IN THE UNITED STATES COURT OF FEDERAL CLAIMS

HEALTH REPUBLIC INSURANCE COMPANY, Plaintiff, on behalf of itself and all others similarly situated, vs. THE UNITED STATES OF AMERICA, Defendant.	No. 1:16-cv-00259 (Judge Davis)

DISPUTE SUBCLASS'S REPLY IN FURTHER SUPPORT OF MOTION TO DISMISS THE GOVERNMENT'S COUNTERCLAIM

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Introduction

As explained in their Motion to Dismiss (Dkt. 103, "Mot."), the Government for years refused to pay money it owed Colorado HealthOp[1] and Meritus, contributing to both entities' insolvencies. Now that the Government has been ordered to make good on its debts, it seeks to apply "offsets" consisting largely of interest that supposedly accrued *after* both entities' insolvencies, when the Government owed them more than they owed it. To add insult to injury, the Government seeks double recovery against Meritus, which already paid these debts in 2017.

The Government's claims fail for four reasons. ***First***, the Government asserts that the McCarran Ferguson Act does not apply because Colorado and Arizona's statutes consolidating insurer liquidation proceedings in one court so that creditors cannot jump ahead of policyholders do not "regulate the business of insurance." That is wrong. As courts in the Second, Fifth, and Tenth Circuits have held, such statutes plainly regulate insurance and protect policyholders, meaning that, under the McCarran Ferguson Act, the statutes granting this Court jurisdiction over the Government's offset claims must yield. Mot. 7–11.

Second, the Government does not dispute that it is a net debtor to Colorado HealthOp and Meritus. *See* Dkt. 112, "Opp." 24–28. Because the Government owes more than it is owed, there was never any balance on which interest could accrue. *See* Mot. 12. Further, Colorado and Arizona statutes prevent the accrual of interest after an insurer's insolvency—state laws that reverse-preempt the Government's interest claim under the McCarran Ferguson Act. Mot. 13–14.

Third, the Government wrongly argues that Colorado law does not govern or else allows its offset claim against Colorado HealthOp. Opp. 28–32. But as Judge Hertling has already held as to the very debts at issue, Colorado law applies and does not permit the Government's non-

[1] All abbreviations are consistent with those used in Colorado HealthOp and Meritus's Motion.

contractual offsets. *Conway v. United States*, 145 Fed. Cl. 514, 524–30 (2019).

Fourth, the Government argues it is entitled to ***double recovery*** against Meritus, arguing that Meritus's 2017 payment of the exact debts the Government now asserts was ineffective because Meritus's setoff relied on the Government's unpaid risk corridors liability. Opp. 32–34. But the point of an offset is to recover unpaid moneys, rendering its argument against Meritus's offset incoherent. Moreover, Meritus's offset is the only reason that Meritus did not seek and recover ***more*** from the Government on its risk corridors claim—because it had already credited its debts to the Government against that claim. Mot. 23–25. For the Government to now argue it is entitled to both reduced liability ***and*** an incremental offset is double-counting.

For these reasons, the Court should grant the Dispute Subclass's Motion to Dismiss.

I. The McCarran Ferguson Act Reverse Preempts 28 U.S.C. §§ 1503 and 2508, the Statutes Giving this Court Jurisdiction over the Government's Counterclaims.

A. Colorado's and Arizona's Jurisdictional Statutes Regulate Insurance and Protect Policyholders

Colorado and Arizona's insurance statutes each vest a single state court with exclusive jurisdiction over all matters relating to an insurer's liquidation. Mot. 8–9; *see also* A.R.S. 20-612(a), (c) (vesting a state court with "exclusive original jurisdiction" over insurer liquidation proceedings, which "shall constitute the sole and exclusive measure of liquidating . . . an insurer); Colo. Rev. Stat. § 10-3-504(2) (similarly providing that "all actions" involving the "dissolution, liquidation, rehabilitation, sequestration, conservation, or receivership of any insurer" be brought in the district court for Denver). By consolidating claims against an insolvent insurer in one liquidation court, these statutes prevent low-priority creditors from leapfrogging higher priority creditors, and they are therefore necessary to achieve the central purpose of both States' laws governing insurer liquidation: ensuring that policyholders are maximally protected

by granting them high priority during liquidation proceedings.[2] *See Munich Am. Reinsurance Co. v. Crawford*, 141 F.3d 585, 593 (5th Cir. 1998) (observing that a similar Oklahoma statute, by "placing ultimate control over all issues relating to the insolvency proceedings in a single court," served to prevent an insurer's assets from piecemeal depletion and therefore "protect[] the relationship between the insurance company and its policyholders.")

These jurisdictional statutes thus were "enacted for the purpose of regulating the business of insurance . . . to further the goal of protecting policyholders," which is the standard for reverse preemption under the McCarran Ferguson Act. *United States v. Fabe*, 508 U.S. 491, 508–09 (1993). Indeed, the Government's position in this case is virtually indistinguishable from that the Supreme Court rejected in *Fabe*: it seeks to rely on general federal statutes that do not regulate the business of insurance (in *Fabe*, a super-priority statute; here, statutes vesting this Court with jurisdiction over the Government's offset claims, 28 U.S.C. § 2508; 28 U.S.C. § 1503) to allow it to receive payment on its claim against insolvent insurers before policyholders, in spite of state statutes providing that policyholders should come first. *Fabe*, 508 U.S. at 508-09. Relying on Sections 2508 and 1503 in this manner would therefore "frustrate [two states'] declared state polic[ies]" of protecting policyholders by consolidating claims against insolvent insurers in a single court, and thereby "interfere with [two] State[s'] administrative regime[s]." *Humana Inc. v. Forsyth*, 525 U.S. 299, 310 (1999); Mot. 7–10.

The Government's opening argument only proves the point. It argues "that these federal statutes impose a mandatory duty [on this Court] to give effect to the United States' offsets." Opp. at 12. However, just as Sections 2508 and 1503 serve the important purpose of

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[2] Both Arizona and Colorado grant policyholders first priority after creditors whose claims arise through the liquidation process, followed by the Government. A.R.S. § 20–629; Colo. Rev. Stat. § 10-3-541(1)(b).

"permit[ting] the government, when sued in [this Court], to have determined in a single suit all questions which involve mutual obligations" so as to better protect *the Government*,[3] Arizona Section 20-612 and Colorado Section 10-3-504(2) serve the identical purpose of allowing insolvent state insurers to have all claims against them decided in a single proceeding, so as to best protect those insurers' *policyholders*. *See Crawford*, 141 F.3d at 593. The Government's argument that the Arizona and Colorado statutes do not "uniquely 'protect policyholders'" and are not "integrally related to the performance of insurance contracts," Opp. 19 (quotations omitted), is belied by its own lengthy explanation of how similar federal statutes designed to consolidate claims involving *the Government* in a single court serve to uniquely protect *the Government's* interests. Opp. 11–13.

Under ordinary preemption principles, a state law that protects one set of stakeholders would yield to a conflicting federal law that protects the Government. But, under the McCarran Ferguson Act, federal laws not concerning insurance give way when they interfere with state laws that protect policyholders—even at the Government's expense. *Fabe*, 508 U.S. at 508–09.

Recognizing that Colorado and Arizona state statutes reverse preempt the statutes giving this Court jurisdiction over the Government's setoff claims does not leave the Government without a forum. Like any creditor, it can assert its claims in Colorado's and Arizona's liquidation courts, where it will receive better treatment than all creditors after policyholders and those involved in the liquidation process. A.R.S. § 20–629(4); Colo. Rev. Stat. § 10-3-541(1)(c).

B. Ample authority demonstrates that federal jurisdictional statutes are preempted under the McCarran Ferguson Act in situations such as these.

As the Government concedes, Courts of Appeals in the Second, Fifth, and Tenth Circuits

[3] Opp. at 12 (citing *Cherry Cotton Mills v. United States*, 327 U.S. 536, 539 (1946)).

have each found that state jurisdictional statutes similar to Colorado's and Arizona's regulate the business of insurance and protect policyholders, and therefore under the McCarran Ferguson Act they reverse preempt contrary federal jurisdictional statutes that do not specifically regulate insurance. Opp. 21 (citing *Crawford*, 141 F.3d 585 (5th Cir. 1998); *Davister Corp. v. United Republic Life Ins. Co.*, 152 F.3d 1277 (10th Cir. 1998); *Stephens v. American Int'l Ins. Co.*, 66 F.3d 41 (2d Cir. 1995)). Add to these the Kentucky and Louisiana Supreme Courts, which have both reached the same conclusion. *See Donelon v. Shilling*, 2019-cv-00514, 2020 WL 2079362 (La. April 27, 2020); *Ernst & Young, LLP v. Clark*, 323 S.W.3d 682, 689 (Ky. 2010).

The Government argues these cases are inapposite because "[t]hose courts considered whether a federal arbitration statute conflicted with a state insurance law that precluded arbitration[.]" Opp. 22. But this simply begs the question. The *reason* the state insurance laws in question were found to preclude arbitration in all but one of these cases was not any specific provision in them disapproving arbitration,[4] but rather because the state statutes in question embraced the same policy as the Colorado and Arizona statutes embrace here: the consolidation of claims against an insolvent insurer in one forum so as to better protect policyholders. *See Crawford*, 141 F.3d at 593 ("Oklahoma's policy of placing ultimate control over all issues relating to the insolvency proceedings in a single court is aimed at protecting the relationship between the insurance company and its policyholders.).[5] The Government's attempt to distinguish these cases as each "involv[ing] clear conflicts" with federal law, Opp. 23, ignores

[4] The exception is *Stephens*, where a Kentucky statute specifically related to arbitration. 66 F.3d at 43. Whether such a provision regulates the insurance and protects policyholders is, if anything, a closer question than whether general jurisdictional statutes consolidating *all claims* in one court do so.

[5] *See also Davister*, 153 F.3d at 1281 ("Allowing a putative creditor to pluck from the entire liquidation proceeding one discrete issue and force arbitration contrary to the blanket stay entered by the Utah state court would certainly impair the progress of the orderly resolution of all matters involving the insolvent company"); *Donelon*, 2020 WL 2079362, at *12 (same); *Clark*, 323 S.W.3d at 690 (same).

the reason for the "clear conflict": they involved state statutes mandating that claims against an insolvent insurer proceed in a single state forum. That reason applies equally here.

To the extent the Government's explanation for these cases turns on some distinction between the Federal Arbitration Act and other kinds of jurisdictional statutes, it makes still less sense. Like the Federal Arbitration Act, federal jurisdictional statutes such as Sections 2508 and 1503 do not regulate the business of insurance, and, like the Federal Arbitration Act, they plainly conflict with a state's policy of consolidating all claims against an insolvent insurer into a single proceeding. Courts employing the exact same logic as *Crawford*, *Davister*, and *Stephens* have held that other federal jurisdictional statutes are displaced under the McCarran Ferguson Act by state statutes consolidating all claims against an insolvent insurer in one state forum—including, in fact, by the Arizona statute at issue in this very case. *See, e.g.*, *United States Fin. Corp. v. Warfield*, 839 F. Supp. 684, 689 (D. Ariz. 1993) ("The provisions [vesting exclusive jurisdiction in one Arizona court] are an integral part of Arizona's scheme for regulating insolvent insurers[.]"); *see id.* ("This process presumably is intended to and does conserve insurance company assets for ultimate payment to policyholders. . .").

Finally, the Government falls back on supposedly contrary authority from other Circuits. Opp. 21–23. But these cases do not deal with this situation, where a creditor advances a claim against an insolvent insurer and seeks to have judgment on that claim paid outside the liquidation process. For instance, in *Suter v. Munich Reins. Co.*, 223 F.3d 150, 161 (3d Cir. 2000), the Third Circuit permitted enforcement of a contractual arbitration clause in an affirmative suit for damages brought by the insolvent insurer's liquidator; no claims were raised *against* the insurer. *Id.* The Court noted that enforcement of the arbitration contract would not impair New Jersey's liquidation act because it was *not* "a suit by a party seeking access to assets of the insurer's

estate," and "even if it were such, the Superior Court would have express authority to enjoin the plaintiff from proceeding in the event that it were to interfere with the proceedings before it." *Id.* The holding was thus premised on the *absence* of claim against the insurer, and the fact that the state liquidation court would have authority to enjoin any such claim. *Id.* Here, by contrast, allowing jurisdiction over the Government's offset claims allows it to recover for affirmative claims against the insolvent insurer, without regard to priority order.

So too in *Amsouth Bank v. Dale*, 386 F.3d 763, 783 (6th Cir. 2004), where the Sixth Circuit found that declaratory actions against insolvent insurers with respect to the *insurers*' potential offensive claims "have only an attenuated connection to regulating the business of insurance." *Id.* The Court noted that its analysis might differ when "creditors attempt to sue insolvent insurance companies in federal court to jump ahead in the queue of claims." *Id.* at 780.

Finally, in *Gross v. Weingarten*, 217 F.3d 208 (4th Cir. 2000), the Fourth Circuit found that allowing diversity jurisdiction in federal court over counterclaims brought by an insolvent insurer's creditors did not impair Virginia's statutory scheme for consolidation of liquidation proceedings, because the creditors "s[ought] only to establish their *rights* to exoneration, contribution, or indemnification." *Id.* at 221 (emphasis added). In the event they prevailed on their claims in federal court, "they would still be required to present their judgments to the Virginia [Insurance] Commission . . . [which would] pay those judgments in accordance with the rehabilitation plan and Virginia's statutes governing the priority of claims." *Id.* at 221–22.

Here, unlike in *Suter*, *Dale*, or *Gross*, Sections 1503 and 2508 would allow the Government to obtain *both* a judgment *and* satisfaction of that judgment against an insolvent insurer outside the state liquidation process. They would therefore conflict with state insurance law to policyholders' detriment, and are therefore preempted by the McCarran Ferguson Act.

C. The source of the Government's substantive rights is irrelevant.

The Government argues that Sections 1503 and 2508 are not reverse preempted because the Government's setoff rights arise under federal common law, not an Act of Congress, Opp. at 15, and substantively derive from under the Affordable Care Act ("ACA"), which relates to the business of insurance, Opp. at 15–16. These arguments miss the point, as Colorado HealthOp and Meritus did not argue that the McCarran Ferguson Act preempted the Government's substantive rights. They argued that Sections 1503 and 2508—federal jurisdictional statutes that do not regulate insurance—were reverse preempted under the McCarran Ferguson Act by state statutes vesting jurisdiction over such claims in a state liquidation court. Mot. 7–11. The source of the Government's ability to offset, or its substantive right to assert these particular offsets, simply says nothing about which court should hear these claims.[6]

II. The Government's Claims for Interest Should be Dismissed.

As explained in Colorado HealthOp and Meritus's Motion, the Government's claims for interest fail for two reasons. *First*, the Government is not entitled to any interest when it is a net debtor, meaning there was no balance on which interest could accrue. Mot. at 12. *Second*, the government's statutory right to charge interest is reverse preempted under the McCarran Ferguson Act by state statutes freezing rights at the moment of insolvency. Mot. at 13–14.

In response, the Government argues that it was authorized to charge interest even though it owed Colorado HealthOp and Meritus more money than they owed it because it is not seeking "prejudgment interest," Opp. at 24, and that the Government's assessment of interest of 15% per annum for years following Colorado HealthOp and Meritus's insolvencies does not interfere with

[6] For the same reason, the Government's invocation of "law of the case" fails. Opp. 15. This Court's previous decision that the Government's *right to assert* offsets was not reverse preempted under the McCarran Ferguson Act does not bear on whether or not the specific statutes vesting this court with jurisdiction over those offsets are preempted. *Health Republic,* 150 Fed. Cl. at 242.

Arizona and Colorado's insurer liquidation laws freezing the assessment of interest at the point of insolvency. Opp. 25–27. Neither argument has merit.

A. As a net debtor, the Government is not entitled to interest.

The Government does not dispute that, excluding its claims for interest, it owes *more* to Meritus and Colorado HealthOp than it seeks. Mot.at 12; Opp. at 25. It also does not dispute that its debts to Meritus and Colorado HealthOp arise out of transactions related to those under which it claims it is owed. Mot. at 12; Opp. at 25. Nor does the Government dispute that under the longstanding "interest on the balance rule," this set of facts would eliminate its entitlement to "prejudgment interest," because there was never any net debt for interest to accrue upon. Mot. at 12; Opp. at 25. *See also Local Oklahoma Bank v. United States*, 59 Fed. Cl. 713, 722-23 (2004). Instead, the Government argues that it is entitled to charge interest *even as a net debtor* because its right to charge interest is supposedly not "prejudgment interest" because the interest rate is set by regulation rather than in the Court's discretion. Opp. at 25.

This argument makes no sense. As an initial matter, the Government is simply wrong to suggest that all "prejudgment interest is discretionary interest that 'may be assessed by the district court after damages have been found.'" Opp. at 25. While courts certainly *may* assess prejudgment interest even when no statute explicitly provides for it, the term refers generally to the interest a party may recover between the moment of injury and the time of judgment, "to compensate for the delay in payment of the damages." *Lam, Inc. v. Johns-Manville Corp.*, 718 F.2d 1056, 1066 (1983). And contrary to the Government's contention that prejudgment interest is purely discretionary and non-statutory, it frequently *is* paid pursuant to specific statutory requirements or formulas. *See id.* (affirming award of prejudgment interest in patent infringement case as required by 35 U.S.C. § 284); *id.* n.7 ("*Even where statutes do not explicitly*

permit the award of prejudgment interest, the district court has discretion to award prejudgment interest.") (emphasis added); *United States v. Fed. Ins. Co.*, 857 F.2d 1457, 1459–60 (Fed. Cir. 1988) (determining "prejudgment interest" according to a fixed statutory rate set out in 19 U.S.C. § 580).

It is therefore unclear what the Government means when it argues that the interest it claims is different from prejudgment interest because "the United States' entitlement to interest [under this regulation] does not depend on obtaining a judgment in its favor or even filing a complaint." Opp. at 25. So too in the cases the Government cites: in each case, the prejudgment interest accrued from the moment of injury, not from the moment the complaint was filed or judgment obtained, because the interest compensates the injured party "for the delay in payment of the damages." *Lam*, 718 F.2d at 1066. Of course, in some sense, the actual *award* of prejudgment interest turns on entry of judgment in the plaintiff's favor, but only in the narrow sense that no interest would be owed if the defendant were not actually liable to the plaintiff. *Id.* That principle applies equally here, as the Government does not claim it would be entitled to collect interest pursuant to 45 C.F.R. § 30.18(a) if a court found that the debts on which it claimed interest were not actually owed. This is the only sense in which "prejudgment interest" turns on the entry of judgment, so the Government's argument that its claim is different from prejudgment interest has no basis.

Indeed, the Government fails to cite any case distinguishing between "prejudgment interest" and interest pursuant to regulatory or statutory formula. As stated above, that distinction flies in the face of ample case law awarding "prejudgment interest" pursuant to statute or regulation. *Fed. Ins.. Co.*, 857 F.2d at 1459–60. In fact, in a case dealing with a predecessor version of the exact regulation at issue here, the Third Circuit made clear that it was appropriate

for DHHS to set forth in advance a regulatory formula specifying the amount of prejudgment interest it would otherwise claim in litigation as a matter of federal common law, belying any notion that interest under 45 C.F.R. § 30.18(a) is somehow categorically distinct from prejudgment interest generally. *Comm. of Pa. Dep't of Public Welfare vs. United States*, 101 F.3d 939, 943-44 (3d Cir. 1996).

Moreover, even if interest under 45 C.F.R. § 30.18(a) were not called "prejudgment interest," the "interest on the balance" rule does not turn on labels or whether the interest rate is set by regulation versus the court's discretion. Rather, it turns on the common-sense proposition that where two parties owe each other money across related transactions, the amount on which interest accrues is the *net balance* between parties. *Oklahoma Bank*, 59 Fed. Cl. at 722-23.

Notably, this rule is fully consistent with the text of 45 C.F.R. § 30.18(a), which provides only for the Government to assess interest in a particular amount "on delinquent debts owed the United States." The Government cites absolutely no authority suggesting (let alone requiring) that the *amount* of "delinquent debts owed to the United States" should be calculated without reference to any offset for what the United States owes the putative debtor, and any such interpretation flies in the face of this Court's case law. *Oklahoma Bank*, 59 Fed. Cl. at 722-23.

The Government asks to charge 15% yearly interest on sums purportedly owed it over a period when the Government itself was under "a legal duty . . . that [had] mature[d] into a legal liability through the insurers' actions" to pay Colorado HealthOp and Meritus substantially more than they owed the Government. *Me. Comm. Health Options v. United States*, 140 S.Ct. 1308, 1320 (2020). That defies common sense and this Court's precedent, and is not mandated by any reasonably construed statute or regulation. The debts owed *by* the Government were larger than the debts owed *to* the Government, which means the Government could not accrue any interest.

B. No interest could accrue after Meritus and Colorado HealthOp's insolvencies.

The Government is also not entitled to interest because the interest it seeks accrued *after* Meritus and Colorado HealthOp's insolvencies, in violation of both states' statutes fixing creditor rights and obligations upon issuance of a liquidation order. Mot. 13. The Government does not dispute that its entitlement to interest arises pursuant to a federal statute (31 U.S.C.§ 3717) that does not regulate the business of insurance, meaning that it is subject to reverse preemption under the McCarran Ferguson Act to the extent it conflicts with relevant state statutes. Opp. 25–27.

Instead, and bewilderingly, the Government first argues that Arizona's statute fixing "[t]he rights and liabilities of the insurer and of its creditors, policyholders, stockholders, members, subscribers and all other persons interested in its estate," Ariz. Rev. Stat. § 20-635, and Colorado's statute fixing "the rights and liabilities of any such insurer and of its creditors, policyholders, shareholders, members," Colo. Rev. Stat. § 10-3-517(2), do not "regulate the business of insurance." Opp. at 26. To the contrary, these statutes (both contained within larger chapters regulating the process of insurer liquidation in detail) plainly regulate the business of insurance by affecting the amount any insolvent insurer has to pay to policyholders, and therefore affecting "the relationship between the insurance company and its policyholders." *Fabe*, 508 U.S. at 501.

The Government next argues that even if these state statutes do regulate the business of insurance, its claiming interest in direct violation of those statutes would not "'invalidate, impair, or supersede' any state law" because "[t]he net proceeds of any judgment that Colorado HealthOp and Meritus receive will be distributed to policyholders and other creditors in the

liquidation proceedings according to their relative priority as determined by state law." Opp. 26.

This is simply sleight of hand. True, the state statutes regulating the ultimate sequence of distribution of "the *net proceeds* of any judgment" *after* the Government has taken its offset will not be superseded. But the state statutes that determine the *amount* of net proceeds will be directly superseded, as there could not be any clearer abrogation of state law than allowing the Government to continue to accrue interest after insolvency in direct violation of Ariz. Rev. Stat. § 20-635 and Colo. Rev. Stat. § 10-3-517(2). The Government's position would thus plainly supersede state statutes "designed to carry out the enforcement of insurance contracts by ensuring the payment of policyholders' claims despite the insurance company's intervening bankruptcy." *Fabe*, 508 U.S. at 504. The Government's position thus directly conflicts with state law protecting policyholders.[7]

Finally, the Government notes that in *Fabe* itself, the Supreme Court found that the federal super-priority statute was only reverse preempted to the extent it conflicted with Ohio's provisions according higher priority to policyholders or creditors whose claims arose during the liquidation process, rather than to any other creditors. Opp. at 26 (citing *Fabe*, 508 U.S. at 493-94). It is hard to see how any similar carve-out could work here, where the statutes fixing rights and obligations at the entry of a liquidation order serve to protect policyholders by fixing *all* parties' rights and obligations at a particular date and time. *See In Re Liquidation of Pine Top Ins. Co.,* 322 Ill. App. 3d 693, 701-02 (2001). In any event, here, the Government's assessment of interest, in direct violation of Arizona and Colorado statutes, would plainly harm

[7] The direct nature of this conflict renders irrelevant the Government's repeated protestation that the McCarran-Ferguson Act "does not create reverse field preemption." Opp. at 26. But because the Government touts this language several times, Opp. 14, 17, 26, it is worth noting the Supreme Court's full reasoning on this point: "While we reject any sort of field preemption, ***we also reject the polar opposite of that view, i.e., that Congress intended a green light for federal regulation whenever the federal law does not collide head on with state regulation***." *Humana*, 525 U.S. at 309 (emphasis added).

policyholders, as it seeks to enlarge its purported offset against its own liability to policyholders through its assessment of interest.

The Government seeks to assess interest pursuant to a federal statute that is not specific to insurance, in direct violation of Arizona and Colorado insurer liquidation statutes fixing obligations at the time of insolvency, to the direct detriment of policyholders. Under the McCarran Ferguson Act, that is impermissible.

III. State law prohibits the Government's offset against Colorado HealthOp.

The Government's offset claim against Colorado HealthOp also fails because it violates Colorado's offset statute. Mot. 14–21. As Judge Hertling explained in *Conway v. United States*, about the exact offset claim that the Government presses here, Colorado law provides the relevant rule of decision and precludes the Government's offset claim. 145 Fed. Cl. 514, 526–530 (2019).

A. Colorado Law Provides the Relevant Rule of Decision.

As Judge Hertling explained in *Conway*, while the Government's possession of the "same offset rights as other creditors" arises under federal common law, determining how that right applies to debts owed the Government under the ACA in the context of Colorado insurer liquidation requires looking to Colorado law. *Id.* This follows from the Supreme Court's guidance that just because federal common law applies does not "mean that federal courts should *create* the controlling law." *Am. Elec. Power Co., Inc. v. Conn.*, 564 U.S. 410, 422 (2011) (emphasis added). This is especially true where the Government's debts arise under the ACA, which contains an explicit non-preemption provision and where state-by-state operation is baked into its structure, belying any federal interest in national uniformity. 42 U.S.C. 18041(d) ("Nothing in this title shall be construed to preempt any State law that does not prevent the

application of the provisions of this title"); *Conway*, 145 Fed. Cl. at 529 ("The ACA's state-by-state structure, the ACA's own non-preemption provision, and the role Congress assigned to HHS in administering the reinsurance and risk-adjustment programs on behalf of states undermine HHS's argument that federal interests require a uniform rule."). Also, applying a federal rule "would disrupt commercial relationships predicated on state law," to the detriment of policyholders who relied on Colorado's provisions granting them highest priority and specifying the extent of any offset rights. *United States v. Kimbell Foods, Inc.*, 440 U.S. 715, 740 (1979)); Mot. 17–18.

The Government ignores Judge Hertling's explanation as to why Colorado law should provide the rule of decision, without addressing the factors that typically inform this analysis. *Compare Conway*, 145 Fed. Cl. at 524–530, *with* Opp. at 28–29. Instead, it simply asserts that "[t]his case is nothing like *Kimbell Foods* because existing federal common law provides for the United States' offsets." Opp. at 29 (citing *United States v. Munsey Trust Co.*, 332 U.S. 234, 240 (1947)). But as Judge Hertling explained, there is no preexisting clear federal rule "answer[ing] the question of whether an agency-creditor has a right to use offset when the rights of the parties are not primarily defined by federal common law, like in state-law insurance liquidation proceedings." 145 Fed. Cl. at 524. The Government cites no case providing such a rule.

Indeed, *Munsey*—the one case cited to explain why some federal rule, rather than Colorado law, should apply, Opp. at 28–29—makes clear why application of Colorado law is appropriate. *Munsey* merely reiterated that "[t]he government has *the same right 'which belongs to every creditor*, to apply the unappropriated moneys of his debtor, in his hands, in extinguishment of the debts due to him.'" 332 U.S. at 239 (quoting *Gratiot v. United States*, 40 U.S. 336, 370 (1841) (emphasis added)). *Munsey* does not answer how the Government's ability

to assert "the same right" as other creditors applies in situations like this, where a state statute defines and circumscribes the assertion of that right by all creditors generally. *See* Section II.B, *infra*.[8] In such instances, for reasons explained in *Conway* and in the Dispute Sub-Class's Motion, selection of a state's ready-made rule is preferable. Mot. at 15–18.

B. Colorado Law Prohibits the Government from Offsetting Colorado HealthOp's Debts Against Its Risk Corridor Judgment.

In Colorado insurer liquidation, the right to assert offsets is defined by Colo. Rev. Stat. § 10-3-529(1), a point on which the Government agrees. Opp. at 32; Mot. at 19–21. It provides:

> Notwithstanding any other provision of this title, mutual debts or mutual credits, whether arising out of one or more contracts between the insurer and another person in connection with any action or proceeding under this part 5, shall be set off, and the balance only shall be allowed or paid. . . .

Colo. Rev. Stat. § 10-3-529(1). As Judge Hertling determined, this statute limits the setoff right to debts "arising out of one or more contracts between the insurer and another person." *See Conway*, 145 Fed. Cl. at 525–26. And because the Government's debts do not "aris[e] out of one or more contracts," the Government cannot rely on Colo. Rev. Stat. § 10-3-529(1); Mot. 19–21.

The Government instead argues that "the statute expressly authorizes offset '*whether*' the debts arise under contract." Opp. at 32; Colo. Rev. Stat. § 10-3-529(1) (emphasis added). That would be very well if the statute provided for offsets of debts "whether arising out of contracts or other sources," but it actually provides for offsets of debts "whether arising out of *one or more* contracts between the insurer and another person." Colo. Rev. Stat. § 10-3-529(6) (emphasis

[8] Indeed, as explained in the Dispute Subclass's opening Motion at 22 n.13, the common law right of offset discussed in *Munsey* and recognized by the Supreme Court in 1841 in *Gratiot* would have been conceived of as an element of "the general common law," which was subject to displacement by state statutes. *See Swift v. Tyson*, 41 U.S. 1, 18 (1842), *overruled by Erie Ry. Co. v. Tompkins*, 304 U.S. 64 (1938). The fact that *Erie*—which was meant to enable more respect for state law—transformed the Government's offset rights into *federal*, rather than general, common law hardly eliminates the relevance of state statutes, particularly where the gravamen of that right is to afford the Government *the same rights* as other creditors.

added). Therefore, the term "whether" serves to allow offsets without reference to the *number* of contracts giving rise to the offset, not to allow offsets arising out of non-contractual sources. *Id.*[9] As Judge Hertling explained in *Conway*, this straightforward reading is buttressed by the statutory context, as the statute's effective date provision specifically provides that the offset statute "shall apply to all *contracts* entered into, renewed, extended, or amended" as of the relevant date. Colo. Rev. Stat. § 10-3-529(6); *Conway*, 145 Fed. Cl. at 525. As such, Colorado allows contractual creditors in insurer liquidation proceedings to apply offsets "arising out of one or more contracts," but it does not allow the sort of non-contractual offsets that the Government asserts here.

It is not clear whether the Government believes it would be entitled to offset under Colorado law even if its reading of the offset statute is deemed incorrect. Opp. at 31–32. To the extent it does so argue, that is plainly wrong. Before the offset statute in question was passed, the Colorado Supreme Court held in *Bluewater Ins. Ltd. v. Tennessee Ins. Co. v. Balzano* that any "equitable right to offset[] would favor the[offsetting parties'] private interest over the interest of policyholders, contrary to law," and had therefore been abrogated by Colorado's insurance liquidation act. 823 P.2d 1365, 1374 (Colo. 1992). The Government argues that *Bluewater* did not actually address this question because it had been "mooted" by an effective waiver of the parties seeking offset. Opp. at 31. But the Colorado Supreme Court made clear in *Bluewater* that, even if there had not been any waiver, it would still have reached the same conclusion, stating "[w]e nevertheless briefly address this issue," and going on to call the asserted equitable offset "contrary to law." *Bluewater*, 823 P.3d at 1374. Colorado law is therefore crystal clear on this

[9] To add another example to that in the Dispute Subclass's Opening Brief, Mot. 19 n.12—which the Government does not address—if a doctor were to say "the patient's recovery, whether arising out of one or more experimental treatments," no listener would think the doctor to have attributed the patient's recovery to a recently taken aspirin.

question, and does not permit the Government's asserted offset. Because Colorado law should provide the rule of decision, that dooms the Government's claim against Colorado Health.

IV. Meritus Paid the Debts Identified in the Counterclaim in Full in 2017.

As explained in the Dispute Subclass's opening motion, in 2017, Meritus, at the Government's request, effected an offset of the same debt that the Government now seeks to collect as against the Government's outstanding Risk Corridors liability to Meritus. Mot. 23–25. Meritus attached all the relevant documents to its motion, including the Government's assertion of the same claim it makes now, letters from Meritus's receiver in liquidation asserting Meritus's intention to setoff its debts to the Government against the Government's (larger) debts to Meritus, and documents showing Mertius's recording of the debts and the Liquidation Court's ratification of the same. *See* Mot. 24 (citing exhibits). These offsets directly reduced the amount of Meritus's claims against the Government; without them, Meritus would have sought and been entitled to recover substantially more in this very litigation. Procedurally, they satisfied *all* requirements for a valid offset. *See, e.g.*, *Johnson v. All-State Const., Inc.*, 329 F.3d 848, 854 (Fed. Cir. 2003) (a valid offset requires "a decision to effectuate a setoff, (ii) some action accomplishing the setoff, and (iii) a recording of the setoff"). Despite the 2017 offset, the Government now seeks double payment on the same already satisfied debt. The Government does not dispute any of this.

Instead, the Government argues that Meritus's offset was invalid because in 2017, the Receiver "[a]t best . . . possessed a claim that could not be paid absent new appropriations from Congress or a court allowing access to the appropriated Judgment Fund," Opp. at 33, which meant that "Meritus, holding no funds in 2017, could not have paid its debts using a judgment it does not even now possess." Opp. at 34. This argument fails in two critical ways.

First, the whole reason why any party ever applies an offset is ***because*** they have not yet been paid, so the Government's observation that Meritus had not been paid in 2017 is the reason Meritus was willing to apply an offset: *i.e.*, in lieu of payment. The Government's apparent argument that Meritus required "a judgment it does not even now possess" in order to effectuate a valid offset is just wrong, and is flatly foreclosed by this Court's repeated determinations that parties ***do not*** need to await the resolution of litigation in order to apply an offset. *See, e.g.*, *Oklahoma Bank*, 59 Fed. Cl. at 722 ("[A] claim need not be reduced to a judgment before set-off is available. ***Rather, set-off can be applied pending resolution of the issue***." (emphasis added)); *Mega Constr. Co. v. United States*, 29 Fed. Cl. 396, 445 (1993); ("For defendant to exercise its common law right of offset, the claim need not be reduced to judgment; the offset may be effected pending resolution of the controversy."); *Mazama Timber Prods., Inc. v. United States*, 6 Cl. Ct. 87, 89 (1984) (collecting cases for the proposition that "[t]o exercise the right of setoff, pending resolution of the controversy, the claim need not be reduced to judgment.").

Second, and relatedly, the Supreme Court's opinion in *Maine Community Health* makes it very clear that the Government was under an obligation in 2017 to pay Meritus, even though it refused to do so. 140 S.Ct. at 1320 (2020) ("Section 1342 imposed a legal duty of the United States that could mature into a legal liability through the insurers' actions—namely, their participating in the healthcare exchanges.") For the Government to be right that Meritus could not apply an offset in 2017, the Government would need to show that it did not actually owe Meritus money at that time—but *Maine Community Health* makes it abundantly clear that the Government *did* owe Meritus money in 2017, just as it owes it now. *Id.* Because the Government was already paid the money it seeks in 2017 via a valid offset, it is not entitled to double payment—just as it is not entitled to interest on an already paid debt. As such, the Government's

claims against Meritus should be dismissed in full.

V. The Government's Futility Argument is Wrong.

The Government finally argues that, even if this Court decides it lacks jurisdiction over the Government's offset claims, dismissal would be futile because "the United States would still apply Colorado HealthOp and Meritus' risk corridors judgment toward their outstanding ACA debt." Opp. at 34. The Government cites 31 U.S.C. § 3728(a), which directs the Secretary of the Treasury to "withhold paying that part of a judgment against the United States Government presented to the Secretary that is equal to a debt the plaintiff owes the Government." *Id.*

Of course, if this Court lacks jurisdiction over the Government's counterclaims because Colorado and Arizona's jurisdictional statutes reverse preempt Sections 1503 and 2508 under the McCarran Ferguson Act, then 31 U.S.C. § 3728(a) would also be preempted for the same reasons. *See* Section I, *supra*. Moreover, one might hope that, should the Government lose on its jurisdictional argument, it might reconsider the substantive merit of its claims for all the reasons outlined above. *See* Sections II, III, IV, *supra*. For these reasons, should this Court decide it lacks jurisdiction over the Government's counterclaims, the Government would have no basis to once again delay payment of its debts, this time pursuant to 31 U.S.C. § 3728(a), and Colorado HealthOp and Meritus would of course challenge any such decision. Either way, this certainly does not change this Court's jurisdictional analysis.

Conclusion

For the foregoing reasons, and those discussed in Meritus and Colorado HealthOp's Motion, the Court should dismiss the Government's counterclaim.

DATED: February 26, 2021

Respectfully submitted,

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