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COMMISSIONER



STATE OF DELAWARE
DEPARTMENT OF INSURANCE

CAPTIVE BULLETIN NO. 14

TO: ALL CAPTIVE MANAGERS, AUDITORS, AND ACTUARIES ACCREDITED IN DELAWARE, AND ALL MEMBERS OF THE DELAWARE CAPTIVE INSURANCE ASSOCIATION

RE: GUIDELINES ON FORMATION OF CAPTIVE INSURANCE COMPANIES ISSUING SIDE A DIRECTORS AND OFFICERS INSURANCE TO DELAWARE CORPORATIONS

DATED: October 10th, 2023

Recent amendments to the Delaware General Corporation Law authorize Delaware corporations to use captive insurance to protect current and former directors and officers against liability even if such corporations would not be empowered to indemnify them. 8 Del. C. § 145(g). As a result of this legislative amendment, the Delaware Department of Insurance (“Department”) is pleased to announce that it continues to accept certificate of authority applications for captive insurance companies intending to write Side A D&O insurance coverage in Delaware. The purpose of this Bulletin is to provide initial guidance to corporations intending to form and operate a Delaware captive for the purpose of providing Side A D&O insurance coverage to a Delaware corporation.

Formation

Due to the unique nature of Side A D&O insurance written by captive insurance companies, it is expected that new Delaware captive insurance companies or separate protected cells of Delaware captives intending to write Side A D&O insurance will be organized and authorized to write D&O insurance exclusively and such insurance coverage will not be authorized in a multi-line Delaware captive.

No Conditional Certificate of Authority

Applications will receive a complete review prior to issuance of a certificate of authority. Until further notice, no applications for conditional certificates of authority pursuant to 18 Del. C. § 6903(g) will be accepted for Delaware captive insurance companies intending to write Side A D&O insurance.

NOTE: This Bulletin is intended solely for informational purposes. It is not intended to set forth legal rights, duties, or privileges, nor is it intended to provide legal advice. Readers should consult applicable statutes and rules and contact the Delaware Department of Insurance if additional information is needed

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Capitalization

All Delaware Side A D&O insurance captives must be, and remain, fully capitalized to cover full limit losses. That is, a Side A D&O insurance captive must be capitalized to pay the highest full limit policy loss (net of reinsurance and incurred but not reported (IBNR) reserves). This capitalization rule applies on a per-claim basis such that a captive insurance company with an outstanding claim that wishes to issue a new policy must be sufficiently capitalized to cover both the outstanding claim and highest limit policy loss under the new policy.

Investments

All Delaware captive insurance companies, including new Delaware captive insurance companies offering Side A D&O Insurance, must submit an investment plan to the Department for approval. The investment portfolio should be sufficiently diversified. Delaware captive insurance company investments are regulated by the Department pursuant to 18 *Del. C.* § 6910.

Policy Form Review and Fronting

The provisions of 8 *Del. C.* § 145(g) require that the terms of Side A D&O insurance policies for Delaware corporations contain the following three conduct exclusions:

1. personal profit or other financial advantage to which the insured was not legally entitled;
2. deliberate criminal or deliberate fraudulent acts, if established by a final, non-appealable adjudication in the underlying proceeding in respect of such claim (which shall not include an action or proceeding initiated by the insurer or the insured to determine coverage under the policy); and
3. knowing violations of the law, if established by a final, non-appealable adjudication in the underlying proceeding in respect of such claim (which shall not include an action or proceeding initiated by the insurer or the insured to determine coverage under the policy).

The Department will review each policy form to ensure that these three exclusions are addressed in the policy. It may be sufficient for the policy to incorporate such exclusions by reference to 8 *Del. C.* § 145(g). Such exclusions are also required in the relevant reinsurance agreement when a Delaware captive insurance company is acting as a reinsurer to a commercial insurer that fronts Side A D&O insurance of a Delaware corporation, if such exclusions are not contained in the direct policy. No Delaware Side A D&O insurance captive may issue a policy until the Department completes its review of an application and issues a certificate of authority.

Claims Administration

The provisions of 8 *Del. C.* § 145(g) include limits on how Side A D&O insurance claims decisions are made with respect to Delaware corporations. Accordingly, Delaware captive insurance companies intending to write Side A D&O insurance will be required to retain either a Department-approved independent third-party claims administrator or a Department-approved independent director. In the event that a Delaware Side A D&O insurance captive's engagement with such claims administrator or independent director is terminated and, as a result, the captive does not have a Department-approved

independent third-party claims administrator or a Department-approved independent director, the captive shall engage a replacement Department-approved independent third-party claims administrator or Department-approved independent director within 30 days after such termination.

Questions concerning this Bulletin may be directed to Stephen Taylor, Director of the Bureau of Captive & Financial Insurance Products, at stephen.taylor@delaware.gov or (302) 577-5280.



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