# Perspectives on Insurer and Reinsurer Insolvency From Across the Industry

Steven Rosenstein
Dustin Plotkin
Andy Meerkins

Novemeber 14, 2025

# Agenda

- **Basics of Insurer Insolvency:**
  - The insolvency process
  - Insurer insolvency versus bankruptcy
  - Powers of the receiver
  - Unique issues in reinsurer insolvency
  - Interplay between insolvency proceedings and arbitration agreements
- **The Receiver's Perspectives**
- **Impacts of Co-Carrier and Policyholder Insolvencies on Solvent Insurers**

# The Insolvency Process

# Placement into Receivership

- An insurer is placed into receivership when the insurer's home-state insurance department deems them to be in financial trouble (e.g., triggering certain statutory risk-based capital levels)
- The insurer may notify the insurance department itself, or the insolvency or potential insolvency may be identified by the department
- A filing for receivership must be approved by a state court to take effect (e.g., "Order of Rehabilitation")
- The state insurance commissioner either appoints a receiver in their place, or administers the receivership themselves
- A moratorium on policyholder actions (e.g., surrenders) may be initiated to prevent a "run on the bank"

# Stages of Receivership

| | Conservation | Rehabilitation | Liquidation |
|---|---|---|---|
| Confidential (ex parte) | Usually | No | No |
| Limited time period | Yes | No | No |
| Finding of insolvency | No | No | Yes |
| Bankruptcy analogy | Not applicable | Chapter 11 | Chapter 7 |

Source: Chicago Fed staff analysis of National Association of Insurance Commissioners (2024)

**Sequence**: These actions are not necessarily sequential. The regulator petitions the state court for the one most appropriate for the situation

# Risk-Based Capital (RBC) Requirements

| RBC Ratio (TAC / ACL) | Action level | Regulatory action |
|---|---|---|
| 300% and above | No action | Above 300% is "safe"; no regulatory actions |
| 200% to 300% | Trend test | Analysis performed to identify whether there is a "negative trend" |
| 150 to 200% | Company Action Level (CAL) | RBC Plan submitted to regulator showing how they will improve their RBC Ratio. Also applies if RBC Ratio is below 300% with negative trend |
| 100% to 150% | Regulatory Action Level | RBC Plan submitted to regulator. Regulator issues a corrective order that the company must follow (e.g., suspend sales of new business) |
| 70% to 100% | Authorized Control Level (ACL) | All Regulatory Action Level requirements apply. If the regulator believes it is in the best interests of the policyholders and creditors, the regulator may put the company under regulatory control (i.e., receivership) |
| Below 70% | Mandatory Control Level | Regulator must put the company under regulatory control (rehabilitation or liquidation) |

- TAC = Total Adjusted Capital (i.e., statutory surplus, with few adjustments)

# Powers of the Receiver

- The receiver:
  - Takes control of all assets;
  - Assumes operational control of the insurer;
  - Determines procedures for the receivership, rehabilitation, and/or liquidation.
- The receiver gets significant deference from the court for procedural decisions.
  - Procedural decisions include things like setting the proof of claim process, deadlines, etc.
  - The court generally isn't going to waste time second guessing the receiver on procedural issues the goal is for the expeditious resolution of the proceedings.
- The receiver does not automatically receive as much deference on substantive matters
  - For example, the actual value of a cedent's claim on an insolvent reinsurer's estate.

# Receivership Process (1 of 2)

- The commissioner files a receivership case in appropriate state court, placing the insurer into receivership
- Receiver assumes control of the troubled insurer, and is initially tasked with determining:
  - The true financial state of the insurer;
  - Whether rehabilitation is possible;
  - If yes, develop, implement, and execute a plan of rehabilitation under the supervision of the court (e.g., modifying policyholder coverages, pursuing the sale of all or part of the business)
  - If no, a plan of liquidation is developed with the Guaranty Associations, and the insurer is placed into liquidation.

# Receivership Process (2 of 2)

- Initial steps and planning phase:
  - The receiver may pursue confidentiality agreements with third parties.
  - Identify issues causing insurer financial distress:
    - I.e., inadequate reserves, extreme claims experience, poor management, etc.
    - This process includes input from regulatory staff, financial examiners and analysts, market conduct examiners, licensing agents, and company directors and officers.
  - Identify key transitional elements/levers:
    - Coordination with guaranty associations (definitions of covered claims/policies important)
    - Service providers/consultants/personnel.
  - Develop working business plan with plans for monitoring

# Liquidation

- If the receiver and the court determine that the insurer cannot be rehabilitated, the Guaranty Associations are triggered, and the insolvent insurer is placed into liquidation

- Liquidations have specific steps:
  - Entry of order of liquidation by the court;
  - Development and approval of liquidation plan and procedures;
  - Evaluation of effect on policies (obligations of P&C insurers or cancelable obligations of life insurers) and establishment of bar date for filing new claims;
  - Triggering of and coordination with guaranty associations;
  - Administration of plan and liquidation of insurer.

# Guaranty Association Limits

- Coverage limits from the Guaranty Association (GA) apply based on Model Law:

| | Coverage limits (slight variation by state of residence) |
|---|---|
| Life insurance | \$500,000 death benefits; \$300,000 net cash surrender/withdrawals |
| Major health insurance | \$500,000 |
| Long-term care | \$300,000 |
| Disability income | \$300,000 |
| Other health insurance | \$100,000 |
| Annuities | \$250,000 in present value of annuity benefits (incl. net cash surrender/withdrawals) |

- GAs are funded by remaining assets of insolvent company, statutory deposits, premiums, reinsurance, litigation proceeds, assessments of member insurers

- NOLHGA (Life & Health) and NCGIF (Property & Casualty) coordinate efforts among the guaranty associations across states

# Insurer Insolvencies v. Bankruptcies (1of 2)

- Insurer insolvency is a state-law matter, rather than subject to federal bankruptcy law and the jurisdiction of bankruptcy courts.
  - Most companies' primary duties are to their shareholders/members/owners, so the priority of a bankruptcy case is to distribute the assets of the company to creditors, then shareholders
  - Insurers, on the other hand, owe their primary duty to policyholders
  - Thus, unlike in bankruptcy, the goal of an insurer receivership is to safeguard the liabilities owed to policyholders (by far the biggest portion of an insurer's liabilities), after which other creditors are paid

# Insurer Insolvencies v. Bankruptcies (2 of 2)

- Insurer insolvencies also differ from bankruptcies other important ways:
  - “Safety Net” organizations, like guaranty associations, which assume policyholder liabilities of liquidated insurers.
  - The likelihood of contract termination in bankruptcy versus the potential transferring policies to other, solvent insurers in insolvency proceedings, thus minimizing the disruption to policyholders.
  - NAIC’s Receivers’ Handbook for Insurance Company Insolvencies sets out recommended procedures, individual states have specific contours.
  - The timeline: bankruptcies take years, receiverships last decades!

# Creditor Priority Scheme

- Priority schemes are generally set by state law.

- NAIC's Receivers' Handbook has default priority scheme (variations in state law):
  - Secured creditors;
  - Special deposit claimants;
  - Class 1 – Receiver's administrative expenses;
  - Class 2 – guaranty association expenses;
  - Classes 3 & 4 – claims for policy benefits;
  - Class 5 – federal government claims;
  - Class 6 – employee compensation (includes wages);
  - Class 7 – general creditors (includes brokers, D&O indemnity claims, reinsurer claims);
  - Class 8 – state & local government claims, some legal fees;
  - Class 9 – claims for penalties, punitive damages, forfeitures;
  - Class 10 – unexcused late-filed claims;
  - Class 11 – surplus notes;
  - Class 12 – interest;
  - Class 13 – equity interests.

# Impacts of Primary Insurer Insolvencies on Reinsurers

- Reinsurance receivables are often a significant portion of a primary insurer's assets, and are a prime target for receivers.
- Typically, ceded reinsurance agreements are continued through rehabilitation, and even through liquidation, unless they terminated according to their terms prior to liquidation or are terminated through the liquidation order.
- As arbitration agreements are ubiquitous in reinsurance contracts, there are frequently issues about whether either party may demand arbitration.

# Arbitration Agreements and Insolvencies (1 of 5)

- Arbitration is a private matter of contract, often confidential, often subject to flexible dispute-resolution processes, and binding only on the parties.
- Insolvency proceedings, on the other hand, are intended to be a centralized and transparent procedure, with an outcome binding on all parties.
- Moreover, state insolvency statutes generally provide some form of ”exclusive jurisdiction” to the court in charge of the receivership.
- The enforceability of agreements to arbitrate (and circumstances for enforceability) can thus be an issue in insolvency proceedings.

# Arbitration Agreements and Insolvencies (2 of 5)

- Generally, insolvency proceedings stay all claims against the insolvent insurer, including arbitrations, and may stay arbitrations brought by the insolvent insurer against others.
- Disputes concerning the enforceability of arbitration agreements can nevertheless arise in several ways:
- If a receiver initiates an action in state-court, the other party may remove the case to federal court and demand arbitration under the FAA;
- The reinsurer or other party may also demand arbitration and, if the receiver refuses to participate, seek to compel arbitration in federal court;
- The reinsurer may also seek to invoke arbitration rights within the insolvency proceedings themselves.

# Arbitration Agreements and Insolvencies (3 of 5)

- If a federal court is asked to compel arbitration, it can give rise to several interesting issues:
- Receivers will often argue that the FAA is reverse-preempted by the McCarran-Ferguson Act. 15 U.S.C. § 1012
- McCarran-Ferguson states that no federal statute is to be construed to ”invalidate, impair, or supersede” state law enacted for the purpose of regulating “the business of insurance.”
- Ordinarily, federal law preempts state law under the Supremacy Clause. McCarran-Ferguson “reverse preempts” federal law for certain cases related to state regulation of the insurance industry.

# Arbitration Agreements and Insolvencies (4 of 5)

- A federal statute, such as the FAA, is reverse-preempted if:
- (1) the federal statute does not relate specifically to the "business of insurance";
- (2) the state law was enacted "for the purpose of regulating the business of insurance"; and
- (3) the federal statute would "invalidate, impair, or supersede" the state law. *See, e.g., Munich Am. Reinsurance Co. v. Crawford*, 141 F.3d 585 (5th Cir. 1998).
- Clearly, the FAA does not relate specifically to the "business of insurance," and courts have generally concluded that state insolvency schemes were enacted to regulate "the business of insurance." *See, e.g., Davister Corp. v. United Republic Life Ins. Co.*, 152 F.3d 1277 (10th Cir. 1998).

# Arbitration Agreements and Insolvencies (5 of 5)

- Questions about whether arbitration provisions may be enforced thus often turn on whether the arbitration would "invalidate, impair, or supersede" the state insolvency scheme.

- These questions often turn on particulars of state law and what is prohibited or allowed by the statute. *Compare Quackenbush v. Allstate Ins. Co.*, 121 F.3d 1372 (9th Cir. 1997) (state law did not prohibit arbitration of liquidator's claims against reinsurer), *with Munich Am. Reinsurance Corp.*, 141 F.3d 585 (5th Cir. 1998) (arbitration would interfere with state scheme prohibiting any disputes from being heard outside specific state court).

- "*In personam*" type actions are more likely to be arbitrable—i.e., an action to establish liability; any effort to collect against the estate is "*In rem*" and less likely to be permitted.

# Scottish Re

- Scottish Re is the first known receivership/liquidation of a US life reinsurer, so it raises unique and novel questions about reinsurer insolvency law.

- Scottish Re went into runoff in 2008 and was placed into rehabilitation in 2019 in Delaware, and the commissioner was appointed as receiver. In 2023, the company was placed into liquidation proceedings, which remain ongoing.

- As a life reinsurer, unique issues involving:
  - Collateral trust issues
  - Valuation of claims
    - Role of rate guarantees
    - Proprietary mortality tables
  - Role of retros
  - Jumbo/STOLI issues

# The Receiver's Perspective

# How the Receiver Develops a Rehabilitation Plan

- Receivers consider numerous factors in developing a rehabilitation plan:
  - Business continuity (i.e., servicing policyholders and paying their claims) is of utmost initial importance
  - Assessment of actions that can be taken to avoid insolvency (e.g., through acquisition)
  - Policyholder-centric focus; balance between maximizing coverage for policyholders and equity among policyholders. Focus is often on ensuring policyholders fair better than they would otherwise under liquidation (with coverages subject to GA limits)
- Rehabilitation Orders and Rehabilitation Plans are often faced with legal challenges brought on by intervenors:
  - Examples include company management, policyholders, state regulators, insurers, agents/brokers, guaranty associations
- Reinsurance is often a major factor for consideration—i.e., receiver will need to consider how it will manage existing reinsurance agreements (both ceded and assumed).

# How the Receiver Approaches Asset Recovery

- Receivers have several tools they can deploy for asset recovery and must carefully balance the levers they will pull.

- Arbitration or litigation is a common tool

- Receiver must consider many factors in prioritizing such actions, including:
  - The likely value to the assets of the insolvent insurer;
  - The relevant fault or relationship between the potential counterparty and the insolvent insurer's financial condition (i.e., is the counterparty and potential acts of that counterparty a reason the insurer is insolvent);
  - The likelihood of success and probable value to the estate;
  - How long the asset recovery process might take; can asset recovery be achieved before the insurer runs out of assets?

# Insurer's Perspectives – When Your Co-Carrier or Insured Becomes Insolvent

# Carrier Insolvency Poses Challenges for Co-Carriers

- When an insurer becomes insolvent, co-insurers are inevitably affected in multiple ways.
- In the case of a primary insurer insolvency, how are excess carriers affected?
  - The majority rule is that excess carriers do not need to "drop down" if an insured at a lower layer becomes insolvent.
  - Policy language is crucial, however, including the question of how "exhaustion" is defined in the policy.
    - For example, courts have focused on whether exhaustion provisions refer to "collectible" or "recoverable" underlying limits.
    - Some courts have found that an excess policy's reference to "collectible" underlying limits might force an excess insurer to drop down.
    - Many policies, however, specifically exclude an obligation to drop down.

# Carrier Insolvency Poses Challenges for Co-Carriers

- But, even in the absence of a formal obligation to drop down, excess carriers are often affected!
  - Even if the policy lacks a duty to defend, the excess carrier may need to take action to protect the policy.
  - Could include defending or associating with the insured in a defense.

# Allocation Issues

- Insurer insolvency can also cause allocation issues for remaining co-carriers, which can vary depending on the type of jurisdiction.
- In an all-sums jurisdiction, an insured is more likely to "pick and spike" a coverage year with more solvent carriers.
  - Those carriers acquire a contribution right against carriers from other years, but if there are insolvent carriers in other years, a contribution target is lost.
  - This means the carriers who are selected will almost certainly have to pay more.

# Allocation Issues

- Pro-rata jurisdictions pose different problems.
- In a pro-rata jurisdictions, there can be disputes concerning whether an insured will be required to "pick up" the pro-rata shares of insolvent carriers, or whether solvent carriers and excess insurers need to pick up larger shares.
  - Some states explicitly require the insured to pick up the insolvent carrier's share.
  - This can be complicated, however, as several jurisdictions have adopted exceptions and rules that affect when an insured can be assigned a portion of loss.

# The Role of State Guaranty Funds

- When an insurer becomes insolvent, the state guaranty fund assumes the insurer's obligations and generally "step into the insolvent insurer's shoes to the extent of its obligation on all covered claims." *Gallagher v. Sidhu*, 109 P.3d 840 (Wash. Ct. App. 2005).

- That means guaranty funds can become involved in coverage and subrogation litigation and disputes.

- Critically, guaranty funds obligation to pay may be more restricted than the policy terms.

- The guaranty fund may provide less fulsome cover than the policy would; including different definitions of "covered claims" than the policy provides, or other restrictions and limitations (e.g., location restrictions, per claim limits, etc.).

- Many guaranty funds do not cover losses also covered by another policy or that all other coverage must first exhaust before the fund will pay. *See, e.g., NAIC Model Act, sec. 12(A).*

# Other Issues Related to Insurer Insolvency

- Occasionally, where an insurer goes insolvent, a policyholder may pursue recovery directly against a reinsurer if there is a "cut through" clause or otherwise can assert rights as a third-party beneficiary.
  - This sort of action is rare, and subject to numerous hurdles and legal challenges.
  - New York law recognizes that cut through provisions can exist and will be enforced. *See, e.g., Jurupa Valley Spectrum, LLC v. Nat'l Indemnity Co.*, 555 F.3d 87 (2d Cir. 2009).
  - Absent a cut-through, a reinsurer is generally not required to pay a claim filed by a policyholder when the insurer is insolvent because there is no privity of contract.
  - A few courts have allowed for policyholders to directly pursue reinsurers, particularly arising out of fronting arrangements or situations where a policyholder may be able to demonstrate that it was an intended third-party beneficiary. *See, e.g., Koken v. Legion Insurance Company, 831 A.2d 1196, 1241 (Pa. Comm. 2003), aff'd, 878 A.2d 51 (Pa. 2005).*

# Other Issues Related to Insurer Insolvency

- Complications can arise where there are old settlement agreements or coverage-in-place agreements with now-insolvent co-carriers.
  - Determining how these agreements will be managed or administered going forward can pose challenges when co-carriers can no longer meet their obligations.

# Issues Facing Insurers When Policyholders Go Bankrupt

- Policyholders may go bankrupt while there are pending claims.
  - Many issues where insurers and claimants may both be looking to maximize insurance assets; complex issues not the focus of today's discussion.
  - But what if the policyholder has a financial obligation under the policy?
  - Provisions that effectuate a forfeiture, modification, or termination of the insurance contract upon a bankruptcy filing are not enforceable.

# Issues Facing Insurers When Policyholders Go Bankrupt

- SIRs v. deductibles: although distinctly different concepts, confusion often arises due to the similar nature of a shared financial obligation by the policyholder and the insurer.

- The insurer's SIR is generally treated like a layer of primary insurance—i.e., the excess carrier need not drop down, but may need to consider paying for a defense to protect the claims. *See, e.g., In re Amatex Corp.*, 107 BR 856 (E.D. Pa. 1989).

- If the specific state law and policy language support it, policyholder "pay first" provisions may be a complete bar to triggering the policy. *See, e.g., Pak-Mor Mfg. Co. v. Royal Surplus Lines Ins. Co.*, 2005 WL 3487723 (W.D. Tex. Nov. 3, 2005) (Texas law). But more common for the SIR to be a layer of coverage, not a complete bar. *See, e.g., Home Ins. Co. of Ill. v. Hooper*, 294 Ill. App.3d 626 (Illinois law).

- Deductibles, on the other hand, generally don't affect the insurer's obligation to pay, but are treated like unsecured claims again the debtor's estate. *See In re Vanderveer Estates Holding LLC*, 328 BR 18 (Bank. E.D.N.Y. 2005).

# Issues Facing Insurers When Policyholders Go Bankrupt

- Loss-sensitive policies/retrospective premiums pose unique challenges.
  - Even where policyholder has unpaid premiums as a result, it is unlikely to affect the insurer's obligation to pay.
  - In many circumstances, the premiums the debtor owes will be general unsecured claims.
  - Post-petition policy terms may be able to acquire administrative claim status.

# What Comes Next for Insurance Insolvencies

# Lessons Learned and Predicting the Next Big Insolvency

- The industry has learned lessons from past insolvencies and is doing a better job of protecting itself against insolvency.
  - Today's insurance and reinsurance companies are more diverse rather than specializing in just one type of insurance
  - The industry has better modeling techniques today to understand and appropriately price risks
  - Reinsurance is more available and sophisticated than in the past

- What will drive the next big insolvency?
  - Past insolvency drivers:
    - Lack of diversity in business written
    - Investment-related losses
    - Relic organizations detached from market that failed to modernize underwriting, claims adjudication