WILLKIE FARR & GALLAGHER LLP

CLIENT ALERT

Colorado Adopts Insurance Company Division Law

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In recent years, several U.S. states have enacted insurance business transfer legislation or promulgated regulations allowing an insurer to transfer its business, or a book of business, to another entity without the need for individual policyholder consent. Separately, a few other U.S. states have taken a step in the direction of corporate reorganization by allowing an insurer to divide into separate companies. We have previously reported on such legislation and regulations in Connecticut, Oklahoma, Rhode Island, Vermont, Illinois, Michigan and Iowa.

On May 17, 2021, Governor Jared Polis of Colorado signed House Bill 21-1013, An Act Concerning the Division of Domestic Stock Insurers into Multiple Resulting Domestic Stock Insurers (the "Colorado Division Law"), which we summarize in this alert.

Law

The Colorado Division Law, which we expect to become effective on September 10, 2021 per Colorado legislative procedure, allows a Colorado domestic stock insurer (a "Dividing Company") to divide into two or more insurance companies (the "Resulting Companies") and allocate its assets and liabilities, including policy liabilities, among the Resulting Companies pursuant to a plan of division approved by the Commissioner of the Colorado Division of Insurance (the "Commissioner"). The Colorado Division Law is similar to insurer division statutes passed in Connecticut in 2017, Illinois and Michigan in 2018, and Iowa and Georgia in 2019.

Application Process

The Dividing Company must submit a plan of division to the Commissioner to divide into two or more insurers. The plan of division must identify each Resulting Company to be created by the division and describe, among other things, the manner of allocating assets, liabilities and reinsurance contracts among the Resulting Companies. The plan of division will also specify whether or not the Dividing Company will survive the division.

Similar to the division law of Iowa, the Colorado Division Law requires the Commissioner to select and retain an independent expert to review the plan of division and issue a report to the Commissioner. Unlike the division law of Iowa, the Colorado Division Law explicitly requires the independent expert report to address the following: (a) the business purpose of the division, (b) capital adequacy and risk-based capital, including consideration of the effects of asset quality, nonadmitted assets, and actuarial stresses to reserve assumptions, (c) cash flow and reserve adequacy testing, including consideration of the effects of diversification on policy liabilities, (d) business plans, (e) the impact, if any, of concentration of lines of business following the proposed division, and (f) management's competence, experience, and integrity. The division laws of Connecticut, Illinois, Michigan and Georgia do not include an explicit requirement for an independent expert review, although they contemplate that the regulator may hire experts and specify that such costs would be borne by the Dividing Company.

Unlike other state division laws, the Colorado Division Law explicitly requires the Commissioner to consider any simultaneous merger or acquisition of a Resulting Company as part of the plan of division and the nature and composition of the assets included in the division. In considering the assets, the Commissioner must consider the risks and quality, including liquidity and marketability, of the proposed portfolio of each Resulting Company, asset and liability matching, and the treatment of the material elements of the portfolio based on statutory accounting practices.

After considering the items described above, under the Colorado Division Law, the Commissioner shall approve the plan of division if the Commissioner finds that a number of requirements similar to the approval standards in other state division laws are met (e.g., the financial condition of the Resulting Companies or any acquirer will not jeopardize the financial stability of the Dividing Company or unfairly prejudice the interests of its policyholders, the interests of policyholders will be adequately protected, and the Resulting Companies will be solvent upon consummation of the division). However, the Colorado Division Law also has separate approval standards applicable to specific lines of business. Similar to the division law in Illinois, if a Resulting Company will be a member insurer under the "Life and Health Insurance Protection Association Act," the Colorado Division Law requires the Commissioner to approve a plan of division if the Resulting Company will be licensed in each line of business in each state in which the Dividing Insurer was licensed, subject to certain limited exceptions. Additionally, if the plan of division allocates policies of long-term care insurance, the Commissioner shall approve the plan of division only if the liabilities of those policies do not constitute more than a *de minimis* amount of the insurance liabilities allocated to any Resulting Company.

Unlike the division laws in Illinois and Connecticut, under which a public hearing is discretionary, the Colorado Division Law, like the division laws of Iowa, Georgia and Michigan, requires the Commissioner to hold a public hearing prior to approving a plan of division. Unlike other state division laws, the Colorado Division Law explicitly requires the Commissioner to provide notice of the hearing to state insurance regulators and appropriate state guaranty associations in states in which the Dividing Company is authorized to do business. Additionally, the Dividing Company must provide 30 days' notice of the public hearing, by either mailing the notice or sending it via electronic means, to all policyholders, contract holders and reinsurers and to other persons with an interest in the proposed division if the Commissioner determines that it would be unreasonable or unfair for the Dividing Company not to provide notice to such other persons.

Effects of Division

After approval by the Commissioner, the plan of division becomes effective after the Dividing Company executes and files a certificate of division with the Commissioner. The Commissioner will also issue a certificate of authority authorizing the Resulting Company to transact insurance business in Colorado, unless the Resulting Company will be the nonsurvivor in a merger occurring simultaneously with the division.

Following a division, each Resulting Company is responsible individually for (i) the policies and liabilities that the Resulting Company issues or incurs after the division; and (ii) the policies and liabilities of the Dividing Company that are allocated to the Resulting Company by the plan of division.

If the Dividing Company survives the division, it remains responsible for the policies and liabilities that are not allocated by the plan of division. If the Dividing Company does not survive the division, each Resulting Company is liable pro rata individually for the liabilities that are not allocated by the plan of division.

Related Transactions

The Colorado Division Law contemplates that a plan of division may be undertaken as part of a larger transaction. As noted above, the Commissioner will consider whether a Resulting Company will be merged or acquired in conjunction with a plan of division. Although the Colorado Division Law does not separately amend the Colorado merger law like other state division laws, the Colorado Division Law includes a provision that permits a Dividing Company to adopt and execute a plan of merger on behalf of a Resulting Company to facilitate the merger and enables the Commissioner to approve the merger as part of its approval of a plan of division. If provided in the plan of division, the merger shall be effective simultaneously with the effectiveness of a division.

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

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