

COMMONWEALTH OF VIRGINIA  
STATE CORPORATION COMMISSION

AT RICHMOND, JUNE 16, 2014

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COMMONWEALTH OF VIRGINIA, *ex rel.*

STATE CORPORATION COMMISSION

v.

CASE NO. INS-2013-00190

RECIPROCAL OF AMERICA and  
THE RECIPROCAL GROUP, in Receivership,

FINAL ORDER

On August 2, 2013, Jacqueline K. Cunningham, the Deputy Receiver ("Deputy Receiver") of Reciprocal of America ("ROA") and The Reciprocal Group, filed an application ("Application") wherein the Deputy Receiver sought an order from the State Corporation Commission ("Commission") for approval of two major steps in this receivership: the increase of claims payments from 95% to 100%, and approval of a proposed Loss Portfolio Transfer Agreement ("LPT Agreement") for ROA's workers' compensation insurance book of business.

Specifically, the Deputy Receiver sought the Commission's entry of: (1) a scheduling order setting a hearing on the proposed increase in the claims payment percentage and the LPT Agreement for ROA's workers' compensation insurance book of business, approving notice procedures, and establishing response dates; and (2) following the hearing, a final Commission order that: (i) authorized the increase from 95% to 100% of the percentage that ROA may pay ("Payment Percentage") on approved claims by Guaranty Associations,<sup>1</sup> policyholders, and insureds for losses, indemnification, or defense costs covered under ROA insurance policies

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<sup>1</sup> The Guaranty Associations are statutory organizations that have been responsible for approximately half the claims in the Workers' Compensation Book (as defined in the LPT Agreement) since the inception of the receivership. The Guaranty Associations include: Alabama Insurance Guaranty Association; Arkansas Property & Casualty Insurance Guaranty Fund; Georgia Insurers Insolvency Pool; Kentucky Insurance Guaranty Association; Mississippi Insurance Guaranty Association; Missouri Property & Casualty Insurance Guarantee Association; North Carolina Insurance Guarantee Association; South Carolina Property & Casualty Insurance Guaranty Association; and Pennsylvania Property & Casualty Insurance Guaranty Association. Hearing Examiner's Report at 2 and n.5.

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(Policy Claims for Economic Damages a/k/a "Direct Claims"); (ii) authorized the payment of an additional 5% distribution or credit to all Guaranty Associations, policyholders, and insureds who had received a 95% distribution on their Direct Claims to account for the difference in payment percentage distributions; (iii) authorized the Deputy Receiver to make full payment on indirect claims if and when she concluded that she could do so without undue risk of unlawful preference; (iv) authorized the continued payment of all administrative expenses and secured creditor claims at 100%; (v) approved the proposed transfer of ROA's workers' compensation insurance business to Providence Washington Insurance Company ("PWIC") in accordance with, and subject to, the terms and conditions of the LPT Agreement;<sup>2</sup> and (vi) approved the steps necessary to implement and consummate the proposed Loss Portfolio Transfer and other transactions contemplated by the LPT Agreement (collectively, "Loss Portfolio Transfer").

On August 14, 2013, the Kentucky Hospitals filed a Notice of Participation.<sup>3</sup> The Kentucky Hospitals are policyholders and "direct insureds" of ROA. Additionally, as subscribers of ROA, the Kentucky Hospitals also have an equity interest in the ROA receivership estate.<sup>4</sup> The Kentucky Hospitals joined the case to protect their interests as policyholders, equity subscribers, and claimants of ROA. Through their participation, the Kentucky Hospitals sought to ensure that no action was taken in this case, including approval of the proposed Loss Portfolio Transfer, which would prejudice or adversely affect either: (i) the priority status of the Kentucky

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<sup>2</sup> Pursuant to the LPT Agreement, claims processing for the workers' compensation book of business will be performed by an affiliate of PWIC, SeaBright Insurance Company ("SeaBright").

<sup>3</sup> The Kentucky Hospitals ("Kentucky Hospitals") include: Appalachian Regional Healthcare; Hardin Memorial Hospital; Highlands Regional Medical Center; Murray-Calloway County Hospital; Owensboro Mercy Health System; Regional Medical Center/Trover Clinic Foundation; Rockcastle Hospital and Respiratory Care Center; St. Claire Regional Medical Center; and T.J. Sampson Community Hospital.

<sup>4</sup> Kentucky Hospitals' Notice of Participation at 1-2.

Hospitals as claimants or their rights, individually and collectively, to seek and obtain payment of their ROA claims; and (ii) their rights as equity subscribers.<sup>5</sup>

On August 29, 2013, the Commission entered a Scheduling Order Setting Hearing, Approving Notice Procedures, and Establishing Response Dates. The Commission set a hearing on the Application for December 4, 2013. In addition, the Commission approved the Deputy Receiver's proposed notice requirements and directed that notice of the Application and hearing be given. Finally, the Commission established a procedural schedule for the case and assigned the case to a Hearing Examiner to conduct all further proceedings on behalf of the Commission and to file a final report.

A public hearing was convened as scheduled on December 4, 2013. The Deputy Receiver appeared by her counsel, Patrick H. Cantilo, Esquire. The Commission's Bureau of Insurance appeared by its counsel, John O. Cox, Esquire. The Kentucky Hospitals appeared by their counsel, Greg E. Mitchell, Esquire, and William J. George, Esquire. The Deputy Receiver's Proofs of Notice by Mailing, Publication, and Posting were accepted into the record as Exhibit A. There were no public witnesses.

On March 31, 2014, the Hearing Examiner filed his Report ("Hearing Examiner's Report" or "Report"). In his Report he found<sup>6</sup> that:

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<sup>5</sup> *Id.* at 2.

<sup>6</sup> As an initial matter, the Hearing Examiner addressed which hospitals have appeared by counsel in this proceeding since the Kentucky Hospitals' Notice of Participation listed nine hospitals as parties to the case, but subsequent pleadings and objections referred to fourteen additional hospitals and deleted one hospital from the original list. The Hearing Examiner found the following hospitals have appeared and have subjected themselves to the Commission's jurisdiction in this case: Appalachian Regional Healthcare; Baptist Health Madisonville; Baptist Health Richmond; Clinton County Hospital; Crittendon Health Systems; Cumberland Hospital; Hardin Memorial Hospital; Harrison Memorial Hospital; Highlands Regional Medical Center; Livingston Hospital & Healthcare Service; Marcum & Wallace Hospital; Marshall County Hospital; Monroe County Hospital; Murray-Calloway County Hospital; Ohio County Hospital; Owensboro Mercy Health System; Pineville Community Hospital; Regional Medical Center/ Trover Clinic Foundation; Rockcastle Hospital and Respiratory Care Center; St. Claire Regional Medical Center; St. Joseph Mt. Sterling (formerly, Gateway Regional Medical Center); T.J. Sampson Community

(1) The Deputy Receiver's request to increase the Payment Percentage to 100% is reasonable and is supported by the evidence.

(2) The Commission may approve the LPT Agreement pursuant to § 38.2-136 C of the Code of Virginia ("Code") without having to obtain policyholder consent to the reinsurance transaction.

(3) Policyholders will not lose any rights or claims afforded under their original policies under the Virginia Property and Casualty Insurance Guaranty Association Act as a result of the Commission's approval of the LPT Agreement.

(4) The Kentucky Hospitals offered no credible evidence that its member hospitals would be harmed as a result of the elimination of the Guaranty Associations' statutory obligation to administer and pay ROA's claims under the terms of the LPT Agreement.

(5) The Kentucky Hospitals offered no evidence that PWIC could not meet its obligations to its policyholders, now or in the future.

(6) The language recommended by the Kentucky Hospitals should be included in the Commission's Final Order to address the issue of covered claims ("Covered Claims").

(7) The Kentucky Hospitals' objections to the cost and efficiency of SeaBright managing ROA's workers' compensation claims have no merit.

(8) SeaBright has the expertise and resources to manage effectively ROA's workers' compensation claims in Kentucky and the other states in which ROA did business.

(9) There is no statutory requirement under Virginia or Kentucky law that PWIC or SeaBright must have a physical presence in either state to transact the business of insurance.

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Hospital; and Twin Lakes Regional Medical Center. Hearing Examiner's Report at 24, 38. We adopt this finding of the Hearing Examiner.

(10) The Commission should deny the Kentucky Hospitals' request to opt out of the LPT Agreement.

(11) The Kentucky Hospitals offered no compelling evidence that PWIC would be unable to meet its financial obligations to its insureds after the Loss Portfolio Transfer.

(12) PWIC has the financial ability to enter into the LPT Agreement with ROA;

(13) The Kentucky Hospitals failed to establish that there were any significant discrepancies in ROA's loss reserves.

(14) There was no compelling business reason for the Deputy Receiver to study the costs of the Kentucky Hospitals assuming their own claims.

(15) The requirement to submit claim files to ROA within 30 days of the LPT Agreement closing date is not unduly burdensome and is necessary to ensure the uninterrupted payment of workers' compensation benefits to injured workers.

(16) The issue of the commutation or assignment of the Gen Re Settlement Trust is moot<sup>7</sup>.

(17) SeaBright is duly licensed in Kentucky to administer the workers' compensation claims of the Kentucky Hospitals.

(18) Kentucky law does not require SeaBright to have a managed healthcare system certified in all 120 counties.

(19) The Kentucky Hospitals failed to produce any compelling evidence that SeaBright's managed healthcare networks cannot deliver workers' compensation benefits in Kentucky.<sup>8</sup>

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<sup>7</sup> The Kentucky Hospitals listed this issue among its objections but did not raise this issue at the hearing, in its post-hearing brief, or in comments to the Hearing Examiner's Report.

<sup>8</sup> Hearing Examiner's Report at 38-39.

The Hearing Examiner recommended that the Commission enter an order:

- (1) Adopting the findings in his Report.
- (2) Approving the proposed increase in the Payment Percentage.
- (3) Approving the LPT Agreement and proposed Loss Portfolio Transfer.

(4) Providing that any amounts due from ROA to PWIC under the LPT Agreement and the Loss Portfolio Transfer shall be treated as a cost and expense of administration under § 38.2-1509 B 1 of the Code, and holding that such payments to PWIC are not on account of an antecedent debt and are not voidable under § 38.2-1513 of the Code.

(5) Relieving the Guaranty Associations from further liability and responsibility for Covered Claims that are part of the "Workers' Compensation Book" (as defined in the LPT Agreement) previously covered by the Guaranty Associations and directing that after the Loss Portfolio Transfer becomes effective, all claimants may only seek payment or reimbursement for the Workers' Compensation Book covered contracts (as defined in the LPT Agreement) from PWIC, except to the extent that the Guaranty Associations fail to return timely the records regarding such claims to the Deputy Receiver.

(6) Providing that PWIC is not responsible or liable for any Indirect Claims and Excluded Losses (as defined in the LPT Agreement) and that no person or entity shall have a valid claim or cause of action against PWIC for any amounts related to or arising in connection with, directly or indirectly, any Indirect Claims and Excluded Losses.

(7) Requiring the Guaranty Associations and policyholders or their third-party administrators who have possession or control of any records or files related to the Workers' Compensation Book to return the same to the Deputy Receiver no later than thirty (30) days after the Deputy Receiver makes a written request for them.

(8) Providing that failure by a Guaranty Association, policyholder, or third-party administrator to return any such file or record within that time will result in forfeiture and waiver by such Guaranty Association, policyholder, or third-party administrator of any right to coverage, payment, or reimbursement by ROA and PWIC for such claims related to such delayed file or record.

(9) Allowing a policyholder to appeal a waiver of coverage under the LPT Agreement for the untimely submission of a claim file by a third party pursuant to the Amended Receivership Appeal Procedure adopted in the Sixth Directive of Deputy Receiver on November 10, 2004<sup>9</sup>.

(10) Providing that no approval or consent is required from (i) any policyholder, insured, or other person covered under any policy that is part of the Workers' Compensation Book, or (ii) any other person or entity in order to effect the assumption by PWIC of the Workers' Compensation Book, or to otherwise effect and consummate the Loss Portfolio Transfer contemplated by, or in connection with, the LPT Agreement.

(11) Approving the retention by the receivership estate of the Gen Re Settlement Trust;<sup>10</sup>

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<sup>9</sup> The Sixth Directive of Deputy Receiver Adopting Amended Receivership Appeal Procedure may be found at: <http://www.reciprocalgroup.com/documents.htm>.

<sup>10</sup> Over the years, the ROA had entered into a number of reinsurance contracts with General Reinsurance Corporation and its subsidiaries and affiliates ("Gen Re"), some covering the Workers' Compensation Book liabilities. As a result of the settlement of a lawsuit, Gen Re established the Gen Re Settlement Trust. Since the Deputy Receiver and Gen Re have not reached an agreement for the commutation or assignment to PWIC of the parties' obligations under the reinsurance agreements and the Gen Re Settlement Trust, the Deputy Receiver will retain the rights and obligations under the Gen Re Settlement Trust after the closing date of the LPT Agreement. Moreover, PWIC has an agreement to provide ROA the necessary reports and support for ROA to seek reimbursements from the Gen Re Settlement Trust. Hearing Examiner's Report at 35-36.

(12) Authorizing the Deputy Receiver to continue seeking an agreement to commute or assign the Gen Re Settlement Trust and, if successful in those efforts, to make the corresponding adjustments in the LPT Agreement with PWIC.

(13) Approving (i) the assignment and transfer of the Transferred Reinsurance and Excess Insurance Contracts (as defined in the LPT Agreement) to PWIC; (ii) the substitution of PWIC for ROA under each of those assigned Transferred Reinsurance and Excess Insurance Contracts; and (iii) the release of ROA from any liability and obligation under those assigned Transferred Reinsurance and Excess Insurance Contracts.

(14) Assigning and transferring to PWIC all of ROA's rights and obligations under the Transferred Reinsurance and Excess Insurance Contracts, as applicable, substituting PWIC for ROA under those assigned Transferred Reinsurance and Excess Insurance Contracts, and authorizing PWIC to assert ROA's rights under such assigned Transferred Reinsurance and Excess Insurance Contracts and recover from the excess insurers and other reinsurers for its own account any amounts that, in the absence of such assignment, would have been recoverable by ROA.

(15) Providing that the Covered Claims being transferred to PWIC as part of the Loss Portfolio Transfer are "claims of other policyholders arising out of insurance contracts" pursuant to § 38.2-1509 B 1 (ii) of the Code, and that the Loss Portfolio Transfer in no way relieves the Guaranty Associations from any future liability and responsibility for the Covered Claims in the event of PWIC's insolvency.

(16) Authorizing the Deputy Receiver to take any steps reasonably necessary to implement these measures and otherwise effect and consummate the LPT Agreement and the transactions contemplated therein.<sup>11</sup>

The Hearing Examiner provided the parties 21 days in which to submit comments.

On April 9, 2014, the Deputy Receiver filed Comments concerning recommendation number 9 in the Hearing Examiner's Report. The Deputy Receiver commented that this recommendation should apply only so long as the receivership remains open and the Amended Receivership Appeal Procedure remains in effect.<sup>12</sup> On April 28, 2014, the Kentucky Hospitals filed Comments to the Report.<sup>13</sup> The Kentucky Hospitals repeated several objections and arguments that it raised in prior filings and at the hearing in this case, which were addressed by the Hearing Examiner.

NOW THE COMMISSION, upon consideration of this matter, is of the opinion that the Hearing Examiner's findings and recommendations are reasonable and should be adopted, along with the Deputy Receiver's requested modification to the Hearing Examiner's recommendation number 9. We further find that the Deputy Receiver has met all the requirements of § 38.2-136 C of the Code.

Accordingly, IT IS ORDERED THAT:

(1) The findings and recommendations contained in the Hearing Examiner's Report are hereby adopted, along with the modification to the Hearing Examiner's recommendation number 9 as described in the Deputy Receiver's April 9, 2014 Comments.

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<sup>11</sup> Hearing Examiner's Report at 39-41.

<sup>12</sup> Comments of Deputy Receiver at 1.

<sup>13</sup> By Order dated April 18, 2014, the Commission allowed the parties an extension of time until April 28, 2014, to file comments to the Hearing Examiner's Report. Doc. Con. Cen. No. 140430035.

(2) This case is dismissed, and the papers herein shall be placed in the file for ended causes.

Commissioner Jagdmann did not participate in this matter.

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.