

IN THE COMMONWEALTH COURT OF PENNSYLVANIA

M. Diane Koken,
Insurance Commissioner of the
Commonwealth of Pennsylvania
Plaintiff

v.

Reliance Insurance Company,
Defendant

No. 269 M.D. 2001

RECEIVED AND FILED
PHILADELPHIA
COMMONWEALTH COURT
OF PENNSYLVANIA
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Consolidated Freightways Corporation,
Petitioner/Intervenor,

v.

M. Diane Koken, Insurance
Commissioner of the Commonwealth
of Pennsylvania,
Respondent/Liquidator,

and

Reliance Insurance Company,
Party-In-Interest

**RESPONSE IN OPPOSITION TO CONSOLIDATED
FREIGHTWAYS CORPORATION'S EMERGENCY
MOTION TO INTERVENE AND TO ENFORCE
PRE-LIQUIDATION AGREEMENT TO SETTLE CLAIM**

M. Diane Koken, the Insurance Commissioner of the Commonwealth of Pennsylvania, as Liquidator for Reliance Insurance Company ("Liquidator"), through her undersigned counsel, opposes Consolidated Freightways Corporation's ("Consolidated") Motion to Enforce Pre-liquidation Agreement to Settle Claim as follows:

BACKGROUND

A. This Court's Order Placing Reliance in Liquidation

1. On October 3, 2001, the Commonwealth Court of Pennsylvania entered its Order ("Liquidation Order") placing Reliance Insurance Company ("Reliance") in liquidation pursuant to Penn. Stat. Ann. tit. 40, §§ 221.1 *et. seq.* ("Pennsylvania Insurance Act"). The Liquidation Order declared Reliance to be insolvent. Order at ¶ 2.

2. The Liquidation Order appointed M. Diane Koken, Insurance Commissioner of the Commonwealth of Pennsylvania, and her successors in office, as Liquidator of Reliance ("Liquidator").

3. The Liquidator is empowered and directed to take immediate possession of Reliance's property, business and affairs and to take such action as the interests of policyholders, creditors or the public may require.

4. As of the date of the Liquidation Order, the Liquidator is charged with a duty to marshal assets in order to maximize the assets of the estate and to protect the interests of all policyholders and creditors as a whole.

5. The Pennsylvania Insurance Act, which governs liquidation of insolvent insurers, expressly sets forth priority of claims and an order of distribution of claims in a liquidation. Pursuant to the Act, after secured claims and administrative expenses and costs, claims for losses covered under policies of insurance are entitled to priority in distribution before claims of general creditors. 40 Pa. Stat. § 221.44. By statute, claims within each class must be paid in full before the members of the next class are paid. 40 Pa. Stat. § 221.44. The Pennsylvania Insurance Act thus requires a fair and equitable distribution of assets among claimants in the same class of priority and prohibits the Liquidator from preferring one claimant over another.

6. The Pennsylvania Insurance Act provides an exclusive remedy and procedure for anyone who has a claim against Reliance. This includes policyholder claims, as well as

general creditor and other claims. The Act requires that all such claims be made through the filing of a “proof of claim.” 40 Pa. Stat. §§ 221.37, 221.38.

7. The statutory proof of claim procedure is exclusive and mandatory. The Liquidation Order expressly provides that “[n]o person shall participate in any distribution of the assets of Reliance unless such claims are filed and presented . . .” Order at ¶19. In recognition of the exclusivity of this claims procedure, the Liquidation Order and the Pennsylvania Insurance Act direct an indefinite stay of all actions against Reliance or the Liquidator. See 40 Pa. Stat. §221.26. The Liquidation Order provides that “[a]ll actions, arbitrations and mediations, against Reliance or the Liquidator shall be submitted and considered as claims in the liquidation proceeding.” *Id.* The Pennsylvania Insurance Act also provides that “[u]pon issuance of an order appointing the commissioner liquidator of a domestic insurer or of an alien insurer domiciled in this Commonwealth, no action at law or equity shall be brought by or against the insurer, whether in this Commonwealth or elsewhere, nor shall any such existing actions be continued after issuance of such order.” 40 Pa. Stat. §221.26.

8. The Liquidation Order, at paragraph 9, provides for the resolution of all claims against Reliance in a single forum – the Commonwealth Court – and directs the Liquidator to implement notice and procedures for filing claims against Reliance.

B. The Pre-Liquidation Settlement Agreement At Issue

9. On October 8, 2001, Consolidated filed a motion with this Court seeking to intervene in this action for the purpose of enforcing a settlement agreement that it claims was reached prior to the date of the Liquidation Order¹. The settlement purportedly requires Reliance to pay \$4.5 million towards the settlement by November 1, 2001.

¹ The Liquidator does not make any determination here with respect to Consolidated’s contention that the settlement agreement is enforceable. However, any dispute over the enforceability of the agreement would be an issue to be determined in the claims filing process after a proper proof of claim is submitted.

10. In its motion, Consolidated alleges that the settlement agreement was agreed to by Reliance prior to the entry of the Liquidation Order and is an enforceable contract. Consolidated requests an order from the Court directing Reliance to pay \$4.5 million in contribution to the settlement.

11. Consolidated's motion must be denied. First, the requested payment would constitute an unlawful preference and would violate the Liquidator's duty to treat all policyholders and creditors fairly. Second, Consolidated's motion is a claim against Reliance which, as with any and all claims against Reliance, must be submitted and adjudicated in the proof of claims proceeding. As of this date, the Liquidator has not yet implemented a claims filing procedure although she anticipates that one will be implemented in due course. Consolidated has not submitted a proper proof of claim pursuant to the statutory claims procedure and the Liquidator has not denied the claim. Accordingly, the claim is not ripe for adjudication by this Court.

ARGUMENT

A. The Requested Payment Would Constitute an Unlawful Preference and Would Violate the Distribution Priority Required by the Pennsylvania Insurance Act.

12. The Liquidation Order, at paragraph 21, expressly prohibits any person from "obtaining of preferences, judgments, attachments . . . against Reliance assets, property . . ."

13. Upon the entry of the Liquidation Order, the Liquidator is required by law to comply with the Pennsylvania Insurance Act and the Liquidation Order, and is charged with the responsibility to protect the interests of all policyholders. She may not, therefore, take any action that favors one policyholder over another, such as permitting a distribution of assets to pay immediately the claim of one policyholder in full.

14. Any payment on the alleged settlement in this case would be a distribution of assets to pay immediately the claim of one policyholder in full and would constitute an

unlawful preference. Consolidated would receive a full recovery on its claim while other policyholders would receive a pro rata share of the distribution of Reliance's assets.

15. The immediate funding of the settlement agreement at issue would also violate the distribution priority required by the Pennsylvania Insurance Act. The funding of the settlement would improperly elevate Consolidated's claim to a priority equal to or higher than administrative expenses which, under the statute, are entitled to the highest priority. In an analogous context, the Supreme Court of Pennsylvania has held that a policyholder who obtains a judgment against an insolvent insurer is not entitled to an elevated priority by virtue of the judgment. See Foster v. Mutual Fire, Marine & Inland Ins. Co., 531 Pa. 598, 614 A.2d 1086(1992); Davis v. Commonwealth Trust Co., 335 Pa. 387, 389, 7A.2d 3, 5(1939). Here, Consolidated's alleged settlement does not elevate the priority of its underlying claim.

16. Pennsylvania courts have addressed the question of whether pre-liquidation settlements must be paid if that payment would contravene the governing statutory scheme and have held that they may not. See Panea v. Isdamer, 773 A. 2d 108, 2001 Pa. Super. LEXIS 429 (Pa. Super. April 10, 2001); Storms ex rel. Storms v. O'Malley, 779 A. 2d 548 (Pa. Super. 2001). In Panea and Storm, the court held that the principle that contracts must be enforced as written must give way to conflicting statutory provisions in Pennsylvania's Property and Casualty Insurance Guaranty Association Act. Here, the enforcement of the settlement agreement would contravene the Liquidator's duty to treat all policyholders fairly and her duty to distribute Reliance's assets in accordance with the distribution priority required by the Pennsylvania Insurance Act.

17. The cases Consolidated relies on, Com. ex rel. Kelly v. Commonwealth Mut. Ins. Co., 450 Pa. 177, 299 A.2d 604 (1973); Com. ex rel. Sheppard v. Central Penn Nat'l Bank, 375 A.2d 874 (Pa. Commw. 1977) and Foster v. Philadelphia Manufacturers, 592 A.2d 131 (Pa. Commw. 1991), are completely inapplicable. These cases merely stand for the proposition that a liquidator who brings a breach of contract action against a third party

seeking remedies under a contract is bound by the provisions of the contract. Here, the Liquidator is not seeking enforcement of the contract. Further, in this case, the Liquidator's immediate funding of the settlement agreement would violate the Pennsylvania Insurance Act and the Liquidation Order.

B. Consolidated Must Pursue its Exclusive Statutory Remedy

18. As alleged above, the Pennsylvania Department Act requires that all claims against Reliance be submitted through a "proof of claim." 40 Pa. Stat. §§ 221.37, 221.38. Under this statutory claims procedure, the Liquidator may deny or allow a claim, in whole or in part. If the Liquidator denies a claim, a claimant may file objections. All disputed claims are ultimately resolved by the Commonwealth Court or by a referee appointed by the Commonwealth Court. 40 Pa. Stat. §221.41. The statutory claims process is mandatory and exclusive, and permits an orderly and fair distribution of Reliance assets in accordance with the distribution priority set forth in the Pennsylvania Insurance Act.

19. The Liquidator is prohibited from paying policyholder claims or claim judgments except through the statutory claims process.

20. Consolidated's motion to enforce the settlement agreement is a claim against Reliance which must be made and ultimately adjudicated in the proof of claim proceeding.

21. Accordingly, Consolidated has a statutory remedy which it is required to pursue, and it may not circumvent the statute by filing a motion with this Court. Pennsylvania courts have held that where a remedy or method of procedure is provided by statute, such as here, the statutory remedy or procedure must be strictly pursued and exclusively applied. Barton v. Northampton County, 19 A. 2d 263 (Pa. 1941); Harcourt v. General Accident Ins. Co., 419 Pa. Super. 155, 615 A. 2d 71 (1992), appeal denied, 534 Pa. 648, 627 A.2d 179 (1993); Concerned Taxpayers of Beaver County v. Beaver County Bd. of Assessment Appeals, 462 A. 2d 347 (Pa. Cmwlth. 1983).

C. Consolidated's Claim for Enforcement of the Settlement Agreement is Not Ripe

22. Pursuant to the Pennsylvania Insurance Act and the Liquidation Order, the Commonwealth Court has "exclusive jurisdiction over all determinations of the validity and amount of claims against Reliance." See 40 Pa. Stat. §§ 221.41, 221.45.

23. The Pennsylvania Insurance Act and the Liquidation Order contemplate that, before this Court adjudicates a claim, an appropriate proof of claim has been filed, the Liquidator has made an adverse determination on the claim and the claimant has filed objections to the Liquidator's determination. None of these preconditions have been met here.

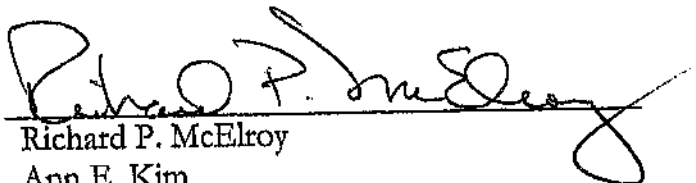
Consolidated filed its motion with this Court prior to a determination as to the validity and amount of its claim in the statutory claims process. Accordingly, Consolidated's motion is premature. Consolidated's claim is not ripe until such time that Consolidated has filed an appropriate proof of claim and the Liquidator has denied the claim.

WHEREFORE, the Liquidator requests that this Court deny Consolidated's Petition to Intervene and Petition to Enforce Pre-liquidation Agreement to Settle Claim.

Respectfully submitted,

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October 24, 2001

CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the preceding Response in Opposition to Consolidated Freightways Corporation's Emergency Motion to Intervene and to Enforce Pre-Liquidation Agreement to Settle Claim was served this 24th day of October 2001, by first class mail, postage prepaid, upon the individuals listed in the attached Master Service List.



ANN E. KIM

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v.

Reliance Insurance Company

No. 269 M.D. 2001 (Commonwealth Court of Pennsylvania)

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