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New Jersey Supreme Court Holds That Incurred But Not Reported Losses Are Not “Absolute” For Purposes Of Insolvent Insurer’s Estate

On December 13, 2007, the New Jersey Supreme Court held that incurred but not reported (“IBNR”) claims are not “absolute” under N.J.S.A. 17:30C-28(a), and cannot be part of a final dividend plan of an insolvent insurer. In re Liquidation of Integrity Ins. Co., ___ N.J. ___, 2007 N.J. LEXIS 1425 (N.J. 2007). This decision is significant to reinsurers as it reinforces their position that they are not required under reinsurance contracts to pay for estimated “long-tail liabilities,” but rather may wait until such liabilities are actually realized.

In December, 1986, the New Jersey courts declared Integrity Insurance Company insolvent. In an attempt to effect an early termination of the Integrity estate, the Commissioner of Insurance filed a Final Dividend Plan with the court. Complicating the termination of the estate was the fact that many of the policies issued by Integrity insured against “long-tail liabilities,” such as environmental contamination and asbestos-related personal injuries. Under New Jersey law, only “absolute” claims against an insurer are entitled to payment from an estate. See N.J.S.A. 17:30-C-28 (a). Instead of waiting for potential “long-tail claims” to become “absolute,” the Commissioner recommended an estimation process, whereby an independent actuarial

consulting firm would estimate the net present value of future claims. Such claims would be considered “absolute” and would be collectable from Integrity’s reinsurers. This approach was accepted by the trial level court.

In an unpublished decision, the Appellate Division reversed, stating that IBNR claims “are actuarial estimates and are, therefore not absolute . . . They are nothing more than an estimate of the value of a potential actual loss that accounts both for the possibility that the loss will not occur and for the possibility that the extent of the loss will differ from the actuarial estimate.” 2007 N.J. LEXIS 1425 at *17. On appeal, the New Jersey Supreme Court agreed with their Appellate Division brethren. The Court explained that “in order for a claim to participate in the liquidation of an insolvent’s estate, the claim, in each of its fundamental respects, must stand on its own, and not by reference to any other claim.” Id. at 25. Because an actuarial estimation entails looking outside of each claim, any such estimation is not “absolute” and is not entitled to payment from the insolvent estate. The Court recognized that its decision will likely delay the final liquidation of Integrity’s estate, potentially for a decade.

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This decision requires that an actual “long-tail claim” be brought against an insolvent insurer’s estate before it can seek reimbursement from its reinsurers; mere estimations are insufficient. Reinsurers are obligated to honor their contracts with insolvent insurers, but such obligations cannot be accelerated by using actuarial estimates of potential future claims.

Should you have any questions regarding this decision, please feel free to contact us.