



Statement of
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On Behalf of the
National Association of Mutual Insurance Companies
to the
United States House
Committee on Financial Services
Subcommittee on Community Development, Housing, and Insurance
Hearing on
Examining the Availability of Insurance for Nonprofits

January 29, 2020

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The National Association of Mutual Insurance Companies (NAMIC) is pleased to provide comments to the U.S. House Financial Services Committee Subcommittee on Community Development, Housing, and Insurance on the availability of insurance for nonprofits.

NAMIC membership includes more than 1,400 member companies. The association supports regional and local mutual insurance companies on main streets across America and many of the country's largest national insurers. NAMIC member companies write \$268 billion in annual premiums.

Introduction

In 1752, Benjamin Franklin started the country's first successful mutual insurance company, helping found the property/casualty insurance industry in the United States. Since that date, the U.S. insurance industry has by and large operated under a state-based regulatory scheme that has endeavored to protect consumers and provide a stable insurance marketplace for insurers to do business. Further, at the federal level, under the McCarran-Ferguson Act in 1945 and subsequent legislation, insurance regulation has been explicitly left to the states to handle with a few notable exceptions, including the creation of Risk Retention Groups.

Risk retention groups (RRGs) have played a role in providing both product and commercial liability insurance in niche markets across the country since their creation over 30 years ago. Today, a tiny fraction of the RRG community is seeking to expand its statutorily allowed insurance offerings into other areas to include commercial property coverages and auto physical damage, the assertion being that there is a demonstrable failure in these markets and crisis of availability for 501(c)(3) organizations. NAMIC members are community leaders across America and support the work that many 501(c)(3)s do in our communities throughout the nation. However, we do not agree that a market crisis exists and believe that an expansion of the scope of RRGs would be unnecessary, inappropriate, and place consumers at more risk.

In short, NAMIC opposes H.R. 4523, the Nonprofit Property Protection Act, for four key reasons:

1. No national insurance availability crisis exists that would warrant circumventing long standing state insurance regulations
2. Because no crisis exists, allowing RRGs to offer commercial property and auto insurance would serve only to create an unlevel regulatory playing field and a competitive advantage for a handful of RRGs in this market
3. The RRG regulatory regime is substantially different and less rigorous, undermining consumer protections and potentially placing 501(c)(3) policyholders at risk
4. States have already created more tailored and effective risk-transfer mechanisms and alternative solutions for 501 (c)(3)s

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No National Commercial Property Insurance Availability Crisis

In 1986 Congress passed the Liability Risk Retention Act in response to what was perceived as a severe disruption in the commercial liability insurance market. This disruption was largely driven by a sharp uptick in the mid-1980s in litigation and subsequent over-sized verdicts that led to a drastic increase in both liability claim frequency and severity. What followed was a sharp contraction in the market for these products due to the lack of tort reform measures to curb abuses.

The LRRRA provided a narrow preemption of the state insurance regulatory system in order to allow RRGs to offer liability insurance coverage across the country in an attempt to alleviate this market disruption. RRGs are group self-insurance mechanisms that are licensed to underwrite product and commercial liability insurance for their owners. By statute, owners of an RRG must be engaged in similar business activities or exposed to similar risks. The most notable feature of this narrow preemption is that it allows RRGs to obtain a charter from a single state and then exempts them from most regulation by any other state in which they operate, other than the chartering state.

This relaxed regulatory regime was designed to address a very specific market disruption specifically for liability insurance. Therefore, any expansion of the LRRRA into other lines of insurance would need a comparable – and demonstrable – market breakdown. H.R. 4523 seeks to expand the scope of RRGs to allow them to write commercial property coverages despite there being no nationwide commercial property insurance crisis that needs to be addressed. We fundamentally disagree with the assertions by proponents of this legislation that non-profits are unable to acquire commercial coverages in the private market.

According to the Urban Institute's National Center for Charitable Statistics latest numbers, there are at least 1.56 million non-profit organizations in the United States¹ and according to Nonprofit Quarterly, roughly 78% of them are 501(c)(3)s.² While we can assume that not all non-profits necessarily have commercial property insurance needs, surely, it would be far more obvious if there was a market crisis of availability happening nationwide for some significant percentage of the over 1.2 million 501(c)(3)s. As the National Association of Insurance Commissioners stated in a recent letter addressed to Chairwoman and Ranking Member of the

¹ These 1.56 million organizations comprise a diverse range of nonprofits, including art, health, education, and advocacy nonprofits; labor unions; and business and professional associations. This broad spectrum, however, only includes registered nonprofit organizations; the total number of nonprofit organizations operating in the United States is unknown. Religious congregations and organizations with less than \$5,000 in gross receipts are not required to register with the IRS, although many do. These unregistered organizations expand the scope of the nonprofit sector beyond the 1.56 million organizations this brief focuses on <https://nccs.urban.org/publication/nonprofit-sector-brief-2018#the-nonprofit-sector-in-brief-2018-public-charities-giving-and-volunteering>

²Also, in 2017 alone there were roughly 80,000 approvals of non-profit, 501(c)(3)s. <https://nonprofitquarterly.org/how-many-nonprofits-1023ez/>.

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House Financial Services Committee, “we are not aware of a crisis in the commercial property insurance market today.”³ It defies logic that the state insurance commissioners, who have historically been the front lines of responding to insurance market disruptions, would be completely unaware if what would have to be such a sizable number of non-profits were unable to find the insurance coverages they needed.

Taking the example of the only RRG NAMIC is aware of that would avail itself of H.R. 4523 if it were to become law, the Alliance of Nonprofits for Insurance has, at most, 20,000 non-profit policyholders⁴ that operate in 32 states. The implication of the arguments made by ANI in arguing that there is a crisis of availability for commercial property coverage for non-profits generally seem to be threefold:

1. All 20,000 of ANI’s associated non-profits who need property coverage are uninsured or close to closing their doors due to the cost of insurance
2. An enormous percentage of the other 98.3% (1,210,000) of 501(c)(3)s which have commercial property insurance needs are uninsured or close to closing their doors due to the cost of insurance
3. Non-profits in the other 18 states where ANI does not do business either do not have a similar availability problem or would not benefit from the proposed solution of H.R. 4523

Again, logic would dictate that given the implications above, the sheer magnitude of the problem would have to be obvious to everyone (and it is not) if there was indeed an availability crisis in the commercial property insurance market.

Further, in previous testimony and other public statements, proponents of H.R. 4523 have conceded that non-profit organizations are able to secure commercial property insurance in the traditional, admitted insurance market. This fact alone belies the notion that the U.S. has a commercial property availability problem. Some suggest that this property coverage somehow “doesn’t count” because it is typically bundled into a policy that includes liability insurance.⁵ Bundling of products is typically a more efficient and cost-effective way of selling insurance products – and, it should be noted, exactly what proponents of H.R. 4523 would like to be able to do – and objecting to this form of offer is not compelling evidence of a market crisis.

In short, NAMIC believes there is no evidence of an availability crisis in the commercial property markets for 501(c)(3)s that would necessitate expanding the LRRRA.

³ Letter from the NAIC, addressed to Reps. Maxine Waters and Patrick McHenry, dated October 23, 2019, ‘RE: The Nonprofit Property Protection Act, H.R. 4523.’

⁴ Based on number of members listed at the group-level by the Nonprofit Insurance Alliance, of which ANI is a subsidiary: <https://insuranceforprofits.org/>

⁵ That property coverages are regularly bundled with liability coverages is a particularly interesting objection, given that it would seem to undercut the entire rationale for continuing to allow RRGs to exist at all.

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H.R. 4523 Creates an Unnecessary Regulatory Loophole

The Nonprofit Property Protection Act seeks to allow RRGs to offer commercial property insurance to non-profits when, as we have seen, there is currently no shortage of available and appropriate products in the market. The predominant reasoning behind the unique regulatory structure of RRGs is to facilitate the offering of insurance products in areas of the market in which conditions have made it difficult to do so. But how were RRGs designed to accomplish this?

Specifically, the LRRRA provides RRGs with one distinctive advantage over traditional insurers: a reduced regulatory burden. Since RRGs are only really regulated in the state in which they are domiciled, they do not face the same burden or costs associated with multi-state solvency and consumer protection regulations. This was understood to be the point from the beginning. During a July 17, 1986 Senate hearing on the LRRRA Sen. Bob Kasten noted:

The measure before the Senate today amends the 1981 act to make it easier for others to form collective purchasing groups and risk retention groups for general liability insurance, without imposing on them conflicting requirements in each state which they operate.⁶

Though arguments have been made that there are other efficiency gains to be had from the RRG structure, multiple studies have failed to find evidence that any efficiencies found were due to anything other than the reduced regulatory burden.⁷ In other words, RRGs have no special mechanism or ability to make risks any less risky and thereby offer a lower-priced product.⁸ The only cost-savings come from regulatory compliance savings and tax treatment.

And this regulatory benefit is significant. Professor Tyler Leverty of the University of Wisconsin has estimated that the structure of RRGs reduces the cost of compliance by 26% in comparison to similar traditional insurers.⁹ RRGs were given this advantage for one reason, which was to ensure products were available in high risk product lines that had availability and extreme affordability issues. However, the commercial property insurance market does not fit this description. Allowing RRGs to sell commercial property coverage already offered in the admitted markets would give them an unfair competitive advantage over traditional insurance companies that abide by the regulatory standards and consumer protections of each state in which they operate.

Ultimately, if there is an interest among RRGs in expanding into other, admitted lines markets, there is an option that some have already utilized which avoided an unfair and unlevel playing

⁶ Testimony of Wisconsin Se. Bob Kasten, July 17, 1986, *Hearing on Risk Retention Amendments*, 132 Cong Rec S 9228.

⁷ See, for example, Born and Boyer, 2011, and Born, et al. 2009.

⁸ Assuming the proper pricing of a risk to avoid adverse selection and maintain solvency.

⁹ Leverty, Tyler. "The Cost of Duplicative Regulation: Evidence from Risk Retention Groups," 2012.

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field while ensuring consumers are protected: reorganize as a traditionally admitted insurance company.

A Less Rigorous Regulatory Regime

The state-based insurance regulatory system in the United States is robust and rigorous, with a central focus on consumer protection. Through major world wars, depressions, and the recent financial crisis the U.S. system of insurance regulation has proven effective and ultimately adaptable. Despite some of the challenges and costs associated with state regulation, it has overseen the flourishing of a highly competitive industry – as one example, there are over 2,600 property/casualty insurance companies across the country. Each state is empowered to determine the best method to regulate their insurance industry based on factors that could be inherent to that state, which is particularly true when it comes to property insurance. States may encounter different situations and perils that lead them to institute various regulations and consumer protections that other states do not find necessary. This, in part, allows for that central focus to be on consumer protection.

As has been previously noted, RRGs are allowed to operate nationwide, but they are only substantially subject to the regulations of the state in which they are domiciled. By definition this means that there is less oversight with fewer regulators. The consumer protections that are built into other aspects of the state-based regulatory system are also lacking under the RRG regulatory regime. For example, RRGs generally do not have to file rate and form filings – a key check on improper market conduct – and they may use GAAP accounting principles as opposed to statutory accounting principles, SAP being widely understood to be more conservative in terms of investments and reserving requirements. In the end, attempts by state regulators to tailor the regulatory conditions in their state would not apply equally to all companies operating there.

These reductions in consumer protections are a concern. But an even more fundamental component of the regulatory system for traditional insurers that protects policyholders is the mandatory participation in all state guaranty funds. Every state has some version of a guaranty fund which is an industry-funded sponsored backstop to protect policyholders in the event of a failure. In the case of an insurance company insolvency in which the assets of the company are insufficient to cover claims, policyholders have recourse through their state guaranty fund. While guaranty funds are state sponsored, they are funded by assessments on traditional insurance companies – only funds from the private sector are utilized. As a result, insurance companies inherently desire adequate regulation to ensure safety and soundness because ultimately, they would pay the price for the failure of an insolvent insurance company.¹⁰ Importantly, RRGs are legally excluded from the guaranty fund system and do not have to pay any assessments due to an insurer failure.

¹⁰ Potential insolvency concerns are why many admitted insurers would be wary of even allowing RRGs to participate in Guaranty Funds.

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Given the above, it should be both unsurprising and troubling that, according to the NAIC, RRGs have historically seen a higher insolvency rate when compared with admitted insurers.¹¹ Unsurprising because the regulatory regime is less rigorous, and troubling because a higher rate of insolvency would mean greater risk to 501(c)(3) policyholders – who would not be protected by guaranty funds – especially if RRGs were allowed to expand to offer commercial property insurance.

Allowing RRGs to Offer Commercial Property Unnecessary

NAMIC does not see evidence that there is a national availability crisis in the commercial property insurance market for 501(c)(3)s. There are insurance coverages – including property coverage – available and marketed directly to these organizations. Even if one were to stipulate an availability issue – which we do not – it does not mean that passage of H.R. 4523 and the expansion of the RRG mandate is the only, best, or even an appropriate remedy. Given that NAMIC’s membership contains numerous, smaller mutual insurance companies that write in multiple states for niche markets, we would strongly reiterate that reorganization as a traditionally admitted insurance company is self-evidently an option for those entities not satisfied with the statutory limitations on their offerings.

Proponents of the legislation tend to focus on arguments that are carefully couched with very specific language, i.e. there are no traditional insurance company filings for standalone commercial auto or property coverage “of the type” used by 501(c)(3) non-profits. In addition to simply “not counting” commercial property coverages offered in a combined product, this argument ignores the myriad other options and mechanisms through which a non-profit could effectively transfer its risk. There exist market mechanisms and transaction structures such as fronting arrangements that can be accomplished with admitted insurers.

If a non-profit has real difficulty in finding the exact coverage it desires in the admitted market, it can have a broker go to the surplus lines market. The surplus lines market offers coverages for unique risks, one type of which are those for which admitted carriers do not offer a filed policy form or rate. Importantly, surplus lines companies are regulated by the domiciliary state and the placement of the coverage is regulated by the home state of the insured. This provides an option for 501(c)(3)s that provide a greater level of regulatory protection than would additional lines of coverage being offered through an RRG.

In the event that an organization cannot find coverage in either the admitted or the surplus lines market, many states have residual market mechanisms to which it could go to acquire a policy. A good example of this type of mechanism is a state Fair Access to Insurance Requirements (FAIR) Plan. FAIR Plans are state programs sometimes subsidized by private insurance companies. These plans often provide insurance to people that cannot otherwise find

¹¹ https://www.naic.org/documents/government_relations_190116_rrg_expansion_issue_brief.pdf.

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coverage on their property due to being a particularly high risk or other related problems. A cursory glance at a sampling of FAIR plan websites for Missouri, New York, Ohio, Washington State, and Washington D.C. all list a standalone commercial property coverage available through the plans.¹² These markets of last resort can provide needed coverage for those truly unable to find coverage in the private market.

Finally, in the event an organization is in a state which either does not have a FAIR plan or the plan does not provide standalone commercial property coverage, there are options to work directly with the state regulators and legislatures to address any localized issues of coverage availability. Obviously, states have the power to address coverage gaps through mechanisms like FAIR plans, or, in the case of California, through other risk-pooling mechanisms that can be created to service specific segments of the non-profit community. And per the NAIC, state insurance commissioners are ready and willing to work with non-profit policyholders having difficulty obtaining needed property coverages to find tailored solutions.¹³

Conclusion

It is NAMIC's view that changing federal law and further preempting state law by allowing RRGs to provide commercial property coverage is unnecessary, unfair, imprudent, and inappropriate, for all of the reasons outlined above. We remain supportive of facilitating the acquisition of needed property coverages for non-profits, but staunchly opposed to utilizing the mechanisms of H.R. 4523 and RRGs to do so. We appreciate the opportunity to offer our comments to the committee today.

¹² <https://www.dcpif.org/>; <http://missourifairplan.com/coverages/>;
<https://www.ohiofairplan.com/Public/Coverages.aspx>; <http://www.nypiua.com/commpol.html>;
<https://www.wafairplan.com/customers/>;

¹³ NAIC Letter to Rep. Waters and McHenry, October 2019.