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COMMITTEE REPORT

May 5, 2016

**S. 978**

Introduced by Senator Hayes

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Read the first time February 23, 2016.

**THE COMMITTEE ON**

**LABOR, COMMERCE AND INDUSTRY**

To whom was referred a Bill (S. 978) to amend Section 38‑9‑330, as amended, Code of Laws of South Carolina, 1976, relating to risk‑based capital plans, so as to increase, etc., respectfully

**REPORT:**

That they have duly and carefully considered the same and recommend that the same do pass:

WILLIAM E. SANDIFER III for Committee.

**A** **BILL**

TO AMEND SECTION 38‑9‑330, AS AMENDED, CODE OF LAWS OF SOUTH CAROLINA, 1976, RELATING TO RISK‑BASED CAPITAL PLANS, SO AS TO INCREASE THE MULTIPLIER FOR A COMPANY ACTION LEVEL EVENT FOR A LIFE AND HEALTH INSURER FROM 2.5 TO 3.0; TO AMEND SECTION 38‑87‑30, RELATING TO THE CHARTERING OF A RISK RETENTION GROUP, SO AS TO DEFINE TERMS, TO PROVIDE THAT A MAJORITY OF A RISK RETENTION GROUPS’ DIRECTORS MUST BE INDEPENDENT DIRECTORS, TO ESTABLISH THE MAXIMUM TERM OF ANY MATERIAL SERVICE PROVIDER CONTRACT, TO REQUIRE THE BOARD OF DIRECTORS TO ADOPT A WRITTEN POLICY, TO REQUIRE THE BOARD OF DIRECTORS TO ADOPT AND DISCLOSE ITS GOVERNANCE STANDARDS, TO REQUIRE THE BOARD TO ADOPT AND DISCLOSE A CODE OF BUSINESS CONDUCT AND ETHICS, TO REQUIRE A RISK RETENTION GROUP TO COMPLY WITH APPLICABLE REGULATIONS, TO ESTABLISH PROCEDURES FOR NONCOMPLIANCE, AND TO SET ESTABLISHED DATES FOR COMPLIANCE; TO AMEND SECTION 38‑87‑40, RELATING TO OUT‑OF‑STATE RISK RETENTION GROUPS, SO AS TO ALLOW AN OUT‑OF‑STATE RISK RETENTION GROUP TO SUBMIT REVISIONS TO ITS PLAN OF OPERATION WITHIN THIRTY DAYS OF APPROVAL BY THE STATE INSURANCE COMMISSION OR WITHIN THIRTY DAYS IF NO APPROVAL IS REQUIRED; AND TO AMEND SECTION 38‑90‑160, AS AMENDED, RELATING TO CAPTIVE INSURANCE COMPANIES, SO AS TO EXTEND THE PROVISIONS OF SECTION 38‑87‑30 TO A RISK RETENTION GROUP LICENSED AS A CAPTIVE INSURANCE COMPANY.

Be it enacted by the General Assembly of the State of South Carolina:

SECTION 1. Section 38‑9‑330(A)(2) of the 1976 Code is amended to read:

“(2) filing of an RBC Report which indicates that a life and health insurer has Total Adjusted Capital which is greater than, or equal to, its Company Action Level RBC, but is less than the product of its Authorized Control Level RBC and ~~2.5~~ 3.0 and has a negative trend;”

SECTION 2. Section 38‑87‑30 of the 1976 Code is amended to read:

“Section 38‑87‑30. (A) A risk retention group, pursuant to the provisions of this title, must be chartered and licensed to write only liability insurance under this chapter and, except as provided elsewhere in this chapter, or Chapter 90 for a risk retention group licensed as a captive insurance company, shall comply with all of the laws, regulations, and requirements applicable to these insurers chartered and licensed in this State and with Section 38‑87‑40 to the extent these requirements are not a limitation on laws, regulations, or requirements of this State.

(B) Before it may offer insurance in any state, each risk retention group chartered in this State shall submit for approval to the director or his designee of this State a plan of operation or feasibility study. The risk retention group shall submit an appropriate revision in the event of any subsequent material change in any item of the plan of operation or feasibility study, within ten days of any such change. The group may not offer any additional kinds of liability insurance, in this State or in any other state, until a revision of such plan or study is approved by the director or his designee.

(C) At the time of filing its application for charter, the risk retention group shall provide to the director or his designee in summary form the following information: the identity of the initial members of the group, the identity of those individuals who organized the group or who will provide administrative services or otherwise influence or control the activities of the group, the amount and nature of initial capitalization, the coverages to be afforded, and the states in which the group intends to operate. Upon receipt of this information, the director or his designee may forward such information to the National Association of Insurance Commissioners. Providing notification to the National Association of Insurance Commissioners is in addition to, and is not sufficient to satisfy, the requirements of Section 38‑87‑40 or any other provision of this chapter.

(D)(1) As used in this section:

(a) ‘Board’ means the governing body of the risk retention group elected by the shareholders or members to establish policy, elect or appoint officers and committees, and make other governing decisions.

(b) ‘Director’ means a natural person designated in the articles of the risk retention group or designated, elected, or appointed by any other manner, name, or title to act as a director.

(c) ‘Disclose’ means to make information available through electronic or other means and to provide the information to members and insureds upon request.

(d) ‘Domestic regulator’ means the Director of the South Carolina Department of Insurance or the director’s designee.

(e) ‘Material relationship’ means a relationship between a person with the risk retention group including, but not limited to:

(i) the receipt in any one twelve month period of compensation or payment of any other item of value by the person, a member of his immediate family or a business with which he is affiliated from the risk retention group or a consultant or service provider to the risk retention group that is greater than or equal to five percent of the risk retention group’s gross written premium for this twelve month period or two percent of its surplus, whichever is greater, as measured at the end of any fiscal quarter falling in this twelve month period. The person or his immediate family member is not independent until one year after the compensation from the risk retention group falls below the threshold;

(ii) a relationship with an auditor in which a director or an immediate family member of a director who is affiliated with or employed in a professional capacity by a present or former internal or external auditor of the risk retention group is not independent until one year after the end of the affiliation, employment or auditing relationship; or

(iii) a relationship with a related entity in which a director or immediate family member of a director who is employed as an executive officer of another company where any of the risk retention group’s present executives serve on that other company’s board of directors is not independent until one year after the end of the service or the employment relationship.

(f) ‘Service providers’ means captive managers, auditors, accountants, actuaries, investment advisors, lawyers, managing general underwriters, or other parties responsible for underwriting, determination of rates, collection of premium, adjusting and settling claims, or the preparation of financial statements. This term does not include lawyers who serve as defense counsel retained by the risk retention group to defend claims unless the amount of fees paid to these lawyers are greater than or equal to five percent of the risk retention group’s gross written premium for the previous twelve month period or two percent of its surplus, whichever is greater as measured at the end of any fiscal quarter falling in this twelve month period.

(2)(a) The board of the risk retention group shall have a majority of independent directors. If the risk retention group is reciprocal, then the attorney‑in‑fact would be required to adhere to the same standards regarding independence of operation and governance as imposed on the risk retention group’s board and subscribers advisory committee under these standards. To the extent permissible under state law, service providers of a reciprocal risk retention group shall contract with the risk retention group and not the attorney‑in‑fact.

(b) A director does not qualify as independent unless the board affirmatively determines that he has no material relationship with the risk retention group. Each risk retention group annually shall disclose these determinations to its domestic regulator. For this purpose, a person who is a direct or indirect owner or a subscriber in the risk retention group, or is an officer, director, or employee of an owner and insured, unless some other position of the officer, director, or employee constitutes a material relationship, as contemplated by Section 3901(a)(4)(E)(ii) of the Liability Risk Retention Act, is considered to be independent.

(3)(a) The term of a material service provider contract with the risk retention group must not exceed five years. The contract, or its renewal, must require the approval of the majority of the risk retention group’s independent directors. The risk retention group’s board may terminate a service provider, contract, audit contract, or actuarial contract at any time for cause after providing adequate notice as defined in the contract. The service provider contract is considered material if the amount to be paid for the contract is greater than or equal to five percent of the risk retention group’s annual gross written premium or two percent of its surplus, whichever is greater.

(b) A service provider contract meeting the definition of material relationship contained in this section may not be entered unless the risk retention group has notified the domestic regulator in writing of its intention to enter into the transaction at least thirty days prior and the domestic regulator has not disapproved it within the period.

(4) The risk retention group’s board shall adopt and approve a written policy in the plan of operation that requires the board to:

(a) assure all owners and insureds of the risk retention group receive evidence of ownership interest;

(b) develop a set of governance standards applicable to the risk retention group;

(c) oversee the evaluation of the risk retention group’s management including, but not limited to, the performance of the captive manager, managing general underwriter, or other party responsible for underwriting, determination of rates, collection of premiums, adjusting or settling claims, or the preparation of financial statements;

(d) review and approve the amount to be paid for all material service providers; and

(e) review and approve, at least annually, the:

(i) risk retention group’s goals and objectives relevant to the compensation of officers and service providers;

(ii) officers and service providers, performance in light of those goals and objectives; and

(iii) continued engagement of the officers and material service providers.

(5) The board shall adopt and disclose governance standards by making the following information available through electronic or other means and providing this information to members and insureds upon request:

(a) the process by which the directors are elected by the owner and insureds;

(b) director qualification standards;

(c) director responsibilities;

(d) director access to management and, as necessary and appropriate, independent advisors;

(e) director compensation;

(f) director orientation and continuing education;

(g) the policies and procedures for management succession; and

(h) the policies and procedures for annual performance evaluation of the board.

(6) The board shall adopt and disclose a code of business conduct and ethics for directors, officers, and employees and promptly disclose to the board of directors any waivers of the code for directors or executive officers, including:

(a) conflicts of interest;

(b) matters covered under the corporate opportunities doctrine under the state of domicile;

(c) confidentiality;

(d) fair dealing;

(e) protection and proper use of risk retention group assets;

(f) compliance with all applicable laws, rules, and regulations; and

(g) requiring the reporting of any illegal or unethical behavior which affects the operation of the risk retention group.

(7) The audit provisions of S.C. Code of Regulations 69‑70 related to audit committees apply to risk retention groups.

(8) The captive manager, president, or chief executive officer of the risk retention group promptly shall notify the domestic regulator in writing if he becomes aware of any material noncompliance with any of these governance standards.

(9) All existing risk retention groups must be in compliance with the governance standards contained in this section by January 1, 2018. New risk retention groups licensed after January 1, 2017, must be in compliance with the standards at the time of licensure.”

SECTION 3. Section 38‑87‑40(1)(b) of the 1976 Code is amended to read:

“(b) The risk retention group shall submit a copy of any material revision to its plan of operation or feasibility study required by Section 38‑87‑30(B) within thirty days of the date of approval of the revision by ~~at the same time that such revision is submitted to~~ the commissioner of its chartering state, or within thirty days of filing if no approval is required.”

SECTION 4. Section 38‑90‑160(D) of the 1976 Code is amended to read:

“(D) Except as provided elsewhere in this chapter, the provisions of Chapter 87, Title 38 apply to a risk retention group licensed as a captive insurance company. The provisions of Section 38‑87‑30(D) apply in full to a risk retention group licensed as a captive insurance company and control if a conflict occurs between that code section and this chapter.”

SECTION 5. If any section, subsection, paragraph, subparagraph, sentence, clause, phrase, or word of this act is for any reason held to be unconstitutional or invalid, such holding shall not affect the constitutionality or validity of the remaining portions of this act, the General Assembly hereby declaring that it would have passed this act, and each and every section, subsection, paragraph, subparagraph, sentence, clause, phrase, and word thereof, irrespective of the fact that any one or more other sections, subsections, paragraphs, subparagraphs, sentences, clauses, phrases, or words hereof may be declared to be unconstitutional, invalid, or otherwise ineffective.

SECTION 6. This act takes effect on January 1, 2017.

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