

SURPLUS LINES (C) TASK FORCE

Surplus Lines (C) Task Force Oct. 20, 2010, Minutes

Surplus Lines Financial Analysis (C) Working Group Sept. 23, 2010, Conference Call – (Attachment One)

Multi-State Surplus Lines Premium Tax (C) Working Group Reporting Form Comments – (Attachment Two)

Surplus Lines (C) Task Force 2011 Proposed Charges – (Attachment Three)

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Draft: 11/4/10

Surplus Lines (C) Task Force
Orlando, FL
October 20, 2010

The Surplus Lines (C) Task Force met in Orlando, FL, Oct. 20, 2010. The following Task Force members participated: James J. Donelon, Chair (LA); Merle D. Scheiber, Vice Chair (SD); Linda S. Hall represented by Gloria Glover (AK); Jim L. Ridling represented by Jimmy Gunn (AL); Steve Poizner represented by Louis Quan (CA); Karen Weldin Stewart represented by Linda Sizemore (DE); Kevin M. McCarty represented by Steve Parton (FL); Michael T. McRaith represented by John Gatlin (IL); Stephen W. Robertson represented by Cynthia Donovan (IN); Sharon P. Clark represented by Frank Goins (KY); Brett Barratt represented by Marie Holt (NV); James J. Wrynn represented by Rolf Kaumann (NY); Robert L. Pratter represented by Steve Johnson (PA); and Alfred W. Gross represented by Brian Gaudiose.

1. Receive State Premium Tax Survey

Bob Schump (NAIC) described a survey commissioned by the Task Force that was distributed to the states requesting information regarding direct written premium and premium taxes related to the total market and the nonadmitted portion. The survey results might provide useful baseline data for the Surplus Lines Implementation (EX) Task Force when considering strategies to address surplus lines issues within the federal Nonadmitted and Reinsurance Reform Act (NRRA) provisions within the federal Dodd-Frank Wall Street Reform and Consumer Protection Act. Survey results were not shared with the industry or other states, as confidentiality was assured to the states as a condition for their response.

Commissioner Donelon accepted the survey results. He stated that the individual state information might prove useful in benchmarking future premium tax reports going forward and providing an understanding of the importance that the surplus lines market plays in the generation of state premium taxes.

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

Ms. Glover provided a summary of the Surplus Lines Financial Analysis (C) Working Group's activities since the Spring National Meeting (Attachment One). She stated that the Working Group met Sept. 23 in a regulator-to-regulator session, pursuant to paragraph 3 of the NAIC Policy Statement on Open Meetings ("Specific companies, entities or individuals"), reviewed three applications by an alien insurer seeking admittance to the *Quarterly Listing of Alien Insurers* and discussed other matters involving insurers already listed.

Ms. Glover moved to adopt the report and minutes. The motion was seconded by Mr. Quan and passed unanimously.

Commissioner Donelon stated that the Task Force is supportive of the Working Group's efforts to maintain insurer solvency within the ranks of the alien surplus lines providers.

3. Receive Comments on NAIC Uniform Nonadmitted Reporting Form

Ms. Donovan referenced comment letters received from regulators and the industry (Attachment Two) following the exposure of a uniform reporting form for surplus lines during the Summer National Meeting. The uniform reporting form was created over the past two years by the Multi-State Surplus Lines Premium Tax (C) Working Group to address the complex reporting of multi-state surplus lines risks.

Ms. Donovan stated that the responses provided useful suggestions for improving the form. However, she conceded that, due to passage of the NRRA — and progress by the Surplus Lines Implementation (EX) Task Force to create a mechanism for the reporting, collection and allocation of surplus lines premium taxes — the uniform reporting form's Excel-based format would not work well in a Web-based environment.

Ms. Donovan stated that the Multi-State Surplus Lines Premium Tax (C) Working Group could leverage its efforts related to the uniform reporting form to craft an "Elements Template" that would include terms and definitions of general agreement that would greatly aid the design of an actual reporting template. Commissioner Donelon stated his belief in the merits of the offer and asked Ms. Donovan, as Working Group chair, whether the Working Group could produce such an "Elements Template" by the 2011 Spring National Meeting. Ms. Donovan replied in the affirmative and accepted the charge.

4. Consider Surplus Lines (C) Task Force 2011 Proposed Charges

Commissioner Donelon read the Task Force's 2011 Proposed Charges (Attachment Three), which included one change from the previous year. The fourth charge from 2010 centered on efforts to "Consider a uniform method of allocating and/or reporting surplus lines and independently procured insurance premium tax on multi-state risks and any other surplus lines issues." This charge was effectively assumed by the Surplus Lines Implementation (EX) Task Force when that Task Force was created in August 2010.

A proposed new charge (to replace the 2010 fourth charge) regards a duty to "Provide assistance, when needed, to address aspects in the surplus lines subtitle of the federal Nonadmitted and Reinsurance Reform Act." This charge anticipates the likely future involvement by this Task Force in reporting to various government agencies regarding the state of the surplus lines market. Some agencies that might request reporting or assistance include the Comptroller General, the Committee on Financial Services of the U.S. House of Representatives and the Committee on Banking, Housing, and Urban Affairs of the U.S. Senate. In addition, the newly created Federal Insurance Office might have a future interest in information from this Task Force. Types of reporting might include the status of efforts to create a mechanism to collect and allocate premium taxes to states on multi-state risks and to promote uniformity with regard to insurer eligibility requirements, broker licensing and other surplus lines matters.

Mr. Goins moved to adopt the Task Force's 2011 Proposed Charges as presented. The motion was seconded by Mr. Gaudiose and passed unanimously.

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

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Draft: 10/13/10

Attachment One
Surplus Lines (C) Task Force
10/20/10

Surplus Lines Financial Analysis (C) Working Group
Conference Call
September 23, 2010

The Surplus Lines Financial Analysis (C) Working Group of the Property and Casualty Insurance (C) Committee met via conference call September 23, 2010. The following Working Group members participated: Gloria Glover, Chair (AK); Louis Quan (CA); Stewart Guerin (LA); and Godwin Ohaechesi (TX).

1. Regulator-to-Regulator Session

The Working Group met in a regulator-to-regulator session pursuant to paragraph 3 of the NAIC Policy Statement on Open Meetings (“Specific companies, entities or individuals”).

During the meeting, the Working Group reviewed applications by alien insurers seeking admittance to the *Quarterly Listing of Alien Insurers* and other matters involving insurers already listed.

Having no further business, the Surplus Lines Financial Analysis (C) Working Group adjourned.

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September 9, 2010

Commissioner James Donelon, (LA) Chair
Surplus Lines (C) Task Force
National Association of Insurance Commissioners
2301 McGee Street
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Dear Commissioner Donelon,

Examination Resources, LLC is an insurance regulatory consulting firm that provides a variety of services for and on behalf of insurance regulators. As such, our goal in providing this comment letter is to hopefully ultimately improve the quality of insurance regulation with regard to multi-state surplus lines premium taxes and the formation of a clearinghouse for the allocation of multi-state surplus lines premium taxes.

Our analysis of the Multi State Workbook includes, but is not limited to, the following issues which we consider should be addressed by state insurance regulators in their future deliberations creating a system of collecting and allocating premium taxes.

- The surplus lines laws of 44 of the 56 U.S. jurisdictions (including American Samoa, District of Columbia, Guam, Northern Mariana Islands, Puerto Rico and the Virgin Islands) provide some form of ocean marine and transportation exemption. Most states provide a complete exemption for “ocean marine” although these exemptions do not necessarily extend to aviation or transport risks. Several jurisdictions do not have a full statutory exemption (or require such business to be written by an eligible surplus lines insurer). These laws do not seem to be factored into the Multi State Workbook and would need to be considered under any future compact or clearinghouse.
- Thirty-seven U.S. jurisdictions have enacted self-procurement/direct placement statutes. These statutes do not seem to be contemplated by

the Multi State Workbook and should be considered in order to have a comprehensive allocation methodology.

- There are 22 U.S. jurisdictions which exempt nonadmitted insurers from surplus lines regulation insurance procured by industrial insureds, and an additional 10 states where an “industrial insured” exemption is recognized with respect to captive insurers only. While the Nonadmitted and Reinsurance Reform Act language provides a definition for an “exempt commercial purchaser”, it does not recognize the variation between statutes concerning the captive issue. Our opinion is that this issue should be deliberated by regulators when developing the Multi State Workbook.

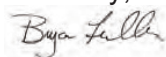
Other issues to be considered relating to creation of nationwide uniform requirements, forms and procedures, such as an interstate compact that provides for the reporting, payment, collection and allocation of premium taxes for nonadmitted insurance include, but are not limited to, the following:

- Our understanding is that Alaska, for example, not only has a 2.7% surplus lines premium tax, but also has a 1% filing fee and a 0.75% tax for wet marine and transportation. The Multi State Workbook does not seem to address filing fees or other fees in all instances.
- Our understanding is that Kentucky, for example, administers their surplus lines premium taxes by municipality so that it would not be appropriate to apply a uniform 3% premium tax across the state unless those statutes were changed.
- Stamping fees do not appear to be addressed appropriately in all jurisdictions according to our understanding of various jurisdictions' surplus lines laws.
- Our understanding is that New Jersey, for example, has recently increased their surplus lines premium taxes to 5% from the 3% listed in the Multi State Workbook.

As a general observation, are Excel spreadsheets an appropriate filing format for such a reporting, payment, collection and allocation mechanism? It would appear that such a format could pose data integrity problems due to cross-pollination of spreadsheets and formulas.

We stand ready to assist, if necessary, as the Working Group and Task Force continue their very important work relating to an opportunity to fix what has been a decades-long problem for the U.S. insurance regulatory community.

Sincerely,



Bryan J. Fuller
Director



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Daniel F. Maher
Executive Director

September 1, 2010

Mr. John Bauer, Esq.
Chief Counsel, Regulatory Affairs
National Association of Insurance Commissioners
2301 McGee, Suite 800
Kansas City, MO 64108-2604

Re: Uniform Surplus Lines Reporting Form Draft

Dear Mr. Bauer,

This is further to the request for comments made by the NAIC Surplus Lines Task Force at its Seattle meeting on August 16th and the subsequent August 18th email request for comments by Robert Schump, IID Manager of the NAIC.

The following comments will primarily address whether the Uniform Surplus Lines Reporting Form (hereinafter the "Form") 1) currently meets or 2) after modifications will be legally able to meet the requirements of the Nonadmitted and Reinsurance Reform Act (hereinafter the "NRRA").

The NRRA provides, among other things, the following:

"...Congress intends that each State adopt nationwide uniform requirements, forms and procedures, such as an interstate compact, that provides for the reporting, payment, collection and allocation of premium taxes...."

"No State other than the home State of an insured may require any premium tax payment for nonadmitted insurance".

The Form shows a column for "%, allocation". However, the Multi-State Surplus Lines Premium Tax (C) Working Group (hereinafter the "Working Group"), which developed the Form, has not addressed what tax allocation formulas will be used by the brokers to determine the percentage of risk in each state. **The Form cannot be completed unless and until allocation formulas are adopted.**

The Working Group, in one of its teleconferences, discussed the possibility that the brokers could use each state's separate tax allocation formula and apply it to the gross premium and then file the Form with each state on each separate multistate transaction. Such an approach would not provide any efficiencies for brokers. It would effectively codify the current inefficiencies, and it would violate the NRRA uniformity requirements and the exclusive jurisdiction of the "home State" provision.

The States could possibly agree to apply the current tax allocation formulas of the insured's home State to the Form. However, since some states do not allocate and instead charge tax on 100% of the premium without regard to the portion of the risk located in other states, this approach is likely to be rejected. For

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the sake of efficiency for the brokers and fairness for the states, uniform allocation formulas need to be adopted by all states, which will require changes to state statutes or regulations. In any event, the Form is not viable until a decision on allocation formulas is made.

The NRRRA presents additional legal hurdles, which the Form probably cannot clear as currently drafted. The NRRRA states "...an insured's home State may require surplus lines brokers....to annually file tax allocation reports with the insured's home State detailing the portion of the nonadmitted insurance policy premium or premiums attributable to properties, risks or exposures located in each state."

The Form currently contemplates applying each state's separate tax rate plus other assessments and charges to the portion of risk/premium allocated to such state. Under the NRRRA's exclusive home State jurisdiction and non home State express preemption provisions, a home State will have no legal authority to require a broker licensee to pay taxes on any portion of the risk at a rate other than the home State's rate absent new statutory authority in the home State. Currently, no state has any provision in its surplus lines law to compel a surplus lines broker to pay taxes other than taxes belonging to that specific state. No state will have authority to collect taxes on behalf of any other state absent a legally binding agreement between such states. The reason the NRRRA contemplates an interstate compact is to permit the states to adopt a uniform law/legal approach to collection, allocation and distribution of taxes. **In any event, a home State cannot assert or impose various tax rates on multistate surplus lines risks as contemplated by the Form unless and until the home State statute requires it and the other states contractually consent to the process.**

The rate of taxation to be applied to a multistate risk remains an outstanding question. The states could apply only the home State's tax rate to all allocations. The states could possibly amend their laws to adopt a single-blended tax rate applicable to multistate risks or possibly permit each state's rate to apply to its allocated portion of risk.

The Form, as currently drafted, does not take into account that some states have different rates of taxation for different classes of business and sometimes apply certain charges (such as fire district charges) to only a portion of the premium for certain classes of business, such as multiperil policies. While this is more a technical problem with the Form, the technology behind the Form may not be sufficiently sophisticated to address all of these issues.

Use of the Form without an interstate compact would require the Form to be filed only in the home State of each insured. Under this scenario, each state would become a separate clearinghouse for collecting data and taxes for redistribution to the other 55 jurisdictions included under the NRRRA. The creation of 56 separate clearinghouses would require dedicated personnel, time, money and equipment from each state to the process. The August 19th email from Bob Schump notes that if the Form were utilized, it is likely to take the form of an electronic or web-based reporting system. Developing software for each state, software that will be compatible with each state's current software and programs, will also be expensive and time consuming. Moreover, any single state's reporting system may not necessarily integrate well, from a data upload standpoint, with the software of the other 55 jurisdictions. The compact alternative could provide one centralized clearinghouse, removing the need for personnel, time,



money and other dedicated resources from each state and allow the states to receive all necessary data and applicable taxes from one single clearinghouse.

Currently, the Form has no web interface supporting software or database and reporting platform.

The Form does not address all of the issues regarding uniformity contemplated by the NRRA.

Two issues stand out in regard to other powers delegated to the states under the NRRA.

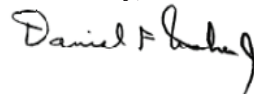
The first is that the Form proposal does not address the NRRA's call for uniform foreign surplus lines insurer eligibility standards. This is a very important issue for states with substantial surplus lines volume.

The second issue relates to independently procured, nonadmitted insurance policies. The Form appears to be geared to reporting by surplus lines licensees. It maybe a bit unrealistic to expect insureds who generally have limited knowledge about surplus lines compliance to complete a Form, where many of the fields of information, such as an insurer's NAIC number, are unknown to them.

In conclusion, the Form could be amended to improve its efficiency but it is not likely to meet all NRRA requirements without a compact. A compact is both uniform legislation and a contract among the compacting states. These are the two essential elements required to implement the NRRA.

Please let me know if you require any additional information.

Yours Truly,



Daniel F. Maher
Executive Director

Cc: Bob Schump
Eugene Nunziata

DFM/oz



September 8, 2010

Ohio's Comments on Multi-State Surplus Lines Premium Tax Report:

Thank you for the opportunity to provide comments on the Uniform Surplus Lines Reporting Form. We greatly appreciate the work that has been done thus far and we look forward to assisting in developing a national solution.

For many years now, Felisa Brown & Maureen Motter have had daily contact with the surplus lines agents and their administrative staff who report the business & pay the surplus lines taxes to Ohio. We have first-hand knowledge of the questions & confusion & errors that take place when reporting to Ohio. Some of our comments/questions are intended to provide or seek clarity on behalf of those persons responsible for completing the form.

We also reflected on the questions & confusion that might arise as states distribute monies to each other on the multi-state risks. Some of our comments/questions are intended to provide or seek clarity for those of us that may possibly be tasked with distributing taxes & fees to states that we are unfamiliar with.

Comments Regarding Columns A thru L:

Column A-It appears that from the definitions tab that this column is to be a transaction or placement number that is entered by the filer. Should we not label as such and allow for multiple digits. It is likely that many filers will use the policy number as the transaction/placement number.

Column B- Are we seeking insured's name, address, city, state & zip or just insured's name, city & state? Would we want to break this into two columns-name in one & address in another? What location information are we seeking on multi-state risk or multiple locations in a single state? Do we want the named insured's location from the top of the dec page? We should clarify what we are seeking as input.

Column D- Is Endorsement to be the selection for mid-term policy changes? It would probably be clearer to use the term Change as opposed to Endorsement, since the policy change may not have always been due to the addition or deletion of an endorsement.

Cancellation should also be included as a type to avoid confusion when reporting.

Column E-It appears from the definitions tab that this is to be an effective date column. For policy changes, are we seeking the effective date of the original policy or the effective date of the change? We should probably clarify. It may be helpful to re-label column to Policy or Change Effective Date or perhaps just Policy Effective Date?

Column F- To avoid filer confusion, recommend that we re-label this to Policy Expiration Date

Column G- In many instances, brokers or administrative staff are not going to know to what annual statement line(s) an insurer has allocated the premium for a particular policy. It is also likely that staff may not know if a policy is claims-made or occurrence. Is this important for us as regulators to know? It is recommended that we provide a listing of types of policies that is loosely based on the annual statement. The following is provided for example purposes. There are perhaps a few items missing, such as workers comp.

27	Boiler & Machinery
26	Burglary & Theft
21	Commercial Auto
5	Commercial Multiple Peril or Package
28	Credit
23	Fidelity & Surety
1	Fire and Allied Lines
17	General Liability
9	Inland Marine
18	Liquor Liability
11	Medical Malpractice
36	Professional Liability
99	Other

Column H-The definition tab states this is the amount of insurance. Are we intending for this to be a limit of liability? Is this amount to represent the aggregate limit of liability? With multiple limits and sub-limits, a person reporting may not know what to enter. In Ohio, we have asked for the aggregate limit of liability & we sometimes get questions because the policy doesn't have an aggregate. We might want to provide clarification. Furthermore, even though we collect this data today, do we really need it?

Column I-If the filer completes correctly, should Column I and **Column N** from the **Grand Total** sheet be equal? If so, perhaps the columns should be labeled the same. This could be pointed out to the filer as a check to see if completed correctly.

Column K- The filer may be confused as to what company should have an NAIC#. Recommend column heading of Insurance Company NAIC#.

Column L- The filer may be confused as to what company's name & address should be entered. Recommend column heading of Insurance Company Name. Do we need insurance company address too? If we think we need address information, should it be a separate column?

Comments Regarding Individual State Worksheets:

The first question is whether it has been confirmed with every state that the individual state spreadsheet is correct? A prior draft of the spreadsheet had not taken into consideration that there are some instances in Ohio where the premium is exempt for tax.

It is recommended that the column headings be more descriptive as to where we anticipate a filer is to enter a dollar amount and where the spreadsheet is formula driven.

Using Alaska as an example, recommend re-label to

Column M- ENTER % of Premium Allocated to State

Column N-Calculated Written Premium & Taxable Fees Allocated to State

Column O-Calculated State Taxes Due Based on Tax Rate of 2.7%

There are about 20 states that appear that would have this recommended identical labeling.

There are then several states that have stamping fees or other taxes that also appear to be a percentage of premium. Similar to Column O, it is recommended that these column headings be re-labeled to Calculated _____ Due Based on Rate of ___%.

There were a few states that it appears that filer will have to enter fees that are taxable or non-taxable. Similar to above, it is recommended that when we expect filers to enter data, the column should be labeled as ENTER. Not being familiar with these states, it is unclear as to how these columns do or do not interact with Column I.

In Ohio, we have premium that is not subject to the surplus lines tax. This exempt premium amount would have to be entered by the filer, so this too should be labeled as ENTER Exempt Premium.

Comments Regarding Grand Total Worksheet:

Since the last few columns of the grand total worksheet are calculated by adding together the individual state spreadsheets, it is recommended that the column headings of the grand total worksheet be labeled CALCULATED. It is also recommended that the columns on the grand total spreadsheet match up with the individual state columns. By having all the various types of state columns (exempt premium, stamping fees, other fees, fire marshal tax, etc.) displayed on the grand total worksheet, the filer will be able to confirm they have entered all the data correctly and completely.

Comments Regarding Distribution of Taxes by Home State:

While we are unfamiliar with other states' laws and processes, we will be responsible as a home state to distribute monies to them. To assist, instructions should clearly indicate which column(s) are amounts that are to be remitted to the state, which column(s) are amounts that are remitted to other entities, to whom these monies should be made payable to & to where these monies should be sent.

Additional Comments/Observations:

A worksheet is labeled foreign country. To whom will this money be remitted?

Since the proposal is a locked spreadsheet with formulas in many cells, will the final product have sufficient number of rows so that multiple files won't be necessary?

For larger-sized brokers, there will likely be a request for submitting this data via a bulk upload as opposed to entering all the data on this form. We were asked to do similar for our on-line reporting system.

Since this form is an electronic form, it appears that signature & notarization would not be feasible. If signature & notarization would be necessary, perhaps a separate form should be considered to address this.

Some questions/observations about the workbook.

1. The CT fees column needs to be unprotected.
2. Entry on "TS" worksheet: Recommend that "fees, etc" be separated from "written premium." Column 1 shows these amounts combined into a single amount - which is effectively being allocated in the same manner as premium, which may not be appropriate.
3. Entry on "TS" worksheet, "same as above" should not be permitted. Data elements should not be dependent on viewing a spreadsheet to interpret what is "above" an entry. If the worksheet went through a data sort, the data "above" would not be a true answer after the sort.

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STATE OF WEST VIRGINIA
Offices of the Insurance Commissioner

JOE MANCHIN III
Governor

JANE L. CLINE
Insurance Commissioner

September 3, 2010

Mr. Robert Schump, IID Manager
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Kansas City, MO 64108-2604

Dear Mr. Schump:

West Virginia is appreciative of the hard work and progress that has been made in the development of a Uniform Surplus Lines Reporting Form. We look forward to the future enhancements that a web-based reporting interface will have in simplifying an inherently complicated process.

The West Virginia section of the excel model needs amended to reflect the following two tax items:

- WV worksheet, Column P – "Other Tax (Regulatory Fee) .5%" should be 0.55% instead.
- Pmt Dates worksheet, Rows 80 & 81 – WV's annual tax & surcharge due date is March 1, not March 25th. The other quarterly due dates are correct. Due dates should be reported as 4/25, 7/25, 10/25 & 3/1.

Thank you for making these changes in the excel model form.

Sincerely,

Michael D. Riley
Assistant Commissioner
WV Offices of the Insurance Commissioner

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**2011 PROPOSED CHARGES
SURPLUS LINES (C) TASK FORCE**

The mission of the Surplus Lines (C) Task Force is to monitor the surplus lines market and its operation and regulation, including the activity and financial condition of U.S. and non-U.S. surplus lines insurers by providing a forum for discussion of issues and to develop or amend model regulation.

Ongoing Maintenance of NAIC Programs, Products or Services

1. Maintain the IID Plan of Operation and its requirements relating to standards for inclusion on the NAIC Quarterly Listing of Alien Insurers ("Quarterly Listing") concerning capital and/or surplus funds, U.S. trust accounts and fitness of management among other criteria. This charge is on-going and will be assumed by the IID Plan of Operation Review Group — *Essential*
2. Provide NAIC/IID financial staff guidance and expertise relative to regulatory policy and practices with respect to individual companies and Lloyd's syndicates that are either listed on or seeking admission to the Quarterly Listing. This charge is on-going and will be assumed by the Surplus Lines Financial Analysis Working Group. The authority of the working group is limited to that of an advisory body, with a goal of formulating recommendations to the Chairs of the Task Force and Property/Casualty Insurance Committee for the appropriate regulatory response. Issues upon which the Surplus Lines Financial Analysis Working Group may formulate a recommendation might include, but are not limited to, approval or disapproval of applicants to the Quarterly Listing, delisting of listed insurers, changes to trust fund requirements, or placement of limitations or restrictions on a listed insurer's business activity in the United States — *Essential*
3. Perform financial analysis of surplus lines market utilizing the NAIC Financial Data Repository and other sources in order to prepare a regulator report — *Important*
4. Provide assistance when needed to address aspects in the surplus lines subtitle of the Nonadmitted and Reinsurance Reform Act — *Important*

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