# Department of Legislative Services

Maryland General Assembly
2018 Session

## FISCAL AND POLICY NOTE
### Third Reader - Revised

Senate Bill 78 (Chair, Finance Committee)(By Request - Departmental - Maryland Insurance Administration)

Finance Economic Matters

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**Insurance - Risk Retention Groups - Revisions**

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This departmental bill adopts changes to the Model Risk Retention Act developed by the National Association of Insurance Commissioners (NAIC). The bill enhances the regulatory framework that governs the formation and operation of risk retention groups (RRG) chartered in the State, including establishing additional governance standards for RRGs; financial and legal audit requirements; and ethics requirements for RRG directors, officers, and employees.

## Fiscal Summary

**State Effect:** Although there are currently no RRGs chartered in the State, the Maryland Insurance Administration (MIA) can handle the bill's enhanced oversight requirements using existing resources if any RRGs charter in the State in future years.

**Local Effect:** None.

**Small Business Effect:** MIA has determined that this bill has minimal or no impact on small business (attached). The Department of Legislative Services concurs with this assessment. (The attached assessment does not reflect amendments to the bill.)

# Analysis

**Bill Summary:**

*Board of Directors' Requirements and Responsibilities*

The board of directors of an RRG must have a majority of independent directors. A director is independent when the board determines he or she has no material relationship with the RRG. The bill specifies the circumstances that constitute a material relationship to an RRG, which generally involves receiving financial compensation or payments from the RRG. A person that is an owner of (or officer, director, or employee of the owner) or subscriber in the RRG is considered independent unless some other position constitutes a material relationship. The RRG must annually disclose its board's determinations to the Insurance Commissioner.

The board must adopt a written policy in its plan of operation that requires the board to (1) assure that all owners and insureds of the RRG receive evidence of their ownership; (2) develop governance standards for the RRG; (3) oversee the evaluation of the RRG's management; (4) review and approve the amount to be paid for all material service providers; and (5) annually review and approve the RRG's goals and objectives, the officers' and service providers' performance, and the continued engagement of the officers and material service providers.

The board must adopt governance standards for its own operations. The standards must include, among other things, (1) a process by which directors are elected; (2) director qualifications; and (3) director responsibilities. The standards must be disclosed by electronic means (such as on the RRG's website) and on the request of members and insureds.

The board must adopt a code of business conduct and ethics to be followed by directors, officers, and employees of the RRG. The code must include provisions that address, among other things, (1) conflicts of interest; (2) confidentiality; and (3) fair dealing. The code must be disclosed by electronic means (such as on the RRG's website) and on the request of members and insureds.

The captive manager and president or chief executive officer of the RRG must promptly notify the Commissioner if they become aware of any material noncompliance with any of these governance standards and requirements.

*Required Audits*

Each RRG must have an audit committee composed of at least three independent board members; however, the Commissioner may waive this requirement if the RRG demonstrates that it is impractical to establish such a committee and the board can otherwise accomplish the purposes of the committee. A nonindependent board member may assist with the committee if invited to do so by the committee, but may not be on the committee. The audit committee must have a written charter. The bill enumerates the responsibilities of the committee, including (1) assisting the board with oversight of financial statements and compliance with legal and regulatory requirements; (2) discussing audited financial statements; and (3) setting hiring policies for the RRG.

*Service Provider Requirements and Responsibilities*

The bill specifies the persons and individuals that are considered service providers and prohibits an RRG from entering into a service provider contract that involves a material relationship unless the RRG notifies the Commissioner at least 30 days in advance and the Commissioner does not disapprove the transaction. The bill also establishes new requirements and limitations for material service provider contracts. A contract is material if the amount of the contract is the greater of (1) 5% of the RRG's annual gross written premium or (2) 2% of its surplus.

*Other Provisions*

If an RRG is a reciprocal, meaning it is managed by an attorney, the attorney must adhere to the same independence of operation and governance standards imposed on an RRG's board or advisory committee. In that case and to the extent possible, service providers must contract with the RRG and not the attorney.

The bill increases the timeframe for an RRG chartered outside of Maryland to submit a copy of any material revision to its plan of operation or feasibility study to the State's Insurance Commissioner. Specifically, a revision of the plan or study must be submitted within 30 days after it is approved by the RRG's chartering state or, if approval is not required by that state, within 30 days after the revision is filed.

**Current Law:**

*Risk Retention Groups Chartered in Maryland*

In order to be chartered in Maryland, an RRG must be licensed as a liability insurance company in conformance with all insurance laws and regulations. When applying for a charter, an RRG must provide specified information to the Commissioner, which must be forwarded to NAIC. Before offering insurance in any state, the RRG must submit a plan of operation or feasibility study to the Commissioner for approval. Any changes to the plan or study must be submitted within 10 days, and the RRG may not offer additional lines of liability insurance in any state until the revision is approved.

*Risk Retention Groups Chartered in Other States*

Before an RRG chartered in another state offers insurance in Maryland, the RRG must submit to the Insurance Commissioner (1) specified information to ensure that the RRG is actually an RRG; (2) a copy of the RRG's plan of operation or feasibility study; (3) a statement of registration designating the Commissioner as its agent for service of legal process; (4) a specified financial statement; (5) a copy of each examination of the RRG; (6) if requested by the Commissioner, a copy of any information or document related to an outside audit of the RRG; and (7) any other information the Commissioner requires to verify the continuing qualification of the RRG.

If an RRG revises its plan of operation or feasibility study, a copy of the revision must be submitted to the Commissioner at the same time that the revision is submitted to the commissioner of the RRG's chartering state.

**Background:** There are currently no RRGs chartered in Maryland.

MIA advises that NAIC adopted changes to its Model Risk Retention Act (which governs RRGs) in 2011. The purpose of the changes was to expand state oversight of RRGs. The bill implements those changes to ensure MIA's continued accreditation as a qualifying examination agency through NAIC.

An RRG is a liability insurance company that is owned by the people it insures; a person who purchases insurance from an RRG is also purchasing an ownership share in that RRG. RRG insurers were created by the federal Product Liability Risk Retention Act of 1981 to allow a form of "self-insurance" for businesses that found it difficult to obtain traditional insurance. The act was broadened to include commercial liability under the Liability Risk Retention Act of 1986.

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## Additional Information

**Prior Introductions:** None.

**Cross File:** None.

**Information Source(s):** Maryland Insurance Administration; National Association of Insurance Commissioners; National Risk Retention Association; Department of Legislative Services

**Fiscal Note History:** First Reader - January 10, 2018
md/jc Third Reader - March 17, 2018
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**ANALYSIS OF ECONOMIC IMPACT ON SMALL BUSINESSES**

**TITLE OF BILL:** **Insurance –Risk Retention Groups – Revisions**

**BILL NUMBER:** **SB 78**

**PREPARED BY:**
**(Dept./Agency)** **Maryland Insurance Administration**

**PART A. ECONOMIC IMPACT RATING**

This agency estimates that the proposed bill:

__X__ WILL HAVE MINIMAL OR NO ECONOMIC IMPACT ON MARYLAND SMALL BUSINESS

OR

____ WILL HAVE MEANINGFUL ECONOMIC IMPACT ON MARYLAND SMALL BUSINESSES

**PART B. ECONOMIC IMPACT ANALYSIS**

Maryland adopted the National Association of Insurance Commissioners' ("NAIC") Model Act #705 "Model Risk Retention Act" in 1996. The Model Act provides the regulatory framework for the formation and operation of risk retention groups and purchasing groups formed pursuant to the federal Liability Risk Retention Act of 1986 ("RRA 1986"). In 2011, the NAIC adopted changes to the Model Act to include further oversight of risk retention groups. This proposal incorporates those changes including governance standards for the board of directors, written policies for plans of operations, auditing, written disclosures, business conduct and ethical standards.