

THE STATE OF NEW HAMPSHIRE

MERRIMACK, SS.

SUPERIOR COURT

BEFORE THE COURT-APPOINTED REFEREE
IN RE THE LIQUIDATION OF THE HOME INSURANCE COMPANY
DISPUTED CLAIMS DOCKET

In Re Liquidator Number: 2011-HICIL-50 and
2011-HIICL-51
Proof of Claim Number: GOVT 18901-11 and
GOVT 18901-12
Claimant Name: Arizona Property & Casualty Ins
Guaranty Fund
Claimant Number:
Policy or Contract Number:
Date Of Loss:

ORDER ON THE MERITS

The Claimant, Arizona Property & Casualty Insurance Guaranty Fund ("the Fund"), has filed a proof of claim with the Liquidator seeking to recover certain administrative expenses the Fund incurred and allocated to the Home insolvency. The Liquidator has disallowed a portion of the claim, and has allocated a portion of the claim with a Class V priority. In two related actions, the Fund requests the Referee allow the remainder of its claim for administrative expenses and allocate all of those expenses to Class I.

Relevant Facts

The 2008 and 2009 Administrative Expenses

Giant Industries, Inc. was an insured under a general liability policy issued by The Home Insurance Company ("Home") for the period August 3, 1980 to August 3, 1981 and under another general liability policy issued by Home for the period August 3, 1982 to August 3, 1983.

In 2008, the Fund and the Liquidator received copies of lawsuits against Giant Industries by various claimants suing for alleged contamination from MTBE. The Liquidator opened two files, one for each policy year in which Home had issued a policy providing coverage to Giant Industries. The Fund opened a separate file for each claim in each policy period: forty for each policy period, for a total of 80 claims against Giant Industries. In addition, the Fund had a "master file."

As part of its proof of claim, the Fund sought a total of \$798,464.26 in administrative expenses for the period January 1, 2006 to September 3, 2010. The expenses requested were based on an allocation to the Home estate of a varying percentage of the Fund's total overhead expenses for those years. The Fund determined its percentage allocation to the Home estate by applying the ratio of the number of open claims it was handling

with respect to Home to its total number of open claims. The Liquidator has allowed some of those expenses.

For the years 2008 and 2009, the Fund sought administrative expenses of \$254,982.86 and \$166,868.92 respectively. In those years, the Fund based its calculation on the open claims count of 82 or 83 with respect to Home, the open claims from Giant Industries. The Liquidator allowed expenses of \$31,000 for each of those years. The Liquidator based its allowance on the expenses the Fund had submitted in years in which the Giant Industries claims were not open. The Liquidator contends that the Fund's allocation of administrative expense to Home based on 80 individual claims files is unreasonable.

The Dues Paid to NCIGF

The Fund's claim for administrative expenses also included dues it paid to the National Council of Insurance Guaranty Funds ("NCIGF"). The NCIGF describes itself as "a non-profit, member funded association that provides national assistance and support to the property and casualty guaranty funds located in each of the fifty states and the District of Columbia." The NCIGF website states the organization "monitors national insurance activities, coordinates information for multi-state insolvencies and provides legal, informational, administrative, communications and public policy and administrative support to our members." The NCIGF indicates it monitors and responds to issues that might impact state guaranty funds and serves as a trusted expert, informing trade and other organizations as they develop model legislation related to state guaranty fund laws.

The dues paid by members of NCIGF are comprised of two parts: a per capita fixed annual membership fee; and a pro-rata portion based on the ratio of premium written by insurers in the guaranty association's state to the premium written in all states, subject to certain caps. As part of its request to the Liquidator, the Fund requested reimbursement of administrative expenses for the dues paid to NCIGF. The Fund used the allocation percentage based on its open claim count to determine the allocation of the dues paid to NCIGF to be reimbursed by the Liquidator.

For the years 2006 to 2010, the Fund sought reimbursement of dues to NCIGF from the Liquidator for \$75,881.97.¹ The Liquidator accepted the requests for the years 2006, 2007, 2008 and 2010. For the year 2009, the Liquidator used the Fund's 2008 number of \$4,365 rather than the Fund's requested amount of \$52,572.44. The Liquidator also assigned all of the dues paid to NCIGF which it did reimburse to Class V. The Liquidator's basis for assignment to Class V was that the dues were not expenses in handling claims.

¹ The specific requests for reimbursement for NCIGF dues were:

2006 - \$5,930.75

2007- \$3,917.36

2008 - \$4,365.72

2009 - \$52,572.44

2010 - \$9,095.70

The Fund seeks to recover the additional dues to NCIFG it allocated to the Home estate for 2009. The Fund also seeks classification of all dues allowed as a Class I claim rather than a Class V claim.

The Relevant Statutes

The New Hampshire Insurers Rehabilitation and Liquidation Act, RSA 402-C ("Act") provides for the order of distribution of claims from the Home estate, stating in pertinent part:

I. ADMINISTRATIVE 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. ...

* * *

V. RESIDUAL CLASSIFICATION. All other claims including claims of any state or local government, not falling within other classes under this section.

RSA 402-C:44.

The New Hampshire Insurance Guaranty Association Act, RSA 404-B provides that the expense of the New Hampshire Insurance Guaranty Association or similar organization in handling claims shall be accorded the same priority as the liquidator's expenses. RSA 404-B:11, II.

The Arizona Revised statutes A.R.S. §§ 20-661 through 20-680 govern the Fund. They are referred to as the "Arizona Guaranty Fund Statutes." The Arizona statute requires the Fund to "investigate claims brought against the fund and adjust compromise, settle and pay covered claims to the extent of the fund's obligation and deny all other claims." A.R.S. §20-664(A)(1). A.R.S. §20-664(A)(6) requires the Fund to handle claims through

its employees or through servicing facilities. The Fund is to reimburse each servicing facility for the claims paid by the facility and for expenses incurred by the facility while handling claims on behalf of the fund and pay the other expenses of the fund authorized pursuant to the statute. A.R.S §20-664(A)(7). The Fund is funded by the assessments of its member insurers, which are to be in such amounts as are necessary to pay the obligations of the fund pursuant to §20-667 subsequent to an insolvency, the expenses of handling covered claims subsequent to an insolvency, the cost of examinations and other expenses authorized pursuant to the statute. A.R.S. § 20-666(A).

The Arizona statute also provides that the Fund “may by resolution bar known claims, whether liquidated or unliquidated, not filed within four months from the date of notice to creditors.” A.R.S. §20-679.

Analysis

I. The Fund’s Request for Reimbursement of Expenses Based on Number of Claims Files Open in 2008 and 2009.

The Fund argues that the Liquidator’s disallowance of administrative expenses because the Liquidator found the Fund’s decision to open a separate claim for each of the 40 Giant Industries claims under each of the two Home policies was unjustified and unreasonable. The Fund asserts that the Liquidator’s analysis is based on a fundamental misunderstanding of the facts and erroneous assumptions about the handling of the Giant Industries claims.

First, the Fund asserts that it was not evident in February 2008 when the claims were first submitted that the claims were time barred. Under the Arizona statute, §20-679, the Fund may bar known claims not filed within four months from the date of notice to creditors. The Fund asserted that all of the Giant Industries claims were time-barred. The bar date the Liquidator and the Fund used for the Giant Industries claims was June 13, 2004. Examination of the files demonstrated to the Fund claims handler that 31 of the Giant Industries claims were not known until after that date, and would not have been time-barred. As to the remainder of the claims, the Fund asserted the time-bar as a basis for denial. The successor to Giant Industries did not agree with the position and filed a declaratory judgment action against the Fund and other insurers. In September 2008, the Fund filed a motion for summary judgment relying on the argument that the claims were time-barred. However, the position was not accepted by the insured, and was not clearly a winning argument against coverage at the time the files were set up early in 2008. The Fund also argues the Liquidator is wrong in its assertion the suit by Giant Industries was dismissed because the claims were time-barred. The pleadings demonstrate the suit was dismissed by agreement because Giant Industries collected its money from other insurers.

Although the time-bar argument has been addressed, the disagreement about how to allocate expenses to the Liquidator focuses mainly on the number of claims set up by the Fund. The Liquidator set up two claims, one for each policy issued by Home, and

included in each claim all of the separate demands for coverage in those two policy years. The Fund set up a "master file" for the Giant Industries claims, as well as separate files for each claim in each policy year for which Home wrote coverage. The Fund argues it needed to set up separate files for each claim and each claim year because each lawsuit represented an unpaid claim, and could therefore constitute a covered claim under the Fund's enabling act, and because each lawsuit potentially triggered coverage under each of the Home policies. Memorandum of Facts and Law of Claimant Arizona Property and Casualty Insurance Guaranty Fund ("Memorandum of the Fund"), p. 11. The Fund has provided copies of the individual claims files, and of the "master file." Each of the claims files has several notes about coverage at the time the files were open. Each claim has a denial letter. Not all the denial letters are identical, but the differences are minimal. It appears that adjustor handling the claims made most of his notes in the master file, although that file has no notations between April 8, 2008 and June 3, 2009, when the file was closed.

The Fund allocates administrative expenses based on the number of open insolvency cases. Affidavit of Michael E. Surguine ¶5. An allocation for each open receivership estate is determined by dividing the number of open claims for a specific insolvency by the total population of open claims being handled by the Fund. *Id.* The total of the administrative expenses incurred by the Fund is then multiplied by the allocation percentage for each estate, and the final calculation is reported to the Liquidator as the funds' administrative expense for the applicable period. *Id.* The Fund recalculates for each quarter.

The Fund is not the only state guaranty fund that calculates administrative expenses this way. Of the fifty-two states or other entities with Guaranty Funds, 6 use the number of open claims, 39 use the time spent on the file, and 7 use a combination of the two. Liquidator's Exhibits to Section 15 Submission, Exhibit 23.

The Fund asserts that it has the choice to determine its allocation based on the number of open claims. The Liquidator does not disagree. The parties do disagree about whether the allocation formula resulted in an unreasonable allocation of expenses to the Liquidator in 2008 and 2009. The Fund also asserts that the Liquidator has the burden to show that the Fund's decision about how to allocate expenses is a "sham or ruse" in order for the Liquidator to deny the claim.

The Fund contends that if its allocation formula is reasonable, the outcome is therefore appropriate and must be accepted. Because the number of open claims files was an acceptable formula to the Liquidator in past years, the Fund contends it must be for 2008 and 2009.

The Fund also argues that the Referee is bound by the evidence submitted and that the evidence demonstrates that the claims handler spent time on the claims and that one can't conclude that time was "not substantial." The claims files have no notations in them for fourteen months. The evidence presented indicates the claims handler did not spend "substantial" time on those files, given the limited notes regarding work done.

The Liquidator concedes that the Fund may open as many files as it chooses. But the Liquidator asserts it is not bound by the Fund's formula where the outcome is not reasonable. The Liquidator argues that the Fund's decision to use an allocation percentage based on the open claims resulted in administrative expense allocations to Home for 2008 and 2009 of \$259,348.48 and \$238,874.19 respectively. These amounts are more than five times greater than those for 2006, 2007 or 2010. More importantly, the choice to set allocations based on open claims files meant that the Fund sought over 40% of its total operating expenses for 2008 and 2009 from Home, as compared to 5% to 7% for 2006, 2007 and 2010. Given these numbers, the Liquidator viewed the Fund's allocations for 2008 and 2009 as unreasonable.

The Liquidator asked the Fund to revise the claims count but did not get a response. Liquidator's Section 15 Submission, p. 8. The Liquidator therefore based its determination on the 2007 allocated number which the Fund had accepted, \$31,084.00. The Liquidator allocated \$31,000 for 2008 and 2009.

RSA Chapter 402-C governs the Liquidator's actions. The Liquidator is charged with protecting the interests of insureds, creditors and the public, generally. He is required to gather the assets of the Home Insurance Company and to pay claims in a manner consistent with his charge. The Liquidator must review each claim submitted within the requirements set forth in the statute and make a determination that comport with his duties under the statute. The evidence demonstrates that the Fund submitted a claim for over 40% of the Fund's total operating expenses for 2008 and 2009, where the entire defense costs of those claims was limited to \$28,817.38. Liquidator's Section 15 Submission, p. 12. The evidence also demonstrates there were no entries in the claims files constituting more than three pages, and none for a period of months. The Liquidator found the submissions for 2008 and 2009 unreasonable. The Referee agrees. The Liquidator's determination is upheld.

II. Dues Paid to NCIGF Based on Number of Claims Files Open in 2008 and 2009.

The Fund asserts that the methodology it used to allocate to the Home as administrative expenses the NCIGF dues for 2009 was proper and that the Liquidator was not justified in disallowing \$48,207.44 of the total sought of \$52,572 for that year. The Fund argues that the reason for the increase in the amount reported for 2009 was higher is that there were 80 more claims being handled.

The Fund's allocation of dues to NCIGF are calculated based on the number of open files for Home as compared to the total number of open files, as explained above. Because the Fund asserts that its allocation was proper, it seeks to have the Liquidator's disallowance of dues paid reversed.

As demonstrated in Section I, the Liquidator does not have the authority to require the Fund to open files using any certain method. The Liquidator's authority is limited to reviewing the assessment of those dues by the Fund within the confines of the

Liquidator's duties. The Liquidator accepted the requests for the years 2006, 2007, 2008 and 2010.

The Liquidator determined that for 2009, the Fund's method for allocating dues expenses led to a significantly higher allocation to Home than in other years. According to the Liquidator, the allocation was five to thirteen times greater than for 2006, 2007, 2008 or 2010. Liquidator's Section 15 Submission, p. 9. The Liquidator therefore substituted the dues allocated for 2008, \$4,365, for the 2009 year, rather than the Fund's request amount because the other outcome. The Referee upholds the Liquidator's determination.

III. Classification of Dues Paid to NCIGF as Class I or Class V.

The Fund also argues the NCIGF dues to be reimbursed should be prioritized as Class I claims. RSA 402-C:44 specifies the classes into which requests for reimbursement fall. Class I claims are comprised of the actual costs of preserving or recovering the assets of the insurer, compensation for services rendered in the liquidation, etc. Class V claims include "all other claims including claims of any state or local government, not falling within other classes..." It has become clear to the Liquidator, and to others monitoring the liquidation proceeding, that there will not be a distribution to those with Class V claims. Therefore, the class into which a claim falls is of particular importance related to the likelihood of reimbursement.

The Fund asserts that the dues paid to NCIGF fall within Class I because they constitute an expense in handling claims. The Fund argues that it has received substantial assistance in handling Home claims through the Fund's membership in the NCIGF. Memorandum of the Fund, p. 16, Affidavit of Michael E. Surguine, ¶19. However, the Fund does not provide any specificity regarding of what that assistance consists. The Fund notes that the NCIGF does not handle claims, but that it assists the Fund in doing so. Memorandum of the Fund, pp. 16-17. The Fund describes the primary benefit for members in the NCIGF as assistance with guaranty funds in claims handling. Affidavit of Mark Steckbeck, Assistant Vice-President, Legal Affairs for NCIGF, ¶6.

The dues are not differentiated between functions of the NCIGF. Although the Fund agrees that certain activities of the NCIGF are not assistance related to the handling of claims, it nevertheless asserts that all of the dues should be classified as a Class I claim not a Class V claim.

The dues paid by the Fund include a pro rata share of the operating costs of NCIGF, as well as an additional amount based on the ratio of premium written by insurers in the guaranty association's states to the premium written in all states. While the NCIGF provides necessary assistance and support to the Fund, that support and assistance is for many functions including: advocacy in law making; education; outreach; and public policy development. These are important functions, but are not specific to claims handling or preserving and recovering assets of the Home estate. Although the Fund has demonstrated that activities assist its personnel in handling claims, the Fund has not

provided any analysis of which portion of the funds are so related. Therefore, the Fund has not met its burden to prove the dues should be entitled to classification as a Class I.

Conclusion

The Referee upholds the Liquidator's determinations.

So ordered.

December 20, 2012
Date:


Referee, Melinda S. Gehris