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Landmark victory for reinsurers: New Jersey Supreme Court holds that IBNR claims do not qualify for participation in the final distribution of Integrity Insurance Company's estate

In a matter of first impression under New Jersey law that potentially impacts both the insurance and reinsurance industry and policyholders of insolvent insurance companies, the New Jersey Supreme Court held that the final dividend plan proposed by the liquidator of Integrity Insurance Company should not be approved because it unlawfully allowed incurred but not reported (IBNR) claims to share in the insolvent insurer's estate (*In the Matter of the Liquidation of Integrity Ins. Co.* A-29-07 (NJ Dec 13, 2007)).

Integrity was placed into liquidation in 1987, and the New Jersey Commissioner of Insurance was appointed to marshal and liquidate the assets of Integrity. Pursuant to New Jersey's Insurer Liquidation Act (the Act), the liquidator established a bar date of March 25, 1988 by which time all claims against Integrity, including claims of policyholders based on losses covered under the insurance policies, had to be filed (see generally N.J.S.A. 17:30C-1 to -31.) The order establishing the bar date permitted claimants who had not yet been presented with specific losses to file "policyholder protection claims". The filing of such a claim would permit a specific claim to be filed when the particulars became known, even if that occurred after the bar date. Approximately 26,000 claims, including thousands of policyholder protection claims, were filed against Integrity by the March 25, 1988 bar date. The liquidator estimated the potential liability on policyholder protection claims - that is, unknown, theoretical losses (eg IBNR) - at more than \$2 billion, a significant portion of which would likely be billed to Integrity's reinsurers.

In 2004, the New Jersey Superior Court, Chancery Division approved the final dividend plan submitted by the liquidator, which included provisions permitting the liquidator to allow policyholders to file IBNR claims and to treat those claims as if they were covered under Integrity's insurance policies. The Reinsurance Association of America (RAA) appealed to the New Jersey Appellate Division, arguing that IBNR losses did not constitute claims within the provisions of the Act, specifically section 17:30C-28, which prohibits approval of a claim unless it becomes 'absolute'. The RAA contended that since IBNR claims

are derived from estimation techniques that are never absolute, they could not be estimated in a reasonable manner sufficient to justify payment under the Act. The Appellate Division agreed and held that IBNR claims did not constitute absolute claims under the Act.

The New Jersey Supreme Court affirmed the Appellate Division's ruling, holding that IBNR claims did not qualify for participation in the final distribution of Integrity's estate under the Act, even if such claims were the result of "the application of sophisticated actuarial methodologies", *In re Liquidation of Integrity*, at 2. The court found that the "overarching legislative intent" of the Act was to bar any contingent claims from participation in Integrity's estate, including IBNR claims, as such claims were not 'absolute'. *Id.* at 12. The court further noted that several cases in other jurisdictions had reached similar conclusions regarding whether IBNR claims could share in an insolvent insurer's estate. See, eg *Quackenbush v Mission Ins. Co.* 54 Cal.Rptr.2d 112, 113 (Ct. App. 1996) (reversing a trial court's approval of a liquidator's plan to estimate, allow and bill reinsurers for IBNR and holding that such claims are barred by a provision of the California Insurance Code similar to section 17:30C-28a of New Jersey's Liquidation Act); *In the Matter of the Liquidation of Am. Mut. Liab. Ins. Co.* 747 N.E.2d 1215, 1233-34 (Mass. 2001) (stating in dicta that allowing IBNR claims to share in an insolvent insurer's estate would be contrary to Massachusetts law and criticizing the Chancery Division's analysis of an earlier plan submitted by Integrity's estate which stated that IBNR claims were cognizable in the insurance company liquidation context).

As a result of the court's decision, Integrity's reinsurers will not be responsible for IBNR claims, thus potentially reducing the liability of those reinsurers by millions. Moreover, the *In re Liquidation of Integrity* decision provides liquidators and

members of the insurance and reinsurance industry with another precedent interpreting insolvency statutes as excluding IBNR claims from participation in an insolvent insurer's estate.

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