

# HOUSE . . . . . No. 1039

By Mr. Murphy of Weymouth, petition of James M. Murphy relative to qualified financial contracts. Financial Services.

## The Commonwealth of Massachusetts

In the Year Two Thousand and Seven.

AN ACT RELATIVE TO QUALIFIED FINANCIAL CONTRACTS.

*Be it enacted by the Senate and House of Representatives in General Court assembled, and by the authority of the same, as follows:*

1 SECTION 1. Section 180A of chapter 175 of the General Laws,  
2 as appearing in the 2004 Official Edition, is hereby amended by  
3 striking in line “2” the letter “L” adding the following:— “L½”

1 SECTION 2. Section 180A of chapter 175 of the General Laws,  
2 as appearing in the 2004 Official Edition, is hereby amended by  
3 adding the following:—

4 “Affiliate” of, or person “affiliated” with, a specific person, is a  
5 person that directly or indirectly through one or more intermediaries,  
6 controls, or is controlled by, or is under common control with, the  
7 person specified.

8 “Control” (including the terms “controlling,” “controlled by” and  
9 “under common control with”) means the possession, direct or indi-  
10 rect, of the power to direct or cause the direction of the management  
11 and policies of a person, whether through the ownership of voting  
12 securities, by contract other than a commercial contract for goods or  
13 nonmanagement services, or otherwise, unless the power is the result  
14 of an official position with or corporate office held by the person.  
15 Control shall be presumed to exist if any person, directly or indi-  
16 rectly, owns, controls, holds with the power to vote, or holds proxies  
17 representing, ten percent (10%) or more of the voting securities of  
18 any other person. This presumption may be rebutted by a showing  
19 that control does not exist in fact. The commissioner may deter-  
20 mine, after furnishing all persons in interest notice and an opportu-  
21 nity to be heard and making specific findings of fact to support the

22 determination, that control exists in fact, notwithstanding the  
23 absence of a presumption to that effect.

24 “Netting agreement” means (1) a contract or agreement (including  
25 terms and conditions incorporated by reference therein), including a  
26 master agreement (which master agreement, together with all sched-  
27 ules, confirmations, definitions and addenda thereto and transactions  
28 under any thereof, shall be treated as one netting agreement), that  
29 documents one or more transactions between the parties to the agree-  
30 ment for or involving one or more qualified financial contracts and  
31 that provides for the netting, liquidation, setoff, termination, acceler-  
32 ation or close out under or in connection with one or more qualified  
33 financial contracts or present or future payment or delivery obliga-  
34 tions or payment or delivery entitlements thereunder (including liqui-  
35 dation or close-out values relating to such obligations or  
36 entitlements) among the parties to the netting agreement; (2) any  
37 master agreement or bridge agreement for one or more master agree-  
38 ments described in Paragraph (1) of this Subsection; or (3) any secu-  
39 rity agreement or arrangement or other credit enhancement or  
40 guarantee or reimbursement obligation related to any contract or  
41 agreement described in Paragraph (1) or (2) of this Subsection; pro-  
42 vided that any contract or agreement described in paragraph (1) or  
43 (2) of this Subsection relating to agreements or transactions that are  
44 not qualified financial contracts shall be deemed to be a netting  
45 agreement only with respect to those agreements or transactions that  
46 are qualified financial contracts.

47 “Person” is an individual, a corporation, a limited liability com-  
48 pany, a partnership, an association, a joint stock company, a trust, an  
49 unincorporated organization, any similar entity or any combination  
50 of the foregoing acting in concert, but shall not include any joint  
51 venture partnership exclusively engaged in owning, managing,  
52 leasing or developing real or tangible personal property.

53 “Qualified financial contract” means a commodity contract, for-  
54 ward contract, repurchase agreement, securities contract, swap  
55 agreement and any similar agreement that the commissioner deter-  
56 mines by regulation, resolution or order to be a qualified financial  
57 contract for purposes of sections one hundred and eighty A through  
58 one hundred and eighty L½.

59 (1) “Commodity contract” means:

60 (a) A contract for the purchase or sale of a commodity for future  
61 delivery on, or subject to the rules of, a board of trade or contract  
62 market under the Commodity Exchange Act (7 U.S.C. § 1, et seq.)  
63 or a board of trade outside the United States;

64 (b) An agreement that is subject to regulation under Section 19  
65 of the Commodity Exchange Act (7 U.S.C. § 1, et seq.) and that is  
66 commonly known to the commodities trade as a margin account,  
67 margin contract, leverage account or leverage contract;

68 (c) An agreement or transaction that is subject to regulation  
69 under Section 4c(b) of the Commodity Exchange Act (7 U.S.C. § 1,  
70 et seq.) and that is commonly known to the commodities trade as a  
71 commodity option;

72 (d) Any combination of the agreements or transactions referred  
73 to in this paragraph; or

74 (e) Any option to enter into an agreement or transaction referred  
75 to in this paragraph.

76 (2) “Forward contract”, “repurchase agreement”, “securities con-  
77 tract” and “swap agreement” shall have the meanings set forth in the  
78 Federal Deposit Insurance Act, 12 U.S.C. § 1821(e)(8)(D), as  
79 amended from time to time.

80 “Transfer” shall include the sale and every other and different  
81 mode, direct or indirect, of disposing of or of parting with property  
82 or with an interest therein, including a setoff, or with the possession  
83 thereof or of fixing a lien upon property or upon an interest therein,  
84 absolutely or conditionally, voluntarily or involuntarily, by or  
85 without judicial proceedings. The retention of a security title in  
86 property delivered to an insurer and foreclosure of the insurer’s  
87 equity of redemption shall be deemed a transfer suffered by the  
88 insurer.

1 SECTION 3. Chapter 175 of the General Laws, as appearing in  
2 the 2004 Official Edition, is hereby amended by adding the  
3 following new section:—

4 180L½ Qualified Financial Contracts

5 A. Notwithstanding any other provision of sections one hundred  
6 and eighty A through one hundred and eighty L½, including any  
7 other provision of sections one hundred and eighty A through one  
8 hundred and eighty L½ permitting the modification of contracts, or

9 other law of a state, no person shall be stayed or prohibited from  
10 exercising:

11 (1) A contractual right to cause the termination, liquidation,  
12 acceleration or close out any netting agreement or qualified financial  
13 contract with an insurer because of:

14 (a) The insolvency, financial condition or default of the insurer at  
15 any time, provided that the right is enforceable under applicable law  
16 other than sections one hundred and eighty A through one hundred  
17 and eighty L½; or

18 (b) The commencement of a rehabilitation proceeding under  
19 section one hundred and eighty B or a liquidation proceeding under  
20 section one hundred and eighty C;

21 (2) Any right under a pledge, security, collateral, reimbursement  
22 or guarantee agreement or arrangement or any other similar security  
23 agreement or arrangement or other credit enhancement relating to  
24 one or more netting agreements or qualified financial contracts;

25 (3) Subject to the final paragraph of section one hundred and  
26 eighty C, any right to set off or net out any termination value, pay-  
27 ment amount, or other transfer obligation arising under or in connec-  
28 tion with one or more qualified financial contracts where the  
29 counterparty or its guarantor is organized under the laws of the  
30 United States or a state or foreign jurisdiction approved by the Secu-  
31 rities Valuation Office of the National Association of Insurance  
32 Commissioners as eligible for netting; or

33 (4) If a counterparty to a master netting agreement or a qualified  
34 financial contract with an insurer subject to a rehabilitation pro-  
35 ceeding under section one hundred and eighty B or a liquidation pro-  
36 ceeding under section one hundred and eighty C terminates,  
37 liquidates, closes out or accelerates the agreement or contract, dam-  
38 ages shall be measured as of the date or dates of termination, liqui-  
39 dation, close out or acceleration. The amount of a claim for  
40 damages shall be actual direct compensatory damages calculated in  
41 accordance with Subsection F below.

42 B. Upon termination of a netting agreement or qualified finan-  
43 cial contract, the net or settlement amount, if any, owed by a non-  
44 defaulting party to an insurer which is the subject of a rehabilitation  
45 proceeding under section one hundred and eighty B or a liquidation  
46 proceeding under section one hundred and eighty C shall be trans-  
47 ferred to or on the order of the receiver for the insurer, even if the

48 insurer is the defaulting party, notwithstanding any walkaway clause  
49 in the netting agreement or qualified financial contract. For pur-  
50 poses of this subsection, the term “walkaway clause” means a provi-  
51 sion in a netting agreement or a qualified financial contract that,  
52 after calculation of a value of a party’s position or an amount due to  
53 or from one of the parties in accordance with its terms upon termina-  
54 tion, liquidation or acceleration of the netting agreement or qualified  
55 financial contract, either does not create a payment obligation of a  
56 party or extinguishes a payment obligation of a party in whole or in  
57 part solely because of the party’s status as a non-defaulting party.  
58 Any limited two-way payment or “first method” provision in a net-  
59 ting agreement or qualified financial contract with an insurer that has  
60 defaulted shall be deemed to be a full two-way payment or “second  
61 method” provision as against the defaulting insurer. Any such prop-  
62 erty or amount shall, except to the extent it is subject to one or more  
63 secondary liens or encumbrances or rights of netting or setoff, be a  
64 general asset of the insurer.

65 C. In making any transfer of a netting agreement or qualified  
66 financial contract of an insurer which is the subject of a rehabilita-  
67 tion proceeding under section one hundred and eighty B or a liquida-  
68 tion proceeding under section one hundred and eighty C, the receiver  
69 shall either:

70 (1) Transfer to one party (other than an insurer which is the sub-  
71 ject of either such proceeding) all netting agreements and qualified  
72 financial contracts between a counterparty or any affiliate of the  
73 counterparty and the insurer which is the subject of the proceeding,  
74 including:

75 (a) All rights and obligations of each party under each netting  
76 agreement and qualified financial contract; and

77 (b) All property, including any guarantees or other credit enhance-  
78 ment, securing any claims of each party under each netting agree-  
79 ment and qualified financial contract; or

80 (2) Transfer none of the netting agreements, qualified financial  
81 contracts, rights, obligations or property referred to in Subparagraph  
82 (1) (with respect to the counterparty and any affiliate of the counter-  
83 party).

84 D. If a receiver for an insurer makes a transfer of one or more  
85 netting agreements or qualified financial contracts, then the receiver  
86 shall use its best efforts to notify any person who is party to the net-

87 ting agreements or qualified financial contracts of the transfer by  
88 12:00 noon (the receiver's local time) on the business day following  
89 the transfer. For purposes of this subsection, "business day" means a  
90 day other than a Saturday, Sunday or any day on which either the  
91 New York Stock Exchange or the Federal Reserve Bank of New  
92 York is closed.

93 E. Notwithstanding any other provision of sections one hundred  
94 and eighty A through one hundred and eighty L $\frac{1}{2}$ , a receiver may  
95 not avoid a transfer of money or other property arising under or in  
96 connection with a netting agreement or qualified financial contract  
97 (or any pledge, security, collateral or guarantee agreement or any  
98 other similar security arrangement or credit support document  
99 relating to a netting agreement or qualified financial contract) that is  
100 made before the commencement of a rehabilitation proceeding under  
101 section one hundred and eighty B or a liquidation proceeding under  
102 section one hundred and eighty C. However, a transfer may be  
103 avoided under chapter 109A if the transfer was made with actual  
104 intent to hinder, delay or defraud the insurer, a receiver appointed for  
105 the insurer, or existing or future creditors.

106 F. (1) In exercising the rights of disaffirmance or repudiation of a  
107 receiver with respect to a netting agreement or qualified financial  
108 contract to which an insurer is a party, the receiver for the insurer  
109 shall either:

110 (a) Disaffirm or repudiate all netting agreements and qualified  
111 financial contracts between a counterparty or an affiliate of a coun-  
112 terparty with the insurer that is the subject of a rehabilitation or liq-  
113 uidation proceeding; or

114 (b) Disaffirm or repudiate none of the netting agreements and  
115 qualified financial contracts referred to in Subparagraph (a) (with  
116 respect to the person or any affiliate of the person).

117 (2) Notwithstanding any other provision of sections one hundred  
118 and eighty A through one hundred and eighty L $\frac{1}{2}$ , any claim of a  
119 counterparty against the estate arising from the receiver's disaffir-  
120 mance or repudiation of a netting agreement or qualified financial  
121 contract that has not been previously affirmed in the liquidation or  
122 immediately preceding rehabilitation proceeding shall be determined  
123 and shall be allowed or disallowed as if the claim had arisen before  
124 the date of the filing of the application for liquidation or, if a rehabil-  
125 itation proceeding is converted to a liquidation proceeding, as if the

126 claim had arisen before the date of the filing of the application for  
127 rehabilitation. The amount of the claim shall be the actual direct  
128 compensatory damages determined as of the date of the disaffir-  
129 mance or repudiation of the netting agreement or qualified financial  
130 contract. The term “actual direct compensatory damages” does not  
131 include punitive or exemplary damages, damages for lost profit or  
132 lost opportunity or damages for pain and suffering, but does include  
133 normal and reasonable costs of cover or other reasonable measures  
134 of damages utilized in the derivatives, securities or other market for  
135 the contract and agreement claims.

136 G. The term “contractual right” as used in this section includes  
137 any right set forth in a rule or bylaw of a derivatives clearing organi-  
138 zation (as defined in the Commodity Exchange Act), a multilateral  
139 clearing organization (as defined in the Federal Deposit Insurance  
140 Corporation Improvement Act of 1991), a national securities  
141 exchange, a national securities association, a national securities  
142 clearing agency, a contract market designated under the Commodity  
143 Exchange Act, a derivatives transaction execution facility registered  
144 under the Commodity Exchange Act, or a board of trade (as defined  
145 in the Commodity Exchange Act) or in a resolution of the governing  
146 board thereof and any right, whether or not evidenced in writing,  
147 arising under statutory or common law, or under law merchant, or by  
148 reason of normal business practice.

149 H. The provisions of this section shall not apply to persons who  
150 are affiliates of the insurer that is the subject of the proceeding.

151 I. All rights of counterparties under sections one hundred and  
152 eighty A through one hundred and eighty L½ shall apply to netting  
153 agreements and qualified financial contracts entered into on behalf  
154 of the general account or separate accounts if the assets of each sepa-  
155 rate account are available only to counterparties to netting agree-  
156 ments and qualified financial contracts entered into on behalf of that  
157 separate account.