SURPLUS LINES (C) TASK FORCE

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Surplus Lines (C) Task Force
San Francisco, CA
December 7, 2009

The Surplus Lines (C) Task Force met in San Francisco, CA on Dec. 7, 2009. The following Task Force members participated: James J. Donelon, Chair (LA); Merle D. Scheiber, Vice-Chair (SD); Jim L. Ridling, represented by Charles Angell (AL); Linda S. Hall (AK); Steve Poizner, represented by Louis Quan (CA); Karen Weldin-Stewart, represented by Linda Sizemore (DE); Kevin M. McCarty, represented by Steven Parton (FL); Michael T. McRaith, represented by Jack Messmore (IL); Carol Cutter, represented by Doug Webber (IN); Sandy Praeger, represented by Ted Clarke (KS); Scott J. Kipper, represented by Marie Holt (NV); Joel Ario, represented by Steve Johnson (PA); Joseph Torti, III, represented by Paula Pallozzi (RI); and Jane L. Kline, represented by Mary Jane Pickens (WV). Other regulators included; Gloria Glover (AK); John Gatlin (IL): Cindy Fillman (PA); and Randy Moses (SD).

1. OPT*ins* Presentation

Joy Morrison (NAIC) presented an overview of the Online Premium Tax for Insurance (OPT*ins*), an application that allows the submission and payment of premium tax filings. Ms. Morrison stated this application is currently in use by a few states for surplus lines purposes. Ms. Morrison stated this application has the potential to be more widely used in connection with the surplus lines brokerage market as well as the domestic insurer market.

Mr. Moses asked whether Ms. Morrison was familiar with the uniform reporting form currently being designed by the Multi-State Surplus Lines Premium Tax (C) Working Group and inquired as to whether OPT*ins* was an alternative to this form or could be used in conjunction with the form. Ms. Morrison said she had seen the form and believed that OPT*ins* would be complimentary to it. David Vacca (NAIC) added that OPT*ins* is a state regulator tool, so ideally it can work and function in whatever way state regulators desire.

2. Legislative Update

Commissioner Donelon directed Amanda Yanek (NAIC) to deliver an update on surplus lines related legislation. Ms. Yanek provided a status report on the Nonadmitted and Reinsurance Reform Act of 2009 (H.R. 2571) that passed unanimously under suspension of the rules in the House on Sept. 9. Since then, much of the language was added to Title V of Sen. Christopher J. Dodd's (CT) comprehensive reform package currently titled Restoring American Financial Stability Act. This legislation has not been officially introduced. On Nov. 19, opening remarks and debate began on the legislation in the Senate under the Senate Banking Committee. Further markup was postponed, but Sen. Dodd expected further debate and markup before the holiday season. Ms. Yanek said the NAIC continues to support the nonadmitted portion of the bill but has expressed some concern with the reinsurance portion.

3. Summary Regarding Surplus Lines License Exemption Survey

Commissioner Donelon requested that Mr. Vacca summarize the responses to a two-question survey regarding the possible application of the commercial lines multi-state exemption of the *Producer Licensing Model Act* to surplus lines producers (Attachment One). The survey resulted from a request by the Producer Licensing (EX) Working Group and garnered 19 state responses and four from industry associations.

Mr. Angell moved that the Task Force receive the report and direct staff to provide the survey responses and summary to the Producer Licensing (EX) Working Group. The motion was seconded by Mr. Parton and passed unanimously.

Director Hall suggested that the survey results and summary also be provided to the NARAB (EX) Working Group, as it was recently found that a majority of states have an underlying producer requirement and that unless there is a requirement for due diligence to be done, it may violate reciprocity. Mr. Donelon agreed and directed staff to share the survey responses and summary with the NARAB (EX) Working Group.

4. Receive Summary of Surplus Lines (C) Task Force Member Survey

Commissioner Donelon asked Mr. Vacca to provide a summary (Attachment Two) of eight responses from Surplus Lines (C) Task Force members to a survey that solicited feedback on methods of achieving goals of the Nonadmitted and Reinsurance Reform Act of 2009 (H.R. 2571). Mr. Vacca stated that individual state responses were not provided, as states were not advised that the responses would be made public. The summary included both significant minority and majority positions on several questions each for the four general sections: Alternative Methods, Compact Considerations, Incidental Exposures, and Uniformity.

Commissioner Donelon stated that based on the limited number of responses, there appeared to be no consensus among Task Force members as to how to implement the reforms outlined in the pending federal legislation.

5. Receive Report of the Multi-State Surplus Lines Premium Tax (C) Working Group

Commissioner Donelon directed Mr. Vacca to present a summary of the Multi-State Surplus Lines Premium Tax (C) Working Group and interim minutes of a conference call conducted Oct. 15 (Attachment Three). Mr. Vacca's summary included a status of the universal premium tax filing form, discussion of the need for uniformity with regard to the premium tax payment cycle, and concern voiced by some states that doubt whether a universal filing form will be usable in their state.

Commissioner Donelon introduced Bernie Heinz (Executive Director, American Association of Managing General Agents) who presented a viewpoint for furthering the possible implementation of the Surplus Lines Insurance Multistate Compliance Compact (SLIMPACT). Mr. Vacca reminded the Task Force of the many elements currently under development, which include the OPT*ins* application, the universal reporting form and Marsh's offer of sophisticated software that calculates premium taxes that would provide the framework necessary to implement the reforms cited in the federal legislation, without a compact.

Mr. Moses asked whether the SLIMPACT alternative would apply solely to multi-state filings or if it would apply to single-state filings and attestations as well. Dan Maher (Excess Line Association of New York) stated that SLIMPACT was essentially a clearinghouse that uses uniform allocation formulas and limited dates for tax payments based on incidental exposures in multi-state exposures. Mr. Maher cited one significant drawback to SLIMPACT would be that states would have to adjust their taxing protocols from multiple considerations to a single formula so that SLIMPACT would have only a one formula to use in computing incidental exposures. Mr. Moses spoke in favor of the uniform premium tax reporting form as his state's preferred method for meeting the demands of both single and multi-state filings.

Director Scheiber moved to receive the summary report and the interim minutes. The motion was seconded by Mr. Parton and passed unanimously.

6. Receive Report of the Surplus Lines Financial Analysis (C) Working Group

Commissioner Donelon requested that Director Hall provide a summary of the Surplus Lines Financial Analysis (C) Working Group's activities during 2009 and minutes of its two interim meetings—March 20 and June 30. Director Hall stated that during 2009, the Working Group met in regulator-to-regulator session and reviewed and approved the applications for four Lloyd's syndicates and two non-Lloyd's insurers. As of Oct. 30, there were 130 entities on the *Quarterly Listing of Alien Insurers* that had an aggregate $4.7 billion held in trust against their U.S. surplus lines liabilities. For 2008, the entities on the *Quarterly Listing of Alien Insurers* wrote direct premiums of $9.1 billion, a 9.0% increase over the $8.3 billion for 2007.

Director Hall moved to receive the report and interim minutes. The motion was seconded by Mr. Quan and passed unanimously.

Having no further business, the Surplus Lines (C) Task Force adjourned.

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Summary of Responses to a Surplus Lines License Exemption Survey

Accepting a research request from the Producer Licensing (EX) Working Group, the Surplus Lines Task Force directed NAIC Staff to create a survey to gauge states' opinion regarding a possible extension of the non-resident licensing exemption for multi-state risks to apply to surplus lines producers. A two-question survey was distributed to all states and Task Force interested parties. 19 states (AR, CA, CO, DE, FL, GA, HI, IN, KS, KY, LA, MD, NH, NJ, OH, SD, VA, WI, and WY) and four industry associations (National Association of Professional Surplus Lines Offices, the National Association of Professional Insurance Agents, and a combined response from: the Excess Line Association of New York, the Surplus Lines Stamping Office of Texas, and the Surplus Lines Association of California) provided responses.

Question #1 asked the responder to *explain whether an exemption from nonresident state producer licensing in situations where there is a multi-state risk would impact a state's ability to properly record and collect surplus lines premium tax.* The majority of states believed that the application of the multi-state commercial exemption to surplus lines producers would severely hamper their ability to record and collect the payment of surplus lines premium taxes.

Question #2 requested the responder to *describe any alternative methods for states to identify and collect premium taxes for multi-state exposures that would* <u>*not*</u> *require nonresident producer licensing.* The most common responses from the states were:

1. Require the surplus lines insurers to report the business and pay the premium taxes.

2. Place the burden on the home state to monitor the business written by licensees and ensure the equitable distribution of premium taxes to the various states.

3. Have the home state collect and remit the taxes on a multiple-state exposure.

4. If the proposed multi-state tax allocation form were required to be filed with every state where premium (risk) is located, this would allow the states to identify and collect premium taxes for multi-state exposures.

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Survey of Surplus Lines Task Force Members Regarding Methods for Achieving Goals of NRRA – Title I

Summary

I. Alternative Methods

- All states agreed that a uniform allocation method of some design is needed.
- Responses were evenly split on the concept of using a compact as the method for implementing tax allocation procedures.
- All but one state believed that state-by-state legislative changes would be required to implement any of the methods.
- Several states were in agreement to create a filing form and to utilize the NAIC as a clearinghouse with other states by contract, but not by compact.

II. Compact Considerations

- Five of eight states viewed a majority of SLIMPACT provisions favorably.
- One state opposed all aspects of a compact.
- Three states favored allowing states to withdraw from a compact commitment.

III. Incidental Exposures

- Most responses indicated an expectation of receiving an allocated share for incidental exposures.
- A majority of states were either unsure of the definition of the term “incidental” or felt that it was not clearly defined.
- Depending on the interpretation of “incidental,” a few states indicated their intent not to collect for incidental risks.

IV. Uniformity

- All states supported the creation and adoption of uniform tax allocation formulas.
- Seven of eight states indicated a willingness to change tax collection due dates to allow for uniform reporting.
- All states favored more uniform standards to ensure that each state had an adequate baseline standard for multi-state risks.

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Multi-State Surplus Lines Premium Tax (C) Working Group
Conference Call
October 15, 2009

The Multi-State Surplus Lines (C) Premium Tax Working Group of the Surplus Lines (C) Task Force met via conference call Oct. 15, 2009. The following Working Group members participated: Cindy Donovan, Chair (IN); Gloria Glover (AK); Pete Tavares (KS); Stewart Guerin (LA); Larry Levine (NY); Steve Johnson (PA); Randy Moses (SD); and Kathy Wilcox (TX).

Ms. Donovan summarized the changes made to the multi-state tax allocation reporting form that resulted from suggestions made during the previous conference call and from emails. The changes included: 1) Renamed the spreadsheet to Quarterly Surplus Lines Premium Tax Report; 2) Added columns for foreign (alien) insurer placements; 3) Included reporting date requirements at the bottom of state columns; 4) Added an area to designate "report prepared by;" and 5) Included a modified affidavit.

Ms. Donovan opened the call to reporting form improvement suggestions and received the following to consider: 1) Add a column or indicator for the home state, possibly just before the grand total column; 2) Clarify with instructions what is meant by an endorsement date—whether this refers to an effective date, a transaction date or an invoice date; 3) Include a column on the form to indicate the allocation method used and develop a list of coded choices. Dan Maher (Excess Line Association of New York) will forward to Ms. Donovan background material on this topic that an earlier group (SLIMPACT) had researched; 4) Under the corporate license section, include the name, telephone number and e-mail address of the placing licensee. This information is needed when contact is required in a large brokerage firm with many licensees; 5) Add a column to the far left of the form to indicate consecutive transaction numbers (i.e., when multiple lines of information are needed to list the various components of a single policy); and 6) Lock down any fields that contain computational formulas and tax rate values so that users may not adjust at their discretion.

Regarding tax rate values, Roger Smith (Marsh) reminded the Working Group to consider that approximately 10 changes to tax rates and stamping or other fees occur each year, some at mid-year. When these changes occur, the form will need to accommodate a different rate to be applied based on the effective date of the rate or fee change or the effective date of the policy or endorsement.

Peggy Dronet (Mississippi Surplus Lines Association—MSLA) commented that her state has developed sophisticated software that retains rate information back many years, as the MSLA applies rates based on effective date and not by reporting date. Ms. Dronet stated that some policy records were lost due to Hurricane Katrina and that the MSLA system was able to apply correct rates to old effective dates. Ms. Dronet wondered if the proposed reporting system would have this flexibility.

Phil Ballinger (Surplus Lines Stamping Office of Texas—SLSOT) expressed doubt that the proposed tax reporting form would be usable in connection with the electronic reporting format that SLSOT has in place presently. Mr. Ballinger was uncertain that the proposed reporting form could accommodate the more than 430,000 surplus lines transactions his office handles annually. In addition, his state's comptroller's office, which collects premium taxes, receives a simplified tax report from SLSOT and would not want to sort through the proposed tax reporting form to locate the Texas-specific tax information.

Mr. Levine indicated that although New York supports much of the Working Group's initiatives, he believed that gaining approval for usage of the proposed reporting form in his state would be a significant challenge.

Ms. Donovan broached the subject of tax payment cycles. Ms. Donovan suggested that quarterly tax payments would create uniformity between the states, with only five states currently requiring monthly tax payments. The other states that currently have annual or semi-annual payment cycles generally would not be opposed to the increased frequency of quarterly payments. However, several states expressed concern that a quarterly payment cycle would not sync well with current reporting periods. Ms. Donovan reminded all that there might be many states that would need to have statutes changed or their practices altered if the goal of uniformity in the treatment of surplus lines taxes is to be achieved.

Having no further business, the Multi-State Surplus Lines Premium Tax (C) Working Group adjourned.
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