

Department of Legislative Services
Maryland General Assembly
2011 Session

FISCAL AND POLICY NOTE
Revised

Senate Bill 694
Finance

(Senators Kelley and Middleton)

Economic Matters

Insurance - Surplus Lines

This bill amends the Maryland Surplus Lines Insurance Law to comply with the federal Nonadmitted and Reinsurance Reform Act of 2010 (NRRA). The bill also requires the Maryland Insurance Administration (MIA) to study the various approaches taken by other states to implement NRRA, paying specific attention to the approaches taken by contiguous states, and report the findings of the study by January 1, 2012. If the Commissioner so requests, qualified surplus lines brokers must provide the Commissioner, to the extent practicable, information regarding written premium on risks located in Maryland and multistate risks so as to provide more information regarding premium tax revenue.

The bill takes effect July 1, 2011.

Fiscal Summary

State Effect: Although the bill's requirement that only an insured's home state may license a surplus lines broker results in a decrease in special fund license fee revenues, this impact is also due to the federal law which takes effect three weeks after the bill. The amount cannot be reasonably estimated because it is not known how many nonresidents will not apply for or renew a license. Given the bill's July 1, 2011 effective date and the study's January 1, 2012 reporting date, MIA can conduct the study with existing resources. Likewise, requiring participation in the National Insurance Producer Database does not increase expenditures because MIA already participates in the database.

Local Effect: None.

Small Business Effect: None.

Analysis

Bill Summary:

Premium Taxes: For policies effective on or after July 21, 2011, the State of Maryland may only collect premium receipts tax payments and reports for nonadmitted insurance if Maryland is the home state of an insured. The bill clarifies that, for policies effective before July 21, 2011, the premium tax receipts must be computed according to the portion of property, risks, or exposures located or to be performed in the State.

If a surplus lines broker is used, each surplus lines broker must provide the Commissioner with a report, on a form that the Commissioner prescribes, on the business subject to tax during the period since the last report. The surplus lines broker must pay the total amount of tax as stated in the report.

If a surplus lines broker is not used, for policies effective on or after July 21, 2011, an insured must provide the Commissioner with a report, on a form that the Commissioner prescribes, on the business subject to tax during the period since the last report. The insured must provide this report on or before March 15 and September 15 of each year or at another interval that the Commissioner directs. The insured must pay the total amount of tax as stated in the report. For policies effective before July 21, 2011, an insured must file the report within 60 days after the date that the insurance was procured.

Nonadmitted Insurers: The bill prohibits the Commissioner from approving a nonadmitted insurer as a surplus lines insurer unless the insurer is authorized in its domiciliary jurisdiction to write the type of insurance it seeks to write. A nonadmitted insurer must also have the necessary capital and surplus (generally at least \$15 million) and file with the Commissioner specified information. A surplus lines broker may not place surplus lines insurance with a nonadmitted insurer that has not been approved by the Commissioner in accordance with these requirements.

However, if a foreign nonadmitted insurer has capital and surplus of \$4.5 million or greater, the Commissioner may affirmatively find that the nonadmitted insurer is acceptable based on specified findings, including the insurer's reputation, quality of management, and underwriting profit and investment income trends.

The bill replaces the Maryland Surplus Lines Insurance Law's requirements for an exemption from the duty to perform a diligent search prior to procurement of a surplus lines insurance policy from a nonadmitted insurer and inserts NRRA requirements.

The Commissioner must participate in the National Insurance Producer Database maintained by the National Association of Insurance Commissioners (NAIC).

Licensing of Surplus Lines Brokers: If a surplus lines broker is licensed in the insured's home state, the broker is not required to obtain a certificate of qualification to act as a broker in this State if Maryland is not the home state of the insured.

Uniform Regulation: The bill requires that the Commissioner cooperate with other states to adopt and implement uniform requirements for nonadmitted insurance in compliance with NRRA. For policies effective on or after July 21, 2011, the placement and regulation of nonadmitted insurance is subject to the statutory and regulatory requirements solely of the insured's home state.

Current Law/Background: According to the National Conference of State Legislatures (NCSL) surplus lines insurance is insurance that is not available from licensed insurers in the state. Because licensed insurers are unwilling to underwrite the risk, a consumer must go to an unauthorized (nonadmitted) insurer. MIA advises that there are currently 135 approved surplus lines insurers and 1,463 surplus lines brokers operating with a certificate of qualification in the State of Maryland.

In Maryland, surplus lines insurance may only be procured from an unauthorized insurer in specified circumstances. A diligent search must first be made among the authorized insurers that are writing the particular kind and class of insurance in the State. A diligent search is completed if the risk is declined by three authorized insurers that are writing the particular kind and class of insurance in the State and by each insurer for which the insurance producer has been appointed that the insurance producer knows, or should know, is actually writing the particular kind and class of insurance on a broad basis. The insurance producer must include the declinations in an affidavit to the Commissioner at the time the surplus lines insurance is placed. A diligent search is not required for any coverage on a list of eligible surplus lines coverages compiled by the Commissioner or if the diligent search is waived by a commercial insured in accordance with the process determined by the Commissioner.

Additionally, if a broker is used to procure the surplus lines insurance from an unauthorized insurer, the broker must be qualified. An applicant for a broker certificate of qualification must be qualified as an insurance producer for property and casualty insurance and be competent and trustworthy, as determined by the Commissioner.

A surplus lines broker may not place surplus lines insurance with an unauthorized insurer that the Commissioner (1) has not approved; (2) has determined to be insolvent or financially unsafe; or (3) has determined to have refused to pay just claims. A surplus lines broker may also place surplus lines insurance with an approved insurer by the Commissioner, including an alien insurer that has qualified with the nonadmitted insurer information office of NAIC.

In order to be approved by the Commissioner, an insurer must annually file (1) a written request for approval as a surplus lines insurer for those surplus lines authorized by the Commissioner; (2) a certified copy of its annual statement showing a line-item account of its surplus lines business written on risks located in the State; (3) a certificate of compliance issued by the insurance department of the insurer's state of domicile; and (4) a certificate evidencing a deposit issued by the official custodian of deposits of the insurer's state of domicile.

The State charges a 3% tax on all gross premiums charged for surplus lines insurance, less any returned premiums. Upon delivery of specified required materials, a surplus lines broker must charge the insured the amount of the tax in addition to the full amount of the gross premium charged by the insurer. If a surplus lines policy covers risks only partly in the State, the tax payable must be computed on the part of the premium that is properly allocable to the risks located in the State.

On or before March 15 and September 15 of each year, a surplus lines broker must file with the Commissioner a semiannual statement that reports on business subject to tax during the preceding half calendar year and pay to the Commissioner the total amount of tax imposed by State law. The Commissioner must verify the semiannual statement and that it contains specified required information.

The Nonadmitted and Reinsurance Reform Act

The U.S. Congress passed the Dodd-Frank Wall Street Reform and Consumer Protection Act in 2010, which included NRRRA. According to the National Association of Professional Surplus Lines Offices, NRRRA simplifies regulatory compliance obligations and premium tax payments for surplus lines brokers involved in multistate transactions by allowing only the insured's home state to collect premium taxes and license a surplus lines broker. NRRRA allows states to enter into a compact to share the premium taxes. NRRRA defines "home state" as the insured's principal place of business or principal residence or, if 100% of the insured risk is located out of the state with the principal place of business or principal residence, the state with the greatest percentage of the insured's taxable premium for that insurance contract.

NRRRA also allows surplus lines brokers to place insurance on behalf of commercial purchasers meeting specified requirements without having to first perform a diligent search requirement. The commercial purchasers must employ a "qualified risk manager" who has the appropriate education and training to properly represent the insured and, in the previous year, had more than \$100,000 in property and casualty insurance premium on a nationwide basis. The commercial purchaser must also meet one specified additional criterion.

NRRA creates uniform national eligibility requirements to be used in every state. This may eliminate situations in which a surplus lines broker conducting multistate transactions is eligible in one state but not another.

NRRA takes effect July 21, 2011. States must pass legislation prior to this date in order to avoid any conflicts with federal law.

State Fiscal Effect: MIA estimates that annual Maryland surplus lines premiums exceed \$400 million. This amount accounts for approximately 1.43% of the total amount in the United States. As noted above, the premium tax for surplus lines is 3%. Therefore, Maryland collects approximately \$12 million in premium tax on surplus lines insurance. This amount represents about 3% of total premium tax revenue in the State. Starting on July 21, 2011, NRRA prohibits any state other than an insured's home state from collecting premium tax payments. This means that, unless a nationwide solution is reached before then, nonadmitted premium tax on multistate risks is collected only by the home state and may not be redistributed to other states.

The bill does not specifically authorize the Commissioner to enter into a compact but does require cooperation with other states. However, if the Commissioner does enter into a compact, Maryland may still collect surplus lines premium tax on property or risks located in the State even though the insured's home state is elsewhere. If the Commissioner chooses to not enter a compact, the State keeps all surplus lines premium tax collected from insureds with Maryland as a home state, even if the insureds have risks located in other states. Thus, the bill's effect on Maryland's surplus lines premium tax collection is unknown.

The bill also complies with NRRA's provision that only an insured's home state may require a surplus lines broker to be licensed. MIA advises that it currently licenses 625 nonresident surplus lines brokers. MIA further advises that it is not possible to predict how many nonresidents will not apply for or renew a license; however, because the licensee population is relatively small and the license fee is \$200, any decline in special fund fee revenue should be minimal and would occur in the absence of the bill anyway.

Additional Information

Prior Introductions: None.

Cross File: Although designated as a cross file, HB 911 (Delegate Rudolph – Economic Matters) is no longer identical. However, HB 959 (Delegate Davis – Economic Matters), which is not designated as a cross file, is identical.

Information Source(s): Maryland Insurance Administration, Comptroller's Office, National Conference of Insurance Legislators, National Conference of State Legislatures, National Association of Surplus Lines Offices, Department of Legislative Services

Fiscal Note History: First Reader - March 1, 2011
ncs/ljm Revised - Senate Third Reader - April 4, 2011
Revised - Updated Information - April 22, 2011

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