Portfolio Media. Inc. | 111 West 19th Street, 5th Floor | New York, NY 10011 | www.law360.com
Phone: +1 646 783 7100 | Fax: +1 646 783 7161 | customerservice@law360.com

Oklahoma's Insurance Business Transfer Act: Objections Overruled?

By **Laura Foggan, John Sarchio, Richard Liskov and Jarad Schaeffner**
(October 19, 2018, 3:24 PM EDT)

Laura Foggan

John Sarchio

Richard Liskov

Jarad Schaeffner

Oklahoma's recently enacted Insurance Business Transfer Act takes effect on Nov. 1, 2018.[1] The Oklahoma act allows any insurer to transfer and novate books of business to an Oklahoma-domiciled insurer without the affirmative consent of policyholders, referred to as an insurance business transfer, pursuant to approval of both the Oklahoma insurance commissioner and the District Court of Oklahoma County. Oklahoma is the latest state to pass a run-off law in response to increasing demand for these types of transactions.

Oklahoma Insurance Business Transfer Act

The Oklahoma act allows for the transfer and novation of property, casualty, life and health policies, as well as any other line of insurance that the commissioner finds suitable. To affect an insurance business transfer, the transferring insurer first files an insurance business transfer plan, or IBT plan, with the commissioner. The IBT plan must include, inter alia:

- The most recent audited financial statements and statutory annual and quarterly reports of both the transferring insurer and the assuming insurer.
- A proposal for implementation and administration of the IBT plan, including the form of notice to be provided to any policyholders affected by the IBT plan and a full description of how such notice will be provided.
- Evidence of approval or nonobjection of the transfer from the chief insurance regulator of the state of the transferring insurer's domicile.
- An opinion report from an independent expert, which must include, inter alia:
    - The independent expert's opinion of the likely effects of the IBT plan on policyholders and claimants, distinguishing between:
        - Transferring policyholders and claimants.

- Policyholders and claimants of the transferring insurer whose policies will not be transferred.

- Policyholders and claimants of the assuming insurer.

- Consideration as to whether the security position of policyholders affected by the insurance business transfer would be materially adversely affected.

The commissioner has 60 business days to review an IBT plan (this period may be extended by an additional 30 business days). The IBT plan must be approved unless the commissioner finds that the IBT plan would have a material adverse impact on the interests of policyholders or claimants. After the commissioner approves the IBT plan, the transferring insurer may petition the district court for approval. Within 15 days after a hearing is scheduled, the transferring insurer must provide notice to certain parties (policyholders receive notice by first-class U.S. mail). The notice to policyholders must provide, inter alia:

- That a policyholder may comment on or object to the transfer and novation.

- A summary of any effect that the transfer and novation will have on the policyholder's rights.

- *That policyholders shall not have the opportunity to opt out of or otherwise reject the transfer and novation.* (emphasis added)

After notice is given, any policyholder or other party that believes it will be adversely affected can present evidence or comments to the district court at the approval hearing, which follows a 60-day comment period. If the district court finds that the IBT plan would not materially adversely affect the interests of policyholders or claimants, then the district court will enter an implementation order. Following district court approval, the assuming insurer becomes directly liable to the policyholders of the transferring insurer, and the transferring insurer's obligations and risks under the transferred policies are extinguished.

Rhode Island Insurance Regulation 68

Like the Oklahoma act, Rhode Island's Insurance Regulation 68 allows any insurer to transfer and novate certain books of business to another insurer pursuant to regulatory and court approval.[2] The process for effecting a transfer and novation under Regulation 68 is similar to the process under the Oklahoma act:

- An insurance business transfer plan is first submitted to the Insurance Division of the Rhode Island Department of Business Regulation.

- The plan must include, inter alia:

    - The most recent audited financial statements and annual reports of the transferring company filed with its domiciliary regulator.

- The form of notice to be provided under the plan to any policyholder or reinsured of the transferring company whose policies are to be transferred and a full description as to how such notice will be provided.

- Approval of the plan from the transferring company's domiciliary regulator.

- An expert report providing an opinion on the proposed transaction.

- The department can only approve the plan if, in the department's opinion, it would have no material adverse impact on the insurer's policyholders, reinsureds or claimants of policies subject to the transfer.

- After the department approves the plan, the assuming company must apply to the Superior Court of Providence County, or the Superior Court, for approval.

- After a hearing is scheduled, the assuming company must provide notice to interested parties.

- A 60-day comment period follows the distribution of the notice.

- Any person who believes he or she will be adversely affected can make a presentation to the Superior Court at the approval hearing.

- The Superior Court will approve the plan if it finds no material adverse impact to policyholders, reinsureds or claimants on the transferred policies.

Although similar in many respects, the Oklahoma act is broader in scope than Rhode Island's Regulation 68. Under Regulation 68, transferring companies can only transfer blocks of property/casualty business to Rhode Island-domiciled commercial run-off insurers. Under the Oklahoma act, however, property, casualty, life and health policies can all be transferred (and potentially any other line of business deemed appropriate by the commissioner). Moreover, the Oklahoma act applies to both active and run-off books of business, whereas Regulation 68 only applies to run-off business.

The laws also differ with respect to notice. Under Regulation 68, the Rhode Island department will send electronic notice to all persons who have requested notice of insurance issues indicating that the plan has been filed and is available for review. Individuals can then file comments with the department within 30 days after the notice, and the department will consider these comments before determining whether it will approve the plan. The Oklahoma act does not provide for notice at the regulatory approval stage. Although both laws do not provide an opt-out provision for policyholders, only the Oklahoma act requires that policyholders be notified that they cannot opt-out of the transfer and novation.

As of the date of this article, no insurance business transfer has been approved under Regulation 68.[3] This past September, however, ProTucket Insurance Company, the first Rhode Island domestic insurer created to take advantage of Regulation 68, received $35,000,000 of funding from its parent company, Pro U.S. Holdings. This funding allows ProTucket to meet minimum capital requirements necessary to assume books of business under Regulation 68.

Assumption Reinsurance Model Act

The Assumption Reinsurance Model Act, which has been adopted by 10 states,[4] regulates the transfer

and novation of insurance contracts through assumption reinsurance agreements. An "assumption reinsurance agreement" is defined as "any contract that both: (1) [t]ransfers insurance obligations or risks, or both, of existing or in-force contracts of insurance from a transferring insurer to an assuming insurer[,] and (2) [i]s intended to effect a novation of the transferred contract of insurance with the result that the assuming insurer becomes directly liable to the policyholders of the transferring insurer and the transferring insurer's insurance obligations or risks, or both, under the contracts are extinguished."[5]

Certain notice and disclosure requirements must be satisfied to effect a novation under the model act. The transferring insurer must provide to each policyholder a notice that states, inter alia, (1) that the policyholder has the right to either consent to or reject the transfer and novation, and (2) the procedures and time limit for consenting to or rejecting the transfer and novation.[6] The model act also requires the insurance commissioner's prior approval for transactions where an insurer domiciled in a state that has adopted the model act assumes or transfers insurance contracts under an assumption reinsurance agreement.[7]

Policyholders have the right to reject the transfer and novation by returning written notice indicating that the assumption is rejected.[8] Policyholders will be deemed to have accepted the transfer if they pay premium to the assuming company during the two-year period after notice is received, provided that the notice clearly states that payment of premium to the assuming insurer shall constitute acceptance of the transfer.[9] A deemed acceptance also occurs if a policyholder fails to accept or reject a second and final notice of transfer within one month after the date of mailing (the second and final notice may be sent if, after no fewer than two years from the mailing of the initial notice, no affirmative consent to, or rejection of, the transfer has been received).[10] A novation only occurs if the policyholder consents to the transfer (with the exception of certain situations where an insurer is in hazardous financial conditions or an administrative proceeding has been instituted against it for the purpose of reorganizing or conserving the insurer).[11]

While both the model act and the Oklahoma act provide mechanisms to transfer and novate books of business from one insurer to another, key differences exist between the two acts. The model act generally requires only regulatory approval of assumption reinsurance agreements, whereas the Oklahoma act requires regulatory and court approval of IBT Plans. The model act allows policyholders to opt-out of the assumption reinsurance agreement by rejecting the transfer and novation. No novation is effected with respect to a policyholder who chooses to reject the transaction. In contrast, if an IBT plan is approved in accordance with the Oklahoma act, the transfer and novation is effected with respect to all policyholders, even those who affirmatively objected to the transfer.[12]

Due Process Arguments Under the Oklahoma Act

The Oklahoma act may prompt constitutional challenges to its allowance of transfers and novations of books of business in the absence of any form of policyholder consent, affirmative or otherwise. Under the Oklahoma act, an insurance business transfer could theoretically be approved over the objection of all policyholders. Most state laws providing for one insurer to transfer its liabilities to another, pursuant to regulatory approval, require at least the tacit consent of policyholders in order for the transfer to take effect by, for example, paying premium to the assuming insurer after notification of the transfer.[13] An issue that may arise is whether the notice and hearing provisions of the Oklahoma act are sufficient to satisfy the requirement of due process.

Policyholders and other interested parties have brought due process claims in various insurance-related contexts in which contractual rights have been modified over their objections. For example, in In re

Ambac Assur. Corp.,[14] interested parties challenged a rehabilitation plan that was approved over their objections by arguing, inter alia, that their due process rights were violated because the court denied their requests for discovery. The interested parties argued that, absent discovery, they lacked sufficient time and information to evaluate the rehabilitation plan, which in turn denied them the right to be meaningfully heard.[15] The Wisconsin Court of Appeals held that the interested parties were not denied due process, despite the denial of their discovery requests, because they were provided notice and an opportunity to be heard, they were given an opportunity prior to the plan approval hearing to file written objections to the plan, they could submit questions to the commissioner (to which the commissioner responded in advance of the hearing), and they had the opportunity to present and cross-examine witnesses at the plan approval hearing.[16] The commissioner also provided the interested parties with hundreds of pages of documents relevant to the rehabilitation plan prior to the hearing.[17]

The Arkansas Supreme Court, in Mendel v. Garner,[18] similarly held that the due process rights of annuity policyholders whose claims were affected by the approval of a rehabilitation plan were not violated, inasmuch as the policyholders were allowed to submit evidence and testimony at the approval hearing.[19] The court stated that "[t]he rehabilitation of insurance companies pursuant to state insolvency statutes does not impair the obligations of contracts" and that "[a] hearing with the submission of evidence and testimony satisfies the constitutional requirement of due process of law."[20]

In LaFarge Corp. v. Com.,[21] the Supreme Court of Pennsylvania held that policyholders and reinsurers appealing a decision of the Pennsylvania Insurance Department that approved a plan of restructure and division of an insurance company were not entitled to an adversarial hearing before the plan could be approved.[22] The court held that due process did not require the insurance department to conduct an adversarial hearing on a plan to restructure and divide an insurance company where notice was published and interested parties were invited to submit written comments and objections.[23] According to the court, additional procedures such as testimony and cross-examination would entail extensive delay, would not materially enhance the interests of the policyholders and reinsurers, and would require the insurance department to engage in evaluation of speculative harm.[24] The court also noted that the insurance department solicited independent expert reports and evaluations concerning the solvency and financial integrity of the proposed restructuring, that everyone who indicated a desire to speak was permitted to make an oral presentation to the commissioner, and that the commissioner analyzed materials and found that the transaction was not injurious to the interest of policyholders and creditors.[25]

If a challenge were brought by policyholders or other parties against the Oklahoma act on due process grounds, Oklahoma would likely argue that the law passes constitutional muster because: (1) the transfer is vetted by the commissioner's review and approval of the IBT plan, which must include, among other things, an independent expert report that analyzes the transaction and considers whether the interests of policyholders would be materially adversely affected; (2) policyholders are provided notice of the transaction and its effect on their rights; (3) policyholders are given a 60-day comment period during which they can comment on and object to the transfer; (4) interested parties can present evidence and comments at the approval hearing; and (5) the commissioner and the district court can only approve the transfer and novation if the transaction does not materially adversely affect the interests of policyholders and claimants.

The Wisconsin, Arkansas and Pennsylvania cases discussed above, as well as decisions in other similar cases, looked to the opportunity for policyholders and other affected parties to have their objections heard in the context of the courts' evaluation of the plans, irrespective of whether their objections were adopted or otherwise acted upon. This central requirement of opportunity to be heard will be at the

center of any due process challenge to the Oklahoma act. Whether the Oklahoma act's procedural safeguards satisfy the demands of due process will also depend upon the importance of the policyholders' interests, the value of any additional safeguards and Oklahoma's interests in proceeding without any additional procedures. The policyholder consent requirement in the Assumption Reinsurance Model Act will be noteworthy but not necessarily controlling in deciding whether the Oklahoma act is constitutional, and whether policyholders and reinsureds who have been afforded an adequate opportunity for the objections to be heard could prevent an IBT plan from taking effect.

Laura Forggan and John Sarchio are partners, Richard Liskov is senior counsel and Jarad Schaeffner is an associate at Crowell & Moring LLP.

[1] Insurance Business Transfer Act, 2018 Okla. Sess. Law Serv. Ch. 232 (S.B. 1101) (West).

[2] R.I. Admin. Code 11-5-68:6.1 et seq.

[3] Although no insurance business transfer has been approved under Regulation 68, the Superior Court has approved a commutation plan under Rhode Island's Voluntary Restructuring of Solvent Insurer's Act. See In re: GTE Reinsurance Co. Ltd., C.A. No. PB 10-3777 (R.I. Super. Ct. filed Apr. 25, 2011).

[4] Colorado, Georgia, Kansas, Maine, Missouri, Nebraska, North Carolina, Oregon, Rhode Island and Vermont.

[5] Assumption Reinsurance Model Act § 3(B).

[6] Id. § 4(A).

[7] Id. § 4(B).

[8] Id. § 5(A).

[9] Id. § 5(B).

[10] Id. § 5(C).

[11] Id. §§ 6-7.

[12] Under Rhode Island's Voluntary Restructuring of Solvent Insurers Act, a Rhode Island-domiciled commercial run-off insurer may extinguish its outstanding liabilities through the implementation of a commutation plan, which must be approved by the Superior Court, as well as (1) 50 percent of each class of creditors and (2) the holders of 75 percent in value of the liabilities owed to each class of creditors. R.I. Gen. Laws § 27-14.5.1 et seq. The Oklahoma act has no similar provision.

[13] See, e.g., Georgia Code § 33-52-4; Nebraska Revised Statutes § 44-6207.

[14] In re Ambac Assur. Corp., 841 N.W. 482 (Wis. Ct. App. 2013)

[15] Id. at 514.

[16] Id. at 514-15.

[17] Id.

[18] Mendel v. Garner, 678 S.W.2d 759 (Ark. 1984)

[19] 678 S.W.2d at 761.

[20] Id.

[21] Ins. Dep't, 735 A.2d 74 (Pa. 1999)

[22] 735 A.2d at 75.

[23] Id. at 78.

[24] Id.

[25] Id.