CLIENT ALERT

Oklahoma Joins Vermont, Rhode Island and Connecticut in Adopting Insurance Business Transfer Law

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In recent years, several U.S. states have enacted legislation meant to approximate the effect of Part VII of the UK Financial Services and Markets Act 2000, which allows an insurer to transfer its business, or a book of business, to another entity through a court approval process without the need for individual policyholder consents. While each state's legislation provides a mechanism for insurance business transfers ("IBTs") without affirmative policyholder consent, there are distinct differences in the transfer process under each law, including in the types of business that may be transferred, whether the transfer must be approved by a court or by the insurance regulator of the state, and whether policyholders may object to or "opt out" of the transfer.

We summarize in this article the provisions of the IBT laws in Vermont, Rhode Island, Connecticut, and Oklahoma, and highlight the differences and commercial implications of each law.

Vermont

Law[1]

In 2014, Vermont adopted the Legacy Insurance Management Act ("LIMA"), which enables a non-admitted insurer from any jurisdiction (the "Transferring Company") to transfer closed blocks of commercial non-admitted insurance policies or

[1] Chapter 147: Legacy Insurance Transfers (Vermont Insurance Code T. 8 § 7111, *et. seq.*).

reinsurance agreements to a Vermont-domiciled company established specifically to acquire a closed block under a legacy insurance transfer plan (the "Assuming Company"). LIMA defines a "non-admitted insurer" as an insurer not licensed to engage in the business of insurance in a state, not including a risk retention group or a captive insurance company,[2] and defines "closed block" as business for which a transferring non-admitted insurer has ceased to offer, write, or sell to new applicants, and for which all policy periods have been fully expired for at least 60 months.[3] Importantly, LIMA allows for affected policyholders and reinsurance counterparties to opt out of the transfer.

Application Process

The Assuming Company must file a transfer plan with the Vermont Commissioner of Financial Regulation (the "VT Commissioner") that includes, among other things: a list of all policies, reinsurance agreements, and policyholders; a certificate of good standing from the Transferring Company's domiciliary regulator, or if such certificate is not obtainable under the laws of the domiciliary regulator, a certificate of the Transferring Company or the controlling party attesting to the good standing of the Transferring Company and its controlling party verified by two executive officers; audited financial statements; an actuarial study of the liabilities that will be transferred to the Assuming Company; a statement from the Assuming Company submitting to the jurisdiction of the VT Commissioner; and a no objection letter from the Transferring Company's domiciliary regulator, or if any such letter is not obtainable under the laws of the domiciliary jurisdiction, a certificate verified by two executive officers of the Transferring Company attesting that the domiciliary regulator has no objection to the transfer.[4]

After the VT Commissioner accepts the transfer plan, the Assuming Company must provide notice to all policyholders and reinsurance counterparties listed in the transfer plan. Such notice must set out, among other things, the right of each policyholder or counterparty to accept or object to the plan and/or to appear at a hearing or file written comments on the plan with the Commissioner. If a policyholder or reinsurance counterparty objects to the plan, the Assuming Company must revise the plan to exclude such policyholder or counterparty and its respective policy/contract from the plan. A policyholder that does not expressly object to the plan in writing within a 60-day comment period is deemed to have accepted the plan. Following the comment period and hearing, if the Commissioner approves the transfer plan the Commissioner will issue an order having "the full force and effect of a statutory novation" and shall provide that the Transferring Company shall have no further rights, obligations or liabilities with respect to the transferred policies.[5]

[2] VT. Ins. Code T. 8 § 7111(13).

[3] VT. Ins. Code T. 8 § 7111(2).

[4] VT Ins. Code T. 8 § 7112.

[5] VT Ins. Code T. 8 § 7113.

Commercial Implications

LIMA is limited in its application to commercial non-admitted policies and reinsurance agreements, and only provides for a novation through an approval order from the VT Commissioner, not a court-ordered novation. In addition, policyholders can opt out of the transfer.

Despite these built-in limitations, there is a question as to whether the VT Commissioner has the authority to bind holders of policies (*i.e.*, contracts) issued by the Transferring Company, particularly with respect to out-of-state policyholders (LIMA requires a non-objection letter from the Transferring Company's domiciliary regulator, but it does not require approval from the regulators of each state where a transferred policy has been issued). Even though LIMA allows policyholders to object to a transfer plan and states that policyholders who fail to object have accepted the plan, it is unclear whether a court would uphold such "deemed consent" if a policyholder were to challenge a novation effected under LIMA.

We understand that, to date, no insurers have utilized LIMA to effect an IBT transaction, so these questions have not been tested.

Rhode Island

Law[6]

In 2002, Rhode Island enacted the Voluntary Restructuring of Solvent Insurers Act (the "RI Commutation Act"), which prescribed a process for a Rhode Island-domiciled "Commercial Run-Off Insurer" (*i.e.*, an insurer whose business includes only the reinsuring of non-life business and/or the insuring of any line of business other than life, workers' compensation and personal lines) to extinguish its outstanding liabilities pursuant to a court-ordered commutation plan, with the approval of 50% of policyholder creditors representing at least 75% of claim value.[7]

In 2016, further to the RI Commutation Act, the Rhode Island Department of Business Regulation (the "Department") introduced Insurance Regulation 68, which provides a new IBT mechanism that allows for the transfer of blocks of U.S. property casualty business from any insurer (the "Transferring Company") into a Rhode Island-domiciled Commercial Run-Off Insurer as defined under the RI Commutation Act (the "Assuming Company"). Unlike the RI Commutation Act, which provides for a whole-company commutation, Regulation 68 enables a Transferring Company to novate books of business to an Assuming Company.

6 "Regulation 68" – Rhode Island Insurance Regulation R27-68-001.

7 R.I. Gen. Laws § 27-14.5.

Application Process

The Assuming Company must submit an Insurance Business Transfer Plan ("IBT Plan") to the Insurance Division of the Department, which should include, among other items: a summary of the IBT Plan; most recently audited financial statements and annual reports of the Transferring Company; evidence of approval of the Transferring Company's domiciliary regulator; and an expert report providing an opinion on the proposed transaction and stating the expert's professional qualifications to assess such a transaction. Once the Department has approved the IBT Plan, the Department will grant permission to the Assuming Company to make an application to the Superior Court of Providence County (the "Court") for approval of the IBT Plan. Regulation 68 does not include a policyholder opt-out provision.

If the IBT Plan is approved, the Court's order will: make a finding that there is no material adverse impact to policyholders, reinsureds, or claimants on the transferred policies; implement a statutory novation with respect to all policyholders and reinsureds and their respective policies and reinsurance agreements under the IBT Plan; and release the Transferring Company from any and all rights, obligations, or liabilities under the transferred policies or reinsurance agreements.

Commercial Implications

The Rhode Island IBT process effects a court-ordered novation of all transferring policies and reinsurance agreements, which arguably offers greater finality than a novation order from an insurance regulator, which could be challenged in court. However, given that Regulation 68 purports to give a Rhode Island court the authority to bind out-of-state policyholders of an out-of-state Transferring Company (with no policyholder opt-out provision), the same jurisdictional questions arise as noted with respect to Vermont.

The Rhode Island Department's goal in revising the RI Commutation Act by promulgating Regulation 68 was to make the state a center of expertise for runoff insurance. To date, we understand that two companies have been formed in Rhode Island to act as Assuming Companies for an IBT. However, as of mid-June 2018, neither company has yet filed an IBT Plan with the Department.

One reason for the relative lack of utilization under Regulation 68 may be that the RI Commutation Act, which defines Assuming Company for purposes of Regulation 68, applied to Rhode Island domestic insurance companies "formed or re-activated for the sole purpose of entering into a voluntary restructuring under [the RI Commutation Act]."[8] Companies interpreted this "sole purpose" language as a requirement that the Assuming Company must ultimately submit a commutation plan to the Department under the RI Commutation Act to extinguish its outstanding commercial liabilities, although this interpretation was not the intent of the Department. As a result, the Rhode Island General Assembly has amended the RI Commutation Act to remove the "sole purpose" language in order to make clear that an IBT under

[8] R.I. Gen. Laws § 27-14.5-1 (emphasis added).

Regulation 68 need not be followed by a commutation of the transferred policies by the Assuming Company.[9] The bill was signed by the Rhode Island Governor on July 2, 2018.

Connecticut

Law[10]

On October 1, 2017, a law took effect that allows Connecticut domestic insurance companies to divide into two or more insurance companies and create isolated blocks of business for a sale to a third party. Companies can also use this process to separate active books of business from runoff blocks. The Connecticut Insurance Department has explained that the bill is essentially the reverse of a merger for a domestic insurer, and that it was modeled on similar legislation in Pennsylvania. The Pennsylvania statute, which is generally applicable to domestic corporations and not insurer-specific, permits Pennsylvania domestic entities to divide following approval of interestholders.[11]

Application Process

Any Connecticut domestic insurer can submit a plan of division to the Connecticut Insurance Commissioner ("CT Commissioner") to divide into two or more insurers. The plan of division must include, among other things: the manner of allocation between the resulting insurers; a description of the policies and other liabilities of the domestic insurer for which the resulting insurers will not be jointly and severally liable; and an outline of the manner of distributing interests in the new insurers to the dividing insurer. If the CT Commissioner finds that the interests of the policyholders and interestholders are protected, the CT Commissioner will issue a certificate of division to the dividing insurer, which is effective once filed with the Connecticut Secretary of State.[12] The CT Commissioner may hold a public hearing on the division if a hearing is deemed by the CT Commissioner to be in the public interest.

Following a division, each resulting insurer is generally responsible (i) individually for the policies and liabilities that the resulting insurer issues or incurs after the division; (ii) individually for the policies and liabilities of the dividing insurer that are allocated to or remain the liability of the resulting insurer, as specified in the dividing insurer's plan of division; and (iii) jointly and severally with the other resulting insurer(s) for the policies and liabilities of the dividing insurer that are not allocated to a particular resulting insurer by the plan of division.

[9] R.I. House Bill 8163.

[10] Uncodified House Bill 7025.

[11] 15 PA Cons Stat § 363 (2014).

[12] Uncodified House Bill 7025 Section 4.

Commercial Implications

Unlike the Vermont and Rhode Island laws, which allow transfers from non-domiciliary insurers to domiciliary insurers, the Connecticut law only allows Connecticut domestic insurers to divide into two or more domestic insurers. Since the law is limited to Connecticut domestic insurers, there may be a stronger argument that the CT Commissioner has the authority to bind out-of-state policyholders, since the CT Commissioner has authority to regulate the dividing insurer.

Another key difference is that the Connecticut law is not limited to certain classes of business (Rhode Island) or to closed blocks (Vermont). Rather, any Connecticut domestic insurer may take advantage of the law's provisions with respect to any line of business. Finally, like Vermont and unlike Rhode Island, the Connecticut law does not provide a court-sanctioned approval process.

Oklahoma

Law[13]

Oklahoma's Insurance Business Transfer Act (the "Transfer Act"), signed into law on May 7, 2018 with a November 1, 2018 effective date, is currently the most direct reflection of the UK's Part VII transfer regime. The Transfer Act allows any U.S. or alien insurer (the "Transferring Company"), without the affirmative consent of policyholders, to transfer and novate a book of business to an Oklahoma-domiciled insurer (including a captive insurer) (the "Assuming Company"). The Transfer Act applies to both insurers and reinsurers, and property, casualty, life, health, and any other line of insurance that the Oklahoma Insurance Commissioner ("OK Commissioner") finds suitable are all included in the definition of "policies" eligible for transfer. Further, the Transfer Act seems to apply to both active and run-off books of business.

Application Process

The Transfer Act requires that the Transferring Company file an Insurance Business Transfer Plan ("IBT Plan") with the OK Commissioner. The application must include, among other items: the most recent audited financial statements and annual and quarterly reports of both the Transferring and Assuming Companies filed with their domiciliary regulators; evidence of approval of the Transferring Company's domiciliary regulator; and an opinion report from a qualified independent expert selected by the OK Commissioner.

The OK Commissioner shall authorize the submission of the IBT Plan to the District Court of Oklahoma County unless he or she finds that the IBT Plan would have a material adverse impact on policyholders or claimants. The Transferring Company then submits the IBT Plan to the Court, which will hold a hearing on the plan. Policyholders may comment on or object to the IBT Plan but do not have the right to opt out of or otherwise reject the transfer and novation. Under the

[13] Oklahoma Senate Bill 1101, to be codified in the Oklahoma Statutes as Section 1681 of Title 36.

Transfer Act, once a novation of the transferred contracts is effected, the Assuming Company becomes directly liable to the policyholders of the Transferring Company and the Transferring Company's insurance obligations and risks under the contracts are extinguished.

Commercial Implications

Like Rhode Island's Regulation 68, the Transfer Act effects a court-ordered novation, which may provide greater finality to the novation process than a regulator-only approval. Importantly, the Transfer Act applies broadly to active and run-off books of business and potentially to any line of business. Oklahoma's Deputy Commissioner has indicated that companies interested in doing run-off transactions in Oklahoma have already contacted him in anticipation of the November 1 effective date of the Transfer Act. However, as noted with respect to Vermont and Rhode Island, a novation under the Transfer Act may be susceptible to a jurisdictional challenge by affected policyholders, particularly since the Act purports to apply to non-U.S. insurers.

The Oklahoma Insurance Department is drafting regulations to implement the Transfer Act and expects to have such regulations in place by November 1, when the Transfer Act becomes effective.

Other States

Illinois currently has a division bill pending that is similar to the Connecticut law discussed above. Illinois House Bill 5160 creates the Domestic Stock Company Division article in the Illinois Insurance Code, and provides that domestic stock companies may divide into two or more insurers. As of July 8, the bill is still in committee.

Georgia Governor Nathan Deal recently vetoed a bill that would have allowed Georgia-domiciled insurers to divide into two or more insurers. Governor Deal stated that he was "unaware of the need for the division process" and that the proposed bill gave the Insurance Commissioner broad discretion without appropriate safeguards should one of the resulting insurers fail to turn a profit. Similarly, Iowa Governor Kim Reynolds vetoed a bill that would allow domestic stock insurers to divide into two or more resulting stock insurers. Governor Reynolds stated that she was supportive of the substance of the bill but could not sign it due to certain health insurance-related provisions that would further destabilize Iowa's health insurance market.

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If you have any questions regarding this client alert, please contact the following attorneys or the attorney with whom you regularly work.

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