

The Florida Senate
BILL ANALYSIS AND FISCAL IMPACT STATEMENT

(This document is based on the provisions contained in the legislation as of the latest date listed below.)

Prepared By: The Professional Staff of the Committee on Banking and Insurance

BILL: SB 730

INTRODUCER: Senator Passidomo

SUBJECT: Insurer Insolvency

DATE: March 3, 2017 REVISED: _____

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	Billmeier	Knudson	BI	Pre-meeting
2.			AGG	
3.			AP	
4.			RC	

I. Summary:

SB 730 amends Florida’s Insurer’s Rehabilitation and Liquidation Act to include various provisions from the National Association of Insurance Commissioners’ “Insurer Receivership Model Act.” The bill:

- Adds the Florida Health Maintenance Organization Consumer Assistance Plan to the list of organizations to which notice of hearings shall be delivered pertaining to the insolvency of a member insurer;
- Provides exclusive jurisdiction to the Circuit Court of Leon County over all assets and property of an insurer in receivership, whether or not such assets or property are located outside of Florida;
- Creates deadlines for written responses from an insurer subject to an order to show cause pursuant to ch. 631, F.S., and establishes a deadline for commencement of a hearing to determine whether cause exists for the Department of Financial Services (DFS) to be appointed receiver;
- Exempts the Office of Insurance Regulation (OIR) from the automatic stay provisions;
- Provides that the DFS may assume or reject unexpired leases or executory contracts of an insurer and pay expenses during the pendency of a receivership under contracts, leases, and other arrangements entered by insurers before commencement of the receivership;
- Provides that officers, directors, and managers, of a liquidated insurer are discharged of authority except as may be delegated by the DFS;
- Limits certain defenses which may be raised by third parties in actions brought by or against the DFS in its capacity as receiver;
- Limits third parties from asserting or raising obligations, claims, and defenses, which were not recorded in the records of the insurer in receivership, with certain exceptions;

- Allows the court more flexibility in approving procedures for the “deem filing” of claims, or claims where the DFS deems a claim filed and can distribute funds, such as a refund of unearned premium, to the claimant without the need of a formal claim;
- Allows the court to set a deadline for the filing of claims;
- Limits allowed claims under insurance policies to the applicable policy limits and disallows claims for post-judgment interest accrued after the liquidation date;
- Adds all costs and expenses related to administrative supervision to Class 1 of the priority of claims to be paid in distribution;
- Adds claims related to healthcare coverage by physicians, hospitals, and other providers of a health insurer or health maintenance organization to Class 2 of the priority of claims to be paid in a distribution;
- Adds claims of residents which arise out of a continuing care contract to Class 2 of the priority of claims to be paid in a distribution;
- Adds claims of certain creditors, including claims for punitive damages, bad faith, or wrongful settlement practices to Class 6 of the priority of claims to be paid in a distribution; and
- Removes certain notice requirements related to early access distributions to guaranty associations.

II. Present Situation:

Receivership is a judicial proceeding in which the Department of Financial Services (DFS) is placed in control of the insurer for the purpose of rehabilitating or liquidating the insurer. The DFS may seek to be appointed receiver¹ through a delinquency proceeding in court for the purpose of rehabilitating an impaired insurer or, if appropriate, liquidating the insolvent company. The primary goal of rehabilitation is to restore the financial solvency of the insurer² while the primary goal of liquidation is to secure and maximize the assets of the insolvent company for the benefit of its policyholders.³ Over the years, the National Association of Insurance Commissioners (NAIC) has drafted various model laws to govern insurer insolvency.⁴ The NAIC adopted the Insurer Receivership Model Act in 2005.⁵

This bill amends various provisions of part I of ch. 631, F.S., governing insurer rehabilitation and liquidation in Florida. Many of the revisions are to adopt portions of the NAIC Insurer Receivership Model Act (Model Act).

¹ The DFS Division of Rehabilitation and Liquidation acts as receiver when the DFS is appointed. *See* <http://www.myfloridacfo.com/Division/Receiver/>.

² *See* <http://www.myfloridacfo.com/Division/Receiver/SummaryofRehabilitationunderChapter631PartIFloridaStatutes.htm> (last accessed February 28, 2017).

³ *See* <http://www.myfloridacfo.com/Division/Receiver/LiquidationSummary.htm> (last accessed February 28, 2017).

⁴ Prior model acts include the Uniform Insurers Liquidation Act and the Rehabilitation and Liquidation Model Act. *See* <https://www.irmi.com/articles/expert-commentary/insurer-insolvency-and-reinsurance> (last accessed February 28, 2017).

⁵ *See* <http://www.naic.org/store/free/MDL-555.pdf> (last accessed February 28, 2017).

Delinquency Proceedings

A delinquency proceeding is a proceeding commenced against an insurer for the purpose of liquidating, rehabilitating, reorganizing, or conserving the insurer.⁶ The circuit court in Leon County has jurisdiction over delinquency proceedings.⁷ Florida law provides for various guaranty associations to protect policyholders in the event an insurer becomes insolvent. Insurers are generally required to be members of the associations related to their lines of business. The DFS must give notice of all hearings pertain to the adjudication of a member insurer to the Florida Insurance Guaranty Association, the Florida Workers' Compensation Insurance Guaranty Association, and the Florida Life and Health Guaranty Association.

Section 631.031, F.S., governs the initiation of delinquency proceedings. It requires the Office of Insurance Regulation (OIR) to notify the DFS upon a determination that one or more grounds for the initiation of delinquency proceedings exist. The OIR must provide the DFS with evidence and documentation of the delinquency. The DFS may commence a proceeding by application to the court for an order directing the insurer to show cause why the relief (such as rehabilitation or liquidation) should not be granted. The DFS has noted periods of extended delay in some cases where the insurer does not respond or the court does not hold a hearing.⁸

Once the DFS files an application or a petition for an order to show cause, s. 631.041, F.S., provides for an automatic stay. The stay prohibits:

- The commencement or continuation of judicial, administrative, or other action or proceeding against the insurer or against its assets;
- The enforcement of a judgment against the insurer obtained either before or after the commencement of the delinquency proceeding;
- Any act to obtain possession of property of the insurer;
- Any act to create, perfect, or enforce a lien against property of the insurer with specified exceptions;
- Any act to collect, assess, or recover a claim against the insurer; and
- The setoff or offset of any debt owing to the insurer with specified exceptions.⁹

The stay applies to all persons except the DFS. According to the DFS, there has been confusion over whether the stay applies to regulatory actions taken by the OIR.¹⁰

Actions by and Against the Receiver

Section 112 of the Model Act prohibits third parties from raising insurer management misconduct as a defense to a claim by the receiver. For example, there have been cases where the insurer's managers set up a scheme to issue high-risk policies without sufficient funds to cover claims. When the insurer became insolvent, the liquidator sued auditors for negligently failing to discover the scheme. The auditors argued that the liquidator, who stands on the shoes of the

⁶ s. 631.011(6), F.S.

⁷ s. 631.021(1)-(3), F.S.

⁸ Department of Financial Services, *Analysis of SB 730* (February 19, 2017).

⁹ s. 631.041(1), F.S.

¹⁰ Department of Financial Services, *Analysis of SB 730* (February 19, 2017).

insurer, cannot prevail because the misdeeds of the insurer's management should be imputed to the liquidator.¹¹ Section 112 of the Model Act prohibits such defenses.

Claims in Excess of Policy Limits

The DFS reports that there has been litigation over when bad faith claims for incidents that occurred before the receivership must be paid.¹² In *Bender v. State*,¹³ the court held that while s. 631.192, F.S., did not prohibit the receiver from paying claims in excess of policy limits, the receiver was not required to under the facts of that case. The DFS reports that the receiver has been ordered to pay claims in excess of policy limits in other cases.¹⁴

Claim Priority

Section 631.271, F.S., sets the priority order in which claims against the receivership will be paid. Class 1 claims, the first claims paid, include the receiver's costs and expenses of administration and the expenses of guaranty associations in handling claims. It does not include costs and expenses of administrative supervision.¹⁵

In general, loss claims under health insurance are Class 2 claims.¹⁶ The DFS considers medical provider claims in HMO receiverships to be Class 6 claims.¹⁷

Current law does not specify which class claims against insurers in excess of policy limits, such as bad faith or punitive damage claims belong.¹⁸ Courts have issued different rulings in different cases with one court holding a bad faith claim is a Class 2 claim and another holding it is a Class 6 claim.¹⁹

III. Effect of Proposed Changes:

The bill makes various changes to ch. 631, F.S., relating to insurer insolvency, rehabilitation, and liquidation. **Section 1** provides that Florida will provide reciprocity in the treatment of policyholders in receivership with states that enact the NAIC Insurer Model Receivership Act.

¹¹ *Thaubalt v. Chait*, 541 F.3d 512, 528 (3rd Cir. 2008); *Schacht v. Brown*, 711 F.2d 1343 (7th Cir. 1982).

¹² Department of Financial Services, *Bill Analysis of SB 730* (February 19, 2017) at p. 3.

¹³ 17 So.3d 770 (Fla. 1st DCA 2009).

¹⁴ Department of Financial Services, *Bill Analysis of SB 730* (February 19, 2017) at p. 3.

¹⁵ The OIR can place an insurer in administrative supervision if it finds the insurer is in an unsound condition or other reasons. *See* s. 624.81, F.S. It may appoint a deputy supervisor to supervise the insurer during the period of administrative supervision. *See* s. 624.87, F.S.

¹⁶ s. 631.271(1)(b), F.S.

¹⁷ Department of Financial Services, *Bill Analysis of SB 730* (February 10, 2017) at p. 3-4.

¹⁸ Department of Financial Services, *Bill Analysis of SB 730* (February 19, 2017) at p. 3.

¹⁹ Department of Financial Services, *Bill Analysis of SB 730* (February 19, 2017) at p. 3.

Delinquency Proceedings

Section 2 amends s. 631.021, F.S., to require the DFS to give notice of hearings to the Florida Health Maintenance Organization Consumer Assistance Plan²⁰ that pertain to the insolvency of a member insurer. It provides that the circuit court in Leon County has exclusive jurisdiction over all insurer assets or property wherever located once it enters an order of rehabilitation or liquidation.²¹ The bill also provides that ch. 631, F.S., constitutes the state's receivership laws, which prevail in any conflict with any other law.²²

Section 3 amends s. 631.031, F.S., to require an insurer subject to an order to show cause to file a response to the order, together with any defenses it may have, no later than 20 days after service of the order to show cause. The response must be filed at least 15 days before the date of the hearing set by the order to show cause. The hearing to determine whether cause exists for the DFS to be appointed receiver must be commenced within 60 days.

Section 4 amends the automatic stay provision of s. 631.041, F.S., to provide that the automatic stay does not apply to the OIR. This will allow OIR to continue to perform its regulatory role as necessary during a receivership.

Section 5 amends s. 631.141, F.S., to allow the DFS to assume or reject any executory contract or unexpired lease of the insurer and allow the DFS to pay any expenses under contracts, leases, employment agreements, or other arrangements entered into by the insurer before receivership. These provisions are from sections 114 and 116 of the Model Act. They give the DFS the flexibility to review contracts and other obligations and determine how to proceed based on the best interest of the receivership.

The bill provides that all officers, directors, and managers of the insurer are discharged except as provided by the DFS. This resolves any conflicts between ch. 631, F.S., and other statutes relating to the dissolution of business entities.

Section 6 makes a technical change to s. 631.152, F.S.

Actions by and Against the Receiver

Section 7 creates s. 631.1521, F.S., which creates section 112 of the Model Act in Florida law. It provides that an allegation by the receiver of improper or fraudulent conduct against any person may not be the basis of a defense by a third party to the enforcement of a contractual obligation owed to the insurer. The bill does not bar a third party from raising a defense that the conduct was materially and substantially related to the contractual obligation for which enforcement is sought. This will limit the ability of third parties to avoid contractual obligations based on improper conduct by, for example, officers of the insurer that is unrelated to the contractual obligation.

²⁰ The Florida Health Maintenance Organization Consumer Assistance Plan is created to protect the subscribers of HMOs against the failure of the HMO to perform its contractual obligations due to its insolvency. *See* s. 631.812, F.S. HMOs are required to be members of the plan. *See* s. 631.815, F.S.

²¹ The language in the bill is from section 105 of the Model Act.

²² Section 102 of the Model Act.

The bill provides that a prior wrongful or negligent action of any present or former officer, manager, director, trustee, owner, employee, or agent of the insurer may not be asserted as a defense to a claim by the receiver under a theory of estoppel, comparative fault, intervening cause, proximate cause, reliance, mitigation of damages, or otherwise. The bill further provides that the affirmative defense of fraud in the inducement may be asserted against the receiver in a claim based on a contract. Evidence of fraud in the inducement is admissible only if it is contained in the records of the insurer. This bill will make it easier, for example, for the DFS to bring claims of professional negligence against accountants or auditors that should have discovered the insurer's insolvency earlier.

The bill provides that an action or inaction by an insurance regulatory authority may not be asserted as a defense to a claim by the DFS. This will prevent, for example, an officer of the insurer from arguing that the OIR should have known of the insolvency sooner and taken steps to prevent it.²³

Section 8 creates s. 631.1552, F.S., based on section 113 of the Model Act. It will require evidence of claims or defenses raised by certain parties other than the DFS to be recorded in the books or records of the insurer. This puts the DFS on notice of the possible claims or defenses. It provides that in a proceeding by the receiver against an affiliate, a controlled or controlling person, or a present or former officer, manager, director, trustee, or shareholder of the insurer may not assert any defense unless:

- Evidence of the defense was recorded in the books and records of the insurer at or about the time the events giving rise to the defense occurred; and
- If required by statutory accounting practices and procedures, such events were reported on the insurer's official financial statements filed with the OIR.

The bill prohibits an affiliate, a controlled or controlling person, or a present or former officer, manager, director, trustee, or shareholder of the insurer from asserting any claim unless:

- The obligations were recorded in the books and records of the insurer at or about the time the obligations were incurred; and
- If required by statutory accounting practices and procedures, the obligations were reported on the insurer's official financial statements filed with the OIR.

Claim Filing

Section 631.181, F.S., generally requires claimants to file a proof of claim with the DFS before receiving a distribution from the estate. There are some situations, such as returning unearned premium, where the DFS can determine the claim without requiring a claimant to submit proof. **Section 9** allows the court to allow alternative procedures and requirements for claim filing and proof of claims. This is consistent with section 701 of the Model Act.

Current law does not have specific authority for the court to set a deadline for the filing of claims. **Section 9** allows the DFS to petition the court to set a claim filing deadline.

²³ Such an argument was made, and rejected, in *Wooley v. Lucksinger*, 61 So.3d 507 (La. 2011).

Claims in Excess of Policy Limits

Section 10 provides that a claim under a policy of insurance may not be allowed for an amount in excess of the applicable policy limits. This is similar to a provision in section 703 of the Model Act. The bill disallows claims for post judgment interest that accrue after the date of liquidation.

Claim Priority

Section 11 provides that the deputy supervisor's costs and expenses of administration are Class 1 claims. All claims related to a patient's healthcare coverage by physicians, hospitals, and other providers of a health insurer or health maintenance organization, and all claims of residents arising out of a continuing care contract are Class 2 claims. It provides that claims against an insurer for wrongful settlement practices, bad faith, and punitive damages are Class 6. The bill provides that interest on allowed claims accrue from the date of liquidation until the claims are adjudicated. The interest rate is the statutory rate calculated according to s. 55.03, F.S.

Miscellaneous Provisions

Section 12 amends s. 631.391, F.S., to require former officers, directors, managers, trustees, agents, adjusters, employees, independent contractors, or a controlling person of an insurer or affiliate to cooperate with the DFS or OIR in any proceeding under ch. 631, F.S., or any investigation preliminary or incidental to the proceeding.

Section 631.395, F.S., provides that an order of liquidation must direct the DFS to coordinate the operation of the receivership with the relevant insurance guaranty fund. The authorization must include authorization to release copies of claim files or other documents related to claims on file with the insolvent insurer. **Section 13** provides that the DFS may release the original documents to the guaranty fund.

Section 631.397, F.S., deals with "early access" distributions by the DFS to guaranty associations to allow the associations to begin paying claims without the need to assess member insurers. Current law requires the DFS to propose a plan to the court within 120 days of the determination of insolvency and give notice of the plan to other insurance commissioners at least 15 days before filing the plan with the court. **Section 14** eliminates the 120-day requirement and the notice to other insurance commissioners. In practice, the DFS coordinates early access distributions with the appropriate guaranty associations so the DFS believes the requirements are not necessary.²⁴

Section 15 provides a July 1, 2015, effective date.

IV. Constitutional Issues:

A. Municipality/County Mandates Restrictions:

None.

²⁴ Department of Financial Services, *Bill Analysis of SB 730* at p. 6-7.

B. Public Records/Open Meetings Issues:

None.

C. Trust Funds Restrictions:

None.

V. Fiscal Impact Statement:**A. Tax/Fee Issues:**

None.

B. Private Sector Impact:

None.

C. Government Sector Impact:

The DFS does not anticipate a fiscal impact.²⁵

VI. Technical Deficiencies:

None.

VII. Related Issues:

None.

VIII. Statutes Affected:

This bill substantially amends the following sections of the Florida Statutes: 631.015, 631.021, 631.031, 631.041, 631.141, 631.152, 631.181, 631.192, 631.271, 631.391, 631.395, and 631.397.

This bill creates the following sections of the Florida Statutes: 631.1521 and 631.1522.

IX. Additional Information:**A. Committee Substitute – Statement of Changes:**

(Summarizing differences between the Committee Substitute and the prior version of the bill.)

None.

B. Amendments:

None.

²⁵ Department of Financial Services, *Bill Analysis of SB 730* (February 19, 2017) at p. 7.

This Senate Bill Analysis does not reflect the intent or official position of the bill's introducer or the Florida Senate.
