

RRG PRELIMINARY MEMORANDUM

RRG Preliminary Memorandum

An RRG Preliminary Memorandum is developed by the domestic state for a risk retention group (RRG) upon approving the initial licensing of the RRG. The information in this document will serve as a summary of key considerations in assessing and approving the license. The information will also serve as the base for developing an Insurer Profile Summary (IPS) once the RRG begins writing business and files its annual statement. The role of the RRG Preliminary Memorandum is for both internal communication within the domestic state and for external communication with other states in which the RRG is authorized to register and has submitted a registration form. In accordance with the federal Liability Risk Retention Act (LRRRA) a non-domestic state must rely on the domestic state to approve which states the RRG may write in. The non-domestic state does not perform their own review of the application for licensing in the domestic state but relies on the information in the RRGs registration form and communication from the domestic regulator. The RRG Preliminary Memorandum is not required, however, its use can help improve transparency and communication between regulators and reduce potential delays in registration. Additional recommendations regarding transparency and communication can be found in the RRG best practices and frequently asked questions documents on the Risk Retention Group (E) Task Force website.

A template that can be used to develop the RRG Preliminary Memorandum is provided below; however, the actual form and content should be determined by each respective state.

**XX DEPARTMENT OF INSURANCE
RRG PRELIMINARY MEMORANDUM
COMPANY NAME
Date of Review**

<p>State Contact List here</p> <p>List States Where Approved to Write Business List all approved states here</p> <p>Accounting Standard GAAP, modified GAAP, SAP</p> <p>Captive Manager List name here List key contact here List phone here List email here</p> <p>Contact at Insurer List name here List phone here List email here</p>
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BUSINESS SUMMARY

Provide a brief description of the risk retention group (RRG) and a summary of the business operations of the RRG. Consider inclusion of the following.

- Purpose of the RRG and the benefits gained by creating the RRG (i.e., is it meeting a need not met in the commercial market, formed by a promoter looking for a group, etc.).
- Describe the approved coverages and comment on their compliance with the LRRRA. Include policy limits and net retention.
- Describe the ownership structure and/or key members, association, or sponsor.
- Describe the capital structure of the RRG. Include minimum capital and surplus requirements, use of letters of credit, surplus notes, ability to raise additional capital, etc.
- Comment on how the business is produced (i.e., direct writings, agent(s), managing general agent (MGA), managing general underwriter (MGU)).

GOVERNANCE

Discuss the makeup of the board of directors and other oversight considerations including compliance with governance requirements in the *Model Risk Retention Act* (#705).

Discuss if the RRG is MGA or producer controlled.

Discuss service providers used.

Confirm background checks were done.

PROFORMA FINANCIAL SNAPSHOT

Proforma financial data may be summarized in a narrative format, chart format, or a combination. Information may include key financial statement items and/or key ratios. Sample data is shown below but the format, number of years of data, line items and ratios included should be customized. Consideration should be given to what information provides the most insight for the newly formed RRG. Information related to the feasibility study, including who performed the study may also be included.

Assets and Liabilities

<u>Years Ended December 31</u>	<u>20XX</u>	<u>20XX</u>
Total Invested Assets	219	253
Other Assets	111	131
TOTAL ASSETS	330	384
LIABILITIES		
Insurance reserves, net	97	95
Other liabilities	169	193
TOTAL LIABILITIES	266	288

Capital and Surplus	64	96
TOTAL LIABILITIES AND C&S	330	384
Operations	<u>20XX</u>	<u>20XX</u>
Premiums, net	218	233
Investment income (net of gains/losses)	1	8
Other income	0	0
Total revenues	219	241
LOSSES, BENEFITS AND EXPENSES		
Incurred losses, net	177	157
Expenses	77	80
Total losses and expenses	254	237
Other	0	2
NET INCOME	(35)	2

AREAS OF INTEREST

Provide a brief summary of the following items when applicable or noteworthy.

- Reinsurance
- Investment policy
- Related Parties
- Restrictions or special requirements such as permitted practices
- Additional details for coverages that require special underwriting, discounting and tail coverages
- Other

IMPACT OF HOLDING COMPANY ON INSURER

Summarize the evaluation of the impact of the holding company system on the domestic insurer. Or state that the RRG is not part of a holding company group. The summary should include whether a disclaimer of affiliation or any other exemption or waiver related to holding company requirements has been granted, and the rationale for the determination.

KEY RISKS AND SUPERVISORY PLAN

Summarize key risks identified and/or items that require further monitoring by the analyst or specific testing by the examiner. In addition, indicate if the Company is or should be subject to any enhanced monitoring, such as monthly reporting, a targeted examination or a more frequent exam cycle. Key risks may relate to the areas of interest above or may be separate considerations. Information should be brief and include prospective considerations.

Document the date of the first expected examination and the planned examination cycle.

Analysis Follow-Up

Examination Follow-Up

Best Practices – Risk Retention Groups

The domiciliary state maintains authority and has responsibility to regulate the formation and operation of a Risk Retention Group (RRG). Therefore, when concerns arise in a non-domiciliary state about a RRG, the best resource is the domiciliary state. This includes concerns about solvency and capital levels, financial condition, or other non-compliance of an RRG as well as operational questions and concerns that should be directed to the domiciliary state.

States are encouraged to examine their RRG laws to make certain that they are consistent with (1) the federal Liability Risk Retention Act (LRRRA) and (2) the NAIC *Model Risk Retention Act* (#705).

Questions/Concerns from Non-domiciliary State

Upon initial registration of an RRG in a non-domiciliary state, it is not uncommon for questions to arise that are best directed to the domiciliary state. Attachment A outlines a sample Inquiry Template that can be used to request this information. The template may be customized as deemed appropriate by the non-domiciliary state. Domiciliary states should respond in a timely manner to such requests.

Questions about operations and financial solvency that arise following initial registration should also be addressed to the domiciliary state.

If significant concerns still exist after communication with the domiciliary state and the non-domiciliary state concludes that the RRG is not compliant with any of the specific procedures set forth in the LRRRA, the following steps may be undertaken:

- a. Refer to your own state RRG statute to ensure compliance of your prospective action;
- b. Provide written notice of any non-compliance directly to the RRG;
- c. Submit a demand for examination of the RRG to the domiciliary regulator, as provided by the LRRRA [15 U.S.C. S3902(a)(1)(E)];
- d. Institute suit in a court of competent jurisdiction.

A non-domiciliary state may request the following from the domiciliary state and similarly, the domiciliary state should be prepared to provide the following to the non-domiciliary state:

- e. Insurer Profile Summary (IPS)
- f. Inquire about the extent of biographical affidavit review and results of background checks
- g. Most recent examination report (may be obtained from I-Site)
- h. Amendments to the RRG's business plan or feasibility study
- i. Verification of domiciliary state approval to expand into non-domiciliary state

Alternatively, the following documents may be used for this request with modifications as necessary:
Attachment A – Inquiry Template (when specific questions or concerns not typically addressed on the above documents arise) may be used for this request with modifications as necessary.
Attachment B – RRG Preliminary Memorandum (for a new RRG in which the IPS is not yet available)

Registration Timeline

The registration process for RRGs should be shorter than the licensing process for other types of insurers as the RRG is responsible only for a complete registration form* and the related attachments. The non-domiciliary state cannot reject a complete registration* that complies with those laws of the non-domiciliary state that are not preempted under the LRRRA. In the event a non-domiciliary state has concerns with an RRG registration, such concerns should be raised with the domiciliary state, who has the authority to regulate the formation and operation of an RRG. The following guidelines take into consideration similar guidelines for ordinary insurance companies, and adherence is at the discretion of each state.

- A non-domiciliary state should review the registration form to ensure all required information is entered on the form within 10 business days of its receipt of the form and notify the Risk Retention Group of the need to submit any missing elements.
- Following receipt of a complete registration*, a non-domiciliary state should notify the RRG within 30 days that its registration is confirmed.
- The domiciliary state should respond to inquiries from a non-domiciliary state in a prompt manner, typically no later than 10 business days after receiving the inquiry.

*Refer to the document titled “Risk Retention Groups: Frequently Asked Questions”, 3(c) for the definition of a complete registration form.

Domiciliary State Responsibilities

When a domiciliary state identifies an RRG as troubled or potentially troubled, the State insurance regulator should make efforts to communicate proactively with other state insurance regulators in which the RRG is registered (consistent with the *Troubled Insurance Company Handbook*). Although the domiciliary regulator is responsible for taking actions involving their domiciliary RRGs, awareness by a non-domiciliary state may help them to proactively do what they can to protect their residents and respond to policyholder complaints or concerns directed to them.

General Licensing Guidance

Domiciliary states should ensure the RRG’s application for licensing, which includes the plan of operation and feasibility study, includes the following, at a minimum:

- information sufficient to verify that its members are engaged in businesses or activities similar or related with respect to the liability to which such members are exposed by virtue of any related, similar or common business, trade, product, services, premises or operations;
- information sufficient to verify that the liability insurance coverage to be provided by the Risk Retention Group will only cover the members of the Risk Retention Group;
- for each state in which it intends to operate, information regarding the liability insurance coverages, deductibles, coverage limits, rates and/or rating/underwriting methodology for each line of commercial liability insurance the group intends to offer;

- historical and expected loss experience of proposed members and national experience of similar exposures to the extent that this experience is reasonably available;
- appropriate opinions/feasibility work by a qualified independent casualty actuary, including a determination of minimum premium participation levels required to commence operation and to prevent a hazardous financial condition;
- pro forma financial statements and projections, including assumptions, on an expected and adverse basis;
- identification of Board of Directors, including independence determination;
- biographical affidavits for all BOD members;
- evidence of compliance with corporate governance standards, including draft policies;
- underwriting and claim procedures;
- marketing methods and materials if available;
- draft insurance policies;
- names of reinsurers and reinsurance agreements, if available;
- investment policies;
- identification of each state in which the RRG intends to write business/register;
- identification of service providers, including fee structure and relationships to members; and
- subsequent material revisions to the plan of operation or feasibility study.

Attachment A – Inquiry Template

The above-subject company has applied for Registration as a Risk Retention Group (“RRG”) in the State of _____ to write _____ liability coverage to its members who are in the business of _____. As you can appreciate, due to the provisions of the Liability Risk Retention Act of 1986 the (state) has limited authority to regulate RRGs and therefore to a large extent, the (state) relies on the RRGs’ domiciliary state to exercise general oversight and responsibility in the areas of licensing, solvency, rates and marketing. As part of our due diligence, we would appreciate any information your office can share with us regarding the company with respect to the following items, some of which may be satisfied by providing the Insurer Profile Summary:

1. Any significant concerns the State of [domicile] has regarding the company.
2. Any issues that may have a significant impact on the company going forward.
3. Any issues regarding the number of consumer complaints the company has in [state of domicile] or other states that may have been brought to your attention.
4. Comments and/or concerns about the financial condition of the company.
5. Comments and/or concerns about the management or performance of the company.
6. Results of any financial analysis and/or market conduct findings.
7. The company’s priority level within the Financial Analysis Division.
8. Any conditions imposed by your Department upon the company’s license.
9. Any significant non-compliance issues with the State of [domicile] regulatory authority including filing requirements and corrective action, if any.
10. Comments regarding the company’s application for registration in the State of [state registering].
11. Approval from State of [domicile] for the RRG to register in the State of [state registering].