

ASSEMBLY, No. 4171

STATE OF NEW JERSEY 214th LEGISLATURE

INTRODUCED JUNE 27, 2011

Sponsored by:

Assemblyman GARY S. SCHAER

District 36 (Bergen, Essex and Passaic)

Assemblyman GARY R. CHIUSANO

District 24 (Sussex, Hunterdon and Morris)

Co-Sponsored by:

Assemblyman Chivukula

SYNOPSIS

Concerns rights of financial counterparties to terminate and settle certain agreements with certain insurers in the event of insolvency or liquidation.

CURRENT VERSION OF TEXT

As introduced.



(Sponsorship Updated As Of: 12/16/2011)

1 AN ACT concerning certain financial agreements and supplementing
2 P.L.1992, c.65 (C.17B:32-31 et seq.).

3

4 **BE IT ENACTED** by the Senate and General Assembly of the State
5 of New Jersey:

6

7 1. a. (1) Notwithstanding any other provision of the “Life and
8 Health Insurers Rehabilitation and Liquidation Act,” P.L.1992, c.65
9 (C.17B:32-31 et seq.) to the contrary, a person shall not be stayed
10 or prohibited from exercising:

11 (a) A contractual right to cause the termination, liquidation,
12 acceleration or close out of any obligation under or in connection
13 with a netting agreement or qualified financial contract with an
14 insurer because of: (i) the insolvency, financial condition or default
15 of the insurer at any time, provided that the right is enforceable
16 under applicable law other than the provisions of P.L.1992, c.65
17 (C.17B:32-31 et seq.); or (ii) the commencement of a formal
18 delinquency proceeding under P.L.1992, c.65 (C.17B:32-31 et
19 seq.);

20 (b) Any right under a security arrangement relating to one or
21 more netting agreements or qualified financial contracts; or

22 (c) Subject to subsection b. of section 29 of P.L.1992, c.65
23 (C.17B:32-59), any right to setoff or net out any termination value,
24 payment amount, or other transfer obligation arising under or in
25 connection with one or more netting agreements or qualified
26 financial contracts where the counterparty or its guarantor is
27 organized under the laws of the United States, a state, or a foreign
28 jurisdiction approved by the Securities Valuation Office of the
29 National Association of Insurance Commissioners as eligible for
30 netting.

31 (2) If a counterparty to a master netting agreement or a qualified
32 financial contract with an insurer subject to a proceeding under
33 P.L.1992, c.65 (C.17B:32-31 et seq.) terminates, liquidates, closes
34 out or accelerates the agreement or contract, damages shall be
35 measured as of the date or dates of termination, liquidation, close
36 out or acceleration. The amount of a claim for damages shall be
37 actual direct compensatory damages.

38 b. Upon termination of a netting agreement or qualified
39 financial contract, the net or settlement amount, if any, owed by a
40 non-defaulting party to an insurer against which a petition has been
41 filed pursuant to P.L.1992, c.65 (C.17B:32-31 et seq.) shall be
42 transferred to the receiver for the insurer or as directed by the
43 receiver for the insurer, even if the insurer is the defaulting party,
44 notwithstanding any walkaway clause in the netting agreement or
45 qualified financial contract. Any limited two-way payment or first
46 method provision in a netting agreement or qualified financial
47 contract with an insurer that has defaulted shall be deemed to be a
48 full two-way payment or second method provision as against the

1 defaulting insurer. Any such net or settlement amount shall, except
2 to the extent it is subject to one or more secondary liens or
3 encumbrances or rights of netting or setoff, be an asset of the
4 insurer.

5 c. In making any transfer of a netting agreement or qualified
6 financial contract of an insurer subject to a proceeding under
7 P.L.1992, c.65 (C.17B:32-31 et seq.), the receiver shall either:

8 (1) Transfer to one party, other than an insurer subject to a
9 proceeding under P.L.1992, c.65 (C.17B:32-31 et seq.), all netting
10 agreements and qualified financial contracts between a counterparty
11 or any affiliate of such counterparty and the insurer that is the
12 subject of the proceeding, including: (a) all rights and obligations of
13 each party under each such netting agreement and qualified
14 financial contract; and (b) all property, including any guarantees or
15 credit support documents, securing any claims of each party under
16 each such netting agreement and qualified financial contract; or

17 (2) Transfer none of the netting agreements, qualified financial
18 contracts, rights, obligations, or property referred to in
19 subparagraph (b) of paragraph (1) of this subsection with respect to
20 such counterparty and any affiliate of such counterparty.

21 d. If a receiver for an insurer makes a transfer of one or more
22 netting agreements or qualified financial contracts, then the receiver
23 shall use his or her best efforts to notify any person who is party to
24 the netting agreements or qualified financial contracts of the
25 transfer by 12 o'clock noon, the receiver's local time, on the
26 business day following the transfer. For purposes of this subsection,
27 "business day" means a day other than a Saturday, a Sunday, or any
28 day on which either the New York Stock Exchange or the Federal
29 Reserve Bank of New York is closed.

30 e. Notwithstanding any other provision of P.L.1992, c.65
31 (C.17B:32-31 et seq.), a receiver may not avoid a transfer of money
32 or other property arising under or in connection with a netting
33 agreement or qualified financial contract or any security
34 arrangement relating to a netting agreement or qualified financial
35 contract that is made before the commencement of a formal
36 delinquency proceeding under P.L.1992, c.65 (C.17B:32-31 et seq.),
37 except that a transfer may be avoided under section 25 of P.L.1992,
38 c.65 (C.17B:32-55) if the transfer was made with actual intent to
39 hinder, delay, or defraud the insurer, a receiver appointed for the
40 insurer, or existing or future creditors.

41 f. (1) In exercising any rights of disaffirmance or repudiation
42 of a receiver with respect to any netting agreement or qualified
43 financial contract to which an insurer is a party, the receiver for the
44 insurer shall either: (a) disaffirm or repudiate all netting agreements
45 and qualified financial contracts between a counterparty or any
46 affiliate of that counterparty and the insurer that is the subject of the
47 proceeding; or (b) disaffirm or repudiate none of the netting
48 agreements and qualified financial contracts referred to in

1 subparagraph (a) of this paragraph with respect to that person or
2 any affiliate of that person.

3 (2) Notwithstanding any other provision of P.L.1992, c.65
4 (C.17B:32-31 et seq.), any claim of a counterparty against the estate
5 arising from the receiver's disaffirmance or repudiation of a netting
6 agreement or qualified financial contract that has not been
7 previously affirmed in the liquidation proceeding or in the
8 immediately preceding rehabilitation proceeding shall be
9 determined and shall be allowed or disallowed: (a) as if the claim
10 had arisen before the date of the filing of the petition for
11 liquidation; or (b) if a rehabilitation proceeding is converted to a
12 liquidation proceeding, as if the claim had arisen before the date of
13 the filing of the petition for rehabilitation.

14 (3) The amount of the claim identified in paragraph (2) of this
15 subsection shall be the actual direct compensatory damages
16 determined as of the date of the disaffirmance or repudiation of the
17 netting agreement or qualified financial contract.

18 g. All rights of a counterparty under this section shall apply to
19 a netting agreement and a qualified financial contract entered into
20 on behalf of, or allocated to:

21 (1) the general account of the insurer; or

22 (2) a separate account of the insurer if the assets of the separate
23 account are available only to a counterparty to a netting agreement
24 and a qualified financial contract entered into on behalf of, or
25 allocated to, that separate account.

26 h. As used in this section:

27 (1) "Actual direct compensatory damages" includes normal and
28 reasonable costs of cover or other reasonable measures of damages
29 utilized in the derivatives market for the contract and agreement
30 claims, but does not include punitive and exemplary damages,
31 damages for lost profit or lost opportunity, or damages for pain and
32 suffering.

33 (2) "Commodity contract" means any of the following:

34 (a) A contract for the purchase or sale of a commodity for future
35 delivery on, or subject to the rules of, a board of trade designated as
36 a contract market by the Commodity Futures Trading Commission
37 under the "Commodity Exchange Act," 7 U.S.C. s.1 et seq., or
38 board of trade outside the United States;

39 (b) An agreement that is subject to regulation under section 19
40 of the "Commodity Exchange Act," 7 U.S.C. s.23, and that is
41 commonly known to the commodities trade as a margin account,
42 margin contract, leverage account, or leverage contract;

43 (c) An agreement or transaction that is subject to regulation
44 under subsection 4c(b) of the "Commodity Exchange Act," 7 U.S.C.
45 s.6c(b), and that is commonly known to the commodities trade as a
46 commodity option;

47 (d) Any combination of the agreements or transactions referred
48 to in this paragraph; or

1 (e) Any option to enter into an agreement or transaction referred
2 to in this paragraph.

3 (3) "Contractual right" includes any right set forth in a rule or
4 bylaw of a derivatives clearing organization as defined in the
5 "Commodity Exchange Act," 7 U.S.C. s.1a(9), a multilateral
6 clearing organization as defined in the "Federal Deposit Insurance
7 Corporation Improvement Act of 1991," 12 U.S.C. s.4421(1), a
8 national securities exchange, a national securities association, a
9 securities clearing agency, or a contract market designated under
10 the "Commodity Exchange Act," 7 U.S.C. s.1 et seq., a swap
11 execution facility registered under the "Commodity Exchange Act,"
12 7 U.S.C. s.1 et seq., or a board of trade as defined in the
13 "Commodity Exchange Act," 7 U.S.C. s.1a(2), or in a resolution of
14 the governing board thereof, and any right, whether or not
15 evidenced in writing, arising under statutory or common law, or
16 under law merchant, or by reason of normal business practice.

17 (4) "Forward contract" means the same as the term is defined in
18 the "Federal Deposit Insurance Act," 12 U.S.C. s.1821(e)(8)(D).

19 (5) "Netting agreement" means:

20 (a) A contract or agreement, including the terms and conditions
21 incorporated by reference in such contract or agreement, including
22 a master agreement, which master agreement, together with all
23 schedules, confirmations, definitions and addenda thereto and
24 transactions under any thereof, shall be treated as one netting
25 agreement, that documents one or more transactions between the
26 parties to the agreement for or involving one or more qualified
27 financial contracts and that provides for the netting, setoff,
28 liquidation, termination, acceleration or close out, under or in
29 connection with one or more qualified financial contracts or present
30 or future payment or delivery obligations or payment or delivery
31 entitlements thereunder, including liquidation or close-out values
32 relating to such obligations or entitlements, among the parties to the
33 netting agreement;

34 (b) Any master agreement or bridge agreement for one or more
35 master agreements described in subparagraph (a) of this paragraph;
36 or

37 (c) Any security arrangement related to one or more contracts or
38 agreements described in subparagraphs (a) or (b) of this paragraph,
39 provided that any contract or agreement described in subparagraph
40 (a) or (b) of this paragraph relating to agreements or transactions
41 that are not qualified financial contracts shall be deemed to be a
42 netting agreement only with respect to those agreements or
43 transactions that are qualified financial contracts.

44 (6) "Qualified financial contract" means a commodity contract,
45 forward contract, repurchase agreement, securities contract, swap
46 agreement, and any similar agreement that the commissioner
47 determines by regulation to be a qualified financial contract for the
48 purposes of this section.

1 (7) "Repurchase agreement" means the same as that term is
2 defined in the "Federal Deposit Insurance Act," 12 U.S.C.
3 s.1821(e)(8)(D). The term "repurchase agreement" shall include a
4 reverse repurchase agreement.

5 (8) "Security arrangement" means any security agreement or
6 arrangement or other credit enhancement or guarantee or
7 reimbursement obligation, including a pledge, security, collateral or
8 guarantee agreement or credit support document.

9 (9) "Securities contract" means the same as that term is defined
10 in "Federal Deposit Insurance Act," 12 U.S.C. s.1821(e)(8)(D).

11 (10) "Separate account" means the same as that term is defined
12 in N.J.S.17B:28-1.

13 (11) "Swap agreement" means the same as that term is defined in
14 the "Federal Deposit Insurance Act," 12 U.S.C. s.1821(e)(8)(D).

15 (12) "Walkaway clause" means a provision in a netting
16 agreement or a qualified financial contract that, after calculation of
17 a value of a party's position or an amount due to or from one of the
18 parties in accordance with its terms upon termination, liquidation or
19 acceleration of the netting agreement or qualified financial contract,
20 either does not create a payment obligation of a party or
21 extinguishes a payment obligation of a party in whole or in part
22 solely because of the party's status as a non-defaulting party.

23

24 2. This act shall take effect immediately.

25

26

27

STATEMENT

28

29 This bill supplements the "Life and Health Insurers
30 Rehabilitation and Liquidation Act," P.L.1992, c.65 (C.17B:32-31
31 et seq.), based, in part, on the National Association of Insurance
32 Commissioner's Insurer Receivership Model Act, to reform the way
33 in which certain qualified financial contracts and netting
34 agreements are treated in the case of insolvency or liquidation of an
35 insurer. The intent of the bill is to provide substantially similar
36 treatment of qualified financial contracts and netting agreements
37 under New Jersey law as is provided under the United States
38 Bankruptcy Code and the Federal Deposit Insurance Act with
39 respect to similar transactions with other financial services entities
40 such as banks and securities brokers.

41 New Jersey domestic life insurers are authorized to enter into
42 swap and other derivative agreements under New Jersey law. These
43 arrangements are important to managing risk because they hedge
44 the insurer's assets and liabilities. This type of financial
45 arrangement, referred to in the bill as a "qualified financial
46 contract," include commodity contracts, forward contracts,
47 repurchase agreements, securities contracts, swap agreements, and
48 any similar agreement as determined by the Commissioner of

1 Banking and Insurance. In addition, the bill regulates “netting
2 agreements,” which are contracts or agreements that provide for the
3 netting, setoff, liquidation, termination, acceleration or close out,
4 under or in connection with one or more qualified financial
5 contracts or present or future payment or delivery obligations
6 among the parties to the netting agreement.

7 This bill provides that financial counterparties will have the
8 contractual right to terminate the netting agreement and to the
9 settlement of the obligations on a net basis if the insurer is placed
10 into a rehabilitation or liquidation proceeding.

11 The bill provides that if a counterparty to a master netting
12 agreement or a qualified financial contract with an insurer subject to
13 a proceeding under the “Life and Health Insurers Rehabilitation and
14 Liquidation Act” terminates, liquidates, closes out or accelerates the
15 agreement or contract, damages shall be measured as of the date or
16 dates of termination, liquidation, close out or acceleration. The
17 amount of a claim for damages shall be actual direct compensatory
18 damages.

19 Upon termination of a netting agreement or qualified financial
20 contract, the net or settlement amount, if any, owed by a non-
21 defaulting party to an insurer against which a petition has been filed
22 pursuant to the “Life and Health Insurers Rehabilitation and
23 Liquidation Act” shall be transferred to the receiver for the insurer
24 or as directed by the receiver for the insurer, even if the insurer is
25 the defaulting party, notwithstanding any walkaway clause (as
26 defined in the bill) in the netting agreement or qualified financial
27 contract.

28 Under the bill, any limited two-way payment or first method
29 provision in a netting agreement or qualified financial contract with
30 an insurer that has defaulted shall be deemed to be a full two-way
31 payment or second method provision as against the defaulting
32 insurer. Any such net or settlement amount shall, except to the
33 extent it is subject to one or more secondary liens or encumbrances
34 or rights of netting or setoff, be an asset of the insurer.

35 In making any transfer of a netting agreement or qualified
36 financial contract of an insurer subject to a proceeding under the
37 “Life and Health Insurers Rehabilitation and Liquidation Act” the
38 receiver is required to either:

39 (1) Transfer to one party, other than an the insurer subject to a
40 proceeding under the “Life and Health Insurers Rehabilitation and
41 Liquidation Act,” all netting agreements and qualified financial
42 contracts between a counterparty or any affiliate of that
43 counterparty and the insurer that is the subject of the proceeding,
44 including: (a) all rights and obligations of each party under that
45 netting agreement and qualified financial contract; and (b) all
46 property, including any guarantees or credit support documents,
47 securing any claims of each party under that netting agreement and
48 qualified financial contract; or

1 (2) Transfer none of the netting agreements, qualified financial
2 contracts, rights, obligations, or property with respect to that
3 counterparty and any affiliate of such counterparty.

4 If a receiver for an insurer makes a transfer of one or more
5 netting agreements or qualified financial contracts, then the bill
6 requires the receiver to use his or her best efforts to notify any
7 person who is party to the netting agreements or qualified financial
8 contracts of the transfer by 12 o'clock noon, the receiver's local
9 time, on the business day following the transfer.

10 Under the bill, a receiver may not avoid a transfer of money or
11 other property arising under or in connection with a netting
12 agreement or qualified financial contract or any security
13 arrangement relating to a netting agreement or qualified financial
14 contract that is made before the commencement of a formal
15 delinquency proceeding under the "Life and Health Insurers
16 Rehabilitation and Liquidation Act," except that a transfer may be
17 avoided if the transfer was made with actual intent to hinder, delay,
18 or defraud the insurer, a receiver appointed for the insurer, or
19 existing or future creditors.

20 The bill also provides that, in exercising any rights of
21 disaffirmance or repudiation of a receiver with respect to any
22 netting agreement or qualified financial contract to which an insurer
23 is a party, the receiver for the insurer shall either: (a) disaffirm or
24 repudiate all netting agreements and qualified financial contracts
25 between a counterparty or any affiliate of such counterparty and the
26 insurer that is the subject of the proceeding; or (b) disaffirm or
27 repudiate none of the netting agreements and qualified financial
28 contracts.

29 Any claim of a counterparty against the estate arising from the
30 receiver's disaffirmance or repudiation of a netting agreement or
31 qualified financial contract that has not been previously affirmed, in
32 the liquidation proceeding or in the immediately preceding
33 rehabilitation proceeding, shall be determined and shall be allowed
34 or disallowed: (a) as if the claim had arisen before the date of the
35 filing of the petition for liquidation; or (b) if a rehabilitation
36 proceeding is converted to a liquidation proceeding, as if the claim
37 had arisen before the date of the filing of the petition for
38 rehabilitation. The amount of any claim arising out of such a
39 situation is the actual direct compensatory damages determined as
40 of the date of the disaffirmance or repudiation of the netting
41 agreement or qualified financial contract.

42 All rights of a counterparty under this bill apply to a netting
43 agreement and a qualified financial contract entered into on behalf
44 of, or allocated to: (1) the general account of the insurer; or (2) a
45 separate account of the insurer if the assets of the separate account
46 are available only to a counterparty to a netting agreement and a
47 qualified financial contract entered into on behalf of, or allocated
48 to, that separate account.

1 Several states have adopted laws similar to the provisions of this
2 bill, thus placing New Jersey domestic life insurers utilizing these
3 financial agreements at a competitive disadvantage with those
4 insurers in states that have amended their laws as well as with
5 federally regulated financial services entities. It is the intent of this
6 bill to keep New Jersey life insurers competitive with insurers and
7 financial counterparties operating in other states.