

REQUEST FOR NAIC MODEL LAW DEVELOPMENT

This form is intended to gather information to support the development of a new model law or amendment to an existing model law. Prior to development of a new or amended model law, approval of the respective Parent Committee and the NAIC's Executive Committee is required. The NAIC's Executive Committee will consider whether the request fits the criteria for model law development. Please complete all questions and provide as much detail as necessary to help in this determination.

Please check whether this is: ☐ New Model Law or ☒ Amendment to Existing Model

1. Name of group to be responsible for drafting the model:

Reciprocal Exchanges (E) Working Group

2. NAIC staff support contact information:

Robin Marcotte, rmarcotte@naic.org

3. Please provide a brief description of the proposed new model or the amendment(s) to the existing model. If you are proposing a new model, please also provide a proposed title. If an existing model law, please provide the title, attach a current version to this form and reference the section(s) proposed to be amended.

The Risk-Focused Surveillance (E) Working Group has made a referral to the Financial Condition (E) Committee with respect to the recent increase in the number of reciprocal exchanges being formed and challenges in assessing the fairness and reasonableness of attorney-in-fact fees being charged to the newly formed reciprocals:

1. The fee structure for management services is often based on a percentage of gross premiums written.
2. Basing the management service fees on a percentage of premium volume creates a conflict of interest, i.e., a potential incentive for the attorney-in-fact to increase its fee revenue by underpricing or accepting risk that may be above its typical underwriting guidelines.
3. Management service fees are also often included in the power of attorney agreement, as opposed to a separate service agreement, which can make the fees less transparent.
4. It's worth noting that the definition of control within *Insurance Holding Company System Regulatory Act (#440)* specifically provides that "...the power to cause the direction of the management and policies" triggers control.

Due to these concerns, the Working Group made the following referral to the Committee:

Request a working group be formed to modify the NAIC *Insurance Holding Company System Regulatory Act* (#440) and/or NAIC *Insurance Holding Company System Model Regulation with Reporting Forms and Instructions* (#450) to clarify that regardless of definitions of control and affiliation, fees charged insurers from the attorney-in-fact are subject to fair and reasonable standards and subject to approval by the Commissioner and under no circumstances should they exceed the cost of such services plus a modest profit.

4. Does the model law meet the Model Law Criteria? ☒ Yes or ☐ No (Check one)

(If answering no to any of these questions, please reevaluate charge and proceed accordingly to address issues).

- a. Does the subject of the model law necessitate a national standard and require uniformity amongst all states? ☒ Yes or ☐ No (Check one)

If yes, please explain why

Model #440 is currently part of the Part A accreditation standards, and must be adopted by all NAIC member jurisdictions on a “substantially similar” basis. The requested modification to Model #440 would require all such transactions between reciprocal exchanges and similar affiliated organizations to meet fair and reasonable standards as it pertains to fees charged the insurer for services. This is considered a necessary change to these standards to prevent insurers from sidestepping these provisions which could be considered to be excessive if they failed to meet such standards.

- b. Does Committee believe NAIC members should devote significant regulator and Association resources to educate, communicate and support this model law?

☒ Yes or ☐ No (Check one)

5. What is the likelihood that your Committee will be able to draft and adopt the model law within one year from the date of Executive Committee approval?

☒ 1 ☐ 2 ☐ 3 ☐ 4 ☐ 5 (Check one)

High Likelihood

Low Likelihood

Explanation, if necessary:

6. What is the likelihood that a minimum two-thirds majority of NAIC members would ultimately vote to adopt the proposed model law?

☒ 1 ☐ 2 ☐ 3 ☐ 4 ☐ 5 (Check one)

High Likelihood

Low Likelihood

Explanation, if necessary:

7. What is the likelihood that state legislatures will adopt the model law in a uniform manner within three years of adoption by the NAIC?

☐ 1 ☒ 2 ☐ 3 ☐ 4 ☐ 5 (Check one)

High Likelihood

Low Likelihood

Explanation, if necessary: Not all state legislatures meet annually, and states are normally afforded more time to complete a change to the Part A Accreditation Standards.

8. Is this model law referenced in the NAIC Accreditation Standards? If so, does the standard require the model law to be adopted in a substantially similar manner?

Yes

9. Is this model law in response to or impacted by federal laws or regulations? If yes, please explain.

No