 hearing.

Attorney George Roussos: Thank you, Mr. Chairman and members of the Committee. My name is George Roussos, R-o-u-s-s-o-s. I am a lawyer in Concord and I appear representing several clients this morning. One is the Reinsurance Association of America, which is, as its name implies, a group of major (large and small) reinsurers writing business throughout the country including New Hampshire.

Mr. Chairman, I have offered a written statement that explains the concerns that the RAA has over the provisions of Section five and what effect they would have upon reinsurance markets and the disposition of insolvencies in New Hampshire generally.

Please see "RAA Statement in Opposition to SB 74", attached hereto and referred to as Attachment #2.

Also, the AIA, which is a property and casualty national trade association of what I will call the ACE companies, which is a group of insurance companies who are parties to the litigation that has been referred to earlier. With me is Pieter Van Tol, who is counsel to the ace companies in that litigation. Pieter is with the Lovells law firm in New York and he is up today to talk about some of the technical aspects of that litigation and how it relates to this proposal.

The American Council of Life Insurance also has expressed concerns that we will go into concerning Section five of this bill.

We were pleased at the comments of Representative Hunt that he does not want to be disruptive to the market place. That is our concern. We have heard testimony earlier by Mr. Smith about the position of the other states and the NAIC and I think he acknowledged that no other state has a provision like this. He went on to say that the NAIC has a policy consistent with what, I'm not quoting him exactly, but consistent with what this bill seeks to do. We respectfully disagree with that. We believe the NAIC has been clear. Its model is what we have in New Hampshire currently. The only talk there has been about changing it in the fashion proposed in Section five of this bill was a proposal made recently to a committee of the NAIC which was, as I understand it, rejected by the NAIC. So, we have a difference of view on the matter which is susceptible of proof one way or the other. But, I tell you, from our position, the NAIC does not approve this proposal.

I think that since there has been this discussion on the fringes about The Home Insurance liquidation and how this relates to it, it might be helpful to you to hear a little bit more about the liquidation and the litigation that is going on right now because, as I think the Department has implied or stated,

that is the reason we're here today is that it has to do with the pending litigation in The Home case. In that case, the court has faced the issue of whether you can call, as administrative fees, the payments to reinsurers that are proposed in The Home liquidation and that would be validated if this legislation were to pass. That is an open question in the courts. You might think that that is reason enough for the Legislature to leave it alone and let the courts rule on what the statute says, not change it in the middle of the course of some significant litigation.

The question, too, has arisen and we don't know the answer, but can we make this apply to pending contracts, existing contracts? There is an element of at least, we think, on fairness to doing so. Nobody bargained to have this treatment of the state when they wrote reinsurance contracts in the first place. We think there may be some constitutional issues and I'm really not sure. We haven't looked into that question.

So, I would ask Pieter, if you will, as counsel on the case, on behalf of the ACE companies, to maybe briefly describe the issues and where that stands as it relates to this legislation.

Pieter Van Tol: Good morning, Senators. Pieter Van Tol from Lovells. I think it is important to understand the context of what we're talking about here.

Administrative expenses, I will just point out, are typically things like paying professionals to come into a bankruptcy case or liquidation after there has been a liquidation or bankruptcy filed. What we have here is a plan by the liquidator to pay $72 million in order to give an incentive to claimants to file claims in the Home's liquidation, which will in turn trigger reinsurance obligations.

Now, the point was made earlier that you could, under a similar scenario, have a pre-petition or pre-liquidation creditor who also has a post-petition or post-liquidation claim. I would submit that is very rare. It may be a law firm that would be doing work beforehand and then maybe afterwards. But, this is a massive payment. It is in no way what you would normally conceive as an operating cost of the Home Insurance Company. It is a payment in order to encourage others to file claims. What it does though is it moves those lower creditors up to a very high ranking.

The NAIC has, in its wisdom, come up with a model and has not seen fit to accept any amendment like the one proposed in Section five because of the dangers that it would unleash. Imagine what would happen if this sort of deal were open to everyone. People would come in and say, "call mine an

administrative expense" and you would have people lining up at the door of the liquidator trying to cut these deals. You would have a massive increase in litigation within the liquidation which obviously reduces the amount that goes to the people who are harmed. In addition, it causes a vast amount of uncertainty.

Reinsurers know how this statute works from state to state and that is how they rate their policies and that is how they reinsure domestic insurance companies. If Section five were to be part of the piece of legislation and a bill that is signed by the Governor, it would wreak havoc on the reinsurance industry and what it would really do is harm consumers' insurance in New Hampshire because their insurance companies, the price of reinsurance would go up and they would pass that along to the consumer. So, if we look at the net benefit here, it is not going to benefit New Hampshire at all.

And, lastly, to Mr. Roussos' point about the state of litigation. Not only is this currently an open issue in the courts, it has been up to the Supreme Court once already and in our materials we included an exchange between counsel for the liquidator and the Supreme Court, which is very compelling, in which the Supreme Court cast some real doubts on whether they were going to accept this as an administrative expense.

Attorney Roussos: Excuse me. That's in the materials that I handed out as part of Pieter's testimony.

Attorney Van Tol: That would be in my letter, Senators, on pages three and four.

In sum, it is really a mischaracterization to call this a technical amendment. It is something that will... It is hard to overstate the importance of the impact it will have on the insurance industry.

With that, I have no further remarks, but would, of course, would be happy to take any questions the Senators may have.

Senator Robert B. Flanders, D. 7: Senator Foster?

Senator Joseph A. Foster, D. 13: A few questions, if I might, Mr. Chairman. Here's what I'm trying to understand. Were this a Chapter 11 case, of course, the bankruptcy trustee could file the claim on its own under the bankruptcy rules, which would let him do it if he saw fit for whatever reason to file a claim. What I understand here is that the liquidator would file claims against itself. The part I'm having a tough time understanding is why isn't

this going to fall to the other reinsurers? Are you saying that when they underwrite, they underwrite expecting a liquidation?

Attorney Van Tol: No.

Senator Joseph A. Foster, D. 13: I mean, is that part of the underwriting standards? It seems to me that it is gratuitous that, but for that happening, there would have been an expense.

Attorney Van Tol: That's an important question. What they do is rate based on where people usually fall in the ranking and the order of priority. The key to remember here is even that idea that there is going to be a windfall, it is litigated issue in the court case that is going on. It is not at all established that these claimants who the liquidators have given an incentive. It is not at all established that they wouldn't make those claims even without the incentive payment. In fact, the bar gate for claims was in June of this year. All the claimants were supposed to receive a payment, but have not gotten one guaranteed filed claims. Often claimants do that because, on the back, the reinsurers will reinsure. So, they will have a set-off claim. Also, it is not a major task to submit a claim. It is a short form. You can put one in. So, I have to back up and say that, as a matter of fact, this would be a hotly disputed fact whether there is even a windfall at all. So, we have to start with that proposition. So, we cannot assume that there is going to be a windfall for the insurers.

Now, what reinsurers do is they look across the country and they have a certain deal and they can figure out, on actuary studies, how much is usually paid out. It is not the case that they don't ever pay anything out. In fact, in the liquidation now we have claims that have come in and have been allowed by my client, the ACE companies. They have not been paid out because that's not the way due process works. But, we have to remove what's going on in this Home liquidation and look at what the impact is going to be nationwide.

Senator Joseph A. Foster, D. 13: Follow up?

Senator Robert B. Flanders, D. 7: Follow up.

Senator Joseph A. Foster, D. 13: So, you're saying that your client's insurance tends to kick in in an insolvency situation? Is that what this does? You are saying you look at the order of priority, which suggests that you are underwriting to insolvency. Otherwise, it wouldn't come into play. Or, do I misunderstand?

Attorney Van Tol: Well, my understanding is that, in this factual situation, we don't know. The liquidator has not been able to put a number on what the ultimate result would be or how much our clients would pay. So, it is premature and misleading to say that there is going to be a windfall or a gain of X amount. I have to say, if it were really the case that it would be massively unfair or there was going to be a windfall to the reinsurers, someone, a group at the NAIC, would have changed that ranking of priority or allow this sort of scheming where you would allow administrative payment as an incentive for creditors to file their claims. But, they rejected it. So, clearly the system, the NAIC, thinks the system works the way it does currently.

Senator Joseph A. Foster, D. 13: Follow up?

Senator Robert B. Flanders, D. 7: Follow up.

Senator Joseph A. Foster, D. 13: I know I must be thick, so I've got to ask this again. What I'm trying to understand is, but for the insolvency, I guess you say maybe the claim wouldn't be filed at all and maybe this is sort of an incentive to file the claim. But, outside of the insolvency, this claim, if it were filed, there would be litigation and it would be paid. So, why does this wreak havoc on the system? That's the part I guess that I am missing. If you're not writing to rehabilitation/liquidation under the liquidation statute, shouldn't we have a system that the only time this applies, in the rare situation where there is a liquidation of an insurance company?

Attorney Van Tol: The reason it would wreak havoc is because you can overturn even this case. Any creditor that is a lower priority creditor would try to go the liquidator and say, "I, too, want my claim classified as an administrative expense" and they could point to the statute and say "The New Hampshire Legislature is allowing me to do this, so I'm submitting my claim as an administrative expense. I'm not a creditor at all. I'm not a class three; I'm not a class four; I'm not a class five. I'm class one because it is an admin expense." Then, imagine the litigation that is going to spin out of that and chew up the liquidator's time and chew up precious assets of the estate.

Senator Joseph A. Foster, D. 13: But, the statute, as I'm reading it, says that occurs in the rare situation where the administrative claim generates assets to the estate. So there is a standard, first of all, put in the statute where there would have to be shown that there would be a benefit. Maybe we can come up with hypotheticals, but I can't think of a heck of a lot where that would happen.

Attorney Van Tol: Well, again, that is in the currently litigated matter whether in fact a payment like this does help collect assets for the estate. The main thing I want to emphasize today is that we are in a vast sea of uncertainty and now is not the time for the Legislature to parade in and say, "Here's what it means". Let's let the court case run its course. We're not on an expensive track here where we are trying to move discovery along. We should be up to the Supreme Court shortly. The Supreme Court was very intrigued about this issue and we should let them rule on it.

Senator Joseph A. Foster, D. 13: Thank you.

Senator Robert B. Flanders, D. 7: I have never been involved in litigation, although I worked for insurance companies for a long time. I guess I have to ask this question and maybe there's no such thing as a stupid question in the Insurance Committee. What your opposition to this is that it is going to cause a group of claims to be made. Am I hearing your testimony that there will be some claims to be made? Who are those claims? What are those claims? Your testimony is that, if these claims are made, it is going to cause more money to come from the reinsurance.

Attorney Van Tol: Sure. I think it would be helpful for everybody to step back and understand or have me try to explain what is going on. The Home, as a company, reinsured a group of people called the AFIA Cedents, simply a person or insurance company that has a reinsurance contract. So, Home reinsures a group called ABCs. Home is in turn reinsured by the ACE companies and other reinsurers. The ACE companies are our clients. What the liquidator has done in this plan is say, "I will pay you the AFIA Cedents, to file your claims in the liquidation. Even though you are classified creditors, I'm giving you this incentive to pay your claims so that the ACE companies and other reinsurers' obligations will kick in because our clients only have an obligation to pay if the Home has an obligation to pay." It is a chain of AFIA Cedents to the Home to the ACE companies and other reinsurers.

So, what I stated earlier is that it is not an established fact that those AFIA Cedents would not file claims but for this incentive payment. That's the liquidator's position and we take that view and that is what is being litigated today as we speak. So, it would be disruptive, not just to the reinsurance issues, but it would be disruptive to the ongoing litigation process and the judicial process in New Hampshire.

Senator Robert B. Flanders, D. 7: Do I understand that, in Section five of SB 74, this whole section, is now pending or will be heard in court?

Attorney Van Tol: The issues being heard in court, Senator, at the Superior Court level... Let me back up. We went to the Supreme Court once on the issue of whether or not these incentive payments could be characterized as administrative expenses. The Supreme Court took oral argument on that issue, remanded to the Superior Court with an order saying, "Please take evidence and make a factual finding on this issue". Judge McGuire, in our opinion, did not follow that dictate and, instead, made a finding that these payments are administrative expenses. We tried to take an interlocutory appeal before the end of the case up to the Supreme Court with the agreement of the liquidator and at Judge McGuire's urging. Unfortunately, the Supreme Court said, "No, we would like to hear it at the end of the case". So, what we're doing now is we are taking discovery on this administrative expense issue and, at the end of the case, the whole ball of wax will go up to the Supreme Court for review, including this issue on whether or not administrative expenses can be paid to lower priority creditors.

Senator Robert B. Flanders, D. 7: Thank you. Any other questions?

Senator Joseph A. Foster, D. 13: So, I take it, your interest on that issue is whether or not they can file, they can have administrative claims in this fashion because? Is your client harmed by this distribution scheme or is it harmed because, by filing the claim, you have ...(inaudible)...

Attorney Van Tol: By both. If I understood your question, it is not harm. At the end of the day, if these administrative payments are allowed, it would trigger claims that are filed by AFIA Cedents and then there is a claims adjudication process to figure out whether they are valid or not.

Senator Joseph A. Foster, D. 13: Assuming they were, though, you would have to pay?

Attorney Van Tol: Assuming they were, we would have to pay. Now, that brings me to another point, which is that we have already seen in this litigation that, unsurprisingly, these incentive payments cause people to put in claims that are of dubious quality. They are time barred claims, claims that have been rejected already. That is another danger of paying someone to go out and find the claims. That's the reason they are chamfered in statutes in all fifty states to prevent people from doing this sort of thing. I'm not saying this is charity but the concept is to not go around digging for claims; let people submit claims in the normal course.

Senator Joseph A. Foster, D. 13: Thank you.

Attorney Roussos: Mr. Chairman, if I may? The magnitude of these claims that are called administrative expenses, I don't think has been brought to the Committee, but we're talking about an amount that I think the Department estimates at $70 million and the percentage I think is basically maybe a little bit more complicated than this. But, fifty percent of the amount that is recovered on claims that are filed would go to the party that files these claims. The only reason this works, and you can call it a gimmick or not, is that they encourage a lower class claimant to file a claim that the claimant may or may not file in order to trigger an obligation by another person who has obligations to the estate.

So, the estate gets all of its money and pays back part of its money on claims that may or may not have been filed and so, we talk about this litigation, but I need to be clear that we represent a large segment of the industry around this country that is looking at this language and saying, "We really are troubled by this". Nothing to do with this lawsuit, but this language may seem to be narrow. We view it as alarmingly broad that at any time there is, where the payments made to these lower class creditors and called administrative expenses, which changes the meaning of that word that you wouldn't understand readily, Senator. If those payments assist or result in the collection and that is just something that interested parties, including guarantee associations, guaranteed funds that come in, meet the obligations, are not going to know now, if this bill passes, what the amounts of their obligations are going to be with the clarity that they have right now.

So, to sum it up, we take a system that has predictability that we all know the rules, which are uniform around the country, and interject this discretionary language to call something an administrative fee when it isn't and that is basically a concern that lawsuits that are not involved in the litigation.

Senator Robert B. Flanders, D. 7: Senator Foster?

Senator Joseph A. Foster, D. 13: I am just going to ask the question again because this is the one thing I don't understand. The administrative expenses of the liquidator or whatever it is called, may be paying out, in and of itself, doesn't affect the underwriting as far as I can tell. That is just something that he has cut a deal because he thinks it is a good deal for him to pass fifty percent to somebody else. Fifty percent to somebody else to get fifty percent the estate wouldn't get otherwise. How does that affect your underwriting? That's the part that I don't understand. He is elevating a class of creditors higher than he should, I guess, the way the statute reads. But, the only reason that really matters to you is to induce somebody to file a claim. Is that right?

Attorney Van Tol: When I was talking about that, Senator... That's a good question. I was talking about prospectively. When the ACE companies underwrote this risk, they did with the assumption that they would have to pay valid claims thereunder. As you say, they don't sit there and say, "What am I going to do in the event of insolvency". Premiums are based on what you might have to pay out. What I am saying is that, in the future, reinsurers are going to look at how they rate risks in New Hampshire and they are going to rate them vastly different because of this statute. In other words, they will be fearful that in the future there is another insurance liquidation that this same gambit will be tried and that they will be caught in more than they anticipated and that they are going to change their rates, which affects insurance rates, which affects how much the average consumer pays for insurance. It is the certain point that Mr. Roussos just made.

Senator Robert B. Flanders, D. 7: Any other questions? If not, thank you for your testimony. Paula Rogers? Andre Bouffard of Benjamin Moore Paints.

Andre Bouffard: Good morning, Mr. Chairman.

Senator Robert B. Flanders, D. 7: If I may, just so that the Committee will know, I believe that your testimony will also be in reference to Section five.

Attorney Jim Bianco: That's correct.

Senator Robert B. Flanders, D. 7: And, you do realize that whoever testifies at noon buys lunch. So, continue please.

Attorney Bianco: Mr. Chairman and members of the Committee, my name is Jim Bianco. I am an attorney here in Concord and along with me is a gentleman from Vermont. There is a company that is involved in litigation. We don't want to be redundant; we just want to lay out our position ...(inaudible)... We just want to be on record to let you know our position in Section five and only Section five. Thank you.

Andre Bouffard: Good morning, Mr. Chairman and members of the Committee. I'm Andre Bouffard and I represent Benjamin Moore Paints. Just in the interest of full disclosure, I should tell the Committee that Benjamin Moore Paints is also a corporate cousin of a reinsurer that has some interest in the outcome of the issues here today. But, I'm here to speak on behalf of Benjamin Moore as a policyholder in the Home insolvency case. The interests of the reinsurers are being covered by Mr. Roussos.

In terms of looking at this from the perspective of policyholders, what I have asked myself is what is the problem here that the liquidator is trying to solve and is this a smart solution to the problem? We have heard what the liquidator's representative had to say this morning. I would submit that no real problem has been articulated here that the Legislature needs to fix at this point. The only problem that exists, so far as I can tell, is that the liquidator is having difficulty with his position in the litigation. Whether these payments can be characterized as administrative expenses has already gone to the Supreme Court once. The Supreme Court expressed a lot of skepticism about whether or not this agreement flies in terms of the existing language in the statute. We are now in the Superior Court and we are hashing out the issue of whether or not indeed the statute should be construed to permit this. That's where the issue should be resolved.

In terms of the solution, I would submit that this is not a smart solution to the problem, if a problem exists. The reason it is not a smart solution is that there are some potentially very catastrophic collateral consequences of what the liquidator is doing here. For example, the ACE group, which you have just heard from, is a reinsurer of the estate and it has taken the position that, by virtue of entering into this agreement, the liquidator has breached his obligation of good faith and fair dealing with the ACE group and the liquidator may very well have voided the contracts that he is seeking to recover under by taking this action. As a policyholder in this estate, Benjamin Moore is concerned about that having happened. The other concern that Benjamin Moore has as a policyholder is that the Home estate has been incurring a large amount of attorneys' fees to advance a position that doesn't seem to be supportable under the statute. Those attorneys' fees are going to be paid as administrative expenses in this estate. Those attorneys' fees and other expenses are going to be paid ahead of policyholder claims like Benjamin Moore and that is one of the many reasons that Benjamin Moore is currently opposing this agreement.

Now, you might ask yourselves, why would a policyholder who might benefit from this agreement actually be opposing it? I got that same question from the Supreme Court when we were arguing the appeal at the Supreme Court. My response today is the same as it was then and that is that I don't know, I don't have enough information right now to say whether or not at the end of the day Benjamin Moore, as a policyholder, is going to be a net beneficiary. I don't know. We have made discovery requests. We have sought information in the Home litigation so that we can get to the bottom of the questions that we have. We may conclude at the end of the day that we are a beneficiary from this agreement, but we don't have the information to make that judgment at this point. That's why we have courts; that's why we have

litigation; and that's why we're involved in the litigation. I think I am going to end there and take any questions that anybody may have.

Tape change.

Due to an equipment failure, the remainder of public testimony on SB 74 was not recorded.

Respectfully submitted,

L Gail Brown

Recorded by Melanie Gates
Transcribed by L. Gail Brown
3/81/05

2 Attachments

Attachment #1

New Hampshire Insurance Department
February 3, 2005

Amendments to Senate Bill 74

- Section 1: No change
- Section 2: No change

- **Section 3: Amend RSA 402:81 I. (a) (1), so that the sentence reads:**

  (1) The original policy to be cancelled; **or**

- **Section 4: Amend RSA 402-C:36, to read as follows:**

  Subject to RSA 402-C:34 the amount recoverable by the liquidator from a reinsurer shall not be reduced as a result of delinquency proceedings **regardless of whether** the reinsurance contract provides, in substance, that in the event of the insolvency of the ceding insurer, the reinsurance shall be payable by the assuming insurer on the basis of the claims allowed against the ceding insurer in the insolvency proceedings, under contract or contracts reinsured without diminution because of the insolvency of the ceding insurer. **Such payments shall be made** directly to the ceding insurer or to its domiciliary liquidator or receiver except:

- **Section 5: Amend RSA 402-C:44, to read as follows:**

  The order of distribution of claims from the insurer's estate shall be stated in this section. The first $50 of the amount allowed on each claim in the classes under paragraphs II, V, and VI except claims of the guaranty associations as defined in RSA 404-B, 404-D, **404-H,** and 408-B shall be deducted from the claim. Claims may not be cumulated by assignment to avoid application of the $50 deductible provision. Subject to the $50 deductible provision, every claim in each class shall be paid in full or adequate funds retained for the payment before the members of the next class receive any payment. No subclasses shall be established within any class.

- Section 6: No change
- Section 7: No change
- Section 8: No change

- **Section 9: Amend RSA 415-A:4-a I.(b)(1), to read as follows:**

  (1) Developed with input from appropriate **[actively participating]** practitioners **[in the licensed entity's service area]** **with professional knowledge or clinical expertise in the area being reviewed** ;

- Section 10: No change

- **Section 11: Amend RSA 420-J:5 I(b), to read as follows:**

  (b) **For medical necessity appeals, at least one** **[The]** person reviewing the **appeal** **[grievance on a first or second level appeal have appropriate medical and professional expertise and credentialing to competently render a determination on appeal]** **is a practitioner in the same or similar specialty who typically treats the medical condition, performs the procedure or provides the treatment at issue in the appeal. A practitioner is considered of the same specialty if he or she has similar credentials and licensure as those who typically treat the condition or health problem in question in the appeal. A practitioner is considered of a**

similar specialty if he or she has experience treating the same problems as those in question in the appeal, in addition to expertise treating similar complications of those problems ;

Section 12: Amend RSA 420-J:5, II(a), to read as follows:

(a) The review shall be conducted by or in consultation with a health care professional **[who has appropriate training and expertise in the field of medicine]** **in the same or similar specialty who typically treats the medical condition, performs the procedure or provides the treatment at issue in the appeal. A practitioner is considered of the same specialty if he or she has similar credentials and licensure as those who typically treat the condition or health problem in question in the appeal. A practitioner is considered or a similar specialty if he or she has experience treating the same problems as those in question in the appeal, in addition to expertise treating similar complications of those problems** ;

- Section 13: No change
- Section 14: No change
- Section 15: No change
- Section 16: No change
- Section 17: No change
- Section 18: No change
- Section 19: No change
- Section 20: No change

(legis05sb74amendments020305)

Attachment #2

RAA

REINSURANCE ASSOCIATION OF AMERICA

STATEMENT

STATEMENT IN OPPOSITION TO SB 74

Hearing Before the New Hampshire Senate Banks and Insurance Committee

February 1, 2005

Marsha A. Cohen, CPCU, ARe
Senior Vice President, State Relations and Education

Matthew T. Wulf
Associate Vice President & Legal Counsel

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Statement of the Reinsurance Association of America in Opposition to SB 74 - Sections 4 and 5

The Reinsurance Association of America (RAA) appreciates the opportunity to offer comments on SB 74. Our comments respectfully address concerns with the proposed amendments in Sections 4 and 5 - Insurers Rehabilitation and Liquidation.

The Reinsurance Association of America (RAA) is a national trade association representing organizations that specialize in reinsurance. Our members are diverse, including large and small, broker and direct, U.S. companies and subsidiaries of foreign companies. Our affiliate membership includes reinsurance brokerage companies and life reinsurers. The RAA represents its members' interests in reinsurance legislative and regulatory issues in all US jurisdictions: before the National Association of Insurance Commissioners (NAIC); before the National Conference of Insurance Legislators (NCOIL); before the US Congress and the Executive Branch; and in various international forums. As a result we are familiar with the common regulatory and legislative practices in the US.

SB 74 is not only a technical bill as it is referred to in the preamble. It proposes to make very substantive changes to current law that may have a detrimental impact on the insurance market in New Hampshire.

Amendments to Sections 4 and 5 will result in the creation of New Hampshire specific deviations from standard insolvency laws throughout the US.

Amendments to SB 74 Section 4 - Insurers Rehabilitation and Liquidation. 402-C: 36 Liability of the Insurer

We oppose the proposed amendments to RSA 402-C: 36 Liability of the Insurer for the following reasons:

1. The addition of the citation "Subject to RSA 402-C: 34" is redundant and unnecessarily confuses the operation of two independent statutory provisions. "Subject to RSA 402-C: 34" references the setoff law. The effect of this amendment is to make the amount due the liquidator subject to setoff, which it already is by operation of current law. The amendment is redundant and confusing.

2. We see no reason to change the "unless" to "where" as it is clear the way it is currently drafted.

3. We oppose deleting the phrase "directly to the ceding insurer or to its domiciliary liquidator or receiver". It is important to maintain language that addresses to

whom the reinsurance proceeds get paid; otherwise you state the exception without stating the rule.

We do agree that RSA 402-C: 36 could be amended to make its meaning clearer.

We recommend redrafting the introductory paragraph of RSA 402-C: 36 to read as stated below. The language that we are suggesting would bring New Hampshire law into conformity with the laws in the majority of the states. (Additions are underscored).

"The amount recoverable by the liquidator from a reinsurer shall not be reduced as a result of delinquency proceedings unless the reinsurance contract provides, in substance, that in the event of the insolvency of the ceding insurer, the reinsurance shall be payable by the assuming insurer on the basis of the claims allowed against the ceding insurer in the insolvency proceedings, under contract or contracts reinsured without diminution because of the insolvency of the ceding insurer. Such payments shall be made directly to the ceding insurer or to its domiciliary liquidator or receiver except:"

Amendments to SB 74 Section 5 - Insurers Rehabilitation and Liquidation; RSA 402-C: 44 Order of Distribution

The amendments propose to amend the priority of distribution section of New Hampshire law to alter the current order of distribution of claims from the estate and create deviations from the laws in all other states in the US.

Priority of distribution laws as currently stated in RSA 402-C: 44 have been adopted in all states and they are based on requirements established by the NAIC Insurers Rehabilitation and Liquidation Model Act.

The issues inherent in determining the priority of payment in liquidation have been fully debated and agreed to by all interested parties including receivers, guaranty funds and all members of the insurance industry. The current laws across the country represent this understanding.

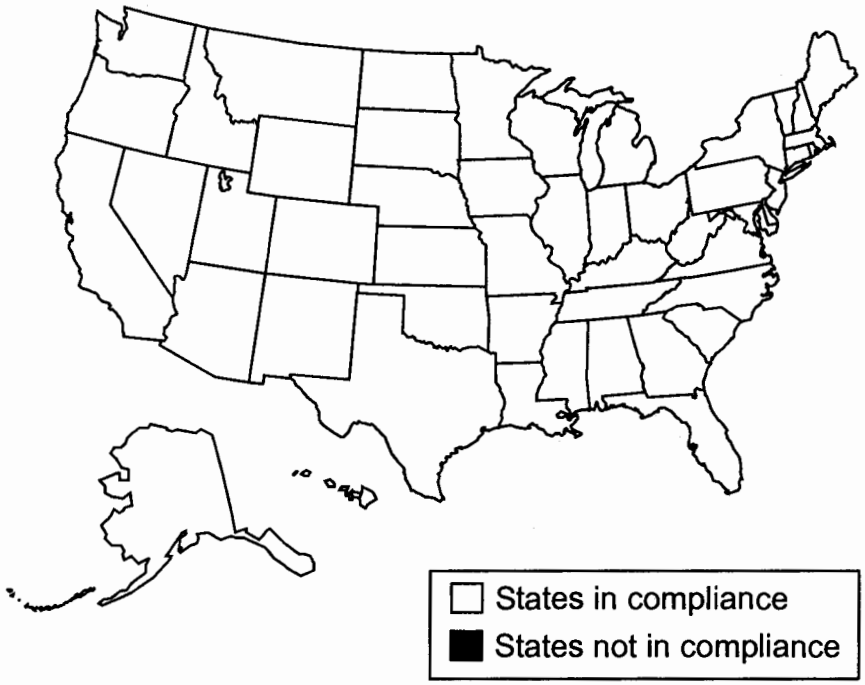
The proposed amendments attempt to make New Hampshire's law stand alone in allowing receivers to pay claimants outside the well-established priority of distribution statute.

The RAA opposes the proposed amendments to RSA 402-C: 44 Order of Distribution for the following reasons:

States NOT in Compliance

with the Priority of Distribution Provisions in the
NAIC Insurers' Rehabilitation and Liquidation Model Act

Current



Proposed SB 74

Only New Hampshire
will not be in compliance

American Insurance Association

NORTHEAST REGION
95 Columbia Street
Albany, NY 12210
518- 462-1695
Fax 518- 465-6023

February 1, 2005

TESTIMONY IN OPPOSITION

Senate Bill 74 (Section 5)

The American Insurance Association (AIA) is a national trade association representing over 435 insurance companies that provide all lines of property and casualty insurance and write more than $120 billion annually in premiums. AIA member companies wrote over twenty-five percent of the property and casualty insurance premiums written in New Hampshire in 2003. AIA opposes Section 5 of Senate Bill 74.

While Senate Bill 74 is characterized as a "technical" bill, it seems that a number of sections go beyond mere technical changes to the insurance laws. Most troubling to us is Section 5, which amends New Hampshire's order of distribution for claims when an insurer is in liquidation proceedings. The amendment would allow claimants who are further down on the payment distribution chain to jump ahead of higher priority claimants by characterizing the lower priority claims as "administrative costs." Such an amendment not only is fundamentally unfair to claimants with higher priority claims, but could result in increased litigation costs, which are ultimately passed on to the consumer.

In addition, while most states have priority of distribution laws, we are not aware of any other state that follows this approach. Furthermore, the National Association of Insurance Commissioners (NAIC) recently rejected this concept when it was presented to them. We believe there is no sound public policy reason for New Hampshire to adopt an amendment violating well-established priority of distribution requirements.

For the foregoing reasons, AIA opposes Section 5 of Senate Bill 74.

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February 1, 2005

By Hand

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Our ref NYPT/80316.01
Matter ref T0718/00023

Robert B. Flanders, Chairman
The New Hampshire Senate
Banks and Insurance Committee
107 North Main Street
Concord, New Hampshire 03301

RE: SENATE BILL 74

Dear Senator Flanders:

This firm represents Century Indemnity Company ("Century"), ACE Property and Casualty Insurance, Pacific Employers Insurance Company and ACE American Reinsurance Company (collectively, the "ACE Companies"). We respectfully submit this letter in connection with the Banks and Insurance Committee's consideration of Senate Bill 74 ("S.B. 74").

Section 5 of S.B. 74, if approved by the New Hampshire Legislature, would add the following language to RSA 402-C:44:

"This section shall not be construed to prohibit any payments, as administrative costs, made to claimants in lower priority classes where those payments assist or result in the collection or recovery of assets or property, including debts, moneys due or claims belonging to the insurer for the benefit of claimants in higher priority classes."

The ACE Companies believe that the adoption of Section 5 would be harmful to New Hampshire consumers, would establish a precedent that could detrimentally affect future liquidations in New Hampshire and elsewhere in the United States, and would interfere with the New Hampshire courts as they consider the issues that are raised by the proposed amendment. As discussed below, Section 5 would alter RSA 402-C:44 in a way that would disrupt the orderly payment of claims in liquidations and would likely raise the cost of insurance for New Hampshire residents. It would also cause other claimants to seek to recast their liquidation claims as administrative expenses, thereby increasing the amount of litigation over the classification of such claims and reducing the funds available to the estate. Furthermore, the amendment in Section 5 is contrary to the intent of the model act on which RSA 402-C:44 is based; the drafters of the model provisions recently resisted the same proposed change to the administrative expense section. The courts have similarly refused to allow deviations from the carefully crafted order of distribution in statutes like RSA 402-C:44, even where, as here, the claimants assert that their claims are administrative expenses. Finally, Section 5 would intrude upon the ongoing litigation between the ACE Companies and the Liquidator of The

Home Insurance Company ("Home"), who has argued that certain proposed payments to Home's claimants may be characterized as administrative expenses. The New Hampshire Supreme Court has considered this issue already and will likely be doing so again in the near future. Deleting Section 5 from S.B. 74 would allow the New Hampshire judicial system to continue its review of the administrative expense issue without interference.

For these reasons, the ACE Companies urge the Committee to reject Section 5.

Background

I. The Order of Distribution Statute

The relevant provisions in RSA 402-C:44 are attached to this letter as an Appendix. The statute sets forth the strict order in which claimants in an insurance liquidation will receive funds from the insurer's estate. (Claimants are grouped together in a "class" under the statute.) The preamble states that this "order of distribution of claims from the insurer's estate shall be as stated in this section." (emphasis added) The statute further provides that "every claim in each class shall be paid in full or adequate funds retained for the payment before the members of the next class receive any payment. No subclasses shall be established within any class." (emphasis added) Thus, the order of distribution in RSA 402-C:44 is mandatory and cannot be varied for any reason. The statute also expressly prohibits payments to some members of a class and not to others.

The relevant classes for the purposes of this discussions are Classes I, II and V. RSA 402-C:44 gives the highest priority ranking to "administrative costs" under Class I, which the statute describes as "[t]he costs and expenses of administration, including but not limited to the following: the actual and necessary costs of preserving or recovering the assets of the insurer; compensation for all services rendered in the liquidation; any necessary filing fees; the fees and mileage payable to witnesses; and reasonable attorney's fees." RSA 402-C:44, I. It is well established that payments for administrative costs relate to expenses that occur post-liquidation; such payments are made to those who are engaged after the insurer is placed in liquidation to assist in the operation of the insurer's estate. The purpose of this section is to make sure that the liquidation does not discourage professionals and others from providing services to the estate for fear that they will not be paid. It is not intended to benefit creditors of the estate who have claims that arose pre-liquidation.

Class II includes claims by the insurer's policyholders, which refers to the beneficiaries of a direct policy issued by the insurer. RSA 402-C:44, II. Class V is the "residual classification," and it includes, among other things, claims by insurance companies (known as "cedents") who purchased reinsurance from the insurer. RSA 402-C:44, V.

II. New Hampshire Court Proceedings Regarding Administrative Costs

In the current liquidation proceedings involving Home, the Liquidator has sought final Court approval for a scheme (the "Proposed Agreement") under which he would settle the claims of a subclass of Class V creditors (known as the "AFIA Cedents") by paying them 50% of the net proceeds (after certain deductions) that are recovered by the estate under reinsurance provided to Home.[1] The

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[1] The AFIA Cedents are reinsured by Home, which is reinsured by Century. Valid payments to the AFIA Cedents under Home's reinsurance contracts would trigger Century's reinsurance obligations.

Liquidator has estimated that the amount of the proposed payments to the AFIA Cedents would be approximately $72 million. In return, the AFIA Cedents agreed to file claims in the liquidation under their reinsurance contracts with Home. It is the Liquidator's position that, absent the incentive payments under the Proposed Agreement, the AFIA Cedents would not bother to file their reinsurance claims and the proceeds under Home's reinsurance would not come into the estate. The Liquidator has, among other things, tried to justify the proposed payment of tens of millions of dollars as "administrative costs" under Class I.

The ACE Companies and others opposed the Proposed Agreement, pointing out that it would violate the mandatory order of distribution set forth in RSA 402-C:44 because it would allow the Liquidator to (i) make claims payments to Class V creditors ahead of other creditors; and (ii) make those payments to a subclass of Class V creditors. The ACE Companies also demonstrated that such a scheme is unprecedented in the United States and would undermine similar statutory provisions in other states. Despite these objections, earlier this year the New Hampshire Superior Court held that the Proposed Agreement was permissible under the Liquidator's broad array of powers. The Superior Court did not expressly address the argument that the proposed payments to the AFIA Cedents could be classified as administrative expenses under Class I.

On appeal, the New Hampshire Supreme Court reversed the Superior Court and remanded the case for further proceedings. The Supreme Court voiced considerable doubt at oral argument that the proposed payments to the AFIA Cedents could be characterized as administrative expenses. The following exchange between the Court and counsel for the Liquidator occurred:

THE COURT:

Let me see if I understand. If this is not an administrative expense, but a payment of a claim to a Class 5 creditor, is that being paid before all of the claimants in Class 2, 3 or 4 are paid?

PETER ROTH:

That is correct.

THE COURT:

That violates the statute.

PETER ROTH:

We are sort of going around in circles, I understand. But it is an administrative expense because it is not in satisfaction of their Class 5 claim.

...

THE COURT:

Why is it an expense? It doesn't look or sound like an expense.

PETER ROTH:

Well, the statute was written very broadly and the statute — excuse me a minute. § 44(1) doesn't speak of how you can parse it out and say well, it's too big or it's to the wrong people. All it says is "including, but not limited to, the actual necessary [sic] costs of preserving or recovering the assets of an insurer" and the courts around the country that have interpreted administrative expenses have looked at that language in similar circumstances in bankruptcy contexts because it is very similar to what is the treatment in bankruptcy courts that finders fee, a percentage of the action, or a contingent fee for a lawyer also can be an administrative claim. Sometimes these claims can be very large — so the size and nature of the payee doesn't determine whether it is an administrative expense or not.

THE COURT:

Well, it looks to me like you are paying and distributing an asset to a claimant that doesn't look and sound like an expense of collecting assets.

(Hearing transcript at 14-15; bold added.)[2]

In an order issued on September 13, 2004, the Supreme Court required the Superior Court to consider on remand whether the payments would fall under Class I. The Supreme Court also ordered the Superior Court to make a full evidentiary record and to support its conclusions with factual findings. However, without allowing discovery on this issue or conducting an evidentiary hearing, the Superior Court ruled that the proposed payments to the AFIA Cedents could be classified as administrative expenses. The parties, at the urging of the Superior Court, requested that the Supreme Court review this ruling on an interlocutory appeal. The Supreme Court declined, which means that the administrative expense issue will be considered after the Superior Court issues a final order on the Liquidator's request for approval of the Proposed Agreement. The parties are currently involved in the discovery process, which will lead to an evidentiary hearing on the issues before the Superior Court. The ACE Companies plan to file an appeal to the Supreme Court if, after the hearing, the Superior Court leaves its ruling on the administrative expense issue intact.

Problems Created By The Proposed Amendment

As the foregoing discussion shows, the proposed amendment is clearly aimed at dictating a result that the Liquidator has thus far been unable to obtain in the New Hampshire court system. New Hampshire should not permit frustrated litigants — whose rights and obligations are being adjudicated in a pending court case — to turn to the Legislature for relief. As a matter of public policy, the Legislature should safeguard the operation and independence of the judicial system. Here, the Liquidator might argue that the proposed amendment has codified his interpretation of the statute, which, as noted above, the Supreme Court has questioned and will be considering again.

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[2] Counsel for the Liquidator referred to finders' fees and contingent payments in a bankruptcy matter, but those examples only serve to prove the ACE Companies' point. Those types of payments are to creditors whose claims arise post-petition when they perform services for the debtor; the administrative expense provisions in the Bankruptcy Code do not apply to pre-petition claims.

In addition to violating public policy and interfering with the judicial process, the proposed amendment would have adverse ramifications for consumers in New Hampshire and for future insurance liquidations, both in New Hampshire and elsewhere.

First, by allowing liquidators to make payments to lower classes of creditors, the amendment would create an incentive for "side deals" with claimants. Some claimants would rush to enter into those arrangements to the detriment of others, creating inevitable litigation over the validity of the deals (because there would still be an argument that the payments do not constitute administrative expenses). This would increase the cost of liquidations in New Hampshire, which would result in less money for distribution to all creditors. The payment of incentives to Class V creditors to file claims would also increase the likelihood of invalid or even fraudulent claims. Indeed, in the Home liquidation, the ACE Companies have seen the submission of reinsurance claims that were previously rejected as invalid.

Second, the proposed amendment would wreak havoc on the orderly liquidation process that reinsurers expect when conducting business in New Hampshire. It is likely that this uncertainty would cause reinsurers to either withdraw from the New Hampshire market or increase the costs for New Hampshire insurers who purchase reinsurance from them. This in turn would increase the cost of insurance products for New Hampshire consumers.

Third, the proposed amendment would have a detrimental effect on liquidations in New Hampshire and elsewhere. The order of distribution in RSA 402-C:44 is based on a model provision that has been adopted in the majority of jurisdictions in the United States. The fixing of priorities in the model act is the result of many years of debate and careful consideration, and it reflects the judgment of the highly experienced professionals involved in insurance liquidations. Those professionals have rejected attempts to give claims under reinsurance contracts a higher ranking, and recently turned down an amendment to the model act provisions that is similar to Section 5.

The courts have also refused to vary the order of distribution, and, in one case directly on point, the court held that lower priority claims may not be reclassified as administrative expenses. *See Oxendine v. Commissioner of Ins. of N.C.*, 494 S.E.2d 545 (Ct. App. Ga. 1997). In *Oxendine*, creditors who had settled claims against the estate prior to the company's rehabilitation argued that the settlements should be considered administrative expenses under the Georgia code (which contains the same language as the current RSA 402-C:44). The *Oxendine* court stated that: "No reasonable definition of 'costs' or 'expenses' can include the claims which appellees assert. These claims are for money which appellees claim from [the] estate and not administrative costs or expenses incurred." *Id.* at 548. The *Oxendine* court also noted that the effect of allowing pre-liquidation claims to be classified as administrative expenses "would be to render meaningless the priority of claims established [by the Georgia statute]." *Id.* Here, too, allowing the Liquidator to transform the payments of the AFIA Cedents' claims into administrative expenses would rewrite the order of distribution and render RSA 402-C:44 meaningless. It would also encourage liquidators in other states that have adopted the model provisions to try to pursue similar schemes, to the detriment of the carefully constructed order of distribution.

* * * *

Accordingly, the ACE Companies respectfully request that the Committee delete Section 5 from S.B. 74. We thank the Committee for accepting this letter and would be happy to provide any further information to assist in its consideration of the proposed amendment.

Respectfully submitted,

Pieter Van Tol

Pieter Van Tol

cc: George Roussos, Esq.

Appendix

402-C:44 Order of Distribution. – The order of distribution of claims from the insurer's estate shall be as stated in this section. The first $50 of the amount allowed on each claim in the classes under paragraphs II, V, and VI except claims of the guaranty associations as defined in RSA 404-B, 404-D, and 408-B shall be deducted from the claim. Claims may not be cumulated by assignment to avoid application of the $50 deductible provision. Subject to the $50 deductible provision, every claim in each class shall be paid in full or adequate funds retained for the payment before the members of the next class receive any payment. No subclasses shall be established within any class.

I. ADMINISTRATION COSTS. The costs and expenses of administration, including but not limited to the following: the actual and necessary costs of preserving or recovering the assets of the insurer; compensation for all services rendered in the liquidation; any necessary filing fees; the fees and mileage payable to witnesses; and reasonable attorney's fees.

II. POLICY RELATED CLAIMS. All claims by policyholders, including claims for unearned premiums in excess of $50, beneficiaries, and insureds arising from and within the coverage of and not in excess of the applicable limits of insurance policies and insurance contracts issued by the company, and liability claims against insureds which claims are within the coverage of and not in excess of the applicable limits of insurance policies and insurance contracts issued by the company and claims of the New Hampshire Insurance Guaranty Association, the New Hampshire Life and Health Insurance Guaranty Association and any similar organization in another state. All claims under life insurance and annuity policies, whether for death proceeds, annuity proceeds or investment values, shall be treated as loss claims. That portion of any loss for which indemnification is provided by other benefits or advantages recovered or recoverable by the claimant shall not be included in this class, other than benefits or advantages recovered or recoverable in discharge of familial obligations of support or by way of succession at death or as proceeds of life insurance, or as gratuities. No payment made by an employer to an employee shall be treated as a gratuity.

III. CLAIMS OF THE FEDERAL GOVERNMENT.

IV. WAGES.

(a) Debts due to employees for services performed, not to exceed $1,000 to each employee which have been earned within one year before the filing of the petition for liquidation. Officers shall not be entitled to the benefit of this priority.

(b) Such priority shall be in lieu of any other similar priority authorized by law as to wages or compensation of employees.

V. RESIDUAL CLASSIFICATION. All other claims including claims of any state or local government, not falling within other classes under this section. Claims, including those of any non-federal governmental body, for a penalty or forfeiture, shall be allowed in this class only to the extent of the pecuniary loss sustained from the act, transaction or proceeding out of which the penalty or forfeiture arose with reasonable and actual costs occasioned thereby. The remainder of such claims shall be postponed to the class of claims under paragraph VIII.