

The Department of Financial Services sent the following four objections to bill A.5718/S.5959 to Asm. David Weprin, chair of the insurance committee:

1. DFS cannot regulate risk retention groups ("RRGs") that are chartered in another state and registered in New York. There are currently no NY-chartered RRGs.
2. RRGs are not subject to the consumer protections of the Insurance Law or regulations promulgated thereunder.
3. DFS cannot review and prior approve policy forms and rates like it does for authorized insurers.
4. There is no guaranty fund protection for RRGs in the event an RRG goes out of business and cannot pay claims to innocent third parties.

Below are the responses to each objection from Pamela Davis, CEO of Alliance of Nonprofits for Insurance (ANI), a Risk Retention Group that provides liability insurance (not auto) to 1,200 nonprofits in New York, and liability + auto insurance to 13,000 nonprofits across the country. ANI is domiciled in Vermont.

#1. DFS cannot regulate risk retention groups ("RRGs") that are chartered in another state and registered in New York. There are currently no NY-chartered RRGs.

This is correct. RRGs are authorized by the Liability Risk Retention Act of 1986 (LRRRA). This federal law preempts state law and enables business and professional associations, as well as nonprofits, to work together to create their own insurance companies called RRGs.

The LRRRA was passed by Congress to solve just the sort of market failure nonprofits are experiencing in New York State right now.

Within the LRRRA, Congress granted states certain authorities, including specifying acceptable means of demonstrating financial responsibility. The relevant portion of the LRRRA is copied below:

d) State authority to specify acceptable means of demonstrating financial responsibility
Subject to the provisions of section 3902(a)(4) of this title relating to discrimination *nothing in this chapter shall be construed to preempt the authority of a State to specify acceptable means of demonstrating financial responsibility as a condition for obtaining a license or permit to undertake specified activities. Such means may include or exclude insurance coverage obtained from an admitted insurance company, an excess lines company, a risk retention group, or any other source regardless of whether coverage is obtained directly from an insurance company or through a broker, agent, purchasing group, or any other person. [Emphasis added]*

However, DFS is overlooking the provisions of section 3902(a)(4) of the LRRRA which specifically prohibits any state from conditioning these financial responsibility requirements simply on the fact that such an insurance company is organized as a RRG that is domiciled in another state.

The LRRRA provides that RRGs may be held to the same financial responsibility requirements of other insurance companies, except that, one of those requirements *may not be to require that RRG to be chartered in the state of NY.*

Relevant portion of the LRRRA is copied below:

(a) Exemptions from State laws, rules, regulations, or orders

Except as provided in this section, a risk retention group is exempt from any [State](#) law, rule, regulation, or order to the extent that such law, rule, regulation, or order would—

(4) otherwise, discriminate against a risk retention group or any of its members, except that nothing in this section shall be construed to affect the applicability of State laws generally applicable to persons or corporations.

There are 140 RRGs insuring thousands of businesses and nonprofits in New York State today. Many have been operating successfully there for decades insuring complex and difficult risks such as allegations of sexual abuse.

These RRGs must be licensed and admitted insurance companies in one state and may operate by registering there and providing quarterly financial information to all states in which they operate.

These RRGs must follow the Risk-Based Capital standards required of every licensed, admitted insurance company across the country.

DFS has access to the financial information of all RRGs and may request additional operational information from the domicile regulator of any RRG.

If DFS has concerns about any RRG operating in New York, it may request the chartering state to conduct a financial examination and if that state refuses to do so, New York may conduct its own examination.

If it uncovers financial concerns about that RRG, it may report those to the National Association of Insurance Commissioners (NAIC) Financial Analysis Working Group (FAWG) which is used by states across the country as a peer review for each regulator's solvency monitoring efforts.

In the nearly 40 years since the LRRRA has been law, it is our understanding that only one regulator asked the chartering regulator to conduct an examination of an RRG and that state complied.

#2. RRGs are not subject to the consumer protections of the Insurance Law or regulations promulgated thereunder.

The following is an excerpt from a Special Report on Financial Regulation of Risk Retention Groups by David Provost, deputy commissioner of captive insurance at the Vermont Department of Financial Regulation:

In order to promote a uniform and effective nationwide regulatory framework, the states and jurisdictions that comprise the National Association of Insurance Commissioners (NAIC) have developed the NAIC Financial Regulation Standards and Accreditation Program. In order to become an accredited jurisdiction, states must meet certain standards deemed necessary to build a sound regulatory framework: Regulators must have adequate statutory and administrative authority to regulate an insurer's corporate and financial affairs; regulators must have the necessary resources to carry out that authority; and insurance departments must have in place organizational and personnel practices designed for effective regulation [before they may be accredited to be the domicile of a risk retention group.] More information on the NAIC accreditation program is available at: http://www.naic.org/documents/committees_f_FRSA_pamplet.pdf

Also, RRGs in New York must comply with the unfair claim settlement practices law of New York and also pay applicable premium and other taxes which are levied on admitted insurers and surplus lines insurers, brokers, or policyholders under the laws of New York State.

#3. DFS cannot review and prior approve policy forms and rates like it does for authorized insurers.

This is correct. The federal LRRRA specifically acknowledged that RRGs would be created because the businesses or nonprofits that started them had not been well-served by the commercial insurance industry.

According to the NAIC, "Few RRGs, if any, are required to submit rate and form filings — rates are typically based on an actuarial analysis of the membership, and one of the advantages of captives is the ability to conform the policy to suit the needs of the membership."

Many states do not regulate rates and forms for commercial risks. It was specifically understood by Congress when it passed the LRRRA that generic rates and policy forms were not adequately serving these business and nonprofits, and there was no value added to have each of the states opine on the policy forms and rates, since RRGs may only insure commercial businesses, which are also the owners of the RRG.

#4. There is no guaranty fund protection for RRGs in the event an RRG goes out of business and cannot pay claims to innocent third parties.

This is correct. It is a provision of the LRRRA that RRGs would not participate in state guarantee funds. However, there are ample controls available to regulators to avoid failure of RRGs. Furthermore, even when an RRG fails, there are typically some assets to pay minimum limits on claims (RRGs typically offer \$1 million auto limits when NY only requires \$25,000/\$50,000/\$10,000.)

And, Risk Retention Groups tend to be small and specialized. In fact, over the past 40 years, the total number of failures of all RRGs nationwide represents about \$500,000 in premium volume — about the size of a single mid-sized commercial insurance company.

Compare that with the actual significant risk being endured by New York consumers now unable to get the use of the carshare they need or of nonprofits having to decline the donation of vehicles to transport medically fragile patients because they cannot find auto insurance. It is a risk well-worth taking.

One final note:

The points above demonstrate that New York has ample opportunity to monitor the solvency and claims handling fairness of RRGs operating in their state, despite the unique nature of RRGs. Nevertheless, even if DFS does not like RRGs offering auto insurance in New York, that is not a sufficient reason to defy complying with federal law.