STATE OF CONNECTICUT

INSURANCE DEPARTMENT

Testimony of Thomas B. Leonardi, Insurance Commissioner
To
Insurance and Real Estate Committee

February 25, 2014

SB 188 - An Act Concerning Captive Insurance Companies

Senator Crisco, Representative Megna, and members of the Insurance and Real Estate Committee, the Insurance Department thanks the Committee for raising **Senate Bill 188: An Act Concerning Captive Insurance Companies**, at the Department's request and appreciates the opportunity to provide the following testimony.

For those that may not know, a captive is an insurance company or entity that is formed to insure or reinsure the risks of its owner(s). With the formation of a captive insurance company, its owners are "entering into the business of insurance." A captive is the formal use by a company of its own financial capital (or access to capital) to retain and "self-finance" its risks. Many of the world's largest organizations use captives, with over 5,000 captive insurance entities existing worldwide. Variations in structure and design are rapidly emerging, offering creative risk solutions to address evolving risk exposures and capital issues.

Captive insurance companies function as an important complement or alternative to the traditional insurance market. They often fill a risk financing need that the commercial insurance market is unable or unwilling to provide. Without risk financing, certain businesses are unable to function effectively and adverse economic consequences may evolve. Examples of commercial insurance market difficulties include:

- Medical Professional Liability (cost & availability)
- Catastrophic Risk Protection – flood, windstorm (cost & availability)
- Products Liability (cost & availability)
- Workers Compensation (cost)
- Healthcare Benefits (cost & availability)

Captives are a powerful tool for businesses of all sizes and orientations, to shape the future of their owners. Captives not only help manage operating costs, but can also optimize operating returns and improve decision making processes. Even more importantly, captives are a vehicle for leading transformational change. They have generated both economic and strategic value through optimizing risk management decisions, as well as optimizing the utilization and deployment of capital. Captives are risk management solutions that not only support corporate strategies, but contribute to the organization's bottom line.

In 2011, with the Governor's leadership and the hard work of the Chairs and members of this committee, the legislature passed enabling legislation for the formation and operation of captive insurance companies in this state. By its efforts, this legislative body made a commitment to an important and growing business segment. These efforts resulted in four captive companies domesticating in Connecticut **(total annual written premium of $54M; total assets of $118M)** and many more applying for entry.

The 2011 enabling legislation was the starting point to making Connecticut a domicile of choice for captives. **SB 188** will build upon that good work. Its passage will reverberate throughout the industry and signal that Connecticut is nimble and responsive to the needs of this ever evolving industry.

SB 188 contains updates to our existing Captive Statutes that include:

- Clarification of definition private passenger motor vehicle insurance provided by a captive insurance company,
- Provisions and process for transfer of domicile (re-domestication) for captive insurance companies,
- Discretionary authority for evaluating credit for existing reinsurance placements, made by re-domiciling captive insurance companies,
- Establishment and purpose of a branch captive insurance company, and
- Clarification of applicability of holding company legislation to captive insurance companies.

This year, the Connecticut Insurance Department is asking that the State Legislature to consider a few statutory modifications that will enhance the captive insurance capabilities in Connecticut, ease the re-domestication process and expand capability in a rapidly evolving market place. These statutory modifications are essential to continue the development of the captive insurance industry in Connecticut, as part of a rapidly evolving and significant business sector in this state.

There is a strong linkage between Connecticut's captive insurance industry and the economic health of the state. Maintaining Connecticut as a viable captive insurance domicile adds significant value and a competitive advantage to this state as the *Insurance Capital of the Nation*. Vermont, the primary competitive domicile in New England, has built a solid reputation. To maintain its leadership position, it has demonstrated its ability to appropriately modify its statutes and respond to the needs of an evolving industry. Other domiciles in the US have recently entered the captive insurance market, passed legislation to modernize or streamline their statutes, and have made significant new resource and service commitments. Captive insurance company owners have a choice in where they will domicile their insurance subsidiary. The industry has and continues to carefully observe how states with captive statutes are maintaining and improving their statutes to evolve with a quick moving and innovative market place.

The strategic importance of captive insurance to Connecticut business is clear and reinforces our need to update our General Statutes to enable the State of Connecticut to support the needs of its businesses and residents. Connecticut has the recognized leadership and experience in risk and insurance. In addition, the State is an integral part of the Tri-State Region, along with New York, providing easy access to both traditional and alternative capital markets.

There is also the potential to utilize captives to solve risk problems facing various constituent groups in our state. The Connecticut Insurance Department and the Department of Energy and Environmental Protection are collaborating and exploring alternatives to address the "insurance" issues facing businesses and residents of the Connecticut shore line. Contractions in the public and private insurance facilities have caused significant premium increases for flood and windstorm insurance following Super Storm Sandy. Captive insurance companies can access traditional and alternative capital markets to provide a more stable risk protection solution for the catastrophic risk exposures of commercial and residential properties.

Captive insurance entities can be important tools for the implementation of the strategic objectives of its owners. One of the most recent captive companies licensed in Connecticut was able to stabilize the costs of its human capital costs through the use of their newly established captive subsidiary. This in turn allowed the owner to launch a program to employ veterans and long term unemployed workers here in Connecticut. Hence, the captive helped facilitate the implementation of its owner's strategic objectives.

The captive insurance environment is Connecticut is indeed growing, vibrant and responsive. More importantly, business and organizations who manage their strategies and capital through captive insurance vehicles, can attract and maintain a qualified and productive workforce, they can add jobs as they grow. This is the real impact and contribution to the Connecticut economy.

The Connecticut Insurance Department respectfully recommends substitute language for **SB 188** ***(please see the attached document)***, which will allow for the alignment of the Connecticut General Statutes with NAIC model acts, relating specifically to risk retention groups (RRG's) domiciling in Connecticut. RRG's are typically formed as captive insurance companies and organized under the laws of this state pursuant to the federal Liability Risk Retention Act of 1986. The first amendment relates to the application of the Risk Based Capital model act to risk retention groups, and the second amendment relates to the Producer Controlled Property/Casualty Insurer model act. Both of these amendments will provide additional consumer-oriented regulatory requirements/scrutiny to risk retention groups forming and licensed prospectively in Connecticut.

The Department again, thanks the Committee for raising **SB 188** and encourages the Committee's support. Thank you.

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Recommended Substitute Language

1. The first technical amendment for drafting:

Sec. 38a-91oo (2): Add the following ….**<u>Sec 38a-72(d) and</u> Sec. 38a-73, which shall apply only to captive insurance companies formed as risk retention groups, as defined in section 38a-91aa.**

2. The second technical amendment for drafting:

Sec 38a-91 (6): Add the following wording at the end of the "licensed insurer" wording…. **<u>other than a risk retention group defined in section 38a-91aa.</u>**