RRGs thriving 25 years after law’s passage; Alternative vehicles provide affordable, stable coverage

Business Insurance

WASHINGTON—Passage of the Liability Risk Retention Act 25 years ago unlocked the potential of risk retention groups to provide a highly efficient way for organizations to band together to form group captives.When Congress passed the LRRA in October 1986, it was the second time lawmakers approved RRG legislation.Five years earlier, lawmakers approved the Product Liability Risk Retention Act to establish the special group captives that—under a pre-emption provision in the law—can write policies for member-owners nationwide after meeting the licensing requirements of the RRG’s domicile.Through that pre-emption provision, an RRG would not have to meet the licensing and capitalization requirements of every state in which it wanted to do business, or purchase—boosting its costs—fronting policies from commercial insurers licensed in states where the RRG had policyholders.Some state mandates, such as requiring an insurer to be in business for a certain number of years before it could conduct business in the state, made it virtually impossible for group captives to be set up quickly and do business in multiple states, said Jon Harkavy, vp and general counsel in Washington with RRG and captive manager Risk Services L.L.C.But the law was a dud. According to a 1986 General Accounting Office report, only one RRG, sponsored by homebuilders, was licensed in the United States under the 1981 law and that RRG soon found itself locked in a legal battle with a state regulator on the group’s authority to write coverage.Settling such regulatory disputes is the focus of the latest RRG legislative efforts, but is one that even backers doubt will win congressional backing (see related story).The impact of the 1986 law was dramatically different than the 1981 law. Within one year of the passage, 38 RRGs had been established, according to the Risk Retention Reporter, a Pasadena, Calif.-based monthly newsletter that tracks the industry.Today, more than 250 RRGs are in operation (see chart, page 15), generating nearly $2.5 billion in premium volume, according to the RRR (see chart, page 16). In all, nearly 15% of all U.S. captives are RRGs, according to Business Insurance data.“The law has been an incredible success,” said

Ed Precourt, senior vp at Marsh Captive Solutions in Burlington, Vt.The LRRA “has provided numerous industries with stable and affordable coverage when the traditional market could not or would not,” said Michael J. Bemi, president in Lisle, Ill., of The National Catholic Risk Retention Group Inc., a Vermont-based RRG.The reason for the 1986 law’s success is simple vs. the 1981 law, which was a delayed congressional response to soaring product liability insurance rates in the 1970s: While the 1981 law limited RRGs’ underwriting authority to product liability and completed operations, the 1986 law had no such restriction.Under the 1986 law, Congress gave RRGs the authority to write all commercial casualty coverage except workers compensation. That opened the door for RRGs to write policies in numerous lines of coverage—most notably medical malpractice and professional liability, where buyers were looking for alternatives to the traditional market’s wide swings in rates and available limits.“We didn’t any longer want to ride the market’s ups and downs. We wanted stability,” said Janice Abraham, president and CEO in Chevy Chase, Md., of Vermont-domiciled United Educators Insurance, a Reciprocal Risk Retention Group, which was licensed about six months after passage of the LRRA.Industries that have set up RRGs and the lines of coverage written are diverse. Architects, attorneys, builders, chemical manufacturers, engineers, hospitals and nonprofit organizations are just a few of the industry sectors whose members have set up RRGs.The risks covered by the groups are equally diverse and include virtually every casualty line—even medical stop-loss coverage.While diverse by industry and coverage written, what many RRGs have in common is an underwriting philosophy in which premiums are tied closely to the risk covered and do not leap or plummet depending on competition.“We have offered 23 years of affordable, stable and high-quality coverage. We have provided stability and predictability of premiums, with no spiking, unlike the traditional market,” Mr. Bemi said.In many cases, RRGs also provide risk management and loss control services that their members, especially smaller firms, could not obtain in the traditional market, said Gary Osborne, president of USA Risk Group Inc., a Montpelier, Vt.-based captive manager.“We have two attorneys on staff to answer employment-related questions and we also provide unlimited in-person and online driver training as well as a series of about a dozen webinars each year. All of these services, and several others, are completely free for member-insureds,” said Pamela Davis, president and CEO of the Vermont-domiciled Alliance of Nonprofits for Insurance, Risk Retention Group in Santa Cruz, Calif.At the same time, RRG executives say the groups continually try to update coverage to reflect new exposures.For example, Ms. Davis said ANI has enhanced policies in numerous ways, including adding interns and students in training to the definition of insured for sexual abuse coverage. That is because they are neither employees nor volunteers since they at times are paid a stipend, putting them into a gray area of coverage, she said. Other ANI enhancements include coverage for cyber liability and reimbursement of wages when an employee is put on leave during a professional liability investigation.The biggest endorsement of how RRGs operate is reflected in their growth.At the end of its first year in 1987, United Educators, whose policyholders include colleges, universities, independent schools, public school districts, public school insurance pools and museums, generated about $7 million in premium volume with about 100 members. Now the RRG provides coverage to nearly 1,200 policyholders with a premium volume of about $140 million, Ms. Abraham said.At the same time, some RRGs report annual policyholder retention rates that would be the envy of any insurer. For example, ANI has enjoyed a retention rate of just over 96%, while National Catholic Risk Retention Group has a 99.1% retention rate, Mr. Bemi said.However, not all RRGs have met with success.In fact, citing information it obtained from the National Assn. of Insurance Commissioners, the GAO in a 2005 report said 22 RRGs failed between 1987 and 2003, with a somewhat higher failure rate when compared with other property/casualty insurers. Still, a comparison between RRGs and other insurers may not be entirely parallel, the GAO said, because the NAIC analysis did not adjust for size and longevity among other factors.In all, the GAO said, RRGs have “had a small but important effect” on increasing the availability and affordability of coverage, especially for organizations with limited access to liability insurance.