

# The ABC's of RPG's

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# Risk Retention Act

History: In order to solve the lack of availability and affordability of liability insurance

Product Liability Risk Retention Act of 1981 (Public Law 97-45)

Liability Risk Retention Act (Public Law 99-563; 15 U.S.C. 3901-3906, 1981, as Amended 1986)

# Risk Retention Act cont.

The concept of Purchasing Groups and Risk Retention Groups:

- PURCHASING GROUPS (PGs): Groups of policyholders who purchase prescribed liability insurance from a commercial insurer or a Risk Retention Group
- RISK RETENTION GROUPS (RRGs): Group captives licensed in one state underwriting prescribed liability insurance

# Risk Retention Act cont.

Both PGs and RRGs must comply with the following criteria:

- Membership must be homogenous
- Scope of insurance is limited to commercial liability, auto or general, but excluding workers' compensation and property

Any business, including non-profit, or public entity is eligible; but can't be owned by an insurance company

# Risk Retention Act

## State Regulation

### Risk Retention Groups:

- Only subject to those state provisions specified in the Act

### Purchasing Groups:

- Only exempt from those state provisions specified in the Act

# Risk Retention Act

## Risk Retention Groups

- A RRG must be chartered and licensed in a state or the District of Columbia
- Except for the chartering state:
  - A RRG is exempt from any state law, rule or regulation that would regulate or make a RRG unlawful, except that any state may require a RRG to:
    - Comply with unfair claims settlement practices
    - Pay applicable premium or surplus lines taxes
    - Participate in a proportional insurance mechanism
    - Register for legal service
    - Submit to financial examination if the chartering state has not initiated such an exam
    - Comply with lawful orders for delinquency or dissolution proceedings
    - Comply with deceptive, false or fraudulent regulatory act prohibition
    - Company with injunction for hazardous financial condition
    - Comply with a prescribed notice in 10 point type advising the insured of no guaranty fund coverage and preemption of many non-domiciliary state consumer protections

# Risk Retention Act

## Purchasing Groups

- Unlike RRGs, PGs are groups of insurance buyers who:
  - Retain no risk
  - Purchase liability insurance from admitted or surplus lines insurers
- State preemptions are limited to prohibitions against:
  - Establishment of a PG
  - Limitations imposed by state fictitious group laws
  - Requirements imposed by state countersignature laws
  - Discrimination against a PG or any of its members
  - Discrimination against nonresident agents

# Risk Retention Act

## Purchasing Groups cont.

- PGs need not be incorporated, but mostly generally are, often under state not-for-profit corporation status
- More than one insurance carrier may insure a PG



# Risk Retention Act

## State Regulation of Purchasing Groups

- States have wider latitude under the Act as to information required for PG registration
- A state may require that the PG insurer be admitted or an eligible surplus lines insurer in the state
- A state may impose its surplus lines laws on a PG transaction involving an eligible surplus lines insurer

# Risk Retention Act

## State Regulation of Purchasing Groups cont.

- The premium tax rate applicable to PG depends upon the status of its insurer as either an admitted or surplus lines carrier in the state of the policyholder
- A state may require form and rate review of coverage offered by a PG insurer

# The RPG Process

- Form an association
  - usually a nonprofit corporation
  - create corporate documents, including by-laws
  - file certificate of incorporation
- Appoint a manager of the RPG
  - often managed by a PA / MGA / MGU
- Register RPG with insurance commissioner in each state
  - list of all insurers and status as admitted / non-admitted
  - manager must be appointed by each carrier in each state
  - pay fees

# Time & Expense

- Initial set up for 50 states: 75-100 hours
  - Based on an experienced person who understands the process
  - 25-50 hours to establish in domiciled state
  - 1 – 1.5 hours per state to file
- Expenses:
  - Hourly labor cost (internal or hired legal)
  - State fees: \$350 - \$750 - \$2,000 initially
    - Renewal fees \$0 to \$400 annually
    - About half the states require renewal fee

# Purpose & Benefits

- Purpose must include more than buying insurance at a cheaper price
  - Risk management and safety
- Must consider RPG loss experience in insurance offering
- Must provide for economies of scale

# Benefits

- Master Policy – named insured is the RPG
  - Consistent insurance solution for similar entities
- Declinations for group can be used to satisfy diligent search (E&S) for all members
- Protection of proprietary rates and forms
  - Can be developed specifically for the RPG
  - Access to RPG is restricted; must go through manager (PA, MGA, MGU)
  - Insulates from non-program poaching of proprietary “stuff”
- Protects program investment by PA, MGA, MGU

# Drawbacks

- Paperwork – registering and filing with each state
- Expenses – fees & cost of preparing paperwork
- No protection from IGA
- Still must comply with most of the state regs
- Liability only – does not apply to property or other first party coverages
- Shared group aggregates
- Cannot use NY FTZ with RPG

## SUMMARY

### States' Reaction to LRRRA

- Negative – Act infringed on their Regulatory Jurisdiction
- Response – Required much more info and deliberate steps than Congress intended
- Registration Process - States seized this LRRRA requirement
  - Changed a simple Four Item registration into a cumbersome licensing process.
  - Developed lengthy standardized NAIC Registration Form
  - Some states have their own forms with even more requirements, e.g. FL, NJ, TX
  - Introduced costly registration fees with annual renewal fees in many states
- Most of the States' requirements serve no public purpose
- Creation of Federal Insurance Office in Dodd-Frank Act remains to be seen how much it will impact State Regulators.
- Otherwise, LRRRA will not be amended anytime soon - Congress has other concerns
- State Regulations/Bureaucracy could Imperil U.S. consumers in the event of another hard market crisis like the mid 1980's

**LRRRA 26 Years Later – Valuable or Not?** - Despite the increasing States' requirements, the TMPAA Panel concluded LRRRA to be very valuable. To support this sentiment, the Panel discussed that in 2012 there are estimated to be 775 RPG's and 255 RRG's and both numbers continue to rise in recent years.

- Advantages for RPG Members
  - Lower premiums
  - Broader coverage
  - Tailored coverage
  - Higher limits
  - Voice - representation on RPG Board and/or crafting of By-Laws
  - Risk Management
  - Dividends
  - Open the door to other coverage lines
  - Spring board to RRG or other Group Captive solutions
- Advantages for Brokers/MGA's
  - Stronger value proposition for Insureds
  - More efficient placement
  - Provides protection for proprietary products when the Program is filed as an RPG Product
  - Easier to form than RRG's
  - Removes state countersignature requirements
  - Non admitted diligent search requirement process easier by aggregating to the RPG as a Group either nationally or by state but not by insured.
  - Enables sale of other product lines to Group
  - Able to charge a fee per policy to offset registration costs and then some



- RPG's can be a starting place to develop more creative benefits for Group
  - Powerful marketing vehicle
  - Yet another strategy to survive in prolonged soft market
  - Advantages for Insurers
    - Lower acquisition costs
    - Lower premiums/more competitive
    - Better spread of business
    - More critical mass
    - Higher hit ratios/renewal retentions
    - Can legally utilize Master Policy approach
    - Quicker process to launch Programs
    - Can lead to RRG – allows more time, less regulations and stay involved on long term basis as reinsurer
    - Non Admitted easier – decertification process in the admitted market can be obtained for the RPG as a whole or at least by state, not by member policy (more of a benefit to the MGA/ Program Administrator but also beneficial to Insurer).
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### **Panel Discussion Questions**

**Question 1** - Are both RRG's and RPG's not protected by the State Guaranty Funds?

**Answer** – The members of the RPG (the insureds) will be protected by State Guaranty Funds if the insurer for the RPG is an admitted carrier; contrarily if the insurer for the RPG is a surplus lines carrier or RRG, then there will be no State Guaranty Fund protection. Thus this issue is entirely determined by the license status of the insurer. The fact that a RPG is employed is irrelevant.

**Question 2** – Does the new Surplus Lines ruling that allows for the taxes to be determined by the state of the principal place of business apply to RPG's written with non admitted insurers to their state of domicile? Or are taxes on non admitted RPG's determined by each RPG member's state?

**Answer** – Again, the use of a RPG is irrelevant to the analysis. If a surplus lines carrier is the insurer, then the "NRRRA" in Dodd-Frank requires the surplus lines broker to pay the surplus lines tax to the "Home State" of the insured at the rate of tax of that state. The "Home State" of the RPG will be irrelevant for NRRRA purposes. "Home State" is defined as the corporate headquarters state (if there is one); if not, then the state where the preponderance of the risk is located. It is the "Home State" of the insured that matters. RRG's are expressly exempt from this requirement in the Law. Whether a captive that is not a surplus lines carrier and not a RRG is subject to the NRRRA requirement is the topic of a vigorous debate and certainly not decided by any court.

**Question 3** – Does the LRRRA preclude RPG’s from having to file rates and forms according to the requirements and regulations of the state insurance departments?

**Answer** – The formation of a RPG does not release the insurer from the filing requirements and regulations of a state. All forms and rates must conform to state law. This also means that a multi-state RPG issued on a master policy must have forms and rates filed in every state in which certificates of participation are issued to RPG members from the master policy. However, it is our experience that when filing the RPG with the various states, only a few states will ask to see the actual policy or certificate.

**Question 4** – If a RPG is formed in Washington D.C. for a governmental entity (including municipalities), are there any tax advantages?

**Answer** – We are not aware of any tax advantages to the RPG unless the RPG was to qualify as a “CAPCO” which means an investor in D.C. Since the RPG is not likely to make a profit, we do not see any advantage. We know no rule exempting the RPG’s insurer from premium tax. Of course, the governmental entities will not pay income tax anyway.