STATE LEGISLATIVE BRIEF

The Model Risk Retention Act

- *In part due to a 2005 GAO report criticizing regulation of risk retention groups (RRGs), the NAIC in 2011 adopted revisions to the Model Risk Retention Act (#705), creating corporate governance standards for RRGs.*
- *The new corporate governance standards were designed to ensure that RRGs implement and operate with effective risk management and internal controls.*
- *The corporate governance revisions to the Model Risk Retention Act became an accreditation standard on Jan. 1, 2017 for jurisdictions that charter RRGs.*

Background

A risk retention group, or RRG, is a corporation or limited liability association formed under the laws of a state for the primary purpose of assuming liability exposures on behalf of its members. RRGs serve as an alternative to the traditional commercial insurance carrier. Members of the group must be engaged in similar activities or have similar liability exposures by virtue of a related or common business. All insureds of an RRG must be owners of the RRG, and all owners of the RRG but be insureds. Congress authorized the creation of RRGs in the 1980s with the passage of the Liability Risk Retention Act (LRRA) in order to increase the availability and affordability of commercial liability insurance. The Act allows RRGs to write various forms of commercial liability insurance. Unlike a traditional insurer that must be licensed in every state in which it does business, an RRG is domiciled in one state but may do business in any other state by completing a registration process.

In 2005, a GAO report found that RRGs can be operated in ways that do not consistently protect the best interests of their insureds. The report called for uniform corporate governance standards that would establish the insureds' authority over outside management companies, who typically run RRGs.

Spurred on by the report's findings, the NAIC began developing corporate governance revisions to the *Model Risk Retention Act*. The purpose of the corporate governance standards is to ensure that insurers implement and operate within effective risk management and internal controls systems, including determining the level of internal economic capital that should be held for solvency purposes.

The standards allow a state insurance department to compel an RRG to comply with various corporate governance requirements related to the board of directors, service provider contracts, a written plan of operation, the audit committee, disclosure of governance standards, and business conduct and ethics. RRGs have one year from the passage of the model to comply with the new requirements and any newly formed RRGs have to be in compliance at the time of licensure. The revisions were subsequently adopted by the NAIC in December, 2011 and became an accreditation standard on Jan. 1, 2017 for jurisdictions that charter RRGs.

Key Points

- ✓ To date, 19 states (AL, AZ, AR, CA, CO, CT, DE, HI, IL, KY, ME, MT, NE, NV, NC, SC, TN, UT, and VT) and DC have adopted the model act.
- ✓ Industry has been largely supportive of the NAIC's work concerning corporate governance requirements.
- ✓ The purpose of the corporate governance standards is to ensure that insurers implement and operate within effective risk management and internal controls systems and include requirements relating to the Board of Directors, service provider contracts, plans of operations, and business conduct and ethics.
- ✓ The model allows RRGs a one year grace period for complying with the corporate governance provisions of the Act. Any RRGs formed after the model's implementation must be in compliance at the time of licensure.

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Implementation of 2011 Revisions to Model Act #705 (Corporate Governance Standards) Model Risk Retention Act – Risk Retention Groups (RRGs)

[status as of January 31, 2018]

Adopted Model #705 [20]

Action under consideration [1]

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This map represents state action or pending state action addressing the topic of the model. This map does not reflect a determination as to whether the pending or enacted legislation contains all elements of the model or whether a state meets any applicable accreditation standards.

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