SB 764

Department of Legislative Services

Maryland General Assembly
2012 Session

FISCAL AND POLICY NOTE
Revised

Senate Bill 764 (Senator Kelley, *et al.*)
Finance Economic Matters

Fraudulent Insurance Acts - Individual Sureties - Contracts of Surety Insurance

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This bill makes it a fraudulent insurance act for an individual surety to solicit or issue a surety bond or contract of surety insurance. This addition to fraudulent insurance acts, however, does not apply to (1) contractors who are authorized to submit individual surety bonds to meet the requirements for bid and performance bonds on certain State projects; and (2) uncompensated bail bondsmen operating in circuit courts.

The bill requires the Maryland Insurance Administration (MIA) to conduct an analysis of the practices of corporate sureties and individual sureties in the State. MIA must submit an interim report on its findings and recommendations to the Senate Finance Committee, the Senate Education, Health, and Environmental Affairs Committee, the House Economic Matters Committee, and the House Health and Government Operations Committee by December 1, 2012. MIA must submit a final report to these committees by December 1, 2013.

The bill takes effect June 1, 2012.

Fiscal Summary

State Effect: Special fund expenditures increase by $128,400 in FY 2013 and $59,300 in FY 2014 to hire two contractual staff to assist MIA in performing and preparing the required analysis and reports. Despite the bill's June 1, 2012 effective date, it is assumed that no costs are incurred in FY 2012. Enforcement can be handled with existing resources. The bill's imposition of existing penalty provisions is not anticipated to materially affect State finances or operations.

(in dollars)	FY 2012	FY 2013	FY 2014	FY 2015	FY 2016
Revenues	$0	$0	$0	$0	$0
SF Expenditure	0	128,400	59,300	0	0
Net Effect	$0	($128,400)	($59,300)	$0	$0

Note:() = decrease; GF = general funds; FF = federal funds; SF = special funds; - = indeterminate effect

Local Effect: The bill's imposition of existing penalty provisions is not anticipated to materially affect local government finances or operations.

Small Business Effect: Minimal.

Analysis

Bill Summary: The bill defines "individual surety" as a person that issues surety bonds or contracts of surety insurance and does not have a certificate of authority issued by the Insurance Commissioner.

A violation of the bill is a felony and punishable by a fine of up to $10,000, imprisonment for up to 15 years, or both if the claim or act that is the subject of the fraud has a value of $300 or more. If the claim or act that is the subject of the fraud has a value of less than $300, a violation is a misdemeanor and punishable by a fine of up to $10,000, imprisonment for up to 18 months, or both.

In conducting the required analysis of corporate and individual sureties, MIA must consult with any person or entity that MIA determines appropriate, including corporate sureties, individual sureties, insurance producers, contractors, the Maryland Department of Transportation (MDOT), the Department of General Services (DGS), and the Maryland Property and Casualty Insurance Guaranty Corporation.

In its analysis, MIA must consider the possibility of licensing individual sureties, the current state of the individual surety market, regulation of individual sureties in other states, the adequacy of current State law, and the existence of any programs, including the Maryland State Bond Development and Financing Authority, that enhance the availability of surety bonds or contracts of surety insurance for specified businesses. MIA must also conduct surveys of (1) the Maryland Property and Casualty Insurance Guaranty Corporation; (2) the Board of Public Works, MDOT, DGS, and a representative sample of corporate sureties and individual sureties; and (3) a representative sample of contractors that have held a surety bond or contract of surety insurance issued by an insolvent insurer.

Current Law: Except in specified circumstances, a person may not act as an insurer and an insurer may not engage in the insurance business in the State unless the person has a certificate of authority issued by the Commissioner. In November 2010, MIA issued a bulletin stating that the certificate of authority requirement includes providing surety insurance or directly or indirectly acting as an insurance producer or otherwise assisting an unauthorized insurer. The Office of Attorney General confirmed this in a January 2011 letter to the Maryland General Assembly.

Only a corporate entity or reciprocal insurer may receive a certificate of authority. However, Chapter 299 of 2006 created a temporary exception (which has since been extended until September 30, 2014) that allows contractors to submit individual surety bonds, or any other security authorized by federal or State regulation or that is satisfactory to the procurement unit awarding the contract, to meet the requirements for bid and performance bonds on certain State procurements. Individual surety bonds are only acceptable if (1) the contractor has been denied corporate surety credit; (2) the individual surety transacts business through a licensed insurance agency; and (3) an affidavit and UCC-1 filing are provided with the bond. Assets allowed by Chapter 299 are:

- cash or certificates of deposit;
- cash equivalents or other assets held by a federally insured financial institution, such as an irrevocable trust receipt;
- U.S. government securities;
- stocks and bonds;
- real property that meets criteria specified in the law; and
- irrevocable letters of credit issued by a federally insured financial institution.

The individual surety must pledge one or more of these assets in an amount equal to or greater than the value of the bonds required for the procurement. The law includes additional rules for calculating the value of assets pledged by the surety whose worth varies over time, such as stocks and real estate. Assets pledged by an individual surety may not be pledged to any other purpose until the asset is released by the unit.

A person that commits a fraudulent insurance act with a value of $300 or more is guilty of a felony and on conviction subject to a fine of up to three times the value of the claim and $10,000 and/or imprisonment for up to 15 years. If the value of the claim is less than $300, a person is guilty of a misdemeanor and on conviction subject to restitution, a fine of up to three times the value of the claim, and $10,000 and/or imprisonment for up to 18 months.

Background: A surety bond is a three-way contract between the State, a contractor, and a surety (typically an insurance company or other established financial company). Surety bonds require the surety to cover any losses incurred by the State if the contractor defaults or otherwise cannot complete a project as promised. Contractors purchase surety bonds in part to assure those seeking their services that they are legitimate businesses and provide reliable services.

An individual surety bond obliges an individual rather than an insurance company to cover the financial losses incurred by the State in the event of a default by a contractor. Individual surety bonds must provide evidence that the individual has the financial resources necessary to cover possible losses.

State Fiscal Effect: Given the complexity of the bill's study reporting requirements, MIA advises that two contractual staff are necessary to perform the required analysis and prepare the reports. The Department of Legislative Services concurs.

Accordingly, general fund expenditures increase by $128,407 in fiscal 2013, which reflects a July 1, 2102 start date and $59,312 in fiscal 2014, which maintains the employees through December 31, 2013. This estimate reflects the cost of hiring two contractual staff to assist MIA in performing data collection; interviewing of insurers, producers, contractors, and any necessary federal or State agency representatives; developing, administering, and analyzing the required surveys; and analyzing current law in Maryland and other states by the required final reporting date of December 1, 2013. It includes salaries, fringe benefits, one-time start-up costs, and ongoing operating expenses.

Contractual Positions	2
Salary and Fringe Benefits	$122,822
Other Operating Expenses	5,585
Total FY 2013 State Expenditures	**$128,407**

MIA advises that the duties of both contractual employees will be completed by the third quarter of fiscal 2014; thus, no fiscal impact is anticipated after fiscal 2014.

Additional Information

Prior Introductions: None.

Cross File: HB 885 (Delegate Jameson, *et al.*) - Economic Matters.

Information Source(s): Maryland Insurance Administration, Department of Legislative Services

Fiscal Note History:	First Reader - March 1, 2012
ncs/mwc	Revised - Senate Third Reader - April 5, 2012

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