

## MODEL RISK RETENTION ACT

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### Section 1. Purpose

The purpose of this Act is to regulate the formation and/or operation of risk retention groups and purchasing groups in this State formed pursuant to the provisions of the federal Liability Risk Retention Act of 1986 (“RRA 1986”), to the extent permitted by such law.

### Section 2. Definitions

As used in this Act

- A. “Commissioner” [director, superintendent] means the insurance commissioner [director, superintendent] of [insert name of state] or the commissioner, director or superintendent of insurance in any other state;
- B. “Completed operations liability” means liability arising out of the installation, maintenance or repair of any product at a site which is not owned or controlled by
  - (1) Any person who performs that work; or
  - (2) Any person who hires an independent contractor to perform that work; but shall include liability for activities which are completed or abandoned before the date of the occurrence giving rise to the liability;

**Drafting Note:** The definition of “completed operations liability” is taken from the definition in the Product Liability Risk Retention Act of 1981 (Product Liability RRA 1981) Section 2(a)(1). A purpose of RRA 1986 was to expand the permissible coverage offered by risk retention groups from product liability and completed operations to general liability insurance, as further defined in RRA 1986. Some risk retention groups that were chartered under the Product Liability RRA 1981 are “grandfathered” by RRA 1986 to the extent that they can continue to provide product liability and completed operations coverage if they meet the criteria established by RRA 1986. The definitions relating to product liability and completed operations coverage, therefore, are relevant to any such groups which may continue to so operate.

- C. “Domicile”, for purposes of determining the state in which a purchasing group is domiciled, means
  - (1) For a corporation, the state in which the purchasing group is incorporated; and
  - (2) For an unincorporated entity, the state of its principal place of business;
- D. “Hazardous financial condition” means that, based on its present or reasonably anticipated financial condition, a risk retention group, although not yet financially impaired or insolvent, is unlikely to be able
  - (1) To meet obligations to policyholders with respect to known claims and reasonably anticipated claims; or
  - (2) To pay other obligations in the normal course of business;

**Drafting Note:** The definition of “hazardous financial condition” stipulates that a regulator, in looking at the financial condition of a risk retention group, can base his conclusions on reasonable expectations of future performance. In determining the present or reasonably anticipated financial condition of a risk retention group, the commissioner may utilize all relevant financial tests, ratios and other factors used in determining the financial condition of authorized insurers, including an analysis of actuarial soundness of rates charged.

- E. “Insurance” means primary insurance, excess insurance, reinsurance, surplus lines insurance, and any other arrangement for shifting and distributing risk which is determined to be insurance under the laws of this state;

**Drafting Note:** Definition taken from RRA 1986 Section 2(a)(1).

- F. “Liability”
  - (1) Means legal liability for damages (including costs of defense, legal costs and fees, and other claims expenses) because of injuries to other persons, damage to their property, or other damage or loss to such other persons resulting from or arising out of
    - (a) Any business (whether profit or nonprofit), trade, product, services (including professional services), premises or operations; or
    - (b) Any activity of any state or local government, or any agency or political subdivision thereof; and

**Drafting Note:** A state may specify acceptable means for managing the liability of the state or its local governments, or any agency or political subdivision thereof, by including or excluding insurance coverage obtained from an admitted insurance company, an excess lines company, a risk retention group, or any other source; or through a broker, agent, purchasing group, or any other person. Similarly, a state may specify acceptable means of demonstrating financial responsibility as a condition for obtaining a license or permit to undertake specified activities pursuant to Section 6(d), RRA 1986.

- (2) Does not include personal risk liability and an employer's liability with respect to its employees other than legal liability under the Federal Employers' Liability Act (45 U.S.C. 51 et seq.);
- G. "Personal risk liability" means liability for damages because of injury to any person, damage to property, or other loss or damage resulting from any personal, familial, or household responsibilities or activities, rather than from responsibilities or activities referred to in Subsection F;
- H. "Plan of operation" or "feasibility study" means an analysis which presents the expected activities and results of a risk retention group including, at a minimum;
  - (1) Information sufficient to verify that its members are engaged in businesses or activities similar or related with respect to the liability to which such members are exposed by virtue of any related, similar or common business, trade, product, services, premises or operations;
  - (2) For each state in which it intends to operate, the coverages, deductibles, coverage limits, rates and rating classification systems for each line of insurance the group intends to offer;
  - (3) Historical and expected loss experience of the proposed members and national experience of similar exposures to the extent that this experience is reasonably available;
  - (4) Pro forma financial statements and projections;
  - (5) Appropriate opinions by a qualified, independent casualty actuary, including a determination of minimum premium or participation levels required to commence operations and to prevent a hazardous financial condition;
  - (6) Identification of management, underwriting and claims procedures, marketing methods, managerial oversight methods, investment policies and reinsurance agreements;
  - (7) Identification of each state in which the risk retention group has obtained, or sought to obtain, a charter and license, and a description of its status in each such state; and
  - (8) Such other matters as may be prescribed by the commissioner of the state in which the risk retention group is chartered for liability insurance companies authorized by the insurance laws of that state;
- I. "Product liability" means liability for damages because of any personal injury, death, emotional harm, consequential economic damage, or property damage (including damages resulting from the loss of use of property) arising out of the manufacture, design, importation, distribution, packaging, labeling, lease, or sale of a product, but does not include the liability of any person for those damages if the product involved was in the possession of such a person when the incident giving rise to the claim occurred;

**Drafting Note:** The definition of "product liability" is identical to that contained in Product Liability RRA 1981, Section 2(a)(3), for a "grandfathered" risk retention group. See Drafting Note following Subsection 2B of this Act.

- J. “Purchasing group” means any group which
- (1) Has as one of its purposes the purchase of liability insurance on a group basis;
  - (2) Purchases such insurance only for its group members and only to cover their similar or related liability exposure, as described in Paragraph (3);
  - (3) Is composed of members whose businesses or activities are similar or related with respect to the liability to which members are exposed by virtue of any related, similar, or common business, trade, product, services, premises, or operations; and
  - (4) Is domiciled in any state;

**Drafting Note:** The Product Liability RRA 1981 contained a very loose definition of “purchasing group.” RRA 1986 offers a more restrictive definition of those groups that can qualify as “purchasing groups.” A purchasing group must only offer liability insurance to its group members, and the insurance must cover their similar or related liability exposure. Further, the group members must have businesses or activities that are similar or related with respect to the liability to which group members are exposed. Finally, the purchasing group must be domiciled in one of the states of the United States, i.e., it cannot be domiciled offshore.

- K. “Risk retention group” means any corporation or other limited liability association:
- (1) Whose primary activity consists of assuming and spreading all, or any portion, of the liability exposure of its group members;
  - (2) Which is organized for the primary purpose of conducting the activity described under Paragraph (1);
  - (3) Which
    - (a) Is chartered and licensed as a liability insurance company and authorized to engage in the business of insurance under the laws of any state; or
    - (b) Before January 1, 1985 was chartered or licensed and authorized to engage in the business of insurance under the laws of Bermuda or the Cayman Islands and, before such date, had certified to the insurance commissioner of at least one state that it satisfied the capitalization requirements of such state, except that any such group shall be considered to be a risk retention group only if it has been engaged in business continuously since that date and only for the purpose of continuing to provide insurance to cover product liability or completed operations liability (as such terms were defined in the Product Liability Risk Retention Act of 1981 before the date of the enactment of the Liability Risk Retention Act of 1986);
  - (4) Which does not exclude any person from membership in the group solely to provide for members of such a group a competitive advantage over such a person;
  - (5) Which
    - (a) Has as its owners only persons who comprise the membership of the risk retention group and who are provided insurance by such group; or

- (b) Has as its sole owner an organization which has as
  - (i) Its members only persons who comprise the membership of the risk retention group; and
  - (ii) Its owners only persons who comprise the membership of the risk retention group and who are provided insurance by such group;
- (6) Whose members are engaged in businesses or activities similar or related with respect to the liability of which such members are exposed by virtue of any related, similar or common business trade, product, services, premises or operations;
- (7) Whose activities do not include the provision of insurance other than
  - (a) Liability insurance for assuming and spreading all or any portion of the liability of its group members; and
  - (b) Reinsurance with respect to the liability of any other risk retention group (or any members of such other group) which is engaged in businesses or activities so that the group or member meets the requirement described in Paragraph 6 from membership in the risk retention group which provides such reinsurance; and
- (8) The name of which includes the phrase “Risk Retention Group;”

**Drafting Note:** RRA 1986 changes the definition of “risk retention group” by further restricting the permissible membership and its activities. A risk retention group must be chartered and licensed as a liability insurance company and authorized to engage in the business of insurance under the laws of one of the fifty states unless it qualifies under the “grandfather” provision of Subsection K(3)(b). In that event, it may only continue to provide product liability or completed operation coverage.

Each of the members of the group must have an “ownership interest” in the group. In addition, all owners must be provided insurance by the group. One purpose of this requirement is to prevent participation by third parties which may not be interested in the specific insurance problems of group members but merely may be interested in making a profit. The single exception to this requirement is when the sole member and sole owner of the organization is an entity consisting of persons, each of whom is a member of the risk retention group and is provided insurance by the group.

The members “who are also the owners” are required to be engaged in businesses or activities “similar or related with respect to the liability to which they are exposed by virtue of any related, similar, or common business, trade, product, services, premises or operation.” This restriction is for the purpose of requiring substantial identity among the members (who are also the owners and insureds) in regard to the nature of the risks faced.

A risk retention group may not provide insurance other than liability insurance. Further, it can only provide reinsurance to another risk retention group if all of that group’s members would qualify for membership in the risk retention group offering the reinsurance. This provision was designed to restrict a risk retention group to only reinsuring its own risks or the similar risks of similarly situated businesses. For example, a risk retention group whose membership consists of grocery store owners, could not reinsure a risk retention group whose membership consists of hazardous waste transporters.

The risk retention group must be chartered and licensed as a liability insurance company and authorized to engage in the business of insurance under the laws of one of the fifty states unless it qualifies under the “grandfather” provision of Subsection K(3)(b).

L. “State” means any state of the United States or the District of Columbia.

### **Section 3. Risk Retention Groups Chartered in this State**

- A.
  - (1) A risk retention group shall, pursuant to the provisions of Section [insert appropriate reference to Insurance Law], be chartered and licensed to write only liability insurance pursuant to this Act and, except as provided elsewhere in this Act, must comply with all of the laws, rules, regulations and requirements applicable to insurers chartered and licensed in this state and with Section 4 of this Act to the extent such requirements are not a limitation on laws, rules, regulations or requirements of this state.
  - (2) Notwithstanding any other provision to the contrary, all risk retention groups chartered in this state shall file with the department and the National Association of Insurance Commissioners (NAIC), an annual statement in a form prescribed by the NAIC and in diskette form, if required by the Commissioner and completed in accordance with its instructions and the NAIC Accounting Practices and Procedures Manual.
- B. Before it may offer insurance in any state, each risk retention group shall also submit for approval to the insurance commissioner of this state a plan of operation or feasibility study. The risk retention group shall submit an appropriate revision in the event of any subsequent material change in any item of the plan of operation or feasibility study, within ten (10) days of any such change. The group shall not offer any additional kinds of liability insurance, in this state or in any other state, until a revision of the plan or study is approved by the commissioner.
- C. At the time of filing its application for charter, the risk retention group shall provide to the commissioner in summary form the following information: the identity of the initial members of the group, the identity of those individuals who organized the group or who will provide administrative services or otherwise influence or control the activities of the group, the amount and nature of initial capitalization, the coverages to be afforded, and the states in which the group intends to operate. Upon receipt of this information, the commissioner shall forward the information to the National Association of Insurance Commissioners. Providing notification to the NAIC is in addition to and shall not be sufficient to satisfy the requirements of Section 4 or any other sections of this Act.
- D. Governance Standards For Risk Retention Groups - Within a year of the effective date of this Act, existing risk retention groups shall be in compliance with the following Governance Standards. New risk retention groups shall be in compliance with the standards at the time of licensure.
  - (1) Board of Directors. The “board of directors” or “board” as used in this section, means the governing body of the risk retention group elected by the shareholders or members to establish policy, elect or appoint officers and committees, and make other governing decisions. “Director” as used in this section, means a natural person designated in the articles of the risk retention group, or designated, elected or appointed by any other manner, name or title to act as a director.
    - (a) Independent Directors. The board of directors of the risk retention group shall have a majority of independent directors. If the risk retention group is a reciprocal, then the attorney-in-fact would be required to adhere to the same standards regarding independence of operation and governance as imposed on the risk retention group’s board of directors/subscribers advisory committee under these standards; and, to the extent permissible under state law, service

providers of a reciprocal risk retention group should contract with the risk retention group and not the attorney-in-fact.

- (i) No director qualifies as “independent” unless the board of directors affirmatively determines that the director has no “material relationship” with the risk retention group. Each risk retention group shall disclose these determinations to its domestic regulator, at least annually. For this purpose, any person that is a direct or indirect owner of or subscriber in the risk retention group (or is an officer, director and/or employee of such an owner and insured, unless some other position of such officer, director and/or employee constitutes a “material relationship”), as contemplated by Section 3901(a)(4)(E)(ii) of the Liability Risk Retention Act, is considered to be “independent.”
- (b) “Material relationship” of a person with the risk retention group includes, but is not limited to:
  - (ii) The receipt in any one 12-month period of compensation or payment of any other item of value by such person, a member of such person’s immediate family or any business with which such person is affiliated from the risk retention group or a consultant or service provider to the risk retention group is greater than or equal to five percent (5%) of the risk retention group’s gross written premium for such 12-month period or two percent (2%) of its surplus, whichever is greater, as measured at the end of any fiscal quarter falling in such a 12-month period. Such person or immediate family member of such person is not independent until one year after his/her compensation from the risk retention group falls below the threshold.
  - (iii) A relationship with an auditor as follows: a director or an immediate family member of a director who is affiliated with or employed in a professional capacity by a present or former internal or external auditor of the risk retention group is not independent until one year after the end of the affiliation, employment or auditing relationship.
  - (iv) A relationship with a related entity as follows: a director or immediate family member of a director who is employed as an executive officer of another company where any of the risk retention group’s present executives serve on that other company’s board of directors is not independent until one year after the end of such service or the employment relationship.
- (2) Service Provider Contracts. The term of any material service provider contract with the risk retention group shall not exceed five (5) years. Any such contract, or its renewal, shall require the approval of the majority of the risk retention group’s independent directors. The risk retention group’s board of directors shall have the right to terminate any service provider, audit or actuarial contracts at any time for cause after providing adequate notice as defined in the contract. The service provider contract is deemed material if the amount to be paid for such contract is greater than or equal to five percent (5%) of the risk retention group’s annual gross written premium or two percent

(2%) of its surplus, whichever is greater.

- (a) For purposes of this standard, "service providers" shall include captive managers, auditors, accountants, actuaries, investment advisors, lawyers, managing general underwriters or other party responsible for underwriting, determination of rates, collection of premium, adjusting and settling claims and/or the preparation of financial statements. Any reference to 'lawyers' in the prior sentences does not include defense counsel retained by the risk retention group to defend claims, unless the amount of fees paid to such lawyers are 'material' as referenced in Section (1)(B) above.
- (b) No service provider contract meeting the definition of "material relationship" contained in Section (1)(B) shall be entered into unless the risk retention group has notified the Commissioner in writing of its intention to enter into such transaction at least 30 days prior thereto and the Commissioner has not disapproved it within such period.

**Drafting note:** For the sake of clarity, the domestic Commissioner's authority is included in this subpart. Some states may prefer the Commissioner's authority as included in this subpart be enacted in Section 11 "Administrative and Procedural Authority Regarding Risk Retention Groups and Purchasing Groups."

- (3) Written Policy. The risk retention group's board of directors shall adopt a written policy in the plan of operation as approved by the board that requires the board to:
  - (a) Assure that all owner/insureds of the risk retention group receive evidence of ownership interest;
  - (b) Develop a set of governance standards applicable to the risk retention group;
  - (c) Oversee the evaluation of the risk retention group's management including but not limited to the performance of the captive manager, managing general underwriter or other party or parties responsible for underwriting, determination of rates, collection of premium, adjusting or settling claims or the preparation of financial statements;
  - (d) Review and approve the amount to be paid for all material service providers; and
  - (e) Review and approve, at least annually:
    - (i) Risk retention group's goals and objectives relevant to the compensation of officers and service providers;
    - (ii) The officers' and service providers' performance in light of those goals the and objectives; and,
    - (iii) The continued engagement of the officers and material service providers.



- (4) **Audit Committee** The risk retention group shall have an audit committee composed of at least three independent board members as defined in Section (1). A non-independent board member may participate in the activities of the audit committee, if invited by the members, but cannot be a member of such committee.
- (a) The audit committee shall have a written charter that defines the committee's purpose, which, at a minimum, must be to:
- (i) Assist board oversight of (1) the integrity of the financial statements, (2) the compliance with legal and regulatory requirements, and (3) the qualifications, independence and performance of the independent auditor and actuary;
  - (ii) Discuss the annual audited financial statements and quarterly financial statements with management;
  - (iii) Discuss the annual audited financial statements with its independent auditor and, if advisable, discuss its quarterly financial statements with its independent auditor;
  - (iv) Discuss policies with respect to risk assessment and risk management;
  - (v) Meet separately and periodically, either directly or through a designated representative of the committee, with management and independent auditors;
  - (vi) Review with the independent auditor any audit problems or difficulties and management's response;
  - (vii) Set clear hiring policies of the risk retention group as to the hiring of employees or former employees of the independent auditor;
  - (viii) Require the external auditor to rotate the lead (or coordinating) audit partner having primary responsibility for the risk retention group's audit as well as the audit partner responsible for reviewing that audit so that neither individual performs audit services for more than five (5) consecutive fiscal years; and
  - (ix) Report regularly to the board of directors.
- (b) The domestic regulator may waive the requirement to establish an audit committee composed of independent board members if the risk retention group is able to demonstrate to the domestic regulator that it is impracticable to do so and the risk retention group's board of directors itself is otherwise able to accomplish the purposes of an audit committee, as described in Section (4)(a).

**Drafting Note:** As an alternative to subsection four "Audit Committee", the state may substitute the NAIC audit provisions applicable to traditional insurers.

**Drafting Note:** As an alternative to Section 4(b), the state may substitute "If an audit committee is not designated by the insurer, the insurer's entire board of directors shall constitute the audit committee."

- (5) **Governance Standards** The board of directors shall adopt and disclose governance standards, where "disclose" means making such information available through electronic (e.g., posting such information on the risk retention group's website) or other means, and providing such information to members/insureds upon request, which shall include:
  - (a) A process by which the directors are elected by the owner/insureds;
  - (b) Director qualification standards;
  - (c) Director responsibilities;
  - (d) Director access to management and, as necessary and appropriate, independent advisors;
  - (e) Director compensation;
  - (f) Director orientation and continuing education;
  - (g) The policies and procedures that are followed for management succession; and
  - (h) The policies and procedures that are followed for annual performance evaluation of the board.
- (6) **Business Conduct and Ethics** The board of directors shall adopt and disclose a code of business conduct and ethics for directors, officers and employees and promptly disclose to the board of directors any waivers of the code for directors or executive officers, which should include the following topics:
  - (a) Conflicts of interest;
  - (b) Matters covered under the corporate opportunities doctrine under the state of domicile;
  - (c) Confidentiality;
  - (d) Fair dealing;
  - (e) Protection and proper use of risk retention group assets;
  - (f) Compliance with all applicable laws, rules and regulations; and
  - (g) Requiring the reporting of any illegal or unethical behavior which affects the operation of the risk retention group.

- (7) Reporting Non-Compliance The captive manager, president or chief executive officer of the risk retention group shall promptly notify the domestic regulator in writing if either becomes aware of any material non-compliance with any of these governance standards.

**Drafting Note:** RRA 1986 allows for the chartering state to apply the full range of its insurance laws to a risk retention group wishing to charter in that state, except for requiring participation in the guaranty fund. The language of this section is derived from Product Liability RRA 1981 Section 3(a)(1) (which was not amended by RRA 1986 as it relates to this issue). The function of the office of the National Association of Insurance Commissioners shall be solely to provide administrative services for its member states and territories. Although RRA 1986 specifically requires that the phrase “Risk Retention Group” be included in the name, the chartering state is not precluded from prohibiting the use of deceptive or misleading words, designations or phrases in the name. Further, a state may require a risk retention group it charters and licenses to locate books and records or administrative functions within that state to the same extent it imposes those requirements on its domestic insurers.

#### **Section 4. Risk Retention Groups Not Chartered in this State**

Risk retention groups chartered and licensed in states other than this state and seeking to do business as a risk retention group in this state shall comply with the laws of this state as follows:

**Drafting Note:** RRA of 1986 exempts a risk retention group from any state law regarding its operation in a state in which it is not domiciled except those laws referred to in RRA 1986. The state of domicile, however, retains under that section the full authority to regulate the formation and operation of the group.

However, if a risk retention group fails to qualify under the definitional requirement of RRA 1986, it will not benefit from this exemption from state law. The commissioner, therefore, would be authorized to apply any of the laws that may be preempted by RRA 1986 because the group will not qualify for the preemption.

##### **A. Notice of Operations and Designation of Commissioner as Agent.**

- (1) Before offering insurance in this state, a risk retention group shall submit to the commissioner on a form prescribed by the NAIC:
  - (a) A statement identifying the state or states in which the risk retention group is chartered and licensed as a liability insurance company, charter date, its principal place of business, and such other information, including information on its membership, as the commissioner of this state may require to verify that the risk retention group is qualified under Section 2K of this Act;

**Drafting Note:** The commissioner may need to take appropriate action in order to preserve the confidentiality of any proprietary or other confidential information, such as lists identifying the specific members of the group and their location.

- (b) A copy of its plan of operations or feasibility study and revisions of such plan or study submitted to the state in which the risk retention group is chartered and licensed; provided, however, that the provision relating to the submission of a plan of operation or feasibility study shall not apply with respect to any line or classification of liability insurance which:
  - (i) Was defined in the Product Liability Risk Retention Act of 1981 before October 27, 1986; and
  - (ii) Was offered before that date by any risk retention group which had been chartered and operating for not less than three (3) years before that date; and

- (2) The risk retention group shall submit a copy of any material revision to its plan of operation or feasibility study required by Section 3B of this Act within 30 days of the date of the approval of such revision by the commissioner of its chartering state, or if no such approval is required, within 30 days of filing.

**Drafting Note:** The plan of operations or feasibility study required under this provision is that submitted to and accepted by the chartering state.

- (3) The risk retention group shall submit a statement of registration, for which a filing fee shall be determined by the commissioner, which designates the commissioner as its agent for the purpose of receiving service of legal documents or process.

B. Financial Condition. Any risk retention group doing business in this state shall submit to the commissioner:

- (1) A copy of the group's financial statement submitted to the state in which the risk retention group is chartered and licensed which shall be certified by an independent public accountant and contain a statement of opinion on loss and loss adjustment expense reserves made by a member of the American Academy of Actuaries or a qualified loss reserve specialist (under criteria established by the National Association of Insurance Commissioners);
- (2) A copy of each examination of the risk retention group as certified by the commissioner or public official conducting the examination;
- (3) Upon request by the commissioner, a copy of any information or document pertaining to any outside audit performed with respect to the risk retention group; and
- (4) Such information as may be required to verify its continuing qualification as a risk retention group under Section 2K.

**Drafting Note:** RRA 1986 also added the opportunity for a state to require that a risk retention group submit a notice of operations and financial condition. The purpose of this provision is to require a risk retention group to give the commissioner of any state in which it intends to operate adequate notice of its intended activity and financial condition so that the commissioner can take appropriate action if the possibility of a potential insolvency or commercial abuse exists.

C. Taxation.

- (1) Each risk retention group shall be liable for the payment of premium taxes and taxes on premiums of direct business for risks resident or located within this state, and shall report to the commissioner the net premiums written for risks resident or located within this state. The risk retention group shall be subject to taxation, and any applicable fines and penalties related thereto, on the same basis as a foreign admitted insurer.
- (2) To the extent licensed agents or brokers are utilized pursuant to Section 12 of this Act, they shall report to the commissioner the premiums for direct business for risks resident or located within this state which the licensees have placed with or on behalf of a risk retention group not chartered in this state.

- 3) To the extent that insurance agents or brokers are utilized pursuant to Section 12 of this Act, each agent or broker shall keep a complete and separate record of all policies procured from each risk retention group, which record shall be open to examination by the commissioner, as provided in [insert appropriate reference to Insurance Law]. These records shall, for each policy and each kind of insurance provided thereunder, include the following:
- (a) The limit of liability;
  - (b) The time period covered;
  - (c) The effective date;
  - (d) The name of the risk retention group which issued the policy;
  - (e) The gross premium charged; and
  - (f) The amount of return premiums, if any.

**Drafting Note:** RRA 1986 does not specify which premium tax rate will be applied. The NAIC has recommended applying the rate for foreign admitted insurers; some states, however, may apply the surplus lines rate.

- D. Compliance with Unfair Claims Settlement Practices Law. Any risk retention group, its agents and representatives shall comply with the Unfair Claims Settlement Practices Act of this state, [insert section of the Insurance Code].

**Drafting Note:** The provisions regarding the liability of risk retention groups to state taxation, compliance with the unfair claims settlement practices law, and registration and designation of the commissioner as agent for purpose of service of process were included in the Product Liability RRA 1981 and continued in RRA 1986.

- E. Deceptive, False, or Fraudulent Practices. Any risk retention group shall comply with the laws of this state, [insert sections of the Insurance Code], regarding deceptive, false or fraudulent acts or practices. However, if the commissioner seeks an injunction regarding such conduct, the injunction must be obtained from a court of competent jurisdiction.

**Drafting Note:** The provision regarding compliance with state laws regarding deceptive, false or fraudulent practices was added by RRA 1986. The chartering state retains all of its authority to deal with an unfair trade practice under all its laws generally, including its insurance law. However, the 1986 Act preempts those portions of non-chartering states' Unfair Trade Practices Acts contained in their insurance laws that relate to methods of competition and acts or practices that are unfair, if such methods, acts or practices are not also deceptive. Nonetheless, state antitrust and state unfair practice laws which apply to commerce generally are applicable and are not preempted by the federal law.

- F. Examination Regarding Financial Condition. Any risk retention group must submit to an examination by the commissioner to determine its financial condition if the commissioner of the jurisdiction in which the group is chartered and licensed has not initiated an examination or does not initiate an examination within sixty (60) days after a request by the commissioner of this state. Any such examination shall be coordinated to avoid unjustified repetition and conducted in an expeditious manner and in accordance with the NAIC's Examiner Handbook.

**Drafting Note:** A provision regarding submission to examination by the nondomiciliary state was included in the Product Liability RRA 1981. However, it was modified to eliminate the requirement that the commissioner had "reason to believe" the risk retention group was in a financially impaired condition. This deletion gives the commissioner greater latitude in requiring the group to submit to an examination.

- G. Notice to Purchasers. Every application form for insurance from a risk retention group, and every policy (on its front and declaration pages) issued by a risk retention group, shall contain in ten (10) point type the following notice:

**NOTICE**

**This policy is issued by your risk retention group. Your risk retention group may not be subject to all of the insurance laws and regulations of your state. State insurance insolvency guaranty funds are not available for your risk retention group.**

**Drafting Note:** A provision regarding the notice to purchasers concerning the limitation of regulatory oversight of risk retention groups and the lack of insolvency guaranty fund protection was added by RRA 1986. The purpose is to allow the states to require minimal disclosure to consumers.

- H. Prohibited Acts Regarding Solicitation or Sale. The following acts by a risk retention group are hereby prohibited:

- (1) The solicitation or sale of insurance by a risk retention group to any person who is not eligible for membership in such group; and
- (2) The solicitation or sale of insurance by, or operation of, a risk retention group that is in hazardous financial condition or financially impaired.

**Drafting Note:** The provision regarding the prohibition of solicitation or sale of insurance by the risk retention group to any person who is not eligible for membership or by a group that is in hazardous financial condition or financially impaired was included in RRA 1986 for the purpose of enhancing state regulatory authority. These provisions have not been included in state insurance codes due to the limitation on the coverages permissibly offered under the Product Liability RRA 1981. This provision is not intended to limit those acts against which a commissioner can take action but rather to expand those acts by identifying acts that would not have been violations of the law prior to the passage of RRA 1986.

- I. Prohibition on Ownership by an Insurance Company. No risk retention group shall be allowed to do business in this state if an insurance company is directly or indirectly a member or owner of such risk retention group, other than in the case of a risk retention group all of whose members are insurance companies.

**Drafting Note:** The prohibition on ownership by an insurance company of a risk retention group was added by RRA 1986 for the purpose of limiting the involvement of fully regulated insurance companies in risk retention groups. The states should also amend the appropriate licensing law applying to authorized insurers to include a similar prohibition. The Congress believed that this was a method to avoid the possibility that fully regulated companies would choose the Risk Retention Act as a vehicle to avoid full regulation.

- J. Prohibited Coverage. The terms of any insurance policy issued by any risk retention group shall not provide, or be construed to provide, coverage prohibited generally by statute of this state or declared unlawful by the highest court of this state whose law applies to such policy.

**Drafting Note:** The provision regarding prohibited coverages was added by RRA 1986 for the purpose of enabling a state to regulate the coverages that could be offered within its borders. The Congress believed that this was a matter of public policy to be determined by each state.

- K. Delinquency Proceedings. A risk retention group not chartered in this state and doing business in this state shall comply with a lawful order issued in a voluntary dissolution proceeding or in a delinquency proceeding commenced by a state insurance commissioner if there has been a finding of financial impairment after an examination under Section 4F of this Act.

- L. Penalties. A risk retention group that violates any provision of this Act will be subject to fines and penalties including revocation of its right to do business in this state, applicable to licensed insurers generally.
- M. Operation Prior to Enactment of this Act. In addition to complying with the requirements of this section, any risk retention group operating in this state prior to enactment of this Act shall, within thirty (30) days after the effective date of this Act, comply with the provision of Subsection A(1) of this section.

**Drafting Note:** A risk retention group which qualifies under the grandfather provision contained in Section 2K(3)(b) is exempt from Subsection M above, so long as it only offers product liability or completed operations coverage.

## **Section 5. Compulsory Associations**

- A. No risk retention group shall be required or permitted to join or contribute financially to any insurance insolvency guaranty fund, or similar mechanism, in this state, nor shall any risk retention group, or its insureds or claimants against its insureds, receive any benefit from any such fund for claims arising under the insurance policies issued by a risk retention group.
- B. When a purchasing group obtains insurance covering its members' risks from an insurer not authorized in this state or a risk retention group, no such risks, wherever resident or located, shall be covered by any insurance guaranty fund or similar mechanism in this state.
- C. When a purchasing group obtains insurance covering its members' risks from an authorized insurer, only risks resident or located in this state shall be covered by the state guaranty fund subject to [insert appropriate reference to Insurance Law].
- D. (OPTIONAL) Notwithstanding [insert appropriate references to JUA provisions], the commissioner may require or exempt a risk retention group from participation in any mechanism established or authorized under the law of this state for the equitable apportionment among insurers of liability insurance losses and expenses incurred on policies written through such mechanism, and such risk retention group shall submit sufficient information to the commissioner to enable the commissioner to apportion on a nondiscriminatory basis the risk retention group's proportionate share of such losses and expenses.

**Drafting Note:** Product Liability RRA Section 3(a)(2) specifically exempts risk retention groups from participation in the state guaranty fund. Section 3(a)(1)(C) of RRA 1986 permits a state to require that a risk retention group participate in JUAs or similar mechanisms on a nondiscriminatory basis. In making such a determination, each state should take into account the different considerations which are applicable to JUAs and to assignments under assigned risk plans, respectively, as well as to the impact on the financial condition of risk retention groups.

## **Section 6. Countersignatures not Required**

A policy of insurance issued to a risk retention group or any member of that group shall not be required to be countersigned as otherwise provided in Section [insert reference] of the Insurance Code.

**Drafting Note:** Product Liability RRA Section 3(a)(3) preempts the states from requiring policies to be countersigned by resident agent or brokers. This section is optional depending on states' existing countersignature laws.

## **Section 7. Purchasing Groups—Exemption from Certain Laws**

A purchasing group and its insurer or insurers shall be subject to all applicable laws of this state, except that a purchasing group and its insurer or insurers shall be exempt, in regard to liability insurance for the purchasing group, from any law that would:

- A. Prohibit the establishment of a purchasing group;
- B. Make it unlawful for an insurer to provide or offer to provide insurance on a basis providing, to a purchasing group or its members, advantages based on their loss and expense experience not afforded to other persons with respect to rates, policy forms, coverages or other matters;
- C. Prohibit a purchasing group or its members from purchasing insurance on a group basis described in Subsection B of this section;
- D. Prohibit a purchasing group from obtaining insurance on a group basis because the group has not been in existence for a minimum period of time or because any member has not belonged to the group for a minimum period of time;
- E. Require that a purchasing group must have a minimum number of members, common ownership or affiliation, or certain legal form;
- F. Require that a certain percentage of a purchasing group must obtain insurance on a group basis;
- G. Otherwise discriminate against a purchasing group or any of its members; or
- H. Require that any insurance policy issued to a purchasing group or any of its members be countersigned by an insurance agent or broker residing in this state.

**Drafting Note:** RRA 1986 establishes that the scope of the exemption from state law for risk retention groups is greater than that for purchasing groups. RRA 1986 in Section 3 states that a risk retention group is exempt from the laws of non-chartering states and then specifies those powers which are retained by those states. In regard to purchasing groups, however, Section 4 of RRA 1986 specifically lists those laws from which a purchasing group is exempt and which are in the nature of prohibiting or otherwise discriminating against purchasing groups. Therefore, a state can apply all other provisions of its laws to purchasing groups and persons dealing with purchasing groups. As noted in regard to risk retention groups, if a purchasing group does not meet any of the criteria specified to define it as a purchasing group, it does not benefit from any federal preemption of state law and all state laws apply.

## **Section 8. Notice and Registration Requirements of Purchasing Groups**

- A. A purchasing group which intends to do business in this state shall, prior to doing business, furnish notice to the commissioner which shall, on forms prescribed by the NAIC:
  - (1) Identify the state in which the group is domiciled;
  - (2) Identify all other states in which the group intends to do business;
  - (3) Specify the lines and classifications of liability insurance which the purchasing group intends to purchase;
  - (4) Identify the insurance company or companies from which the group intends to purchase its insurance and the domicile of such company;



- (5) Specify the method by which, and the person or persons, if any, through whom insurance will be offered to its members whose risks are resident or located in this state;
  - (6) Identify the principal place of business of the group; and
  - (7) Provide such other information as may be required by the commissioner to verify that the purchasing group is qualified under Section 2J of this Act.
- B. A purchasing group shall, within ten (10) days, notify the commissioner of any changes in any of the items set forth in Subsection A of this section.

**Drafting Note:** The notice provisions regarding purchasing groups are designed to require that purchasing groups provide adequate information to the commissioner so that an evaluation can be made as to whether a purchasing group is (a) bona fide and (b) is likely to operate in a manner and to purchase insurance coverage that is consistent with the laws of the state.

- C. The purchasing group shall register with and designate the commissioner (or other appropriate authority) as its agent solely for the purpose of receiving service of legal documents or process, for which a filing fee shall be determined by the commissioner, except that such requirements shall not apply in the case of a purchasing group which only purchases insurance that was authorized under the federal Products Liability Risk Retention Act of 1981, and:
  - (1) Which in any state of the United States
    - (a) Was domiciled before April 1, 1986; and
    - (b) Is domiciled on and after October 27, 1986;
  - (2) Which
    - (a) Before October 27, 1986 purchased insurance from an insurance carrier licensed in any state; and
    - (b) Since October 27, 1986 purchased its insurance from an insurance carrier licensed in any state; or
  - (3) Which was a purchasing group under the requirements of the Product Liability Risk Retention Act of 1981 before October 27, 1986.
- D. Each purchasing group that is required to give notice pursuant to Subsection A of this section shall also furnish such information as may be required by the commissioner to:
  - (1) Verify that the entity qualifies as a purchasing group;
  - (2) Determine where the purchasing group is located; and
  - (3) Determine appropriate tax treatment.

- E. Any purchasing group which was doing business in this state prior to the enactment of this Act shall, within thirty (30) days after the effective date of this Act, furnish notice to the commissioner pursuant to the provisions of Subsection A of this section and furnish such information as may be required pursuant to Subsections B and C of this section.

**Drafting Note:** The provision regarding registering with and designating the commissioner as legal agent is designed to allow the commissioner to take prompt legal action against the purchasing group by facilitating proper legal service of process. The purchasing groups “grandfathered” out of this registration requirement are only those that were prior to April 1986, and continue to be, domiciled in one of the United States, that purchase insurance only from U.S. carriers, that qualified as a purchasing group under the Product Liability Risk Retention Act of 1981, and that do not currently purchase insurance other than that authorized under the Product Liability RRA 1981.

## **Section 9. Restrictions on Insurance Purchased by Purchasing Groups**

- A. A purchasing group may not purchase insurance from a risk retention group that is not chartered in a state or from an insurer not admitted in the state in which the purchasing group is located, unless the purchase is effected through a licensed agent or broker acting pursuant to the surplus lines laws and regulations of such state.

**Drafting Note:** Although Section 4(f) of RRA was one of the most significant provisions dealing with regulation of insurance purchased by purchasing groups, the term “located” was not defined in the federal act.

- B. A purchasing group which obtains liability insurance from an insurer not admitted in this state or a risk retention group shall inform each of the members of the group which have a risk resident or located in this state that the risk is not protected by an insurance insolvency guaranty fund in this state, and that the risk retention group or insurer may not be subject to all insurance laws and regulations of this state.

**Drafting Note:** This provision, with respect to non-admitted insurers, applies only if a state requires this notice to policyholders in the state with respect to other insurers not covered by insurance insolvency guaranty funds.

- C. No purchasing group may purchase insurance providing for a deductible or self-insured retention applicable to the group as a whole; however, coverage may provide for a deductible or self-insured retention applicable to individual members.
- D. Purchases of insurance by purchasing groups are subject to the same standards regarding aggregate limits which are applicable to all purchases of group insurance.

**Drafting Note:** A state may prescribe limitations with respect to aggregate limits to all purchases of group insurance, as long as such limitations are not applied in a manner which discriminates against purchasing groups.

## **Section 10. Purchasing Group Taxation**

Premium taxes and taxes on premiums paid for coverage of risks resident or located in this state by a purchasing group or any members of the purchasing groups shall be:

- A. Imposed at the same rate and subject to the same interest, fines and penalties as that applicable to premium taxes and taxes on premiums paid for similar coverage from a similar insurance source by other insureds; and

Paid first by such insurance source, and if not by such source by the agent or broker for the purchasing group, and if not by such agent or broker then by the purchasing group, and if not by such purchasing group then by each of its members.

**Drafting Note:** The term “insurance source” refers to admitted, licensed and authorized carriers on the one hand and non-admitted, surplus line carriers on the others. The enacting states may wish to include applicable taxing provisions of its Code.

## **Section 11. Administrative and Procedural Authority Regarding Risk Retention Groups and Purchasing Groups**

The commissioner is authorized to make use of any of the powers established under the Insurance Code of this state to enforce the laws of this state not specifically preempted by the Risk Retention Act of 1986 including the commissioner’s administrative authority to investigate, issue subpoena, conduct depositions and hearings, issue orders, impose penalties and seek injunctive relief. With regard to any investigation, administrative proceedings or litigation, the commissioner can rely on the procedural laws of this state. The injunctive authority of the commissioner, in regard to risk retention groups, is restricted by the requirement that any injunction be issued by a court of competent jurisdiction.

**Drafting Note:** This provision regarding the administrative and procedural authority retained by the states under Sections 3(f) and 4(g) of RRA 1986 is designed to permit the commissioner to investigate for potential hazardous financial condition or market conduct abuses and to take appropriate action where necessary. It clarifies that no federal preemption takes place regarding the procedural and administrative authority of the commissioner.

However, RRA 1986 requires that any injunction sought by the commissioner must be obtained from a court of competent jurisdiction. See RRA 1986 Section 3(a)(1)(G), Section 3(e), and Section 3(f). However, this restriction on the injunctive authority of the commissioner does not carry over to any action that the commissioner may take under its state administrative procedural law regarding purchasing groups. Section 4 of RRA 1986, which addresses the limited preemption from state law provided to purchasing groups, does not refer to any restriction on the commissioner’s injunctive authority. More specifically, the “savings clause” regarding state authority, RRA Section 4(g), makes no mention of such requirement.

## **Section 12. Duty of Agents or Brokers to Obtain License**

### **A. Risk retention groups.**

- (1) No person, firm, association or corporation shall act or aid in any manner in soliciting, negotiating or procuring liability insurance in this state from a risk retention group unless such person, firm, association or corporation is licensed as an insurance agent or broker in accordance with Section [insert appropriate reference to Insurance Law].

### **B. Purchasing groups.**

- (1) No person, firm, association or corporation shall act or aid in any manner in soliciting, negotiating or procuring liability insurance in this state for a purchasing group from an authorized insurer or a risk retention group chartered in a state unless such person, firm, association or corporation is licensed as an insurance agent or broker in accordance with Section [insert appropriate reference to Insurance Law].
- (2) No person, firm, association or corporation shall act or aid in any manner in soliciting, negotiating or procuring liability insurance coverage in this state for any member of a purchasing group under a purchasing group’s policy unless such person, firm, association or corporation is licensed as an insurance agent or broker in accordance with Section [insert appropriate reference to Insurance Law].

- (3) No person, firm, association or corporation shall act or aid in any manner in soliciting, negotiating or procuring liability insurance from an insurer not authorized to do business in this state on behalf of a purchasing group located in this state unless such person, firm, association or corporation is licensed as a surplus lines agent or excess line broker in accordance with [insert appropriate reference to Insurance Law].

**Drafting Note:** The RRA (1986) does not preempt state law with respect to licensing and regulation of agents and brokers, with the exception of the elimination of the residence requirement and of countersignature laws, as provided in Subsection C of this section, and Sections 6 and 7H of this Act.

- C. For purposes of acting as an agent or broker for a risk retention group or purchasing group pursuant to Subsections A and B of this section, the requirement of residence in this state shall not apply.
- D. Every person, firm, association or corporation licensed pursuant to the provisions of [insert appropriate references to Insurance Law], on business placed with risk retention groups or written through a purchasing group, shall inform each prospective insured of the provisions of the notice required by Subsection G of Section 4 of this Act in the case of a risk retention group and Subsection B of Section 9 of this Act in the case of a purchasing group.

### **Section 13. Binding Effect of Orders Issued in U.S. District Court**

An order issued by any district court of the United States enjoining a risk retention group from soliciting or selling insurance, or operating in any state (or in all states or in any territory or possession of the United States) upon a finding that such a group is in hazardous financial or financially impaired condition shall be enforceable in the courts of the state.

### **Section 14. Rules and Regulations**

The commissioner may establish and from time to time amend such rules relating to risk retention groups as may be necessary or desirable to carry out the provisions of the Act.

### **Section 15. Severability**

If any clause, sentence, paragraph, section or part of this act or the application thereof to any person or circumstances, shall, for any reason, be adjudged by any court of competent jurisdiction to be invalid, such judgement shall not affect, impair or invalidate the remainder of this act, and the application thereof to other persons or circumstance, but shall be confined in its operation to the clause, sentence, paragraph, section or part thereof directly involved in the controversy in which such judgement shall have been rendered and to the person or circumstances involved.

## Section 16. Effective Date

This Act will be effective on [insert date].

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*Chronological Summary of Actions (all references are to the Proceedings of the NAIC).*

*1983 Proc. I 6, 35, 789-790, 795, 799-805 (adopted).*

*1987 Proc. I 11, 20, 744, 857-865 (amended and reprinted).*

*1987 Proc. II 15, 24, 774-775, 776-788 (amended).*

*1991 Proc. II 25, 58, 976, 992-1003 (amended and reprinted)*

*2011 Proc. 3<sup>rd</sup> Quarter Vol. I 114, 119, 132-134, 339 (amended).*

*2022 (technical edit).*