

IN THE COMMONWEALTH COURT OF PENNSYLVANIA

Joel S. Ario :
Acting Insurance Commissioner of the :
Commonwealth of Pennsylvania, :
Plaintiff :
v. : No. 269 MD 2001
Reliance Insurance Company, :
Defendant :

Re: *Objection of Tradicion Seguros S.A.
to Liquidator's NOD in POC No. 2070713*

**RECOMMENDATION OF THE REFEREE IN THE MATTER OF
OBJECTION TO NOTICE OF DETERMINATION
BY TRADICION SEGUROS S.A. (FORMERLY LA PATAGONIA
CIA ARGENTINA DE SEGUROS S.A.)
CLAIM NO. 2071713**

Robert E. J. Curran, Esquire, duly appointed Referee on September 14, 2007 in the Matter of Objection of Notice of Determination by Tradicion Seguros S.A. (formerly La Patagonia Cia Argentina de Seguros S.A.) of Claim No. 2071713, hereby recommends to the Honorable James Gardner Collins, President Judge Emeritus of the Commonwealth Court of Pennsylvania, that Claim No. 2071713 be given a Class (e) Priority.

PROCEDURAL HISTORY

Tradicion Seguros S.A., formerly known as La Patagonia Cia Argentina de Seguros S.A., entered into a reinsurance contract with Reliance Insurance Company on May 1, 1996. The contract of insurance was for a twenty percent (20%) share of the losses incurred by La Patagonia's insured, Movistar S.A.

The Pennsylvania Commonwealth Court entered an Order declaring Reliance insolvent and ordered Reliance into liquidation effective October 3, 2001.

La Patagonia submitted a Proof of Claim dated December 12, 2003 to Reliance seeking reinsurance recovery for a loss incurred by its policyholder.

On June 22, 2007 Reliance issued a Notice of Determination assigning Class (e) Priority under 40 P.S. § 221.44 (e) which applies to claims of general creditors.

Thereafter, on or about July 26, 2007, La Patagonia filed objections to the Liquidator's determination of the Proof of Claim Class (e).

On August 23, 2007, Reliance, through its Liquidator, filed a response to the objection of La Patagonia to Notice of Determination on POC No. 2070713.

Thereafter, on or about September 14, 2007, Robert E. J. Curran, Esquire was appointed Referee by Order of Judge James Gardner Colins.

Subsequently a letter was written to Mr. Julio C. Paterno, counsel for the claimant, requesting supporting documents referred to in the Objection and also soliciting any legal argument that claimant desired to make in support of its claim. On October 3, 2007 Julio C. Paterno responded as per the letter attached hereto as **Exhibit "A"**. Subsequent thereto on November 15, 2007, S. Emy Poulad, Esquire, Association General Counsel for Reliance in Liquidation, responded to the October 3, 2007 letter of the Claimant, a copy of which is attached hereto as **Exhibit "B"**.

At this juncture the relevant pleadings and additional briefing for Proof of Claim No. 2070713 are before the Referee for a decision on the Objection of the Claimant.

PARTIES LEGAL POSITION

The Claimant's theory of recovery as set forth in its letter of October 3, 2007 is threefold.

First, the Claimant takes the position that since the legislature is silent as to the priority for claims under a reinsurance agreement, that silence should be interpreted against the Liquidator.

Second, the Claimant attempts to distinguish between a reinsurance contract which is a Stop Loss contract as opposed to a facultative certificate.

Third and last, the Claimant argues that their claim is not a claim for “nonassessable” policies and therefore should not be assigned a Class (e) Priority.

It is the Liquidator’s position that these claims raised by the Claimant have been previously disposed of by prior decisions of the Commonwealth Court and that the issue is nothing more than what priority should be assigned to a reinsurance claim.

DISCUSSION

Tradicion Seguros S.A., formerly known as La Patagonia Cia Argentina de Seguros S.A., (La Patagonia) is an insurance carrier which entered into a reinsurance contract with Reliance Insurance Company (Reliance) effective April 1, 1996. This was facultative reinsurance with Reliance taking a 20% share of the losses incurred by La Patagonia’s insured, Movistar S.A. Reliance had no insurance policy with any party, only the reinsurance contract with La Patagonia. A Proof of Claim was submitted by Claimant seeking reinsurance recovery for a loss by its policyholder, which loss occurred on September 13, 1996. Reliance then issued its Notice of Determination assigning a Class (e) Priority under 40 P.S. Section 221.44 (e), which applies to claims of general creditors. The Liquidator’s position is that a claim under a contract of reinsurance is classified as a claim of a general creditor and assigned a Class (e) Priority.

The Referee finds that there is no factual dispute as to the facts of the insurance policy and the type of policy. The policy is a policy for reinsurance and therefore based upon the prior

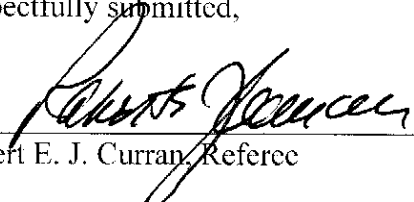
decisions of the Commonwealth Court, specifically M. Diane Koken, Insurance Commissioner of the Commonwealth of Pennsylvania v. Reliance Insurance Company, Objections of Stop Loss Mutual Insurance Company to Notices of Determination (Comm. Ct. Pa. No. 269 M.D. 2005), the Liquidator has properly assigned a Class (e) Priority to the claim. The controlling statute, 40 P.S. Section 221.44, directs that a policy of reinsurance is properly assigned a Class (e) Priority as a claim of a general creditor. In light of the previous decisions of this Court and prior recommendations of various referees as cited in the Liquidator's Brief, it is unnecessary to further analyze the issue of the proper claim level of policies of reinsurance.

The assignation of lower priority to reinsurance contract claims than to policy holder claims is consistent with the public policy of protecting the interest of direct insured's, which is paramount under Pennsylvania Law. Because of the prior rulings of this Court, Pennsylvania Law and public policy consistent with the unanimous opinion of those courts which have expressly considered the issue, the Referee is bound by the prior decisions of this Court which have held that reinsurance contracts are entitled to the priority of general creditors and not that of a policyholder's claim under an insurance policy.

RECOMMENDATION

WHEREFORE, for all the foregoing reasons, it is the recommendation of the Referee that Claim No. 2071713 be given a Class (e) Priority.

Respectfully submitted,


Robert E. J. Curran, Referee

Date: December 21, 2007

EXHIBIT “A”



Tradición Seguros S.A.
Una empresa del Grupo La Caja.

Buenos Aires - October 3, 2007

FREE TRANSLATION

Mr Robert E. J. Curran, Esquire
Curran and Byrne, P.C.
606 East Baltimore Pike
P.O. Box 30
Media, PA 19063
(610) 565-4322

Dear Mr. Curran,

We address to you in your position of appointed Referee on our Objection to the Notice of Determination issued with regard to Proof of Claim n° 2070713 filed in the liquidation of Reliance Insurance Company. This notification was made, together with the respective Order, by Reliance through its letter of September 17 of 2007, which was received in our Offices the 28th of the same month.

Let us express our position in relation with the priority level assigned to the above mentioned claim, through the following considerations.

- 1) In the presentation of Reliance Insurance Company (In Liquidation) of August 21, 2007 answering the "Objection to the Notice of Determination issued on Proof of Claim" it is specified that there are not in the legislation rules for appropriation of privileges with regard to the contracts of reinsurance. This is mistakenly interpreted by them as an argument to their favor on the base that the silence implies a bias to not assigning a priority of higher level.

On the contrary we observe that we are in presence of operations that takes part of their own activity, that is to assume risks receiving a premium as compensation. As such they cannot be assimilated then to acquired general commitments.

In turn, we should understand that when specific norms don't exist the approach to them should be the supplementary application of those one's near to tune to the activity, as those relative to the Insurance regulations.

- 2) Reliance leans on in a judgement of the Court of the year 2005, on which it would have been interpreted that the contracts of reinsurance have the object to protect an insurance company against business risks. They also refer to the existence of other similar sentences.

Demonstrating the juridical difference on the posture that we reject, it is necessary to clarify that there exist different categories of reinsurance.

- Those that protect the result of a business as Stop Loss covers. These kind of coverings are closer to the concept mentioned by Reliance.
- There are the automatic contracts that refer to risk cessions over a complete portfolio, including all policies issued under the wording conditions. In this case the agreement requires a full wording with general and particular conditions.



Tradición Seguros S.A.
Una empresa del Grupo La Caja.

- In turn there are contracts that protect the retention with excess of loss covers.
 - Very different, like the case that we are considering, are the **facultative** placements that are concerted through a cover note **under original conditions** (see the document attached in Reliance presentation as "Exhibit A" corresponding to the in force period of coverage of the claim). In these cases **the reinsurer participates directly with a quota in a only one policy emitted by the insurer**. That is to say that there is not a retention to protect.
- 3) The explanatory note included by Reliance in their letter of June 22 2007 on the Classification of Priority Levels of Claims under the section e) presents a lacking of punctuation signs (points and comas). Our interpretation is that our claim doesn't frame inside the category of " nonassessable " as they are completely paid losses and as such with a certain figure (u\$s 39.089,51). Notice that we have other three presentations of our losses (PoC's n°2070725, 2070727 and 2070711) on which we have not practiced objection being still estimated figures under outstanding losses reserves.

We have devoted a considerable effort and expenses in fulfilling the provision of the required documentation that supports our credits. Consequently, we manifest that while we ask you to consider according to law our points of view, if the applicable legislation is sufficiently determining to specifically interpret that under the category b) falls **only local** policies of **direct** insurance, irrespective of the type of reinsurance involved (the explanatory notes are not clear enough and not necessarily explanatory of their scopes, only mentioning in this category "claims under policies for losses"), it is not our intention to incur in additional expenses in the treatment of this matter. Therefore we will accept the referee's fair juridical definition, founded on the elements already gathered in the cause, without necessity of fixation of hearings or further steps.

Sincerely,

JULIO C. PATERNÓ
GERENCIA DE REASEGURO

EXHIBIT “B”

Reliance Insurance Company (IN LIQUIDATION)

75 Broad Street, 10th Floor
New York, NY 10004

S. Emy Poulad
VP, Associate General Counsel
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E-mail: Emy.Poulad@RelianceInsurance.com



Reliance

November 15, 2007

VIA FAX AND REGULAR MAIL

Robert E.J. Curran, Esq.
P.O. Box 30
8 West Front Street
Media, PA 19063

Re: Proof of Claim Number: 2070713
Claimant: Tradicion Seguros S.A. (formerly La Patagonia Cia Argentina de Seguros S.A.)

Dear Referee Curran,

This letter is submitted in response to Tradicion Seguros, S.A.'s letter to you dated October 3, 2007. Below, we respond to each of the three points raised by the Claimant in its letter.

- The Claimant is asserting that since the legislature is silent as to the priority for claims under a reinsurance agreement, that silence should not be interpreted in our favor. However, the Commonwealth Court reasoned that the "distinction between direct insurance and reinsurance is clearly evident from a plain reading of the statute" and "furthers the General Assembly's intent which has been the fair distribution of assets to policyholders, *i.e.*, the consumers of insurance." December 8, 2005 Memorandum Opinion at 5, citing Grode v. Mutual Fire, Marine & Inland, 572 A.2d 798, 801 n. 5 (Pa. Commw. Ct. 1990) ("the equitable purpose of rehabilitation and liquidation is to protect *first of all* consumers of insurance") (citation omitted) (Exhibit B to the Response of the Liquidator to Objection of Tradicion Seguros, S.A., hereinafter "Response").

Additionally, as we outlined in detail in our Response, the priority of claims under a reinsurance contract has been dispositively addressed in this liquidation in a number of cases. (All the cases are attached as exhibits to our Response). In case after case, the Court has upheld that claims under a reinsurance contract are properly assigned class E priority under 40 P.S. §221.44. Similarly, the Court should uphold a Class E priority for this claim.

- The Claimant is attempting to distinguish this case from the case decided by the Commonwealth Court in a Memorandum Opinion dated December 8, 2005 (Exhibit B to the Response), by pointing out that in that case the reinsurance was a Stop Loss cover whereas in this case, the reinsurance is a Facultative Certificate. "There are two basic types of reinsurance policies – facultative and treaty. In facultative reinsurance, a ceding insurer purchases reinsurance for a part, or all of a single insurance policy. Treaty reinsurance covers specified classes of a ceding insurer's policies." Unigard Security Ins. Co. v. North River Insurance Co., 4 F.3d 1049 (2nd Cir. 1993). Claimants are correct in the distinction but it is a distinction without substance and the Claimant do not provide us with any authority as to why this Court should recognize such a distinction.

In this case, Tradicion Seguros ceded to Reliance 20% under a Facultative Certificate pursuant to which Reliance reinsured Tradicion Seguros for a policy of insurance that Tradicion Seguros had issued to Telefonica De Argentina S.A.

However, the rationale for upholding that claims under a reinsurance contract should be assigned priority E as general creditor under 40 P.S. §221.44 is the same whether the reinsurance contract is a Treaty or Facultative Certificate. (Please refer to our Response at pages 2-5). None of the decisions cited in our Response distinguish between a Treaty or Facultative Certificate and some of the decisions do not even identify the types of reinsurance contract at issue concluding that reinsurance contracts are classified as claims for general creditors. See e.g., In re Liquidation of Reserve Ins. Co., 122 Ill. 2d 555, 524 N.E.2d 538 (1988); Neff v. Cherokee Ins. Co., 704 S.W.2d 1 (Tenn. 1986).

- Lastly, the Claimants argue that their claim is not a claim for "nonassessable" policies. Class E priority under 40 P.S. §221.44 is for "Claims under nonassessable policies for unearned premium or other premium refunds **and claims of general creditors.**" The claim presented by this Claimant is a claim for **general creditor** and is, therefore, properly assigned Class E priority under 40 P.S. § 221.44 as per the decisions by this Court and other Courts all of which are outlined in our Response.

In conclusion, consistent with prior rulings by this Court, Pennsylvania law, public policy and the unanimous opinion of those Courts which have expressly considered the issue, all holding that claims under reinsurance contracts are entitled to the priority of a general creditors' claim under 40 P.S. §221.44(e), it is the Liquidators position that it correctly assigned class (e) priority to the Claimant's Notice of Determination.

Sincerely


SEP/lt
c. Julio C. Paterno
Gerencia de Reaseguro
Mark Beck
Reliance Insurance Company (In Liquidation)