

## BUSINESS TRANSACTED WITH PRODUCER CONTROLLED PROPERTY/CASUALTY INSURER ACT

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### Section 1. Short Title

This Act may be cited as the Business Transacted with Producer Controlled Insurer Act.

### Section 2. Definitions

As used in this Act:

- A. “Accredited state” means a state in which the insurance department or regulatory agency has qualified as meeting the minimum financial regulatory standards promulgated and established from time to time by the National Association of Insurance Commissioners (NAIC).
- B. “Control” or “controlled” has the meaning ascribed in [cite insurance law section incorporating NAIC Model Insurance Holding Company Act];
- C. “Controlled insurer” means a licensed insurer that is controlled, directly or indirectly, by a producer.
- D. “Controlling producer” means a producer who, directly or indirectly, controls an insurer.
- E. “Licensed insurer” or “insurer” means a person, firm, association or corporation duly licensed to transact a property/casualty insurance business in this state. The following, among others, are not licensed insurers for the purposes of this Act:
  - (1) All residual market pools and joint underwriting authorities or associations; and
  - (2) All captive insurers other than risk retention groups as defined in 15 U.S.C. Section 3901 et seq. and 42 U.S.C. Section 9671 (for the purposes of this Act, captive insurers are insurance companies owned by another organization whose exclusive purpose is to insure risks of the parent organization and affiliated companies or, in the case of groups and associations, insurance organizations owned by the insureds whose exclusive purpose is to insure risks to member organizations and group members and their affiliates).
- F. “Producer” means an insurance broker or brokers or any other person, firm, association or corporation, when, for any compensation, commission or other thing of value, the person, firm, association or corporation acts or aids in any manner in soliciting, negotiating or procuring the making of an insurance contract on behalf of an insured other than the person, firm, association or corporation.

**Drafting Note:** The term “producer” as used in this Act is not intended to include an exclusive agent or any independent agent acting on behalf of the controlled insurer and a subagent or representative of the agent, who acts as such in the solicitation of, negotiation for, or procurement or making of an insurance contract, if the agent is not also acting in the capacity of an insurance broker in the transaction in question. States that define both insurance agent and insurance broker should substitute the term “insurance broker” and an appropriate definition for the term “producer,” and rename the Act accordingly.

**Section 3. Applicability**

This Act shall apply to licensed insurers as defined in Section 2 of this Act, either domiciled in this state or domiciled in a state that is not an accredited state having in effect a substantially similar law. All provisions of the Insurance Holding Company Act, to the extent they are not superseded by this Act, shall continue to apply to all parties within holding company systems subject to this Act.

**Section 4. Minimum Standards**

A. Applicability of section.

- (1) The provisions of this section shall apply if, in any calendar year, the aggregate amount of gross written premium on business placed with a controlled insurer by a controlling producer is equal to or greater than five percent (5%) of the admitted assets of the controlled insurer, as reported in the controlled insurer's quarterly statement filed as of September 30 of the prior year.
- (2) Notwithstanding Paragraph (1) of this subsection, the provisions of this section shall not apply if:
  - (a) The controlling producer:
    - (i) Places insurance only with the controlled insurer, or only with the controlled insurer and a member or members of the controlled insurer's holding company system, or the controlled insurer's parent, affiliate or subsidiary and receives no compensation based upon the amount of premiums written in connection with such insurance; and
    - (ii) Accepts insurance placements only from non-affiliated subproducers, and not directly from insureds; and
  - (b) The controlled insurer, except for insurance business written through a residual market facility such as [cite example], accepts insurance business only from a controlling producer, a producer controlled by the controlled insurer, or a producer that is a subsidiary of the controlled insurer.

B. Required contract provisions. A controlled insurer shall not accept business from a controlling producer and a controlling producer shall not place business with a controlled insurer unless there is a written contract between the controlling producer and the insurer specifying the responsibilities of each party, the contract has been approved by the board of directors of the insurer, and it contains the following minimum provisions:

- (1) The controlled insurer may terminate the contract for cause, upon written notice to the controlling producer. The controlled insurer shall suspend the authority of the controlling producer to write business during the pendency of any dispute regarding the cause for the termination.
- (2) The controlling producer shall render accounts to the controlled insurer detailing all material transactions, including information necessary to support all commissions, charges and other fees received by, or owing to, the controlling producer.
- (3) The controlling producer shall remit all funds due under the terms of the contract to the controlled insurer on at least a monthly basis. The due date shall be fixed so that premiums or installments thereof collected shall be remitted no later than ninety (90) days after the effective date of a policy placed with the controlled insurer under this contract.

- (4) All funds collected for the controlled insurer's account shall be held by the controlling producer in a fiduciary capacity, in one or more appropriately identified bank accounts in banks that are members of the Federal Reserve System, in accordance with the provisions of the insurance law as applicable. (However, funds of a controlling producer not required to be licensed in this state shall be maintained in compliance with the requirements of the controlling producer's domiciliary jurisdiction).
  - (5) The controlling producer shall maintain separately identifiable records of business written for the controlled insurer.
  - (6) The contract shall not be assigned in whole or in part by the controlling producer.
  - (7) The controlled insurer shall provide the controlling producer with its underwriting standards, rules and procedures, manuals setting forth the rates to be charged, and the conditions for the acceptance or rejection of risks. The controlling producer shall adhere to the standards, rules, procedures, rates and conditions. The standards, rules, procedures, rates and conditions shall be the same as those applicable to comparable business placed with the controlled insurer by a producer other than the controlling producer.
  - (8) The contract shall specify the rates and terms of the controlling producer's commissions, charges or other fees and the purposes for those charges or fees. The rates of the commissions, charges and other fees shall be no greater than those applicable to comparable business placed with the controlled insurer by producers other than controlling producers. For purposes of this paragraph and Paragraph (7) of this subsection, examples of "comparable business" includes the same lines of insurance, same kinds of insurance, same kinds of risks, similar policy limits and similar quality of business.
  - (9) If the contract provides that the controlling producer, on insurance business placed with the insurer, is to be compensated contingent upon the insurer's profits on that business, then the compensation shall not be determined and paid until at least five (5) years after the premiums on liability insurance are earned and at least one year after the premiums are earned on any other insurance. In no event shall the commissions be paid until the adequacy of the controlled insurer's reserves on remaining claims has been independently verified pursuant to Subsection D(1) of this section.
  - (10) The contract shall specify a limit on the controlling producer's writings in relation to the controlled insurer's surplus and total writings. The insurer may establish a different limit for each line or sub-line of business. The controlled insurer shall notify the controlling producer when the applicable limit is approached and shall not accept business from the controlling producer if the limit is reached. The controlling producer shall not place business with the controlled insurer if it has been notified by the controlled insurer that the limit has been reached.
  - (11) The controlling producer may negotiate but shall not bind reinsurance on behalf of the controlled insurer on business the controlling producer places with the controlled insurer, except that the controlling producer may bind facultative reinsurance contracts pursuant to obligatory facultative agreements if the contract with the controlled insurer contains underwriting guidelines including, for both reinsurance assumed and ceded, a list of reinsurers with which such automatic agreements are in effect, the coverages and amounts or percentages that may be reinsured, and commission schedules.
- C. Audit Committee. Every controlled insurer shall have an audit committee of the board of directors composed of independent directors. The audit committee shall annually meet with management, the insurer's independent certified public accountants, and an independent casualty actuary or other independent loss reserve specialist acceptable to the commissioner to review the adequacy of the insurer's loss reserves.

**Drafting Note:** Insert the appropriate title for the chief insurance regulatory official wherever the term commissioner appears.

**D. Reporting requirements.**

- (1) In addition to any other required loss reserve certification, the controlled insurer shall annually, on April 1 of each year, file with the commissioner an opinion of an independent casualty actuary (or other independent loss reserve specialist acceptable to the commissioner) reporting loss ratios for each line of business written and attesting to the adequacy of loss reserves established for losses incurred and outstanding as of year-end (including incurred but not reported) on business placed by the producer; and
- (2) The controlled insurer shall annually report to the commissioner the amount of commissions paid to the producer, the percentage such amount represents of the net premiums written and comparable amounts and percentage paid to noncontrolling producers for placements of the same kinds of insurance.

**Section 5. Disclosure**

Prior to the effective date of the policy, the producer shall deliver written notice to the prospective insured disclosing the relationship between the producer and the controlled insurer; except that, if the business is placed through a subproducer who is not a controlling producer, the controlling producer shall retain in his or her records a signed commitment from the subproducer that the subproducer is aware of the relationship between the insurer and the producer and that the subproducer has or will notify the insured.

**Section 6. Penalties**

- A.
  - (1) If the commissioner believes that the controlling producer or any other person has not materially complied with this Act, or any regulation or order promulgated under this Act, after notice and opportunity to be heard, the commissioner may order the controlling producer to cease placing business with the controlled insurer; and
  - (2) If it is found that because of such material non-compliance the controlled insurer or any policyholder thereof has suffered any loss or damage, the commissioner may maintain a civil action or intervene in an action brought by or on behalf of the insurer or policyholder for recovery of compensatory damages for the benefit of the insurer or policyholder, or other appropriate relief.
- B. If an order for liquidation or rehabilitation of the controlled insurer has been entered pursuant to [insert state's rehabilitation and liquidation statute], and the receiver appointed under that order believes that the controlling producer or any other person has not materially complied with this Act, or any regulation or order promulgated hereunder, and the insurer suffered any loss or damage therefrom, the receiver may maintain a civil action for recovery of damages or other appropriate sanctions for the benefit of the insurer.
- C. Nothing contained in this section shall affect the right of the commissioner to impose any other penalties provided for in the Insurance Law.
- D. Nothing contained in this section is intended to or shall in any manner alter or affect the rights of policyholders, claimants, creditors or other third parties.

**Section 7. Effective Date**

This Act shall take effect on [insert date]. Controlled insurers and controlling producers who are not in compliance with Section 4 of this Act on its effective date shall have sixty (60) days to come into compliance and shall comply with Section 5 beginning with all policies written or renewed on or after [insert a date 60 days after the effective date of this Act].

*Chronological Summary of Actions (all references are to the Proceedings of the NAIC).*

*1989 Proc. I 14, 913-915, 915-918 (adopted at special plenary session September 1988).*

*1991 Proc. II 25, 58, 1091, 1096-1099 (amended and reprinted).*

*2012 Proc. 3<sup>rd</sup> Quarter, Vol. I 113, 117, 392-400 (amended).*

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**This chart is intended to provide readers with additional information to more easily access state statutes, regulations, bulletins or administrative rulings related to the NAIC model. Such guidance provides readers with a starting point from which they may review how each state has addressed the model and the topic being covered. The NAIC Legal Division has reviewed each state’s activity in this area and has determined whether the citation most appropriately fits in the Model Adoption column or Related State Activity column based on the definitions listed below. The NAIC’s interpretation may or may not be shared by the individual states or by interested readers.**

**This chart does not constitute a formal legal opinion by the NAIC staff on the provisions of state law and should not be relied upon as such. Nor does this state page reflect a determination as to whether a state meets any applicable accreditation standards. Every effort has been made to provide correct and accurate summaries to assist readers in locating useful information. Readers should consult state law for further details and for the most current information.**

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**KEY:**

**MODEL ADOPTION:** States that have citations identified in this column adopted the most recent version of the NAIC model in a **substantially similar manner**. This requires states to adopt the model in its entirety but does allow for variations in style and format. States that have adopted portions of the current NAIC model will be included in this column with an explanatory note.

**RELATED STATE ACTIVITY:** Examples of Related State Activity include but are not limited to: older versions of the NAIC model, statutes or regulations addressing the same subject matter, or other administrative guidance such as bulletins and notices. States that have citations identified in this column **only** (and nothing listed in the Model Adoption column) have **not** adopted the most recent version of the NAIC model in a **substantially similar manner**.

**NO CURRENT ACTIVITY:** No state activity on the topic as of the date of the most recent update. This includes states that have repealed legislation as well as states that have never adopted legislation.

NAIC MEMBER	MODEL ADOPTION	RELATED STATE ACTIVITY
Alabama		ALA. CODE §§ 27-6B-1 to 27-6B-6 (1993) (previous version of model).
Alaska		ALASKA STAT. § 21.27.570 (1995) (previous version of model).
American Samoa	NO CURRENT ACTIVITY	
Arizona		ARIZ. REV. STAT. ANN. §§ 20-487 to 20-487.04 (1991/1993) (previous version of model).
Arkansas		ARK. CODE ANN. §§ 23-63-1101 to 23-63-1106 (1993/2009) (previous version of model).
California	CAL. INS. CODE §§ 1216 to 1216.6 (1993/2013).	
Colorado		COLO. REV. STAT. §§ 10-4-1201 to 10-4-1206 (1992) (previous version of model).
Connecticut		CONN. GEN. STAT. §§ 38a-91 to 38a-91d (1993/2014) (previous version of model).
Delaware		DEL. CODE ANN. tit. 18, §§ 1650 to 1655 (1992/2014) (previous version of model).
District of Columbia		D.C. CODE §§ 31-401 to 31-408 (1993) (previous version of model).
Florida		FLA. STAT. § 626.7491 (1992/2012) (previous version of model).

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NAIC MEMBER	MODEL ADOPTION	RELATED STATE ACTIVITY
Georgia		GA. CODE ANN. §§ 33-48-1 to 33-48-4 (1991) (previous version of model); GA. COMP. R. & REGS. 120-2-64 (1993) (contract provisions) (portions of previous version of model); Dir. 93-RS-5 (1993).
Guam	NO CURRENT ACTIVITY	
Hawaii		HAW. REV. STAT. §§ 431:11A-101 to 431:11A-105 (1992) (previous version of model).
Idaho		IDAHO CODE ANN. §§ 41-1701 to 41-1706 (1993) (previous version of model).
Illinois		215 ILL. COMP. STAT. 107/1 to 107/99 (1992/2010) (previous version of model).
Indiana		IND. CODE §§ 27-1-35-1 to 27-1-35-19 (1994) (previous version of model).
Iowa		IOWA CODE §§ 510A.1 to 510A.6 (1992/1993) (previous version of model).
Kansas		KAN. STAT. ANN. §§ 40-37a01 to 40-37a06 (1992/2005) (previous version of model).
Kentucky	KY. REV. STAT. §§ 304.3-400 to 304.3-430 (1992/2015).	
Louisiana		LA. REV. STAT. ANN. §§ 22:551 to 22:556 (1992/2009) (previous version of model).
Maine		ME. REV. STAT. ANN. tit. 24-A, §§ 6401 to 6407 (1993) (previous version of model).
Maryland		MD. CODE ANN., INS. §§ 8-101 to 8-109 (1991/2002) (previous version of model); MD. CODE REGS. §§ 31.04.13.01 to 31.04.13.03 (1993).
Massachusetts		MASS. GEN. LAWS ch. 175, §§ 174F to 174K (1993) (previous version of model).
Michigan		MICH. COMP. LAWS §§ 500.1451 to 500.1459 (1994) (previous version of model).

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NAIC MEMBER	MODEL ADOPTION	RELATED STATE ACTIVITY
Minnesota		MINN. STAT. §§ 60J.06 to 60J.11 (1992) (previous version of model).
Mississippi		MISS. CODE ANN. §§ 83-59-1 to 83-59-11 (1992) (previous version of model).
Missouri		MO. REV. STAT. §§ 382.400 to 382.410 (1993/2009) (previous version of model).
Montana		MONT. CODE ANN. 33-2-1501 to 33-2-1517 (1993/2013) (previous version of model).
Nebraska		NEB. REV. STAT. §§ 44-5701 to 44-5708 (1992) (previous version of model).
Nevada		NEV. ADMIN. CODE §§ 693A.600 to 693A.770 (1996) (previous version of model).
New Hampshire		N.H. REV. STAT. ANN. §§ 402-G:1 to 402-G:5 (1993) (previous version of model).
New Jersey		N.J. REV. STAT. §§ 17:22D-1 to 17:22D-5 (1993/1996) (previous version of model); N.J. ADMIN. CODE §§ 11:2-37.1 to 11:2-37.7 (1993/2001).
New Mexico		N.M. STAT. ANN. §§ 59A-12C-1 to 59A-12C-7 (1993) (previous version of model).
New York		N.Y. ADMIN. CODE tit. 11, §§ 80-2.0 to 80-2.5 (Reg. 52-A) (1992/1997) (previous version of model).
North Carolina		N.C. GEN. STAT. § 58-3-165 (1991) (previous version of model).
North Dakota		N.D. CENT. CODE §§ 26.1-26.5-01 to 26.1-26.5-07 (1993) (previous version of model).
Northern Marianas	NO CURRENT ACTIVITY	
Ohio		OHIO REV. CODE ANN. §§ 3905.61 to 3905.65 (1991) (previous version of model).
Oklahoma		OKLA. STAT. tit. 36, §§ 1671 to 1677 (1992) (previous version of model).

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<b>NAIC MEMBER</b>	<b>MODEL ADOPTION</b>	<b>RELATED STATE ACTIVITY</b>
Oregon		OR. REV. STAT. §§ 732.810 to 732.814 (1993/2013) (previous version of model).
Pennsylvania		40 PA. CONS. STAT. §§ 47-301 to 47-305 (1993/1994) (previous version of model).
Puerto Rico	NO CURRENT ACTIVITY	
Rhode Island		R.I. GEN. LAWS §§ 27-48-1 to 27-48-6 (1992) (previous version of model).
South Carolina		S.C. CODE ANN. § 38-21-95 (1993) (previous version of model).
South Dakota		S.D. CODIFIED LAWS §§ 58-44-1 to 58-44-16 (1992) (previous version of model).
Tennessee	TENN. CODE ANN. §§ 56-6-601 to 56-6-604 (1991/2014).	
Texas	NO CURRENT ACTIVITY	
Utah		UTAH CODE ANN. §§ 31A-23a-701 to 31A-23a-704 (1992/2003) (previous version of model).
Vermont		VT. STAT. ANN. tit. 8, §§ 4815 to 4824 (1992) (previous version of model); Regulation 94-2 (1994).
Virgin Islands	NO CURRENT ACTIVITY	
Virginia		VA. CODE ANN. §§ 38.2-1341 to 38.2-1346 (1993) (previous version of model); ADMIN. LETTER 1993-16 (1993).
Washington		WASH. REV. CODE ANN. §§ 48.97.005 to 48.97.900 (1993) (previous version of model).
West Virginia		W. VA. CODE §§ 33-36-1 to 33-36-7 (1992/1993) (previous version of model).
Wisconsin		WIS. ADMIN. CODE INS. §§ 45.01 to 45.07 (1993) (previous version of model).
Wyoming		WYO. STAT. ANN. §§ 26-45-101 to 26-45-108 (1992) (previous version of model).

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This model law was developed in response to a New York case where a broker controlled an insurer and which resulted in legal liability issues about conflict of interest. **1987 Proc. II 834.**

In addition to New York, other states have had concerns about the basic conflict of interest which arises in the case of a parent company placing business with a controlled insurer. The working group was willing to consider disclosure as a means of resolving the difficulty. **1988 Proc. I 829.**

Industry assumed a position favoring complete written disclosure by the producer to the insured of its affiliation with an insurer prior to the time coverage is bound. They considered disclosure and reporting to be a viable alternative to the strict liability in the subgroup's draft of the Business Transacted with Producer Controlled Property/Casualty Insurer Act. **1988 Proc. II 775-778.**

The producer controlled model was developed in response to regulators' concerns about situations in which a producer exercises such extensive control over an insurer that the insurer's solvency could be at risk. If the producer placed a significant amount of the insurer's business, the producer had the potential ability to impair the insurer's solvency. The producer controlled insurer model imposed certain safeguards to establish an audit trail of transactions between the controlling producer and the controlled insurer in an attempt to prevent such effects. **1994 Proc. 2nd Quarter 907.**

The model became part of the accreditation standards for states in 1989, (**1989 Proc. II 35**) but at a special plenary session in April of 1991 (**1991 Proc. II 10**) the model was taken out of the standards due to concerns that had surfaced. After adoption of a revised model, states were encouraged to replace the earlier model with the new version as soon as possible. **1991 Proc. II 1090.** The model again was included in the financial regulation standard, and states had two years to complete the adoption process. **1991 Proc. II 10.**

In December of 1993 a new charge was given to the Special Issues (E) Committee to draft amendments to clarify the intent of the model act. The chair of the committee explained that the working group would attempt to clarify which producers fall within the scope of the act. **1993 Proc. 3rd Quarter 838.**

The chair noted that the Business Transacted with Producer Controlled Property/Casualty Insurers Act was drafted prior to the Managing General Agents Act and the Reinsurance Intermediary Act. As a result of the development process of the subsequent models, the working group was charged to review the producer controlled insurer model to make sure that the definition of producer was consistent with the goal of the model. **1994 Proc. 2nd Quarter 907.**

**Section 1. Short title**

Originally the title of the model was drafted as "Broker Transactions with Controlled Insurer Model Act." Insurance association commentators urged return to a title limiting the scope of the model to brokers controlling insurers. They assumed the change to focusing on "producers" was to conform this model to the NAIC goal of single producer licensing and regulation; they opined this was an area of activity where the traditional distinction between agents and brokers was of paramount importance. **1988 Proc. II 768.**

**Section 2. Definitions**

B. The first draft of the model act contained only one section other than the title. It prohibited placing business with a controlled insurer and defined control. The definition was similar to the definition of control found in the Holding Company Act. **1987 Proc. II 836.**

When the model was amended in 1991, the definition was deleted and the drafters instead referenced the definition of control found in the Holding Company Act. **1991 Proc. II 1090.**

One industry comment received was that the rebuttal presumption provision in the definition of "control" in the Holding Company Act should be included in this Act. It was noted that this definition referenced the Holding Company Act definition in its entirety. **1991 Proc. II 1096.**

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**Section 2** (cont.)

E. The definition of captive insurer was modified just before adoption. It had included a clause “not permitted to participate in any state guaranty fund” but in some states captives are formed under regular insurance code provisions. The drafters also changed the word “main” to “exclusive” to further define captive insurers. **1989 Proc. I 914.**

The working group was careful to structure the language to address problems posed by captive insurers, and that in no way, shape, form or fashion would the bill apply to these captives. **1989 Proc. I 914.**

F. The definition of producer caused concern among brokers by limiting coverage to producers acting “on behalf of an insured.” They suggested that there would be problems sorting out when a producer was acting as an agent on behalf of a company and when a producer was acting on behalf of an insured. **1988 Proc. II 766.**

The committee agreed that the definition of producer was not meant to include internal pooling programs among affiliates. **1989 Proc. I 914.**

In 1994 the working group formed to look at revisions to the model met for the first time. One of the members of the group immediately moved to delete the drafting note after the definition of producer. She said the drafting note mentions brokers, and some states do not distinguish between agents and brokers, so confusion arose in application of the definition. **1994 Proc. 1st Quarter 654.**

The chair of the working group noted that confusion has arisen in states regarding the application of the model definition and most of the confusion stems from the drafting note, which unduly limits the intent of the drafters. **1994 Proc. 1st Quarter 654.**

An insurance association representative said her organization supported the drafting note and did not want it deleted. Her organization thought the note clarified the intent of the model. A regulator said some states relied on the drafting note when they passed the model act and questioned whether deletion of the drafting note would require states to go back to their legislatures to amend the law. **1994 Proc. 1st Quarter 654.**

The working group chair stated that solvency and consumer protection were the primary goal of the drafters, and the drafting note resulted in a conflict with those two objectives. The working group decided to solicit comments on the motion to delete the drafting note. **1994 Proc. 1st Quarter 654.**

A regulator agreed that there was a need to clarify the definition of producer because many states had difficulty interpreting the intent of the Act. He opined that omitting the drafting note may not be sufficient to eliminate the confusion. **1994 Proc. 2nd Quarter 907.**

At the next meeting of the working group a draft was presented that contained a revised definition of producer and a preamble that discussed the purpose of the model. The preamble mentioned that persons subject to the producer controlled insurer act are also subject to the holding company act. An insurance association representative wondered if the proposed preamble was an indirect attempt to manipulate the definition of control in the holding company act. **1994 Proc. 3rd Quarter 776-778.**

After the working group adopted the revised definition, a commissioner said it was important for the Special Issues Committee to realize that the proposed amendments would change the meaning of the statute by including agents, not just brokers, within its scope. Another regulator agreed that the working group proposal was a material change, and the commissioner pointed out the charge to the working group was merely to clarify the definition of producer. **1994 Proc. 4th Quarter 939.**

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**Section 2F (cont.)**

When the proposal was considered by the Executive Committee for adoption or referral to the Financial Regulation Standards and Accreditation Subcommittee, the Executive Committee voted not to refer the amendments or adopt them. One commissioner pointed out that the proposed amendments amounted to more than a clarification of the definition of producer; rather, they were a substantive change in the scope of the model act. **1994 Proc. 4th Quarter 30-31.**

**Section 3. Applicability**

This section was added when the model was revamped in 1991. **1991 Proc. II 1097.**

It was suggested that the model might be better adopted as a regulation pursuant to the authority of the Holding Company Act. One of the drafters agreed that a state could choose to adopt the draft as a regulation if it felt it possessed the authority to do so. **1991 Proc. II 1090.**

**Section 4. Minimum Standards**

The first draft of the model was very brief and consisted of a prohibition on placing business with a controlled insurer. There were no exceptions in that discussion draft. **1987 Proc. II 835-836.**

The second draft still contained a flat prohibition against placing any business with a controlled insurer. **1988 Proc. I 831-832.**

Before adoption of the model act, hearings were held and substantial commentary was received from interested parties. One commentator said that disclosure and financial reporting (loss reserve certification) were the only approaches that should be utilized, and that the proposed legislation imposed responsibilities on brokers that were too harsh. **1988 Proc. II 760.**

The section was completely rewritten in 1991. The requirements for what should be included in the contract were substantially amplified. The minimum contract provisions contained in the Managing General Agents Act have now been included in this model act. **1991 Proc. II 1090, 1097-1098.**

B. Section 4B calls for a written contract between the controlling or affiliated producer and the insurer. Industry commentators questioned the intent of this section and wondered if it would be different from the usual broker/agent agreements with carriers. **1988 Proc. II 766.**

Some of the drafts included a provision that producers must attempt to locate coverage with a nonaffiliated insurer and provide insureds with written notice of that alternative coverage. The process would have been similar to the declination process required when business is placed in the excess and surplus lines market. Industry representatives urged deletion of this burdensome procedure. **1988 Proc. II 762, 766.**

Some of the earlier drafts also contained a provision requiring an actuarial opinion on the adequacy of premium for each policy. The insurance agency urged deletion of this provision, saying it would create an insurmountable burden and would be of questionable assistance in monitoring for solvency. **1988 Proc. II 766.**

Members of the industry urged an addition to the section to provide a minimum volume requirement to eliminate burdensome reporting requirements for small amounts of business that do not warrant regulatory attention. **1988 Proc. II 767.**

**Section 5. Disclosure**

This section was taken out of Section 3 of the original model and reproduced as a separate section when the model was amended in 1991. **1989 Proc. I 917, 1991 Proc. II 1099.**

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**Section 6. Penalties**

A. The committee expressed frustration at some of the far-fetched arguments heard when drafting the model act. The bill is a measured, structured, well defined act resulting from thousands of hours of labor. If a broker owns and controls an insurance company, maintains adequate books, and does not violate sound underwriting principles, or if he violates the act but can show that the violation did not cause the insolvency, then he would not be responsible. Even if it is found that the violation caused the insolvency, a broker would only be responsible to reimburse the state guaranty funds for his own book of business. **1989 Proc. I 914-915.**

Because of concerns expressed about the ability of the commissioner to impose penalties upon a controlling producer, the model was changed to authorize a court proceeding to impose penalties for violation of the Act. **1991 Proc. II 1099.**

One insurance industry spokesperson commented that the original model had only offered a remedy when the controlled insurer was in liquidation, but that the present model also gives the commissioner the right to bring a civil action upon any determination of a violation and damages. One of the drafters replied that the purpose of the change was to allow the commissioners to take action before an insolvency occurred. **1991 Proc. II 1096.**

B. The sixth draft of the original model included a new section which placed a liability on the part of the controlling producer to reimburse state guaranty funds for any payments in excess of gross earned premiums, unless the insolvency arose out of events not attributable to the producer. **1988 Proc. II 763.**

It was made clear that the liability of a producer would be limited to the losses produced by the individual producer's book of business. **1988 Proc. II 760.**

Some of the earlier drafts held producers strictly liable for insolvencies of affiliated or controlled insurers. Broker association representatives took the position that producers had been singled out for special scrutiny and regulatory restraints when no evidence had been presented that producer affiliation made an insurer more or less likely to become financially impaired than other membership structures. **1988 Proc. II 767.**

It was observed that the penalty provision in Subsection B was substantially different that the penalty provision contained in Section 6A(2) in that Section A requires a finding that material noncompliance with the Act had resulted in loss or damages to the insurer, while Section B did not contain similar language. Section 6B was amended to resolve the problems pointed out. **1991 Proc. II 1096.**

**Section 7. Effective Date**

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*Chronological Summary of Actions*

*September 1988: Adopted.*

*June 1991: Substantially amended. Added more contract requirements, provided court procedures.*

*March 1995: The NAIC considered amendments to the model that were designed to clarify the definition of producer and the intent of the model. The amendments were rejected by the Executive Committee.*