

## INSURER RECEIVERSHIP MODEL ACT

### ARTICLE VII. CLAIMS

#### Section 711. Qualified Financial Contracts

- A. Notwithstanding any other provision of this Act, including any other provision of this Act permitting the modification of contracts, or other law of a state, no person shall be stayed or prohibited from exercising:
- (1) A contractual right to cause the termination, liquidation, acceleration or close out of obligations under or in connection with any netting agreement or qualified financial contract with an insurer because of:
    - (a) The insolvency, financial condition or default of the insurer at any time, provided that the right is enforceable under applicable law other than this Act; or
    - (b) The commencement of a formal delinquency proceeding under this Act;
  - (2) Any right under a pledge, security, collateral, reimbursement or guarantee agreement or arrangement or any other similar security arrangement or arrangement or other credit enhancement relating to one or more netting agreements or qualified financial contracts;
  - (3) Subject to any provision of Subsection 609B, any right to set off or net out any termination value, payment amount, or other transfer obligation arising under or in connection with one or more qualified financial contracts where the counterparty or its guarantor is organized under the laws of the United States or a state or a foreign jurisdiction approved by the Securities Valuation Office (SVO) of the NAIC as eligible for netting; or

- (4) If a counterparty to a master netting agreement or a qualified financial contract with an insurer subject to a proceeding under this Act terminates, liquidates, closes out or accelerates the agreement or contract, damages shall be measured as of the date or dates of termination, liquidation, close out or acceleration. The amount of a claim for damages shall be actual direct compensatory damages calculated in accordance with Subsection F below.
- B. Upon termination of a netting agreement or qualified financial contract, the net or settlement amount, if any, owed by a non-defaulting party to an insurer against which an application or petition has been filed under this Act shall be transferred to or on the order of the receiver for the insurer, even if the insurer is the defaulting party, notwithstanding any walkaway clause in the netting agreement or qualified financial contract. For purposes of this subsection, the term “walkaway clause” means a provision in a netting agreement or a qualified financial contract that, after calculation of a value of a party’s position or an amount due to or from one of the parties in accordance with its terms upon termination, liquidation or acceleration of the netting agreement or qualified financial contract, either does not create a payment obligation of a party or extinguishes a payment obligation of a party in whole or in part solely because of the party’s status as a non-defaulting party. Any limited two-way payment or first method provision in a netting agreement or qualified financial contract with an insurer that has defaulted shall be deemed to be a full two-way payment or second method provision as against the defaulting insurer. Any such property or amount shall, except to the extent it is subject to one or more secondary liens or encumbrances or rights of netting or setoff, be a general asset of the insurer.

**Drafting Note:** This provision requires that, upon termination of a netting agreement, the non-defaulting party will be required to pay to the defaulting party (the insurer) any net or settlement amounts owed to the insurer, notwithstanding any provision in the netting agreement that provides that the non-defaulting party is not required to make payments to the defaulting party. In short, this provision renders “limited two-way payment” provisions in master swap agreements unenforceable against a defaulting insurer.

- C. In making any transfer of a netting agreement or qualified financial contract of an insurer subject to a proceeding under this Act, the receiver shall either:
- (1) Transfer to one party (other than an insurer subject to a proceeding under this Act) all netting agreements and qualified financial contracts between a counterparty or any affiliate of the counterparty and the insurer that is the subject of the proceeding, including:
    - (a) All rights and obligations of each party under each netting agreement and qualified financial contract; and
    - (b) All property, including any guarantees or other credit enhancement, securing any claims of each party under each netting agreement and qualified financial contract; or
  - (2) Transfer none of the netting agreements, qualified financial contracts, rights, obligations or property referred to in Paragraph (1) of this subsection (with respect to the counterparty and any affiliate of the counterparty).
- D. If a receiver for an insurer makes a transfer of one or more netting agreements or qualified financial contracts, then the receiver shall use its best efforts to notify any person who is party to the netting agreements or qualified financial contracts of the

transfer by 12:00 noon (the receiver's local time) on the business day following the transfer. For purposes of this subsection, "business day" means a day other than a Saturday, Sunday or any day on which either the New York Stock Exchange or the Federal Reserve Bank of New York is closed.

- E. Notwithstanding any other provision of this Act, a receiver may not avoid a transfer of money or other property arising under or in connection with a netting agreement or qualified financial contract (or any pledge, security, collateral or guarantee agreement or any other similar security arrangement or credit support document relating to a netting agreement or qualified financial contract) that is made before the commencement of a formal delinquency proceeding under this Act. However, a transfer may be avoided under Section 606A if the transfer was made with actual intent to hinder, delay or defraud the insurer, a receiver appointed for the insurer, or existing or future creditors.
- F. (1) In exercising the rights of disaffirmance or repudiation of a receiver with respect to any netting agreement or qualified financial contract to which an insurer is a party, the receiver for the insurer shall either:
- (a) Disaffirm or repudiate all netting agreements and qualified financial contracts between a counterparty or any affiliate of the counterparty and the insurer that is the subject of the proceeding; or
  - (b) Disaffirm or repudiate none of the netting agreements and qualified financial contracts referred to in Subparagraph (a) (with respect to the person or any affiliate of the person).
- (2) Notwithstanding any other provision of this Act, any claim of a counterparty against the estate arising from the receiver's disaffirmance or repudiation of a netting agreement or qualified financial contract that has not been previously affirmed in the liquidation or immediately preceding conservation or rehabilitation case shall be determined and shall be allowed or disallowed as if the claim had arisen before the date of the filing of the petition for liquidation or, if a conservation or rehabilitation proceeding is converted to a liquidation proceeding, as if the claim had arisen before the date of the filing of the petition for conservation or rehabilitation. The amount of the claim shall be the actual direct compensatory damages determined as of the date of the disaffirmance or repudiation of the netting agreement or qualified financial contract. The term "actual direct compensatory damages" does not include punitive or exemplary damages, damages for lost profit or lost opportunity or damages for pain and suffering, but does include normal and reasonable costs of cover or other reasonable measures of damages utilized in the derivatives, securities or other market for the contract and agreement claims.

**Drafting Note:** The intended effect of this provision is that, except where the receiver has expressly affirmed a netting agreement or qualified financial contract, the claim of a counterparty against the estate of an insolvent insurer (after completion of the netting and setoff processes) will have no greater priority than the claim of a general creditor.

- G. The term "contractual right" as used in this section includes any right set forth in a rule or bylaw of a derivatives clearing organization (as defined in the Commodity Exchange Act), a multilateral clearing organization (as defined in the Federal Deposit Insurance Corporation Improvement Act of 1991), a national securities

exchange, a national securities association, a securities clearing agency, a contract market designated under the Commodity Exchange Act, a derivatives transaction execution facility registered under the Commodity Exchange Act, or a board of trade (as defined in the Commodity Exchange Act) or in a resolution of the governing board thereof and any right, whether or not evidenced in writing, arising under statutory or common law, or under law merchant, or by reason of normal business practice.

- H. The provisions of this section shall not apply to persons who are affiliates of the insurer that is the subject of the proceeding.
- I. All rights of counterparties under this Act shall apply to netting agreements and qualified financial contracts entered into on behalf of the general account or separate accounts if the assets of each separate account are available only to counterparties to netting agreements and qualified financial contracts entered into on behalf of that separate account.

## ARTICLE I. GENERAL PROVISIONS

### Section 104. Definitions

For the purposes of this Act:

- Q. “Netting agreement” means (1) a contract or agreement (including terms and conditions incorporated by reference therein), including a master agreement (which master agreement, together with all schedules, confirmations, definitions and addenda thereto and transactions under any thereof, shall be treated as one netting agreement), that documents one or more transactions between the parties to the agreement for or involving one or more qualified financial contracts and that provides for the netting, liquidation, setoff, termination, acceleration or close out under or in connection with one or more qualified financial contracts or present or future payment or delivery obligations or payment or delivery entitlements thereunder (including liquidation or close-out values relating to such obligations or entitlements) among the parties to the netting agreement; (2) any master agreement or bridge agreement for one or more master agreements described in Paragraph (1) of this subsection; or (3) any security agreement or arrangement or other credit enhancement or guarantee or reimbursement obligation related to any contract or agreement described in Paragraph (1) or (2) of this subsection; provided that any contract or agreement described in Paragraph (1) or (2) of this subsection relating to agreements or transactions that are not qualified financial contracts shall be deemed to be a netting agreement only with respect to those agreements or transactions that are qualified financial contracts.
- W. “Qualified financial contract” means any commodity contract, forward contract, repurchase agreement, securities contract, swap agreement and any similar agreement that the commissioner determines by regulation, resolution or order to be a qualified financial contract for the purposes of this Act.
- (1) “Commodity contract” means:
- (a) A contract for the purchase or sale of a commodity for future delivery on, or subject to the rules of, a board of trade or contract market under the Commodity Exchange Act (7 U.S.C. § 1, *et seq.*) or a board of trade outside the United States;
  - (b) An agreement that is subject to regulation under Section 19 of the Commodity Exchange Act (7 U.S.C. § 1, *et seq.*) and that is commonly known to the commodities trade as a margin account, margin contract, leverage account or leverage contract;
  - (c) An agreement or transaction that is subject to regulation under Section 4c(b) of the Commodity Exchange Act (7 U.S.C. § 1, *et seq.*) and that is commonly known to the commodities trade as a commodity option;
  - (d) Any combination of the agreements or transactions referred to in this paragraph; or
  - (e) Any option to enter into an agreement or transaction referred to in this paragraph.

- (2) “Forward contract,” “repurchase agreement,” “securities contract” and “swap agreement” shall have the meanings set forth in the Federal Deposit Insurance Act, 12 U.S.C. § 1821(e)(8)(D), as amended from time to time.

**Drafting Note:** This definition of “qualified financial contract” is intended to be consistent with definitions applicable under federal law in instances of insolvency of other types of financial institutions. It is not the intention of this provision, or of Section 711, to affect the scope of permissible investments of insurers or the valuation thereof, or to modify any other regulatory framework applicable to investments or investment practices of insurers.