S T A T E O F T E N N E S S E E
OFFICE OF THE
ATTORNEY GENERAL
PO BOX 20207
NASHVILLE, TENNESSEE 37202

March 7, 2002

Opinion No. 02-026

Excess Insurance under the Insurance Guaranty Association Laws

QUESTION

The Tennessee Insurance Guaranty Association Act, Tenn. Code Ann. §§ 56-12-101, *et seq.*, provides that it applies to "all kinds of direct insurance, but shall not be applicable to . . . [e]xcess insurance." Tenn. Code Ann.§ 56-12-103(11). Are workers' compensation excess, or aggregate, policies excluded by this statutory scheme?

OPINION

Yes, any policy that falls within the category of "excess insurance" as the Department of Commerce and Insurance defines that term is excluded by Tenn. Code Ann. §§ 56-12-101, *et seq*., for insolvencies arising after March 31, 1999.

ANALYSIS

This opinion concerns the scope of the Tennessee Insurance Guaranty Association Act, Tenn. Code Ann. §§ 56-12-101, *et seq.* (the "Guaranty Act"). This statutory scheme establishes the Tennessee Insurance Guaranty Association. The association is liable for claims under certain insurance policies issued by an insolvent insurance company. The purpose of the statutory scheme is to avoid excessive delay in payment and avoid financial loss to claimants or policyholders because of the insolvency of an insurer, and to provide an association to assess the cost of this protection among insurers. Tenn. Code Ann. § 56-12-102. Section 56-12-103 describes the scope of the statute:

> This part shall apply to *all kinds of direct insurance, but shall not be applicable to:*
>
> (1) Life, annuity, health or disability insurance;
>
> (2) Mortgage guaranty, financial guaranty or other forms of insurance offering protection against investment risks;

> (3) Fidelity or surety bonds, or any other bonding obligations;
>
> (4) Credit insurance, vendors' single interest insurance, or other collateral protection insurance or any similar insurance protecting the interests of a creditor arising out of a creditor-debtor transaction;
>
> (5) Insurance of warranties or service contracts, including insurance that provides for the repair, replacement, or service of goods or property, or indemnification for repair, replacement or service for the operational or structural failure of the goods or property due to a defect in materials, workmanship, or normal wear and tear or provides reimbursement for the liability incurred by the issuer of the agreements or service contracts that provide such benefits;
>
> (6) Title insurance;
>
> (7) Ocean marine insurance;
>
> (8) Any transaction or combination of transactions between a person (including affiliates of such person) and an insurer (including affiliates of such insurer) which involves the transfer of investment or credit risk unaccompanied by transfer of insurance risk;
>
> (9) Any insurance provided by or guaranteed by government;
>
> (10) Any insurance issued on a limited or unlimited assessable basis; or
>
> *(11) Excess insurance.*

(Emphasis added). The statute does not define the meaning of the term "excess insurance." That term was included in this list when the statute was rewritten by 1999 Tenn. Pub. Acts Ch. 48. That act applies only to insolvencies arising after the act became effective on March 31, 1999.

The question is whether the Guaranty Act now covers excess insurance policies purchased by workers' compensation self-insurers' pools. Creation of these pools is authorized under Tenn. Code Ann. § 50-6-405. The Commissioner of Commerce and Insurance is authorized to promulgate rules and regulations as are deemed necessary to provide for the solvency, administration and enforcement of such pooling agreements. Tenn. Code Ann. § 50-6-405(c)(1)(C). Each employer member of an approved pool of self-insurers is classified as a self-insurer to the extent deemed necessary by the Commissioner of Commerce and Insurance. *Id.* Subsection (e) of the same statute authorizes the Commissioner to require the employer to secure "excess catastrophe reinsurance coverage."

Regulations governing workers' compensation self-insurers' pools appear at Tenn. Rules and Regulations Chapter 0780-1-54. Rule 0780-1-54-.04 lists qualifications for initial approval and continued authority to act as a workers' compensation self-insurance group. Under subsection (2) of the Rule, to obtain and maintain its certificate of approval, a workers' compensation self-insurance group must, among other requirements, obtain:

> Specific and aggregate *excess insurance* in a form, in an amount and by an insurance company acceptable to the commissioner. The commissioner may establish minimum requirements for the amount of specific and aggregate *excess insurance* based on differences among groups in their size, types of employments, years in existence and other relevant factors and may permit a group to meet this requirement by placing, in a designated depository, securities of the type referred to in paragraph (b) of this subsection.

Rule 0780-1-54-.04(2)(c) (emphasis added). We assume that your question refers to a policy obtained by a workers' compensation self-insurers' pool to satisfy this requirement. Presumably, any policy that the Department of Commerce and Insurance has accepted as satisfying this requirement is "excess insurance" as the Department defines that term. This regulation was promulgated in 1986. The Guaranty Act was amended in 1999 to exclude "excess insurance." Tenn. Code Ann. § 56-12-103(11). For this reason, we think the Guaranty Act, for insolvencies arising after March 31, 1999, does not apply to any policy that falls within the category of "excess insurance" obtained by a workers' compensation self-insurers' pool under the regulation.

The request states that some self-insurers' pools have argued that these excess insurance policies are covered under the Guaranty Act because they are "direct insurance." The statute does not define the term "direct insurance." Courts in other states interpreting similar guaranty association laws have defined direct insurance as:

> an insurance contract between the insured and the insurer which has accepted the risk of a designated loss to such insured, which relationship is direct and uninterrupted by the presence of another insurer.

Iowa Contractors Workers' Compensation Group v. Iowa Insurance Guaranty Association, 437 N.W.2d 909, 913 (Iowa 1989), *citing Zinke-Smith, Inc. v. Florida Insurance Guaranty Association, Inc.*, 304 So.2d 507, 508-09 (Fla.App. 1974), *cert. denied*, 315 So.2d 469 (Fla. 1975). In *Iowa Contractors,* the Iowa Insurance Guaranty Association sought to avoid liability for claims made under an excess insurance policy that a self-insured workers' compensation pool had bought from a company that had become insolvent. The policy required the insurance company to pay the pool if a single claim exceeded a certain amount, or if the pool's aggregate claims exceeded a certain amount. The association argued, first, that the policy was not "direct insurance" within the meaning of the statute and, second, that

the policy was "reinsurance" outside the coverage of the statute.

The Iowa Supreme Court rejected both arguments. The Court relied on the state's insurance guaranty statutes and its workers' compensation statute. The Court found that the excess policy was a direct insurance policy between the insurance company and the self-insured pool, which was simply a group of self-insured employers. The Court also cited its long-established rule favoring broad interpretation of workers' compensation coverage in reaching this conclusion. The Court concluded that the policy was not "reinsurance" because the self-insured pool could not be regarded as an insurer under Iowa law. The New Mexico Supreme Court reached a similar conclusion with regard to the New Mexico insurance guaranty statutes. *In re Mission Insurance Company*, 112 N.M. 433, 816 P.2d 502 (1991). *See also Doucette v. Pomes*, 247 Conn. 442, 724 A.2d 481 (1999) (an employer that opted to self-insure against workers' compensation claims was not an "insurer" within the meaning of insurance guaranty statutes that excluded insurers' claims from coverage). *But see South Carolina Property and Casualty Insurance Guaranty Association v. Carolinas Roofing and Sheet Metal Contractors Self-Insurance Fund*, 315 S.C. 555, 446 S.E.2d 422 (1994) (a workers' compensation self-insurance pool was an "insurer" under the South Carolina guaranty association act, and the guaranty association was therefore not obligated to cover its claim on the insolvency of its catastrophic insurance coverer).

Courts, therefore, have reached different results when considering whether state guaranty laws cover a claim by a workers' compensation self-insurers' pool under an excess insurance policy issued by an insolvent insurer. In all the cases discussed above, the state guaranty association laws expressly included "direct insurance" and excluded claims by an insurer from the definition of claims covered under the law. Like these statutes, the Guaranty Act covers "direct insurance" and excludes claims by an insurer from its definition of "covered claim." Tenn. Code Ann. § 56-12-103; Tenn. Code Ann. § 56-12-104(7)(B)(iii). It is not clear whether, under Tennessee law, a workers' compensation self-insurers' pool would be considered an insurer whose claim was excluded from coverage under the Guaranty Act, or whether a policy of excess loss insurance purchased by the pool would be considered "direct insurance" under Tenn. Code Ann. § 56-12-103.

Even if such an excess loss policy were found to be "direct insurance" under that portion of the statute, however, we think it would still be excluded from coverage under subsection (11), which expressly excludes "excess insurance." None of the statutes in the cases discussed above contained that exclusion. Tenn. Code Ann. § 56-12-103 provides that the Guaranty Act applies to "all kinds of direct insurance . . .." The list that follows, however, excludes many types of insurance that could, depending on the particular policy, fall within the definition of "direct insurance" as that term is defined by courts in other jurisdictions. For example, subsection (1) of the statute excludes life, annuity, health or disability insurance. Another statutory scheme, Tenn. Code Ann. §§ 56-12-201, *et seq.*, establishes the Tennessee Life and Health Insurance Guaranty Association responsible for, among other claims, *direct*, nongroup life, health, annuity and supplemental policies. Tenn. Code Ann. § 56-12-204(b)(1) (emphasis added). It is clear, then, that the exclusion in Tenn. Code Ann. § 56-12-103(1) includes *all* life, annuity, and health insurance, whether direct or indirect. The list of insurance excluded from coverage under Tenn. Code Ann. § 56-12-

103 should therefore be interpreted to exclude all policies, whether direct or not, providing the types of insurance included in the list. For this reason, the Guaranty Act now excludes all excess insurance policies, whether direct or not. Whether any particular policy falls within the category of "excess insurance," of course, should be determined by the Department of Commerce and Insurance. But we think the term would include any policy that the Department has already accepted as meeting the requirements for excess insurance under its rules governing workers' compensation self-insurance pools.

Material received in connection with your request also refers to an argument that Tenn. Code Ann. § 56-12-103(11) was intended to exclude surplus lines insurance, not excess insurance purchased by self-insured workers' compensation pools. We find nothing in the Guaranty Act or other insurance laws to support this argument.

PAUL G. SUMMERS
Attorney General and Reporter

MICHAEL E. MOORE
Solicitor General

ANN LOUISE VIX
Senior Counsel

Requested by:

Honorable Anne B. Pope
Commissioner of Commerce and Insurance
500 James Robertson Parkway
Nashville, TN 37243-5065