COMMONWEALTH OF VIRGINIA

STATE CORPORATION COMMISSION

AT RICHMOND, JANUARY 8, 2004

COMMONWEALTH OF VIRGINIA, ex rel.

STATE CORPORATION COMMISSION,
Applicant,

v.

CASE NO. INS-2003-00024

INS-2003-00239

RECIPROCAL OF AMERICA and
THE RECIPROCAL GROUP,
Respondents.

ORDER ON RECONSIDERATION

On November 12, 2003, the Commission entered an Order[1] directing the Deputy Receiver of ROA[2] to make payments to certain claimants that are indemnity or wage-replacement payments, as requested in the Application; the Order did not authorize physician, hospital, or other health care facility payments at the present time. The Commission also referred to a Hearing Examiner the question of whether the Self-Insured Trusts and Group Self-Insurance Associations or employers thereof that were the subject of the Application constitute "other policyholders arising out of insurance contracts" pursuant to § 38.2-1509 B 1(ii) of the Code of Virginia.[3]

On December 1, 2003, the Indiana Insurance Guaranty Association, the Kansas Insurance Guaranty Association, the Mississippi Insurance Guaranty Association, and the Tennessee Insurance Guaranty Association ("Guaranty Associations") filed the Certain Guaranty

[1] The Order was in response to the Application for Order Authorizing the Continuation of Workers' Compensation Disability Payments by Reciprocal of America and The Reciprocal Group for Workers' Compensation Claims Denied Coverage by State Guaranty Associations, filed by the Deputy Receiver of ROA on July 11, 2003 ("Application").

[2] Reciprocal of America and The Reciprocal Group are collectively referred to herein as "ROA."

[3] *Application of Reciprocal of America and The Reciprocal Group, For a Determination Whether Certain Workers' Compensation Insurance Policy Payments May be Made to Claimants Formerly Covered by SITs and GSIAs*, Case No. INS-2003-00239. All statutory cites herein are to the Code of Virginia.

Associations' Petition for Rehearing or Reconsideration ("Petition").[4] Therein, the Guaranty Associations request that the Commission rehear or reconsider its November 12, 2003, Order in this matter. The Guaranty Associations assert that the Commission erred in permitting the aforementioned payments and that the Commission has authorized an unlawful preference in violation of § 38.2-1509 B. The Guaranty Associations request that the Commission deny the Application.

By Order entered on December 2, 2003, the Commission granted the Petition for the purpose of receiving responses thereto from all parties in this case. The Commission also directed the Deputy Receiver of ROA not to make any of the aforementioned payments until we have decided the issues addressed in the Petition. We also directed the Hearing Examiner to proceed in Case No. INS-2003-00239 without waiting for us to render a decision on the Petition.

Responses to the Petition were filed by the Deputy Receiver of ROA, the Virginia Property and Casualty Insurance Guaranty Association ("VPCIGA"), the Virginia Uninsured Employer's Fund ("UEF"), and the Coastal Region Board of Directors and Alabama Subscribers and the Kentucky Claimants[5] (collectively referred to herein as "Coastal"). Additionally, on December 23, 2003, the Guaranty Associations filed a Motion for Leave to File Reply to Deputy Receiver's Response in Opposition to Petition for Rehearing or Reconsideration and the Guaranty Associations' Reply to Deputy Receiver's Response in Opposition to Petition for Rehearing or Reconsideration. We hereby grant such Motion, and we have considered all of the aforementioned pleadings in reaching our decision on the Petition.

The Guaranty Associations assert that we have misunderstood the term "preference" in § 38.2-1509 B 1(ii) of the Code of Virginia. The Guaranty Associations contend that their

[4] The Guaranty Associations also filed a Petition for Suspension of Order Pending Appeal. On December 9, 2003, the Guaranty Associations filed a Notice of Appeal.

[5] The "Kentucky Claimants" include Clark Regional Medical Center, T.J. Samson Community Hospital, Pineville Community Hospital, Highlands Regional Medical Center, Twin Lakes Medical Center/Trover Clinic Foundation, Murray-Calloway County Hospital, Owensboro Mercy Health Center, Harrison Memorial Hospital, River Valley Behavioral Health Hospital, Muhlenberg Community Hospital, and Lincoln Trail Hospital.

payment of certain workers' compensation insurance policy claims, and not others, does not create a preference, because such payments are being made from the funds of the Guaranty Associations, not from the assets of the ROA estate. Moreover, the mandate in § 38.2-1509 B 1(ii) that assets be "apportioned without preference" governs the manner in which the Commission may disburse the assets of the ROA estate.[6] The Guaranty Associations further assert that the Commission may not disburse any assets of the estate until it first authorizes an early access distribution to all guaranty associations.[7]

The VPCIGA filed its Response to the Petition on December 15, 2003.[8] The VPCIGA supports the Petition and also asserts that the Commission has confused the concept of a "preference" in the amounts that are paid from the assets of the estate of ROA with the amounts received by various claimants from all sources. The VPCIGA also contends that the Commission must disburse assets to guaranty associations before any distribution is made to other claimants.

Coastal supports the Commission's Order of November 12, 2003, and requests that the Commission "overrule" the Petition. Coastal states that the assertions by the Guaranty Associations, if accepted, would turn the Virginia statutory scheme designed for the protection of policyholders and claimants into a mechanism to protect guaranty associations and the insurers that underwrite them.

The UEF also supports the Commission's Order of November 12, 2003, and disagrees with the Guaranty Associations' characterization of what constitutes a preference. The UEF

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[6] Petition at 3-5.

[7] Petition at 6-7.

[8] The VPCIGA also filed the Application of Virginia Property and Casualty Insurance Guaranty Association for Disbursement of Assets, together with a Proposed Plan for Disbursement of Available Assets and a proposed Early Access Agreement ("VPCIGA Application"). By separate Order, we will establish a procedural schedule for the VPCIGA Application, *Application of Virginia Property and Casualty Insurance Guaranty Association*, Case No. INS-2003-00267, and refer such case to a Hearing Examiner.

contends that the Commission properly balanced the equities in determining the priority between the Guaranty Associations and individual injured workers.

The Deputy Receiver of ROA disagrees with the Guaranty Associations also. The Deputy Receiver of ROA asserts that, while he may be bound by the Guaranty Associations' settlement of covered claims pursuant to § 38.2-1609 B, the determination of what constitutes a "covered claim" has not been left to the Guaranty Associations. The Deputy Receiver of ROA also argues that the provisions of Chapter 15 of Title 38.2 are broad enough to permit the Commission to reach the equitable result obtained by the November 12, 2003, Order. The Deputy Receiver further states that the payments authorized by the Commission in its November 12, 2003, Order amount to, at most, approximately $73,000 per week.[9]

NOW THE COMMISSION, having considered the pleadings and arguments of the parties, and the applicable law, finds as follows. We deny the Guaranty Associations' request that we reverse our November 12, 2003 Order. We also deny their request to suspend the execution of that Order pending an appeal.

The "preference" definition proffered by the VPCIGA and the Guaranty Associations is not acceptable for construing the provisions of § 38.2-1509. We must, in our role as the arbiter of this dispute, construe all of the provisions of the law together. Further, in carrying out our role as receiver of ROA, we must consider all the circumstances before us, both factual and legal.

The Guaranty Associations and the VPCIGA suggest that payments made by guaranty associations and received by claimants are completely divorced from payments made from estate assets. The fallacy of this proposition is demonstrated by the VPCIGA when, along with its response including this argument, it also files an application to be reimbursed, from the estate assets, for the payments it has already made for what it has determined are "covered claims."

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[9] Deputy Receiver's Response in Opposition to the Guaranty Associations' Petition for Rehearing or Reconsideration, filed December 15, 2003, at 8.

Ultimately, the guaranty associations expect to be paid very significant sums from the estate assets. The VPCIGA states that it has paid "covered claims" in an amount aggregating $4,257,549 and estimates that it will be required to pay additional "covered claims" in the amount of $33,286,111.[10] As long as the guaranty associations are looking to and receive estate assets for payment, their actions cannot be ignored as they request. Estate assets will fund, at least in part, the payments made by the guaranty associations. This is a reality we must consider.

Also, as we noted in our November 12, 2003 Order, there has as yet been no determination by this Commission that any claims (including those that are being paid by the various guaranty associations and those that are not being paid) have been properly classified as policyholder claims or "covered claims." The guaranty associations have made determinations that certain claims are "covered claims" and others are not. The Deputy Receiver of ROA disagrees with a number of these determinations. Estate assets are now being requested to repay the VPCIGA for what it has determined are "covered claims." If the estate assets are paid as requested, estate assets will have funded a preference if the Deputy Receiver is correct. Indeed, as we noted earlier, the preference may be continuing.

The Guaranty Associations also suggest that if we act in this case, we must do the same for each and every possible claimant regardless of their claim.[11] Such simply is not the case. As other parties have explained[12] and as referenced in our earlier order, we can and must make judgments. Such is the nature of equity proceedings. As we noted in our Order of November 12, 2003, other provisions of Chapter 15 of Title 38.2, such as §§ 38.2-1502, 38.2-1507, and 38.2-1508, permit us to act as we do here.

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[10] VPCIGA Application at 3.

[11] Petition at 4.

[12] Response of Certain Respondents to Certain Guaranty Associations' Petition for Rehearing or Reconsideration, filed on December 15, 2003, by Coastal and the Kentucky Claimants, at 5; Virginia Uninsured Employer's Fund's Response to Certain Guaranty Associations' Petition for Rehearing or Reconsideration, filed on December 15, 2003, at 2; Deputy Receiver's Response in Opposition to the Guaranty Associations' Petition for Rehearing or Reconsideration, filed on December 15, 2003, at 5-6.

In this case, however, reliance on such equitable powers should not be necessary. We are faced here with potentially conflicting preferences. If the VPCIGA and the Guaranty Associations are correct, there may be a small preference if payments are made as we direct.[13] If the Deputy Receiver is correct, a preference is occurring now with funds that are to be reimbursed by the estate. This preference may be equally small vis-à-vis the estate and its impact on other claimants, but it can be, and perhaps already has been, catastrophic to the individuals affected by the loss of their daily sustenance. This conflict is real, both factually and legally. We are compelled by the circumstances to address now the request for resumption of these payments, even if provisionally while related and underlying issues are resolved in an orderly manner.

As we noted earlier, in reality, when a payment is made before a final disbursement, there can never be a one hundred percent guarantee there will never be a preference. The VPCIGA itself noted that payments may be made that might create a preference as long as they "can be subsequently adjusted so that ultimately there is no preference."[14] Of course, reality may intervene so that "ultimately" there may still be a preference. Our job, however, is to seek to ensure that "ultimately" there will be no preference. Our approach here does just that.

Requiring payments to be made now, pending resolution of underlying issues, should reduce the preferences created if the Deputy Receiver is correct.[15] In order to limit the exposure to preferences if the Deputy Receiver is wrong, we have referred the "claims of other policyholders arising out of insurance contracts" issue to a Hearing Examiner.[16] If a

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[13] See text and note at note 17, *infra*.

[14] Objection of Virginia Property and Casualty Insurance Guaranty Association to Payment by Reciprocal of America and The Reciprocal Group of Workers' Compensation Claims, filed on August 14, 2003, at 5.

[15] If payments begin within several weeks of this Order, these claimants will have been deprived of almost six months of payments, funded, at least in part, by estate assets that were paid to other similarly situated claimants. There is no way for these claimants, from a practical if not legal standpoint, to make up for this loss.

[16] *Application of Reciprocal of America and The Reciprocal Group, For a Determination Whether Certain Workers' Compensation Insurance Policy Payments May be Made to Claimants Formerly Covered by SITs and GSIAs*, Case No. INS-2003-00239.

determination is ultimately made in that case that these claimants are not "policyholders arising out of insurance contracts" under § 38.2-1509 B 1(ii), then the authorized payments would cease, and the Deputy Receiver would be required to seek aggressively to recover the money disbursed from the ROA estate from all available sources. In this event, any preference should be very small.[17]

On the other hand, if a determination is made that these claims do constitute "claims of other policyholders arising out of insurance contracts," then we will be squarely presented with the question of whether they also constitute "covered claims" under § 38.2-1603.[18] Such a scenario would require us to confront first the issue of whether we have jurisdiction to determine what constitutes a "covered claim," or, as the Guaranty Associations argue, if that determination is left to the unfettered discretion of the associations.[19]

If we find in due course that we do have jurisdiction to reach that question, and we ultimately find that the workers' compensation payments authorized constitute "covered claims," then the preferences will have been reduced but not eliminated.[20] If, on the other hand, we determine that we do not have jurisdiction to reach the question of what constitutes a "covered claim" or that we have such jurisdiction and conclude that the claims in question are not "covered claims," then a small preference may be possible, but extremely remote.[21]

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[17] As noted in our November 12, 2003 Order, such sources would include, but not be limited to, guaranty associations, uninsured employers' funds, employers, self-insurance guaranty associations, and surety bonds. The determination of whether the claimants are "policyholders arising out of insurance contracts" should be completed in the next several months. Even assuming that the determination takes six months from the date of this Order, the maximum exposure would be approximately $1.9 million (26 weeks x $73,000) or less than .5% of estate assets. This amount, of course, could be greatly reduced or eliminated by the actions of the Deputy Receiver.

[18] Indeed, the VPCIGA Application, which seeks payment from the ROA estate, may result in our having to make such a determination if the Deputy Receiver of ROA seeks to offset any payments made by him that he asserts should have been made by various guaranty associations. See, Transcript at 180-181.

[19] Petition at 3-4.

[20] As noted earlier, the claimants now to be paid from the assets of the ROA estate have already gone almost six months without any payment.

[21] If it is determined that these claimants are "policyholders" but do not possess "covered claims," then any possible preference will almost certainly be eliminated. First, the policyholders will have gone without any payment for

Thus, there remain fundamental issues underlying this matter yet to be determined by the Commission directly, or upon report by a Hearing Examiner. The decision now, therefore, is at most an interim step in the final disposition of the issues presented by the guaranty associations in their filings, and in the manner in which they have elected to proceed.

As a further and related pending matter, the Commission agrees that the provisions of § 38.2-1509 provide for distributions to guaranty associations once "an application has been filed with the Commission." We will act on the VPCIGA Application in accordance with the pertinent statutory provisions. In the meantime, however, the scheme established by the General Assembly in Chapters 15 and 16 of Title 38.2 does not require or allow us to refrain from authorizing any disbursements from the estate of an insurer until we can conclude to an absolute certainty that no preferences will ultimately result from our action. Inaction here constitutes the action of denying benefits and such denial may create a preference. Thus, both action and inaction create the potential for preferences. What we direct today will reduce both the potential for preferences and the extent of any preferences that may ultimately exist.

We also deny the Guaranty Associations' request to suspend our Order pending an appeal of this decision. Without addressing the finality issue,[22] we note that suspending our Order would create a greater opportunity for the creation of a preference.

Accordingly, IT IS ORDERED THAT:

(1) The Guaranty Associations' Motion for Leave to File Reply to Deputy Receiver's Response in Opposition to Petition for Rehearing or Reconsideration is GRANTED;

(2) The Guaranty Associations' Petition for Rehearing or Reconsideration is DENIED;

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approximately six months; if it takes six months to reach this decision, there would be no preference as long as the policyholders ultimately are paid at the rate of 50%. If it takes longer than six months to reach a decision or the payout rate is less than 50%, then the payout rate can be "adjusted" for the remainder of the receivership and the final payout, so that "ultimately there is no preference." Moreover, the Deputy Receiver will, as stated earlier, aggressively seek to recover funds disbursed from the ROA estate from all available sources. Thus, in this instance it is highly unlikely that "ultimately" there will be any preference.

[22] Pursuant to § 12.1-39, only a "final finding, decision settling the substantive law, order, or judgment of the Commission" is appealable to the Supreme Court of Virginia. See also, art. IX, § 4 of the Constitution of Virginia.

(3) The Order of November 12, 2003 is reinstated, effective as of the date of this Order, subject to review upon further proceedings;

(4) The Guaranty Associations' Petition for Suspension of Order Pending Appeal is DENIED; and

(5) This matter is continued.

MORRISON, COMMISSIONER, DISSENTING,

I continue to believe that § 38.2-1509 does not permit the conclusion reached by the majority. I do not agree that the supposed "equitable powers" of this Commission permit us to authorize a preference prohibited by § 38.2-1509. Therefore, I must dissent from the majority's conclusion that assets of the ROA estate may be disbursed at this time to make certain worker's compensation payments.

AN ATTESTED COPY hereof shall be sent by the Clerk of the Commission to all persons on the official Service List in this matter. The Service List is available from the Clerk of the State Corporation Commission, c/o Document Control Center, 1300 East Main Street, First Floor, Tyler Building, Richmond, Virginia 23219.