

IN THE COMMONWEALTH COURT OF PENNSYLVANIA

M. Diane Koken
Insurance Commissioner of the
Commonwealth of Pennsylvania, in her
official capacity as Statutory Liquidator
of Reliance Insurance Company

Plaintiff,

v.

Ingram Micro, Inc.

Defendant

NO. 664 M.D. 2003

M. Diane Koken
Insurance Commissioner of the
Commonwealth of Pennsylvania, in her
official capacity as Statutory Liquidator
of Reliance Insurance Company

Plaintiff,

v.

Mitsui & Co. (U.S.A.), Inc.,

Defendant

NO. 666 M.D. 2003

M. Diane Koken
Insurance Commissioner of the
Commonwealth of Pennsylvania, in her
official capacity as Statutory Liquidator
of Reliance Insurance Company

Plaintiff,

v.

H.J. Heinz Company, H.J. Heinz
Company, L.P., H.J. Heinz Finance
Company, and Portion Pac, Inc.

Defendant

NO. 668 M.D. 2003

FILED
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M. Diane Koken :
Insurance Commissioner of the :
Commonwealth of Pennsylvania, in her :
official capacity as Statutory Liquidator :
of Reliance Insurance Company :

Plaintiff, :

v. :

Apple Computer, Inc., :

Defendant :

NO. 671 M.D. 2003

**THE STATUTORY LIQUIDATOR'S MOTION
FOR RECONSIDERATION AND TO VACATE
THE JANUARY 26, 2006 ORDER**

I. INTRODUCTORY STATEMENT

On January 26, 2006, this Court issued a Memorandum Opinion and Order holding that payments involved in these four trade credit insurance cases were not preferences under 40 P.S. § 221.30. The Court based this ruling on a conclusion that the debts under the trade credit insurance policies accrued in 1999 when Reliance Insurance Company issued the policies. Because the debt accrued outside of the one year reachback period under 40 P.S. 221.30, the Court found that the payments at issue were not preferences.

As the Court acknowledged in the Opinion, none of the defendants argued that the debts accrued when the trade credit insurance policies were issued in 1999. Defense counsel did not miss a winning argument. On the contrary, defense counsel, several of whom are experienced bankruptcy lawyers, correctly recognized that, if the debts accrued **before** Reliance made the payments, as this Court ultimately concluded, then they were indisputably "antecedent debts",

with the result that the **subsequent payments within one year preceding the filing of the petition for liquidation** would be preferences under the statute.

It is respectfully submitted that the Court inadvertently missed the fact that the statute explicitly focuses on the date of the **payments**, not the dates when the debts accrued. The statute makes it very clear that it is the time of **payment** that determines whether or not the payment or other transfer of property is a preference under 40 P.S. § 221.30. The only correct approach under the plain meaning of the statute is to determine first whether the debt is an "antecedent debt," and, if so, the statute requires the Court to take a second step of determining whether the payments occurred within one year of the filing of the petition for rehabilitation (as all of these payments indisputably did) and a third step of determining whether one of the four criteria enumerated in the statute applied on the **date of the payments**.

The Opinion of the Court determined that these debts were antecedent debts. However, the Court then failed to focus on the critical next two steps -- *i.e.*, the dates of payment and the financial condition of Reliance at the time of the **payments**, as required by the clear and unambiguous text of the statute.

The Liquidator is giving consideration and weight to this Court's bottom line conclusion that the payments involved in these four cases should not be regarded as voidable preferences under 40 P.S. § 221.30. However, because the legal analysis used by the Court to reach that result is an incorrect construction of the statute, which could cause significant confusion in other important cases, the Liquidator is compelled to file this motion and request that the Court reconsider and vacate the January 26, 2006 order.

Plaintiff, M. Diane Koken, as Insurance Commissioner for the Commonwealth of Pennsylvania, in her official capacity as the Statutory Liquidator of Reliance Insurance Company

(the "**Liquidator**") respectfully requests that the Court grant reconsideration and vacate its January 26, 2006 order.

II. ARGUMENT

A. The Court Committed Clear Error

I. *The Court Failed to Consider the Payment Date.*

Analysis of whether the payments made to the defendants are preferential necessarily begins with 40 P.S. § 221.30, entitled "**Voidable preferences and liens**" of the Insurance Department Act:

A preference is a *transfer of any of the property of an insurer* to or for the benefit of a creditor, for or on account of an antecedent debt, made or suffered by the insurer *within one year* before the filing of a successful petition for liquidation under this article the effect of which transfer may be to enable the creditor to obtain a greater percentage of this debt than another creditor of the same class would receive. *If a liquidation order is entered while the insurer is already subject to a rehabilitation order, then transfers otherwise qualifying shall be deemed preferences if made or suffered within one year* before the filing of the successful petition for rehabilitation or within two years before the filing of the successful petition for liquidation, whichever time is shorter.

40 P.S. § 221.30(a) (emphasis supplied). Therefore, according to the plain statutory language, when the transfers (i.e., the payments) were made by Reliance is dispositive. If the payments were made within the one-year reachback period, the payments are preferential.

The transfer's timing is extremely important because the transfer must occur within the preference period to be recoverable. The one-year period is an essential element of a preference under Article V. Cases construing the preference statute of the Bankruptcy Code (the "**Code**")¹

¹ Insurance Department cases often turn to authorities from the federal bankruptcy context on these issues. Although there is no authority directly on point, the Bankruptcy Code is illustrative and provides guidance here. See, e.g., Wilcox v. CSX Corp., 70 P.3d 85, 2003

provide that it is the time of payment, not when the debt arose, that determines whether or not the payment is a preference. For a cash or wire transfer, the transfer occurs upon delivery or when the creditor receives the payment. *See, e.g., Barnhill v. Johnson*, 503 U.S. 393 (1992) (transfer of check occurs upon honor); *In re Healthco Int'l.*, 132 F.3d 104, 106 (1st Cir. 1997) (wire transfers in satisfaction of antecedent debts during reachback period preferential because time of transfer was when wire payment was received); *In re Lee*, 108 F.3d 239 (9th Cir. 1997) (delivery of debtor's check constitutes transfer); *In re Tennessee Chemical Co.*, 112 F.3d 234 (6th Cir. 1997) (noting that when debtor uses check to make preferential transfer, date of transfer is the date the check was delivered); *In re Toone*, 140 B.R. 605 (Bankr. D. Mass. 1992) (cashier's check provides for immediate transfer for preference purposes); *In re Barefoot*, 952 F.2d 795 (4th Cir. 1991) (setting aside wire transfers as preferences occurring within 90 days of the filing of the bankruptcy petition); *In re Roblin Industries, Inc.*, 127 B.R. 722 (Bankr. W.D.N.Y. 1991) (delivery date); *In re Wingspread Corp.*, 120 B.R. 8 (Bankr. S.D.N.Y. 1990) (holding that transfer occurs upon delivery). The basic rationale for the date of delivery approach is that "in the commercial arena, for most purposes, payment by check is the end of a commercial transaction." *In re Virginia Information Systems Corp.*, 932 F.2d 338, 341-42 (4th Cir. 1991).

The payments made to the Defendants all fall within one year of Reliance's May 29, 2001 rehabilitation petition.² As stated in the Court's Order and as is admitted by the Defendants,

Utah LEXIS 51 (Utah 2003) (turning to federal bankruptcy code for guidance on antecedent debt issue).

² The reachback period is one year before the filing of the rehabilitation petition in this case because the liquidation order was entered while Reliance was already subject to a rehabilitation order pursuant to 40 P.S. § 221.30(a).

Reliance made payments to the Defendants on their trade credit insurance claims on the dates and in the amounts set forth below:

<u>Defendant</u>	<u>Date of Payment</u>	<u>Amount of Payment</u>
Heinz	August 21, 2000	\$1,248,837.98
Ingram	April 10, 2001 and May 8, 2001	\$240,827.24 \$888,085.52
Mitsui	August 28, 2000	\$927,576.04
Apple	August 7, 2000	\$1,639,327.56

The statute and case law make it very clear that the *time of payment* is the critical fact that determines whether or not a payment constitutes a preference. The date the transfer is made is of vital importance because it determines if the transfer is a preference; the date the debt arose merely establishes the right to payment. The Court however, concluded that since the insurance policies were effective in 1999, more than one year before the rehabilitation petition, the payments on those debts could not be preferential. The statute and the case law plainly reveal that the Court's reasoning is flawed. It is not the effective dates of the insurance policies that are controlling; it is the dates that the pre-petition transfers were made that are critical.

2. *The Transfer Date is Critical Because the Statute Directs Attention to the Insurer's Financial Condition at the Time of Payment and Whether Certain Creditors are Preferred at the Time of Payment.*

The cornerstone of the Article V insolvency structure is the principle that equal treatment for those similarly situated must be achieved. It would be highly inequitable to disregard what transpires prior to the filing of the rehabilitation petition; to do so would encourage a race among creditors, engender favoritism by the debtor, and result in an inequitable distribution of assets.

The preference statute is intended to prevent a debtor, whether intentionally or unintentionally, from favoring one creditor over another in paying out its limited resources.

Thus, for example, if an insolvent insurer were to pay all of its oldest debts and none of its more recently accrued debts a month before the filing of the rehabilitation petition, every single payment would be a preference under 40 P.S. § 221.30. The same would be true if the insolvent insurer paid all of its most recently accrued debts and none of the older debts at that time. By focusing on the date of payment, the statute ensures that creditors are treated equally, with all creditors ultimately receiving their proper distribution from the estate under the standards set forth in 40 P.S. § 221.44, as opposed to some receiving 100% based on nothing more than their good luck in obtaining payment during the year before the filing of the rehabilitation petition.

The fact that Reliance issued policies in 1999 is of no import. Rather, 40 P.S. § 221.30 directs the Court to evaluate the insurer's financial condition when the preferential transfers are made. The payment by an insolvent insurer of a pre-existing debt during the reachback period is a preference. It is objectionable because, on the date of payment, it diminishes the insurer's assets to the detriment of its other creditors who have equally valid claims for payment against the estate at that time. Under the plain language of the statute and from the standpoint of treating similarly situated creditors equally, it does not matter when the debt accrued, so long as it accrued before the payment. If payment of the debt occurred within one year of the filing of the rehabilitation petition, the transfer of the insurer's funds was a preference under 40 P.S. § 221.30.

3. *The Court Erred When it Solely Considered the Effective Date of the Insurance Policies in its Preference Analysis.*

The Court correctly acknowledges that the debts owed by Reliance under the trade credit policies are "antecedent debts" for purposes of the preference statute.³ The Court expressed the view that because each respective insurance policy became effective in 1999, the debts were antecedent. However, the claim amounts paid in the preference cases were not paid by Reliance until much later after the policy inception dates, after the claims arose and after the resolution of the underlying claims against the insured. Although the Liquidator disagrees with the Court's conclusion that a debt can arise under an insurance policy before a claim is even presented to the insurer, the fact remains that the Court correctly held that the debts involved in these cases are "antecedent debts."

The date on which the debt arises is important in determining whether the debts were antecedent, but the Court must go a step further and look to the actual transfer date or the date of payment to determine whether a payment is preferential. In its analysis, the Court seems to equate the date the antecedent debt accrued with the transfer date when finding that "[t]he debt arose . . . nearly 2 years prior to the rehabilitation order." These dates are not interchangeable. The antecedent debt date is when the debt arose; the transfer date is the date the payment was actually made. As such, the Court should reconsider its Order since the payments occurred within the statutory preference period.

³ The Liquidator does not endorse the holding that the obligation to pay a claim attaches on the effective date of the policy. As previously asserted, it is the Liquidator's position that an insurer has an obligation to insure a claimant from the date of execution, but does not have an obligation to pay a claim until a loss claim is filed. Nevertheless, the Liquidator and the Court agree that the debts accrued before Reliance paid the claims.

III. CONCLUSION

For the foregoing reasons, Plaintiff M. Diane Koken, Insurance Commissioner for the Commonwealth of Pennsylvania in her official capacity as Statutory Liquidator of Reliance Insurance Company respectfully requests that this Court reconsider the portion of its Order dated January 26, 2006 relating to whether the Statutory Liquidator established that the transfers at issue are preference payments.

Dated: February 9, 2006

M. DIANE KOKEN,
INSURANCE COMMISSIONER FOR THE
COMMONWEALTH OF PENNSYLVANIA IN HER
OFFICIAL CAPACITY AS STATUTORY LIQUIDATOR OF
RELIANCE INSURANCE COMPANY

By: 
One of her Attorneys

Joseph C. Crawford
Amy Onder
WOLF, BLOCK, SCHORR & SOLIS-COHEN, L.L.P.
1650 Arch Street, 22nd Floor
Philadelphia, PA 19103-2097
(215) 977-2000

Attorneys for Plaintiff

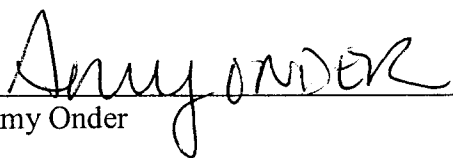
CERTIFICATE OF SERVICE

The undersigned hereby certifies that the foregoing Plaintiff's Motion for Reconsideration to Amend Order was served by first class mail on February 9, 2006 on the following:

Frederick P. Santarelli
Elliott Greenleaf & Siedzikowski, P.C.
Union Meeting Corporate Center V
925 Harvest Drive
Suite 300
Blue Bell, PA 19422
Local Counsel for Defendant, Apple Computer, Inc.
and Counsel for Defendant, Ingram Micro

Philip Warden
Pillsbury Winthrop LLP
50 Fremont Street
P.O. Box 7880
San Francisco, CA 94120-7880
Counsel for Defendant, Apple Computer, Inc.

James R. Potts
Duane Morris LLP
1650 Market Street
One Liberty Place
Philadelphia, PA 19103
Attorneys for Defendants, Mitsui & Co.
(U.S.A.), Inc., H.J. Heinz Company, H.J.
Heinz Company, L.P. and H.J. Heinz
Finance Company



Amy Ouder