Risk Retention Group Legislation Marks 30th Anniversary

Written by Karrie Hyatt

Risk retention groups (RRGs) were enabled by Congress thirty years ago this October through the signing of the federal Liability Risk Retention Act (LRRA). RRGs have been both reviled and influential in the alternative risk transfer sector and have carved out a unique niche for themselves in the insurance marketplace.

RRGs are self-insurance mechanism that allow for member-owned liability insurance companies to organize in one U.S. state domicile and to conduct business throughout the United States. This allows member-owned RRGs to more effectively provide liability coverage to their member-insureds while being able to stabilize premiums and, in many cases, keep costs down. They offer a range of liability coverage, primarily in the healthcare arena, but also for higher educational facilities, accountants, lawyers, land trusts, and more.

History and Background

Leading up to the legislation that would create RRGs, Congress initially created the Product Liability Risk Retention Act passed 1981. After years of an especially hard insurance market, when the availability and affordability of commercial liability insurance had become extremely limited, Congress amended the original act to broaden the scope of the law to include all forms of third-party liability coverage. Essentially, what the LRRA did was to preempt state regulation to allow RRGs providing liability coverages to their member-owners to do business in states other than their state of domicile without the inconvenience of using fronting companies. While this is a key aspect in the operation of RRGs, it has also been a major source of criticism.

In the early years, RRGs were quickly established, and some quickly went out of business, but many RRGs have proved remarkable staying power. One of the very first RRGs was Ophthalmic Mutual Insurance Company (OMIC), which was formed a few months after the LRRA was signed into law by President Reagan. The RRG was formed to serve members of the American Academy of Ophthalmology (AAO) and has been doing so since 1987.

According to Timothy Padovese, president and CEO of (OMIC), "The formation of OMIC not only injected competition into the current market; it also created a new niche for specialty-specific insurance products and services. OMIC became an expert in ophthalmic specific risk management and our members now rely on us to provide critical information and resources that protect them such as patient education and consent forms. OMIC has a very specialized expertise gained over nearly thirty years in business and we publish suggested protocols and procedures that are widely used among ophthalmologists to reduce risk to claims and lawsuits."

Purposely tailored risk management and a close knowledge of specialized industries is what can distinguish RRG operations from the traditional insurance market. While the expertise of RRGs operating in the last ten years is generally recognized, it was not so in the beginning.

"Thirty years ago, risk retention groups had a limited history in the medical malpractice market and had not been tested sufficiently by navigating difficult market conditions," said Padovese.

"Some were not adequately funded and failed. The uneven performance of early RRGs allowed for some traditional companies to define our structure as unstable and risky. Over the past three decades, RRGs have grown in size and our track record has been very good, in many cases outperforming the traditional markets. States regulating RRGs with strict oversight and high standards have improved the way RRGs are viewed by competitors in the insurance industry as well as by hospitals and other third party entities. We have become a strong and viable alternative to the traditional insurance market and our members truly see us as value added."

Owner Benefits and Perks

Risk retention groups have proven to be a successful alternative to obtaining liability insurance from the traditional market. In addition to being able to cover members over multiple states, the LRRA was intended to help members keep liability coverage costs low. Member-owners of RRGs can avoid the ups and downs of the insurance market and keep their premium rates stable. They also have more control over their own coverage. This can be especially important for physicians and hospitals, as well as for taxi and truck drivers where rates can be particularly volatile.

"OMIC's sponsoring organization … wanted to create its own insurance company that would serve its members nationwide," said Padovese. "Before OMIC was created in 1987, the rates charged ophthalmologists were disproportionally high in relation to the risk involved and when compared with other specialties. This was not only unfair, but also a threat to ophthalmic practice."

Benefits that were not specifically intended, but are still an important aspect of RRGs' success is their ability to implement effective loss control and risk management practices, and even to issue dividends to members for good loss experience. For many members, the additional benefits are more important than the potential savings and rate stability.

The National Catholic RRG (TNCRRG) was established in 1987 and began operations in 1988 to provide liability insurance to Catholic archdioceses, dioceses, religious institutes, and related Catholic entities. The RRG has been a leader in providing member benefits outside premium savings. According to Michael Bemi, director, president and CEO, "TNCRRG provides coverage that is—within our niche—widely regarded to be the broadest, most comprehensive available. We provide this coverage with very competitively priced premiums—though we have neither desire nor intention to be 'the cheapest' in the market. When compared to the traditional commercial market, our premiums have remained very stable over the 'long haul.' … We provide a number of very valuable risk and claims management services for our members [including] our safe environment program and our free claim audits of members' TPAs, among others."

Yet the reason that owners still turn to RRGs is their ability to operate across state lines. "The onerous process previously required to open for business and operate in each individual state had dissuaded the [AAO] from moving forward, but when the Risk Retention Act was passed it opened the door for the [AAO] to begin putting together the foundation for the company that would eventually become OMIC. As a risk retention group, OMIC could operate across state lines efficiently and at a lower cost. OMIC has provided members stable and competitive rates and consistent dividend returns since 1987."

Facing Obstacles

According to Bemi, *"RRGs are primarily confronted with three challenges: the persistent very soft market—awash in excess capital—which leads to occasional predatory (and often naive) competition and resultant loss of business; the inability to underwrite any property or Worker's Compensation coverage, which precludes RRGs from obtaining the benefit of portfolio/diversity effect and also lessens RRG attractiveness to a potential buyer; and the remaining (though greatly diminished over the years) hostility of certain regulators."*

Risk retention groups have faced sharp criticism throughout the last thirty years, similar to the criticism faced by the captive sector as a whole. As a new type of insurance, they were an unknown quantity and many state regulators took an immediate aversion to them. This viewpoint has not entirely gone away, but on the whole, after thirty years, RRGs are better understood and more respected. In the 1980's, there were only a handful of states that had captive law and were active in forming captives. RRGs fit right into the burgeoning captive industry and found a foothold in domiciles such as Vermont and Hawaii.

As the captive marketplace has matured, so has industry attitudes towards captives and RRGs. "Initially, some states were wary of the single state regulation model," said Padovese. "But seeing the success of companies like OMIC, all states now support RRGs. Challenges occasionally arise with regard to discriminatory RRG reporting and operating requirements by some states, hospitals, or facilities. It is important that we work in conjunction with PIAA, National Risk Retention Association, Vermont Captive Insurance Association, and other organizations to respond when unfair or burdensome regulations are introduced in order to protect the original intent and integrity of the Risk Retention Act."

Since the beginning, another major obstacle facing RRGs is the LRRA's limitation to only providing liability coverages. For many well-established groups this has been an incredibly restrictive factor. For many RRGs whose members want to purchase non-liability coverage, they have to use fronting carriers or go to another carrier. Nearly all of the attempts to expand the LRRA with new legislation has included adding property coverage. Workers' Compensation would also be a welcome addition, but comes in a distant second from RRGs' need to be able to write property.

As risk retention groups were established to offer relief to a very difficult insurance market, when the market improves, it becomes hard for RRGs to offer the savings benefits to their members. During most of the 1990s, the RRG marketplace contracted as capital became readily available and insurance prices plummeted. The hard market of the early 2000's saw a meteoric rise in the number of operating RRGs, the number more than doubling. After the financial market collapse nearly a

decade ago, RRGs have been struggling, with many RRGs closing their doors.

Yet even through the continued soft market that the industry is currently experiencing, RRGs continue to form and succeed, especially those that were well-established before 2007.

RRGs Have Changed the Insurance Marketplace

Since 1987, RRGs have had a strong influence on the liability insurance market. According to Padovese, "Almost immediately, malpractice insurance rates fell, and for everyone in our specialty market. Even ophthalmologists insured by multispecialty carriers started paying less. Competition forced multispecialty carriers to pay close attention to the rates, coverages, and services offered to ophthalmologists or risk losing business. Professional liability coverage for ophthalmologists improved and rates have remained stable for thirty years."

Bemi also believes that risk retention groups have made the liability insurance marketplace more competitive. "While I can't prove this proposition, I believe that in certain market niches—such as educational, religious and healthcare institutions—RRGs have forced the traditional market participants to 'up their game' or lose the business. This provides a benefit to all market participants and their insureds."

"As for the captive market," continued Bemi, "while RRGs are a specialized segment of that market, distinguished in a number of ways, I think that RRGs—largely via the National Risk Retention Association—have frequently 'led the way' for the broader captive marketplace, specifically in the arenas of advocacy and education." ■

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