05-5032

UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

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US COURT OF APPEALS
FEDERAL CIRCUIT

JOHN A. GREENE,
Receiver for the Great Global Assurance Company,

Plaintiff-Appellee,

v.

UNITED STATES,

Defendant-Appellant.

Appeal from the United State Court of Federal Claims
in 96-CV-169, Judge Marian Blank Horn.

BRIEF OF NATIONAL ASSOCATION OF INSURANCE COMMISSIONERS AS *AMICUS CURIAE* IN SUPPORT OF THE APPELLEE AND IN SUPPORT OF AFFIRMANCE OF THE COURT OF FEDERAL CLAIMS' JUDGMENT

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UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

JOHN A. GREENE v. UNITED STATES

No. 05-5032

CERTIFICATE OF INTEREST

Counsel for the amicus curiae, the National Association of Insurance Commissioners, certifies the following:

1. The full name of the amicus curiae represented by me is the National Association of Insurance Commissioners.

2. The National Association of Insurance Commissioners is a non-profit Delaware corporation and has no parent corporation or stock.

3. There are no other law firms, partners or associates that appeared for the party or amicus now represented by me in the trial court or agency or are expected to appear in this court.

June 13, 2005

Stephen S. Kaye

TABLE OF CONTENTS

Page

TABLE OF AUTHORITIES..ii

STATEMENT OF IDENTITY AND INTEREST OF *AMICUS CURIAE* AND SOURCE OF AUTHORITY TO FILE.................1

SUMMARY OF ARGUMENT..5

ARGUMENT..6

I. Guaranty Associations work for the protection of policyholders in the event of insurer insolvency. 6

II. The McCarran-Ferguson Acts provides for state regulation of the insurance industry and allows state law to preempt federal law for the purposes of regulating the business of insurance. 8

A. States may prioritize claims of a guaranty association over those of the federal government for the purpose of regulating the business of insurance. 8

B. Arizona law gives priority to the claims of the guaranty association over those of the federal government. 10

III. The Government's appeal misinterprets Arizona law and legal precedent and ignores the purpose of guaranty associations, promoting a policy that would lead to a "perverse result."............11

CONCLUSION..13

CERTIFICATE OF SERVICE..15

TABLE OF AUTHORITIES

Page

Cases:

Boozell v. United States, 979 F. Supp. 670 (N.D. Ill. 1997)....................9
Greene v. United States, 62 Fed. Cl. 418, (2004)..........................10, 13
Ruthardt v. United States, 303 F.3d 375 (1st Cir. 2002).....................9, 13
United States Dept. of Treasury v. Fabe, 508 U.S. 491 (1993).....8, 9, 10, 12

Statutes:

15 U.S.C. §§ 1011-1015 (2000)..*passim*
31 U.S.C. § 3713 (2000)..3, 11
ARIZ. REV. STAT. § 20-611 (1977)..11
ARIZ. REV. STAT. § 20-629 (1977)..11
ARIZ. REV. STAT. § 20-629 (2001)..10

Miscellaneous:

Life and Health Insurance Guaranty Association Model Act (Nat'l Assoc. of Ins. Comm'rs 1970) (amended 1999)....................................4
National Association of Insurance Commissioners, Amicus Curiae (Friend of the Court) Briefs, http://www.naic.org/legal/amicus_curiae.htm....2
National Association of Insurance Commissioners, NAIC Mission Statement, http://www.naic.org/about/mission.htm......................2
National Association of Insurance Commissioners, The NAIC Financial Regulation Standards and Accreditation Program, http://www.naic.org/frs/accreditation/docs/FRSA_pamphlet.pdf.......3
National Association of Insurance Commissioners White Paper, "Communication and Coordination Among Regulators, Receivers and Guaranty Associations" (Spring 2005)..............................7
Post-Assessment Property and Liability Insurance Guaranty Association Model Act (Nat'l Assoc. of Ins. Comm'rs 1969) (amended 1996).....4

INTRODUCTION

The National Association of Insurance Commissioners ("NAIC") files its *amicus curiae* brief in support of Appellee Receiver and in support of affirmance of the opinion in the court below. This case arises out of a complaint filed by the Insurance Commissioner of Arizona, acting as receiver for the Great Global Assurance Company, seeking a refund of federal income tax. The Court of Federal Claims granted summary judgment in favor of Great Global.

The issues presented in this case are of great importance to the NAIC and its members. The insurance regulator's role as receiver is primarily directed at ensuring the timely and appropriate payment of policyholder claims. The NAIC supports affirmance of the opinion below to protect the ability of its members to fully exercise this vital consumer protection function.

STATEMENT OF IDENTITY AND INTEREST OF AMICUS CURIAE AND SOURCE OF AUTHORITY TO FILE

The amicus curiae, the NAIC, is a non-profit Delaware corporation whose membership consists of the chief insurance regulatory officials of each state, the five territories, and the District of Columbia. Created in 1871, it is the nation's oldest association of state government officials..

The mission of the NAIC is:

> [t]o assist state insurance regulators, individually and collectively, in serving the public interest and achieving the following fundamental insurance regulatory goals in a responsive, efficient and cost effective manner, consistent with the wishes of its members: protect the public interest; promote competitive markets; facilitate the fair and equitable treatment of insurance consumers; promote the reliability, solvency and financial solidity of insurance institutions; and support and improve state regulation of insurance. [1]

Any member of the NAIC may request the filing of an amicus curiae brief.[2] Such requests require approval by the Executive Committee of the NAIC, which is made up of at least 15 of the NAIC's 50-plus members.[3]

NAIC members, as the chief insurance regulators in each state and as the officer of each state charged with handling insurer receiverships for that state, have a vested interest in ensuring the prompt payment of policyholder claims against insolvent insurers. Once an insurance company has been placed in receivership, the state's guaranty association provides the mechanism for payment of policyholder claims. Adoption of the position the Government put forth on this appeal would have a substantially negative

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[1] *See* National Association of Insurance Commissioners, NAIC Mission Statement, *available at* http://www.naic.org/about/mission.htm (last modified June 10, 2005).

[2] *See* National Association of Insurance Commissioners, Amicus Curiae (Friend of the Court) Briefs, *available at* http://www.naic.org/legal/amicus_curiae.htm (last visited June 10, 2005).

[3] *Id.*

effect on the ability of guaranty associations to protect the rights of policyholders.[4]

The NAIC established a Financial Regulation and Accreditation Program in June of 1989. This program was intended to ensure that each accredited state has established certain baseline requirements for a state-based system of insurance regulation. Protection of policyholders is a key component of each element of the accreditation program. The paramount role that insolvency supervision plays in insurance regulation is reflected in the accreditation program:

> A system of effective solvency regulation provides crucial safeguards for America's insurance consumers [by requiring] that regulators have adequate statutory and administrative authority to regulate an insurer's corporate and financial affairs.[5]
>
> For a state to be accredited by the NAIC its:
>
> [s]tate law should set forth a receivership scheme for the administration, by the insurance commissioner, of insurance companies found to be insolvent as set forth in the NAIC's Insurers Rehabilitation and Liquidation Model Act.[6]

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[4] The NAIC has an additional interest in this case in that its members, in their capacity as receivers, can be held personally liable for not granting priority to a proper claim by the Federal government. 31 U.S.C. § 3713(b) (2000).

[5] *See* National Association of Insurance Commissioners, The NAIC Financial Regulation Standards and Accreditation Program, *available at* http://www.naic.org/frs/accreditation/docs/FRSA_pamphlet.pdf (last visited June 10, 2005).

[6] *Id.*

The NAIC proposed its Model Guaranty Association Act in 1969, and it was eventually adopted in all 50 states, the District of Columbia, Puerto Rico and the Virgin Islands. The NAIC created this model in order to:

> ...provide a mechanism for the payment of covered claims under certain insurance policies, to avoid excessive delay in payment and to the extent provided in this Act minimize financial loss to claimants or policyholders because of the insolvency of an insurer, and to provide an association to assess the cost of such protection among insurers.[7]

The Model established procedures whereby solvent insurance companies, through contributions to the guaranty association, assist in the payment of claims from insolvent insurers.

Given the NAIC's long-standing interest in promoting effective solvency regulation through, in part, the guaranty association system, the NAIC and its members have a compelling interest in maintaining a system where the claims of the state guaranty association are given the priority afforded them by state statute. This case is the latest in a series of cases in which the United States has asserted that Federal claims should be paid

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[7] *See* Post-Assessment Property and Liability Insurance Guaranty Association Model Act § 2 (Nat'l Assoc. of Ins. Comm'rs 1969) (amended 1996). Shortly after the adoption of this model, the NAIC adopted its Life and Health Insurance Guaranty Association Model Act in 1970 to address insolvencies of life and health insurers. Life and Health Insurance Guaranty Association Model Act (Nat'l Assoc. of Ins. Comm'rs 1970) (amended 1999).

before the claims of guaranty associations. The NAIC has filed amicus briefs in most of these cases that have reached the appellate courts.

The NAIC has sought leave to file this brief pursuant to Fed. R. App. P. 29(b).

SUMMARY OF ARGUMENT

The Court of Federal Claims in the decision below acknowledged that state guaranty associations assume the role of policyholders during the receivership process and correctly emphasized the importance of this role in the protection of insurance consumers. The court went on to correctly find that state prioritization of claims of state guaranty associations constituted the business of insurance. As such, Arizona's statutory priority scheme preempts federal law under the McCarran-Ferguson Act, 15 U.S.C. §§ 1011-1015 (2000). Arizona's priority statute gives the claims of policyholders that have been assigned to the state guaranty association priority over claims of the Federal government.

The arguments put forth by the Government for reversal of the lower court's decision fly in the face of established precedent and misinterpret applicable Arizona law as well as the role and purpose of state guaranty associations. The Government's policy argument would not only rob states of their power to regulate insurance but deprive policyholders of the security

that their claims will be paid in a timely manner even if their insurance company fails.

This Court should affirm the decision of the Court of Federal Claims.

ARGUMENT

I. **Guaranty Associations work for the protection of policyholders in the event of insurer insolvency.**

State insurance departments are responsible for the regulation of the insurance companies operating within their jurisdiction. One of the crucial services that state insurance regulators provide is supervision and settlement of the estates of insolvent insurance companies. As policyholders are the most vulnerable victims of a failed insurance company, the state is responsible for making sure that policyholders are not robbed of the intended benefits or protection of their insurance contract. Guaranty associations were created as a way to ensure the claims of policyholders were paid promptly in the event of insolvency.[8]

A recently adopted NAIC White Paper entitled, "Communication and Coordination Among Regulators, Receivers and Guaranty Associations" discusses the importance of guaranty associations to regulators and policyholders:

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[8] The NAIC recognized the importance of guaranty associations and proposed its Model Guaranty Fund Act in 1969, discussed *supra*.

> Guaranty Associations share the common goal of consumer protection with regulators. In fact, guaranty associations provide the mechanism by which policy claimants with covered claims receive timely claim payments. In most cases, without guaranty associations, such payments would, at a minimum, be delayed for several years. Even at the point when payment could be made from an insolvent estate, such payment would likely only be a fraction of the benefit that would have been received from the insurer before insolvency. This makes guaranty associations the primary source of policyholder protection.[9]

The importance of guaranty associations in protecting policyholders is well established and was recognized by the trial court in this case. The amicus brief submitted by the National Organization of Life and Health Insurance Guaranty Associations and the National Conference of Insurance Guaranty Funds in support of the Receiver accurately describes how the guaranty fund system works to protect policyholders. The brief of the appellee aptly summarizes the benefits of guaranty associations as providing increased funds to pay policyholders' claims, providing quicker payment to policyholders, and spreading the risk and burden of insolvency to other insurance companies.[10] The NAIC joins in these descriptions of the benefits

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[9] The entire NAIC membership affirmed the white paper at the 2005 NAIC Spring National Meeting. *See* National Association of Insurance Commissioners, Executive (EX) Committee/Plenary (March 13, 2005) *available at* http://www.naic.org/receivership/documents/exec_plenary.doc (last visited June 10, 2005).

[10] Receiver's Brief, at 34.

of the guaranty fund system as part of a comprehensive system of state-based insurance regulation.

II. The McCarran-Ferguson Acts provides for state regulation of the insurance industry and allows state law to preempt Federal law for the purposes of regulating the business of insurance.

The ability of states to prioritize claims against insolvent insurers is an important aspect of the regulation of the business of insurance and in the protection of policyholders. The McCarran-Ferguson Act provides for state regulation of the insurance industry and allows Federal law to be preempted by state laws whose purpose is regulating the business of insurance.[11] The application of McCarran-Ferguson by the courts centers on the analysis of whether a particular state regulation constitutes the regulation of the business of insurance. Case law establishes that state statutes granting higher priority to claims against an insurer's estate that serve to protect the interests of policyholders are the regulation of the business of insurance.

A. States may prioritize claims of a guaranty association over those of the Federal government for the purpose of regulating the business of insurance.

Appellee correctly argues that *United States Dept. of Treasury v. Fabe*[12] and its progeny stand for the proposition that claims of state guaranty

[11] 15 U.S.C. § 1012(b).
[12] *United States Dept. of Treasury v. Fabe*, 508 U.S. 491 (1993).

associations are entitled to priority in a receivership context. In *Fabe*, the Supreme Court found that state statutes regulating the priority of policyholder claims were laws enacted to regulate the business of insurance.[13] As these state statutes have the purpose of regulating the business of insurance, they preempt federal law under the McCarran-Ferguson Act.

Subsequent Federal cases have correctly followed *Fabe's* rationale in determining that state regulation of guaranty associations, because they also protect the interest of the policyholder, constitutes the "business of insurance" and therefore also falls under the exclusive province of state law. *Boozell v. United States*[14] and *Ruthardt v. United States*[15] both recognize that the purpose of guaranty associations is the protection of policyholders and that making payments to a guaranty association is the same as making a payment to a policyholder.

The trial court in this case correctly followed the established precedent in deciding that Arizona's priority statute is regulation of the business of insurance and that, under McCarran-Ferguson, the Arizona priority statute prevails, noting "[t]he Arizona statute is designed to carry out

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[13] *Id.* at 508.
[14] *Boozell v. United States,* 979 F. Supp. 670 (N.D. Ill. 1997).
[15] *Ruthardt v. United States,* 303 F.3d 375 (1st Cir. 2002).

the completion of insurance contracts by ensuring payment of policyholder's claims despite an insurance company's intervening bankruptcy, as required under *Fabe*."[16]

B. Arizona law gives priority to the claims of the guaranty association over those of the Federal government.

Arizona's priority statute[17] is part of a comprehensive regulatory scheme for the supervision of insolvent insurers. The trial court correctly found that regardless of which version of the Arizona statute (1977 or 2001) would apply, the result would be the same, stating:

> whether the statute itself places guaranty funds ahead of federal claims, or guaranty funds are assigned by statute, the result is the same—guaranty funds serve to directly protect the policyholder and, therefore, enjoy a higher priority than the claims pursued by the IRS.[18]

We agree with the court's findings. Under the 2001 Arizona Guaranty Fund Statute,[19] the state prioritizes the claims of the guaranty association over those of the Federal government as it clearly has the ability to do under the McCarran-Ferguson Act and as acknowledged by *Fabe* and its progeny. Arizona had the power to prioritize guaranty association claims under the

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[16] *Greene v. United States*, 62 Fed. Cl. 418, at 439 (2004).
[17] ARIZ. REV. STAT. § 20-629 (2001).
[18] *Greene* at 440.
[19] ARIZ. REV. STAT. § 20-629 (2001).

1977 version of this statute as well.[20] While the Government's tax claim may have had "preferred" status under the 1977 law,[21] that does not support the unsubstantiated leap required to claim that it was entitled to be "paid first."[22] ARIZ. REV. STAT. § 20-629.E (1977) provided that policyholder claims had preference and priority over general creditors. Under the 1977 statutes, the Government was an unsecured creditor with preferred status with regard to other general creditors, yet as permitted under McCarran-Ferguson, Arizona gave higher priority to policyholder payments, including those assigned to guaranty associations. Thus, whether explicitly or implicitly, the Arizona statute grants guaranty association claims higher priority than those of the Federal government.

III. The Government's appeal misinterprets Arizona law and legal precedent and ignores the purpose of guaranty associations, promoting a policy that would lead to a "perverse result."

The Government's argument not only misinterprets the Arizona statute to suggest that the McCarran-Ferguson Act does not even apply, but also discounts the importance of guaranty associations in the protection of policyholders. In pursuing its super-priority under the Federal priority statute, the Government improperly ignores state law and tries to cut off an

[20] ARIZ. REV. STAT. § 20-629 (1977).
[21] ARIZ. REV. STAT. § 20-611(8) (1977).
[22] Government's Brief at 23-26.

important source for the renewal of guaranty association funding. If guaranty associations were unable to recoup some of the funds that are paid out to claimants of insolvent insurance companies, the resources of these associations would eventually dwindle and they would no longer be able to provide the protection to policyholders for which they were created. By equating guaranty associations with average creditors of an insurance company and bumping guaranty associations out of the state's realm of prioritization, the Government seeks to overturn a crucial component of state insurance regulation—that of protection of the policyholder.

The Government narrowly interprets *Fabe* to apply only to payments to "policyholders".[23] The Supreme Court did in fact characterize its *Fabe* holding as narrow but clearly explained that this was necessary to prevent ordinary creditors, not related to the central contract of insurance, from claiming they were entitled to priority over government claims because they somehow provided a benefit to policyholders.[24] The Government forgets the role of a guaranty association and ignores the fact that guaranty associations take the place of policyholders and subrogate their rights during insolvency proceedings. Guaranty associations step into the shoes of the policyholder

[23] Government's brief at 47.
[24] *Fabe*, 508 U.S. at 508.

and therefore claims of the guaranty association are entitled to the same priority afforded to policyholders.

The First Circuit in *Ruthardt* addressed the importance of reimbursing guaranty associations and how reimbursement works towards the protection of policyholders.[25] The court also discussed the unfair results if the Federal government's claim was superior to guaranty associations, noting:

> If the policyholder makes a direct claim against the estate, that claim is satisfied out of estate assets ahead of the United States. If (for speed and certainty) the policyholder is instead paid by the guaranty fund, and the guaranty fund then seeks to recoup, the United States' position in this case would mean that the same assets of the estate are subject to a priority claim of the United States. This would be a perverse result.[26]

The trial court here agreed with respect to the Arizona Guaranty Fund[27], as do we. Allowing the Federal government to get paid from the estate assets before the guaranty association would in effect penalize a state for attempting to protect policyholders by facilitating and expediting claim payments to policyholders via guaranty associations.

CONCLUSION

The NAIC respectfully requests that this court affirm the opinion below with a finding that, because it regulates the business of insurance,

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[25] *Ruthardt*, 303 F.3d at 382.
[26] *Id.*
[27] *Greene*, 62 Fed. Cl. at 437-438.

Arizona law may grant priority to claims of the state guaranty association over those of the Government.

Dated: June 13, 2005

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I hereby certify that the Brief of Amicus Curiae in No. 05-5032 was served by first class, postage pre-paid U.S. mail, on June 13, 2005, upon the following parties:

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