GUIDELINE FOR ADMINISTRATION OF LARGE DEDUCTIBLE POLICIES IN RECEIVERSHIP

Drafting Note: Having the necessary statutory authority specific to large deductible workers’ compensation products in receiverships is key to the successful resolution of these insurers. There are currently two statutory authority options available, and there are differences across states as to which authority has been adopted: 1) Section 712 of the NAIC Insurer Receivership Model Act (#555—IRMA), Administration of Loss Reimbursement Policies; and 2) the National Conference of Insurance Guaranty Funds (NCIGF) Model Large Deductible Legislation, Administration of Large Deductible Policies and Insured Large Deductible Collateral. Both provide statutory guidance that articulates the respective rights and responsibilities of the various parties, which greatly enhance a state’s ability to manage complex large deductible programs in liquidation. Generally, both approaches provide for the collection of reimbursements, resolve disputes over who gets the reimbursements and ensure that the claimants are paid. The provisions in each of the two options generally complement each other, except for conflicting provisions regarding the issue of the ultimate ownership of, and entitlement to, the deductible recoveries and large deductible collateral as between the estate and the guaranty association. The issue is whether the guaranty associations, on behalf of the claimants, are entitled to any deductible reimbursements or whether they are a general estate asset that is shared pro rata by the guaranty associations and the uncovered claimants.

As of the drafting of this Guideline, the NCIGF model approach has been adopted by several states using varying language. However, the NCIGF model has evolved over time based on additional experiences from insolvencies and the NCIGF continues to modify its model as warranted. The NAIC has developed the following Guideline based largely on the principles and structure of the NCIGF model with certain modifications made by the NAIC Large Deductible Workers’ Compensation (E) Working Group of the Receivership and Insolvency (E) Task Force. The following statutory language is not an amendment to the NAIC receivership models but is intended as a Guideline for use by states as an alternative to IRMA Section 712, Administration of Loss Reimbursement Policies.

Administration of Large Deductible Policies in Receivership

This Guideline shall apply to workers’ compensation large deductible policies issued by an insurer subject to delinquency proceedings under [insert cite to state’s receivership statute]. Large deductible policies shall be administered in accordance with their terms, except to the extent such terms conflict with this Guideline. This Guideline does not apply to policies where the insurer has no liability for the portion of a claim that is within the deductible or self-insured retention.

A. Definitions.

For purposes of this Guideline:

(1) “Large deductible policy” means any combination of one or more workers’ compensation policies and endorsements and contracts or security agreements entered into between an insured and the insurer in which the insured has agreed with the insurer to:

(a) Pay directly the initial portion of any claim covered under the policy up to a specified dollar amount which the insurer would otherwise be obligated to pay, or the expenses related to any claim; or

(b) Reimburse the insurer for its payment of any claim or related expenses under the policy up to the specified dollar amount of the deductible.

The term “large deductible policy” includes policies which contain an aggregate limit on the insured’s liability for all deductible claims, a per-claim deductible limit or both. The primary purpose and distinguishing characteristic of a large deductible policy is the shifting of a portion of the ultimate financial responsibility under the large deductible policy to pay claims from the insurer to the insured, even though the obligation to initially pay claims may remain with the insurer, and the insurer remains liable to claimants in the event the insured fails to fulfill its payment or reimbursement obligations.

Drafting Note: States may wish to establish a minimum dollar deductible threshold for application of this statute based on local conditions. Because the payment of the entire amount of the claim remains the unconditional obligation of the insurer,
the insured’s loss reimbursement obligation should not be treated as a “deductible” for the purpose of any applicable exclusion from guaranty association coverage, even though these policies are commonly referred to as “large deductible policies.”

Large deductible policies do not include policies, endorsements or agreements which provide that the initial portion of any covered claim shall be self-insured and further that the insurer shall have no payment obligation within the self-insured retention. Large deductible policies also do not include policies that provide for retrospectively rated premium payments by the insured or reinsurance arrangements or agreements, except to the extent such reinsurance arrangements or agreements are put in place as security for the policyholder’s large deductible obligations.

(2) “Deductible claim” means any allowed claim, including a claim for loss and defense and cost containment expense (unless such expenses are excluded), under a large deductible policy to the extent it is within the deductible.

(3) “Large deductible collateral” means any cash, letters of credit, surety bond, or any other form of security posted by the insured, or by a captive insurer or reinsurer, to secure the insured’s obligation under the large deductible policy to pay deductible claims or to reimburse the insurer for deductible claim payments. Large deductible collateral may also secure an insured’s obligation to reimburse or pay to the insurer as may be required for other secured obligations.

(4) “Commercially reasonable” means to act in good faith using prevailing industry practices and making all reasonable efforts considering the facts and circumstances of the matter.

(5) “Other secured obligations” means obligations of an insured to an insurer other than those under a large deductible policy, such as those under a reinsurance agreement or other agreement involving retrospective premium obligations the performance of which is secured by large deductible collateral that also secures an insured’s obligations under a large deductible policy.

B. Handling of Large Deductible Claims.

Unless otherwise agreed by the responsible guaranty association, all large deductible claims that are also “covered claims” as defined by the applicable guaranty association law, including those that may have been funded by an insured before liquidation, shall be turned over to the guaranty association for handling.

(1) If a deductible claim is not covered by any guaranty association, the receiver shall draw on available large deductible collateral to pay the claim; or make other arrangements with the insured to ensure the timely payment of the claim. The receiver shall pay the claim promptly from the large deductible collateral unless the insured pays the claim directly or there is no available large deductible collateral.

(2) Deductible claims paid by the insured or by the receiver in accordance with this Guideline shall not be treated as distributions of estate assets under [insert cite to state’s liquidation priority distribution statute]. To the extent the insured, or a third-party administrator on behalf of the insured, pays the deductible claim, pursuant to an agreement by the guaranty association or otherwise, the insured’s payment of a deductible claim in whole or in part will extinguish the obligations, if any, of the receiver and/or any guaranty association to pay that claim or that portion of the claim. No credit or charge for an imputed or constructive distribution of any kind shall be made against the receiver or a guaranty association on the basis of an insured’s payment of a deductible claim.

Drafting Note: This provision addresses so called “orphan claims,” which are situations where, because of variations in state law or for other reasons, claims generally covered by the guaranty fund system are not provided such protection. States should take steps, through statutory revision or otherwise, to avoid orphan claims, especially for workers’ compensation insurance. However, if such claims do exist, this provision permits the receiver to utilize available large deductible collateral, or other funds provided by the employer, to ensure that they continue to be paid. Alternative language that states may consider is as follows: “In cases where a deductible claim is not a guaranty association covered claim and the claimant has no other remedy either from the employer or other resources available in a state, the receiver may pay the claim to the extent of the deductible with available Large deductible collateral as described in subsection E(2) below.”

C. Deductible Claims Paid by a Guaranty Association.

To the extent a guaranty association pays any deductible claim for which the insurer would have been entitled to reimbursement from the insured, a guaranty association shall be entitled to the amount of the reimbursement, and
available large deductible collateral as provided for under subsection E to the extent necessary to reimburse the guaranty association. Such amounts shall be paid to the guaranty association net of any of the receiver’s collection costs as described in subsection F. Reimbursements paid to the guaranty association pursuant to this subsection shall not be treated as distributions under [insert cite to state’s liquidation priority distribution statute] or as early access payments under [insert cite to state’s early access statute].

To the extent that a guaranty association pays a deductible claim that is not reimbursed either from large deductible collateral or by an insured’s payments, or incurs expenses in connection with large deductible policies that are not reimbursed under this subsection, the guaranty association shall be entitled to assert a claim for those amounts in the delinquency proceeding, except as provided in subsection D(5).

Nothing in this subsection limits any rights of the receiver or a guaranty association that may otherwise exist under applicable law to obtain reimbursement from insureds for claims payments made by the guaranty association under policies of the insurer or for the guaranty association's related expenses, such as those provided for pursuant to [insert cite to state’s guaranty association net worth provision], or existing under similar laws of other states.

D. Collections

(1) The receiver shall take all commercially reasonable action to ensure that the large deductible collateral remains adequate to secure the insured’s obligations, and to collect reimbursements owed for deductible claims as provided for herein:

(a) Paid by the insurer prior to the commencement of delinquency proceedings;
(b) Paid by a guaranty association upon receipt by the receiver of notice from a guaranty association of reimbursable payments;
(c) Paid or allowed by the receiver; or
(d) Approved by the receiver for payment.

(2) If the insured does not make payment within the time specified in the large deductible policy, or within sixty (60) days after the date of billing if no time is specified, the receiver shall take all commercially reasonable actions to collect any reimbursements owed.

(3) Neither the insolvency of the insurer, nor the receiver’s or insurer’s inability to perform any of its obligations under the large deductible policy, shall be a defense to the insured’s reimbursement obligation under the large deductible policy.

(4) An allegation of improper handling or payment of a deductible claim by the insurer, the receiver and/or any guaranty association shall not be a defense to the insured’s reimbursement obligations under the large deductible policy.

(5) If the receiver declines to seek or is unsuccessful in obtaining reimbursement from the insured for a large deductible obligation and there is no available large deductible collateral, a guaranty association may, after notice to the receiver, seek to collect the reimbursement due from the insured on the same basis as the receiver, and with the same rights and remedies including without limitation the right to recover reasonable costs of collection from the insured. The guaranty association shall report any amounts so collected from each insured to the receiver. The receiver shall provide the guaranty association with available information needed to collect a reimbursement due from the insured. The receiver shall notify all other guaranty associations that have paid large deductible claims on behalf of the same insured. Amounts collected by a guaranty association pursuant to this paragraph shall be treated in accordance with subsection C. The expenses incurred by a guaranty association in pursuing reimbursement shall not be permitted as a claim in the delinquency proceeding at any priority, except as agreed by the receiver at or before the time the expenses are incurred; however, a guaranty association may net the expenses incurred in collecting any reimbursement against that reimbursement.

E. Large Deductible Collateral

(1) Subject to the provisions of this subsection, the receiver shall utilize large deductible collateral, when available, to secure the insured’s obligation to fund or reimburse deductible claims or other secured
obligations or other payment obligations. A guaranty association shall be entitled to large deductible collateral as provided for in this subsection to the extent needed to reimburse a guaranty association for the payment of a deductible claim. Any payments made to a guaranty association pursuant to this subsection shall not be treated as distributions of estate assets under [Insert cite to state’s liquidation priority distribution statute] or as early access payments under [Insert cite to state’s early access statute]. Such payments shall extinguish the receiver’s obligations to the guaranty association with respect to any claim or portion of a claim that has been reimbursed from large deductible collateral.

(2) All claims against the large deductible collateral shall be paid first to reimburse claim payments made by the insurer, the receiver, or the guaranty associations to reimburse their deductible claim payments on large deductible policies. After these obligations are satisfied, remaining claims shall be paid in the order received and no claim of the receiver, except in accordance with this subsection, shall supersede any other claim against the large deductible collateral.

(3) Notwithstanding any agreement between the insured and the insurer, the receiver shall draw down large deductible collateral to the extent necessary in the event that the insured fails to:

(a) Perform its funding or payment obligations under any large deductible policy;

(b) Pay deductible claim reimbursements within the time specified in the large deductible policy or within sixty (60) days after the date of the billing if no time is specified;

(c) Pay amounts due the estate for pre-liquidation obligations;

(d) Timely fund any other secured obligation; or

(e) Timely pay expenses.

(4) Excess large deductible collateral may be returned to the insured when deemed appropriate by the receiver after a periodic review of claims paid, outstanding case reserves, and allowance for adverse development and claims incurred but not reported as determined by the receiver.”

F. Administrative Fees

(1) The receiver is entitled to recover through billings to the insured or from large deductible collateral all reasonable expenses that the receiver incurred in fulfilling its collection obligations under this Guideline. All such deductions or charges shall be in addition to the insured’s obligation to reimburse claims and related expenses and shall not diminish the rights of claimants or guaranty associations.

(2) To the extent the receiver cannot collect such expenses pursuant to paragraph (1), the receiver is entitled to deduct from the large deductible collateral or from the deductible reimbursements reasonable and actual expenses incurred in connection with the collection of the large deductible collateral and deductible reimbursements.

(3) To the extent such amounts are not available from reimbursements or large deductible collateral, the receiver, or guaranty associations if provided under an agreement with the receiver under subsection D(5), shall have a claim against the estate as provided pursuant to [insert cite to state’s liquidation priority distribution statute].

Drafting Note: State policymakers should decide whether this provision, when enacted, should apply to existing liquidations.
1. Description of the Project, Issues Addressed, etc.

In 2018, the Receivership Large Deductible Workers’ Compensation (E) Working Group of the Receivership and Insolvency (E) Task Force was given charges in response to issues arising out of the 2016 Workers’ Compensation Large Deductible Study by the NAIC/International Association of Industrial Accident Boards and Commissioners (IAIABC) Joint (C) Working Group to recommend possible enhancements to the U.S. receivership regime.

In 2018, the Working Group heard presentations from the National Conference of Insurance Guaranty Funds (NCIGF) and nine states/insurers with experience with a receivership involving large deductible workers’ compensation. The Working Group also conducted a survey of states’ laws, practices and recommendations, to which 27 states responded. It was clear through this work that having statutory authority specific to large deductible workers’ compensation products in receiverships was key to the successful resolution of these insurers. As a result of its work, on Nov. 16, 2018, the Working Group presented the Task Force with its recommendation regarding statutory authority.

The Working Group recommended state adoption of clear statutory authority that articulates the respective rights and responsibilities of the various parties in large deductible workers’ compensation business receiverships. Having clear statutory authority in place can avoid much of the confusion, and sometimes expensive and prolonged litigation, for both the receiver and the guaranty funds. Clear statutory authority can also avoid collections delays that dilute recoveries.

Based on the study, the Working Group recommended that states adopt statutory authority regarding large deductible workers’ compensation products in receiverships. Prior to the development of the new guideline, there were two options available:

1) Insurer Receivership Model Act (#555—IRMA) Section 712—Administration of Loss Reimbursement Policies; or

2) NCIGF Model Large Deductible Legislation.

Twelve states have adopted the NCIGF model using varying language (California, Florida, Indiana, Illinois, Louisiana, Michigan, Missouri, New Jersey, Pennsylvania, Texas, Utah and West Virginia). Most of these states follow the NCIGF approach and have amended their insurance liquidation acts to clarify the following when to secure competing claims such as deductible amounts owed the insurer and retroactive premium balances: 1) the ownership of the deductible reimbursements or collateral drawdowns; 2) claims-handling matters; 3) collection responsibility; and 4) allocation of collateral.

After recommending to the Task Force that states adopt clear statutory, the Working Group discussed differences between Model #555 and the NCIGF model during 2019 and 2020. While Section 712 is part of Model #555, it was the opinion of the Working Group that the alternative language to Section 712 should be drafted as a guideline because it does not meet the two-pronged test to be a model law. Therefore, the Working Group agreed to draft a new model guideline for the Administration of Large Deductible Policies in Receivership as an alternative to Model #555, Section 712—Administration of Loss Reimbursement Policies. The new model guideline is based largely on the principles and structure of the NCIGF model with certain modifications.

2. Name of Group Responsible for Drafting the Model and States Participating

The Receivership and Insolvency (E) Task Force is responsible for Model #555. The 2020 members of the Task Force are: Texas (Chair), District of Columbia (Vice Chair), Alaska, American Samoa, Arkansas, California, Colorado, Connecticut, Florida, Illinois, Iowa, Kansas, Kentucky, Maine, Massachusetts, Michigan, Missouri, Montana, Nebraska, New Jersey, North Carolina, Oklahoma, Pennsylvania, Rhode Island, South Carolina, Tennessee and Utah.

The Receivership Large Deductible Workers’ Compensation (E) Working Group evaluated the issues and drafted the draft model guideline relating to Section 712 of Model #555 based on the NCIGF principles from the NAIC model (available on the NCIGF website).

The 2020 members of the Working Group are: Pennsylvania (Co-Chair); Oklahoma (Co-Chair), Alaska, Arkansas, Florida, Georgia, Illinois, Maine, Missouri, Nebraska, New Jersey, New Mexico and Texas.
An informal drafting group was formed in 2020 consisting of Donna Wilson (OK), Toma Wilkerson (FL), Robert Wake (ME), James Kennedy (TX), Barbara Cox (NCIGF) and Rowe Snider (Locke Lord LLP).

3. Project Authorized by What Charge and Date First Given to the Group

The Receivership Large Deductible Workers’ Compensation (E) Working Group of the Receivership and Insolvency (E) Task Force was given the following charge beginning in 2018:

“Study states’ receivership laws and practices regarding receivership of insurers with significant books of large deductible workers’ compensation business, and evaluate the need for a model act/rule, or amendments to existing models, that governs the rights and duties of the various parties regarding large deductible business in insolvencies, including, but not limited to, consideration of a provision that expressly permits the collection of large deductibles from insureds during an insolvency proceeding. Provide any other recommendations for possible enhancements to the U.S. receivership regime based on this study.”

4. A General Description of the Drafting Process (e.g., drafted by a subgroup, interested parties, the full group, etc.). Include any parties outside the members that participated.

The Receivership Large Deductible Workers’ Compensation (E) Working Group, chaired by Donna Wilson (OK) and Laura Lyon Slaymaker (PA), drafted the model guideline. Open conference calls were held where interested parties participated. The information drafting group included four state insurance regulators and two industry volunteers.

5. A General Description of the Due Process (e.g., exposure periods, public hearings or any other means by which widespread input from industry, consumers and legislators was solicited).

a. The Working Group held five open conference calls between August 2018 and November 2018 where it: 1) heard presentations from the NCIGF; 2) heard presentations from nine states and insurers with experience with a receivership involving large deductible workers’ compensation; and 3) reviewed survey results from 27 states regarding their laws, practices and recommendations.

b. The Working Group began by amending the NCIGF model as an alternative approach to Section 712 of Model #555. The Working Group held five open meetings between February 2019 and December 2019. During its Dec. 2, 2019, meeting, the Working Group exposed a new draft model guideline for a 60-day public comment period ending Jan. 31, 2020. The guideline is an alternative approach to Model #555, Section 712 based on the NCIGF model and amended to reflect administrative fees, a state-specific citation for the definition of “large deductible” and the guaranty association entitlement to the net amount of the reimbursement. In conjunction with the model guideline, NAIC legal staff drafted a memorandum explaining the difference between a guideline and a model law.

c. The Working Group received two comment letters during the exposure period from Maine and the NCIGF.

d. The Working Group met via open meeting March 2, 2020 and formed a drafting group to further amend the draft guideline to address comments received. The drafting group met four times between March 2020 and September 2020.

e. On Sept. 30, 2020, via open meeting, the Working Group exposed a revised draft Guideline for Administration of Large Deductible Policies in Receivership for a 30-day period ending Oct. 30, 2020. The revised guideline was re-drafted based largely on the principles and structure of the NCIGF model with certain modifications. It is based on the principles rather than the NCIGF model because the NCIGF model approach has been adopted by several states using varying language. The NCIGF model has evolved over time based on additional experiences from insolvencies and continues to be modified as warranted by the NCIGF.

f. All exposure drafts were distributed to more than 120 interested parties and posted to the Working Group’s public web page. Barbara Cox (NCIGF) and Rowe Snider (Locke Lord LLP) actively participated in the drafting group.

g. The Working Group adopt the guideline on Nov. 5, 2020.
h. The Receivership and Insolvency (E) Task Force adopted the guideline on Nov. 19, 2020.

i. The Financial Condition (E) Committee adopted the guideline at the Fall National Meeting on Dec. 8, 2020.

6. A Discussion of the Significant Issues (items of some controversy raised during the due process and the group’s response).

Deductible Reimbursements and Collateral
The primary distinction between the NCIGF and Model #555, Section 712—Administration of Loss Reimbursement Policies, is the issue of deductible reimbursements and collateral. Twelve states have adopted large deductible policy laws based on the NCIGF model principles using varying language. It should be noted that no state has enacted the reinsurance approach described below in Model #555. Therefore, it was the decision of the Working Group to include the NCIGF approach to collateral within the Guideline.

- The NCIGF model “secured claim” approach: Claims within the deductible are primarily the obligation of the policyholder. Under this approach, deductible reimbursements are earmarked to pay those claims, and any collateral posted by or on behalf of the policyholder is held to ensure that those claims are paid. Accordingly, when the guaranty association takes pays a claim within the deductible, it earns the benefit of the reimbursement due from the policyholder and the right to draw on the collateral, if necessary, or to initiate a draw by the receiver, for the benefit of the guaranty fund.

- Model #555 Section 712 “reinsurance” approach: The insurer’s obligation to pay all covered claims and the policyholder’s obligation to reimburse the insurer are unconditional and each is independent of the other. Under this approach, deductible reimbursements are a general asset of the estate and the guaranty fund only benefits from the deductible reimbursements in proportion to its share as a creditor of the estate. The receiver has the right to collect all deductible reimbursements, drawing on collateral as necessary. Any reimbursements paid to the guaranty association are treated as early access distributions and offset from future recoveries from the estate.

7. Any Other Important Information (e.g., amending an accreditation standard).

None