Testimony of

Director Chlora Lindley-Myers

Missouri Department of Commerce and Insurance

On Behalf of the National Association of Insurance Commissioners

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Regarding:

Examining the Availability of Insurance for Nonprofits

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Chairman Clay, Vice Ranking Member Gooden, and members of the subcommittee, thank you for the invitation to testify today. My name is Chlora Lindley-Myers. I serve as the Director of the Missouri Department of Commerce and Insurance, and am also an officer of the National Association of Insurance Commissioners (NAIC).[1] I am pleased to be testifying today on the NAIC's behalf.

As state insurance regulators, our focus is on the dual objectives of protecting insurance consumers and ensuring competitive and stable markets in our states. Nonprofit organizations serve a critical role in our country and we recognize the importance of ensuring that these organizations, like all insurance consumers, have access to insurance that meets their needs. We understand some have raised concerns regarding the availability of commercial property coverage for nonprofits. They have also argued that HR 4523, the Nonprofit Property Protection Act, which allows Risk Retention Groups (RRGs) to write commercial property coverage for nonprofits and further preempts state regulatory protections for policyholders, is the appropriate mechanism for addressing such concerns. On both accounts, we respectfully disagree.

The Regulation of RRGs

By way of background, during the 1980s, the availability of liability insurance became severely restricted. As a response, in the 1981 Product Liability Risk Retention Act, subsequently amended in 1986 and known now as the Liability Risk Retention Act (LRRA), Congress authorized a narrow exception to the usual state insurance regulatory framework through the creation of RRGs. RRGs are liability insurance companies owned by their members and required to be chartered or licensed as a liability insurance company under the laws of a state. They are permitted to insure liability risks, and their members must be engaged in similar business practices and face similar liability exposures. Even though RRGs may operate in multiple states and many do, they are only required to be licensed in one, their domiciliary state. Unlike other areas of commercial insurance, the regulatory authorities of non-domiciliary states are significantly curtailed. Outside of their domiciliary state, RRGs are not subject to financial examinations unless the domiciliary state has failed or refused to examine the RRG. A non-domiciliary state's regulatory oversight is limited to requiring RRGs to comply with laws related to unfair claim settlement practices, deceptive and fraudulent acts, paying taxes, and "register[ing]" with the state to receive service of legal documents.

These limitations are significant because it means RRG policyholders in non-domiciliary states do not get the benefits of the full panoply of regulatory protections that the state insurance system normally provides, and the RRG is not subject to the more robust oversight that multiple sets of eyes can offer. This is particularly concerning as several RRGs do not even provide coverage to policyholders in their domiciliary state where they are subject to regulation. In 2018, only approximately 30% of all RRGs wrote business in their state of domicile. This means that under

[1] As part of our state-based system of insurance regulation in the United States, the National Association of Insurance Commissioners (NAIC) provides expertise, data, and analysis for insurance commissioners to effectively regulate the industry and protect consumers. The U.S. standard-setting organization is governed by the chief insurance regulators from the 50 states, the District of Columbia, and five U.S. territories. Through the NAIC, state insurance regulators establish standards and best practices, conduct peer reviews, and coordinate regulatory oversight. NAIC staff supports these efforts and represents the collective views of state regulators domestically and internationally. For more information, visit www.naic.org.

HR 4523, an RRG already subject to weaker regulatory requirements based thousands of miles away with no presence in Missouri would be able to write property coverage for Missouri policyholders, and I would have extremely limited oversight or ability to take action to protect those policyholders should anything happen. The same limitation would apply to your state's insurance commissioner and your constituents as well.

Further, while it is true all states are required to establish a baseline level of regulatory requirements for RRGs in order to obtain NAIC accreditation, those baseline standards are specifically designed for the purpose of RRG regulation. These standards specifically relate to the liability lines of business RRGs are entitled to write, are subject to the limitations in the LRRA, and, are not the same requirements utilized for admitted market regulation. In this regard, the minimum capital requirements are different, the types of assets that can be used for capital are different, the accounting systems can be different, and, as a result, the thresholds for intervention can be opaque to regulators. Essentially, because RRGs are narrowly focused on their members' liability risk, the LRRA allowed them to operate on an unlevel playing field with relaxed treatment relative to traditional commercial insurers. Expanding the lines of coverage an RRG can write, as HR 4523 would do, expands the unlevel playing field and exposes nonprofits to greater risk with fewer regulatory protections.

Historically, RRGs have also had a higher rate of insolvencies when compared to admitted carriers. Over the past ten years, RRGs entered receivership at nearly two times the failure rate of admitted carriers. In the event of an insolvency, RRG policyholders do not have the same protections as admitted carrier policyholders. In the case of an admitted carrier insolvency, the state-run guaranty fund steps in to pay outstanding claims when the failed insurer's assets are insufficient. The LRRA, however, prohibits RRGs from participating in the state guaranty fund system. Consequently, in the event of an insolvency, RRG policyholders can only collect on claims if the company has sufficient assets to pay them.

Availability of Coverage

While the passage of the LRRA may have been viewed as appropriate in the 1980's to address a widespread availability crisis, no such crisis exists today that would merit this drastic and unnecessary preemptive deregulatory legislation that would undermine policyholder protections for some of the most vulnerable consumers of the commercial insurance markets. Traditional admitted carriers do provide coverage to small and medium-sized nonprofits, albeit some offer it in the form of a full businessowner's policy (BOP) that contains both commercial liability and property coverages.

Further, state insurance departments have received few, if any, complaints from nonprofit policyholders indicating that they are unable to obtain the coverage they require. While we are aware that monoline commercial property coverage is less common, the fact that commercial property coverage for nonprofits is offered through a full businessowner's policy that contains both commercial liability and property coverages is not indicative of a market crisis. Instead, it suggests that that the bundled product is the preferred approach in the market, and that admitted carriers are now able to offer liability coverage they were unable or unwilling to do in the 1980s when the LRRA was enacted. In fact, the issue of availability was explored by this subcommittee

in 2017 and at that hearing, industry representatives provided testimony representing that nonprofits can purchase commercial property insurance in the private market and have a wide selection of insurers from which to choose.[2] As stewards of the insurance markets in our states, we are aware of no material change in market conditions today that would suggest otherwise. Proponents of this legislation have highlighted a preference, not a market in crisis worth further preemption of the state based regulatory system and erosion of policyholder protections.

Notwithstanding any questions surrounding availability, we are troubled by the idea of less-regulated RRGs providing commercial property coverage where there are more appropriate existing alternatives. First, nonprofit policyholders could seek coverage from traditional admitted market carriers and receive the robust regulatory protections that the state insurance regulatory system can offer. Second, though we strongly encourage nonprofits to seek coverage in the admitted market, in the event they are unable to obtain coverage, they could find coverage in the surplus lines market. While surplus lines regulation is admittedly different than that of the admitted market, there are greater regulatory protections for surplus lines policyholders in non-domiciliary states than those afforded to RRG policyholders. Regardless of where a surplus lines carrier is domiciled, the regulator of the policyholder's home state has authority over the placement of surplus lines insurance. For example, the policyholder's home state can sanction the surplus lines broker, revoke their license, and hold them liable for the full amount of the policy. State insurance regulators can also use their authorities under the state Unfair Trade Practices Act and similar statutes to protect insurance consumers, including ensuring that claims are paid, the insurer or broker is not misrepresenting what is in the policy, as well as remedying other bad conduct.

As for those RRGs that wish to sell commercial property coverage, we encourage them to explore converting to an admitted carrier or affiliating with one, thereby ensuring that their policyholders have access to the most robust consumer protections. While such conversion or affiliation takes time, and comes with some cost, the policyholder members of the RRG will be the beneficiaries of greater regulatory protections and a reduction in financial risk that far outweigh the burden or expense associated with such conversion or affiliation. The NAIC is aware of six RRGs that operated for at least ten years as an RRG and then converted to an admitted carrier.

Additional Concerns Regarding the Nonprofit Property Protection Act, HR 4523

In addition to the significant overarching concerns the NAIC has with RRGs writing commercial property coverage, the NAIC also has additional concerns with the Nonprofit Property Protection Act. While we appreciate that HR 4523 attempts to instill some minimum criteria that RRGs must meet to be eligible to provide property insurance, we believe the criteria are insufficient to provide the necessary regulatory protections for the most vulnerable of the commercial insured and we strongly disagree with assertions that the bill is drafted so narrowly that it would not in any way interfere with the normal function of the property and casualty market. This bill would allow RRGs to provide commercial property insurance in any state without being subject to the regulatory requirements that the state departments of insurance determined is best for its residents. It also

[2] *See* Examining Insurance for Nonprofit Organizations, Hearing Before the House of Representatives Subcomm. On Hous. and Ins., 115 Cong. (2017) (Statement of Tom Santos, American Insurance Association at 11-12, and Statements for the Record of the Independent Insurance Agents and Brokers of America at 2-4 and National Associate of Mutual Insurance Companies at 1, 4-5.)

precludes them from conducting an examination or taking action to protect policyholders in their states except in the most limited circumstances. This is a significant divergence from the normal regulatory practices of the property and casualty market. As regulators, our goal is to incentivize policyholders to obtain coverage and insurers to write in markets that have more robust regulatory protections. This legislative proposal undermines that critical objective.

HR 4523 also attempts to establish an availability test; however, the criteria used to demonstrate availability is exceedingly narrow and not a credible measure of availability. The legislation requires the state to identify three or more admitted carriers currently providing monoline businessowner's property coverage to nonprofits, and that make obtaining the coverage "easily accessible." However, in cases such as these, the relevant market for purposes of evaluating availability of a product should, along with the monoline coverages, include BOPs that bundle liability and property coverage as well as companies that may not have in-force policies but are legitimately planning to provide the coverage within a reasonable amount of time. The proposed test also appears to allow RRGs to begin writing the coverage and continue to do so in perpetuity even if the commissioner subsequently finds the coverage is available in the market by non-RRG writers.

In conclusion, we are seriously concerned that allowing RRGs to sell commercial property coverage would create more risks for the RRGs and, ultimately, their insureds. The limited oversight of non-domiciliary states in the RRG regulatory framework, coupled with the lack of state-run guaranty fund protection and increased risk of insolvencies associated with RRGs, could expose nonprofit organizations and those who rely upon them to unnecessary risks. We encourage any nonprofit policyholders that have difficulties with obtaining property coverage to contact their state insurance regulators so that we can seek to address such issues through appropriately tailored state-based regulatory solutions as we do with all other lines of insurance. We appreciate your consideration of our views and thank you for the opportunity to testify today.