

ASSEMBLY, No. 249

STATE OF NEW JERSEY

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Sponsored by:

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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

Introduced Pending Technical Review by Legislative Counsel



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

1 full two-way payment or second method provision as against the
2 defaulting insurer. Any such net or settlement amount shall, except
3 to the extent it is subject to one or more secondary liens or
4 encumbrances or rights of netting or setoff, be an asset of the
5 insurer.

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

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

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

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

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

42 f. (1) In exercising any rights of disaffirmance or repudiation
43 of a receiver with respect to any netting agreement or qualified
44 financial contract to which an insurer is a party, the receiver for the
45 insurer shall either: (a) disaffirm or repudiate all netting agreements
46 and qualified financial contracts between a counterparty or any
47 affiliate of that counterparty and the insurer that is the subject of the

1 proceeding; or (b) disaffirm or repudiate none of the netting
2 agreements and qualified financial contracts referred to in
3 subparagraph (a) of this paragraph with respect to that person or
4 any affiliate of that person.

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

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

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

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

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

28 h. As used in this section:

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

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

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

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

45 (c) An agreement or transaction that is subject to regulation
46 under subsection 4c(b) of the "Commodity Exchange Act," 7 U.S.C.

1 s.6c(b), and that is commonly known to the commodities trade as a
2 commodity option;

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

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

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

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

23 (5) "Netting agreement" means:

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

38 (b) Any master agreement or bridge agreement for one or more
39 master agreements described in subparagraph (a) of this paragraph;
40 or

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

1 (6) "Qualified financial contract" means a commodity contract,
2 forward contract, repurchase agreement, securities contract, swap
3 agreement, and any similar agreement that the commissioner
4 determines by regulation to be a qualified financial contract for the
5 purposes of this section.

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

10 (8) "Security arrangement" means any security agreement or
11 arrangement or other credit enhancement or guarantee or
12 reimbursement obligation, including a pledge, security, collateral or
13 guarantee agreement or credit support document.

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

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

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

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

28
29 2. This act shall take effect immediately.
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32 STATEMENT

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

46 New Jersey domestic life insurers are authorized to enter into
47 swap and other derivative agreements under New Jersey law. These

1 arrangements are important to managing risk because they hedge
2 the insurer's assets and liabilities. This type of financial
3 arrangement, referred to in the bill as a "qualified financial
4 contract," include commodity contracts, forward contracts,
5 repurchase agreements, securities contracts, swap agreements, and
6 any similar agreement as determined by the Commissioner of
7 Banking and Insurance. In addition, the bill regulates "netting
8 agreements," which are contracts or agreements that provide for the
9 netting, setoff, liquidation, termination, acceleration or close out,
10 under or in connection with one or more qualified financial
11 contracts or present or future payment or delivery obligations
12 among the parties to the netting agreement.

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

17 The bill provides that if a counterparty to a master netting
18 agreement or a qualified financial contract with an insurer subject to
19 a proceeding under the "Life and Health Insurers Rehabilitation and
20 Liquidation Act" terminates, liquidates, closes out or accelerates the
21 agreement or contract, damages shall be measured as of the date or
22 dates of termination, liquidation, close out or acceleration. The
23 amount of a claim for damages shall be actual direct compensatory
24 damages.

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

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

41 In making any transfer of a netting agreement or qualified
42 financial contract of an insurer subject to a proceeding under the
43 "Life and Health Insurers Rehabilitation and Liquidation Act" the
44 receiver is required to either:

45 (1) Transfer to one party, other than an the insurer subject to a
46 proceeding under the "Life and Health Insurers Rehabilitation and
47 Liquidation Act," all netting agreements and qualified financial

1 contracts between a counterparty or any affiliate of that
2 counterparty and the insurer that is the subject of the proceeding,
3 including: (a) all rights and obligations of each party under that
4 netting agreement and qualified financial contract; and (b) all
5 property, including any guarantees or credit support documents,
6 securing any claims of each party under that netting agreement and
7 qualified financial contract; or

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

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

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

27 The bill also provides that, in exercising any rights of
28 disaffirmance or repudiation of a receiver with respect to any
29 netting agreement or qualified financial contract to which an insurer
30 is a party, the receiver for the insurer shall either: (a) disaffirm or
31 repudiate all netting agreements and qualified financial contracts
32 between a counterparty or any affiliate of such counterparty and the
33 insurer that is the subject of the proceeding; or (b) disaffirm or
34 repudiate none of the netting agreements and qualified financial
35 contracts.

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

1 of the date of the disaffirmance or repudiation of the netting
2 agreement or qualified financial contract.

3 All rights of a counterparty under this bill apply to a netting
4 agreement and a qualified financial contract entered into on behalf
5 of, or allocated to: (1) the general account of the insurer; or (2) a
6 separate account of the insurer if the assets of the separate account
7 are available only to a counterparty to a netting agreement and a
8 qualified financial contract entered into on behalf of, or allocated
9 to, that separate account.

10 Several states have adopted laws similar to the provisions of this
11 bill, thus placing New Jersey domestic life insurers utilizing these
12 financial agreements at a competitive disadvantage with those
13 insurers in states that have amended their laws as well as with
14 federally regulated financial services entities. It is the intent of this
15 bill to keep New Jersey life insurers competitive with insurers and
16 financial counterparties operating in other states.