



The NRRA: A New Era for Surplus Lines

An Overview

Association of Lloyd's Brokers

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Chicago IL



What NRRA Does – Brokers

One State Concept

- I. Only one state – the “home state” of the insured -- may tax a surplus lines transaction
- II. Only one state – the “home state” of the insured -- may regulate a surplus lines placement



What NRRA Does

- What is “home state” of Insured?
 - Principal place of business
 - “Nerve center” test
 - Hertz vs. Friend





What NRRA Does – Broker Licensing

- State must participate in NAIC (NIPR) electronic database licensing surplus lines brokers by July 21, 2012
- If not – can't collect fees

What NRRA Does – Companies Uniform Eligibility Standards

1. Domestic Surplus Lines Companies

- Two NAIC Model Bill Requirements
 - Licensed in domiciliary state
 - Capital & surplus -

Greater of state requirement or
\$15,000,000

2. Alien Surplus Lines Companies

- NAIC Quarterly Listing of Alien Insurers



What NRRA Does – Insureds Streamlined Access



- Exempt Commercial Purchaser (ECP)
 - No diligent search requirement
 - Broker disclosure
 - Insurance “may or may not be available from Admitted Market”
 - “With greater protection” (coverage)
 - “More regulatory oversight”
 - Insured must provide subsequent written request to procure or place insurance with surplus lines carrier

What NRRA Does

Definition of ECP

Exempt Commercial Purchaser

- Employs/Retains Qualified Risk Manager
- Annual P/C Premium \$100,000
- Meets one other requirement:
 - Net worth - \$20,000,000
 - Annual revenue - \$50,000,000*
 - Full time employees - 500 / 1,000**
 - Not-for-profit or public entity
 - annual budget - \$30,000,000*
 - Municipal population - 50,000

*Subject to CPI every 5 years

** Affiliate



What NRRA Does Other Provisions



- Congressional “intent” for each state to adopt nationwide uniformity in surplus lines taxation – ***requirements, forms and procedures***
 - Applies to entire surplus lines tax system
 - Single and Multi-state surplus lines transactions

What NRRA Does Other Provisions



Tax Compacts

- Imposes restrictions on voluntary interstate tax sharing compacts by limiting broker reporting to an annual tax allocation report
- Subject to the congressional “intent” of nationwide uniformity

NRRA:

- *Does not authorize a tax compact*
- *Does not mandate a tax compact*
- *Does not require a tax compact*
- *Sets no deadline for tax compact implementation*

Tax Sharing Compacts

Two Proposals

NIMA – Nonadmitted Insurance Multistate Agreement

- NAIC sponsored
- Little structure – “agreement”
- Detailed Allocation Formula
- No clearinghouse established
- twelve states – 8/1/2011

SLIMPACT– Surplus Lines Insurance Multistate Compliance Compact

- NCOIL sponsored
- Traditional compact
- Promotes uniformity
- Contains consumer protections
- No clearinghouse established
- Nine states – 8/9/2011



Tax Sharing Compacts

- Are these compacts stable?
 - Some states will lose money
 - Zero sum game
 - State Voluntary tax sharing compacts have not worked in the past
 - Only “International Fuel Tax Agreement” (IFTA) in existence – Legislated by congress
 - Insureds pay for clearinghouse costs
 - IFTA – States / provinces absorb costs



Tax Assessment Blues

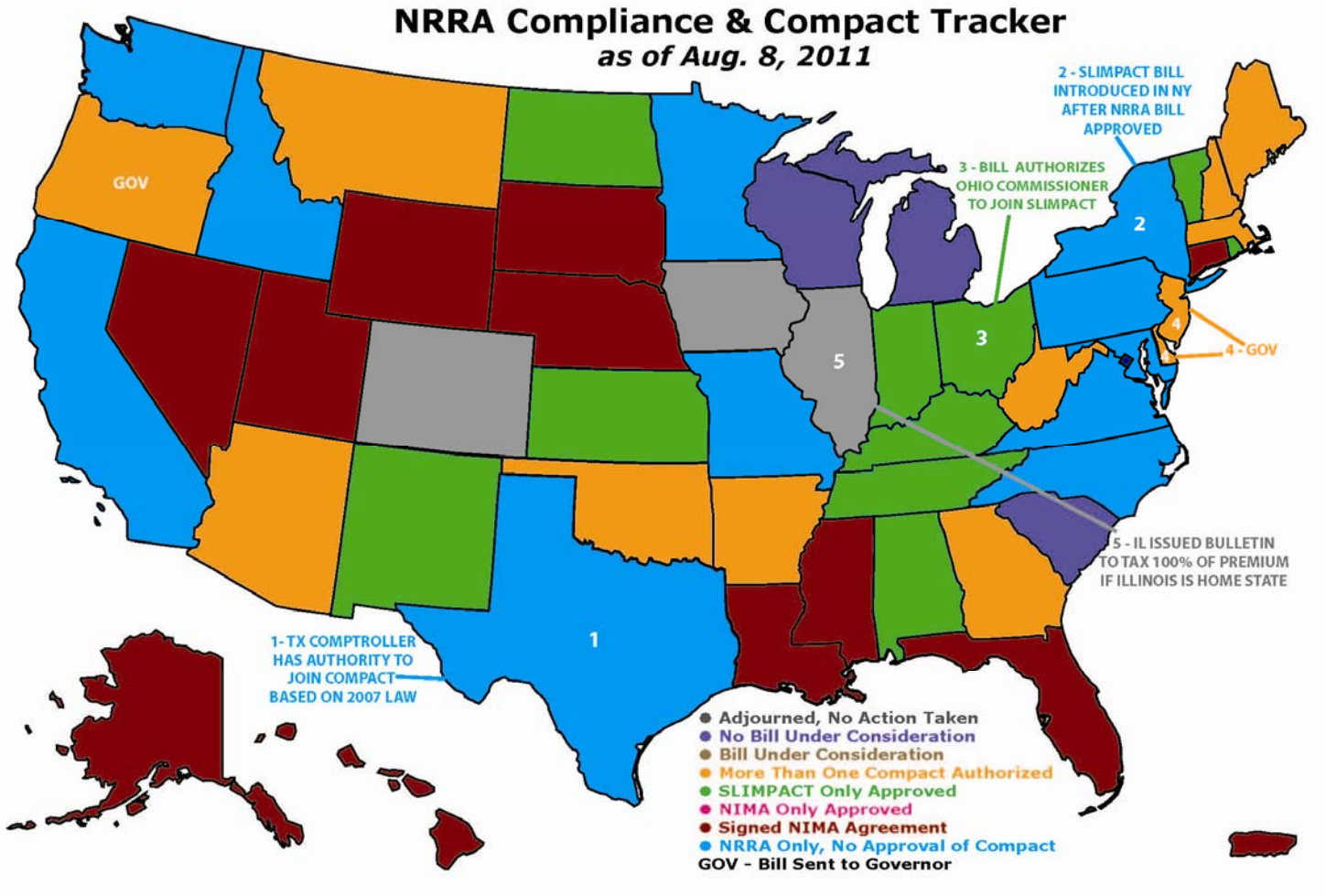


- Most states now tax surplus lines at 100% of premium
- States that assess using other state rates are: GA, HI, KS, LA, ND, NE, NH, OK, VT
- States that assess at pro rata (allocated share) are: CO, CT, IA.

*These laws are unclear – our best analysis as of 7/21/2011

NRRA State Compliance

July 21, 2011



What NRRA Does

Reinsurance Provisions

1. Prohibits a state from denying credit for reinsurance if the state of domicile of the ceding insurer recognizes the credit.
2. Reserves to the reinsurer's domiciliary state the sole responsibility for regulating the reinsurer's solvency.
3. Prohibits a state from requiring a reinsurer to provide financial information other than that required to be filed with the domiciliary state.

Effective date: July 21, 2011





Thank you!

Surplus Lines and Reinsurance Provisions of Dodd-Frank

DEWEY & LEBOEUF

Model for Future Federal Regulation of Insurance?

Mark R. Goodman
Chicago

Nonadmitted and Reinsurance Reform Act of 2010 (Title V, Subtitle A of Dodd-Frank)

- Does not adopt a Federal regulatory scheme
- Specific preemptive provision to address:
 - Industry concerns regarding multi-state regulation and taxation of surplus lines insurance
 - Industry concerns regarding non-domiciliary state regulation of reinsurance agreements and credit for reinsurance

Some basic background:

- Commerce clause of U.S. Constitution – gives the federal government the non-exclusive power to regulate “interstate commerce”
- Supremacy clause of U.S. Constitution – provides that where a federal law and a state law conflict, the federal law controls
- *E.g.*, where federal law and a state’s law both regulate some aspect of interstate commerce, if there is a conflict between the federal and state law, then the federal law will control, *i.e.*, will “pre-empt” the conflicting state law

Reinsurance

- Problem

Non-domicile states attempting to regulate:

- (1) credit for reinsurance requirements in addition to (and more onerous than) requirements of the ceding company's state of domicile, and
- (2) certain reinsurance contract terms (e.g., choice of law, use of arbitration in liquidation, etc.).

Solution

Section 531:

- Prohibits any state, except ceding company's state of domicile, from denying credit for reinsurance (as long as state of domicile is either NAIC accredited or "has financial solvency requirements substantially similar to the requirements necessary for NAIC accreditation); and
- Preempts any other laws of non-domiciliary state that (1) restricts or eliminates arbitration, (2) requires a particular state's law govern contract, (3) attempts to impose terms not in the contract or (4) otherwise applies that state's law to reinsurance agreements.
- Does not restrict what state of domicile can do.

Surplus Lines Insurance

- Problem

For multi-state risks^{*}, multiple states attempting to:

- (1) regulate a surplus line placement (by requiring surplus line broker to be licensed in that state, by imposing its own insurer eligibility requirements, by imposing its own declination and other placement, requirements, etc.), and
- (2) tax the transaction (i.e., surplus line tax allocation requirement).

ONEROUS, COMPLICATED AND NON-UNIFORM

^{*} Different states take different positions as to what is a multi-state risk

Solution – Part 1

Sections 521 and 522:

- Provides that surplus line broker needs to comply with surplus line law of, pay surplus line taxes to, only one state – the “home state” of the insured.
 - If an individual, his or her state of principal residency
 - If a business, its principal place of business (of member of affiliated group that has largest percentage of premium)
 - ◆ Tests for principal place of business.
 - ⑦ Headquarters/nerve center
 - ⑦ Location of bulk/most of operations
 - If 100% of risk is outside of above, then state “to which the greatest percentage of the insured’s taxable premium for that insurance contract is allocated.”

Solution – Part 2

Section 524:

- Provides that no state, including insured's home state,
 - can establish insurer eligibility requirements other than those in sections 5A(2) and 5C(2)(a) of NAIC Non-Admitted Insurance Model Act (*i.e., authorized to write line of business in its state of domicile, and has capital and surplus equal to the greater of minimum capital and surplus or \$15 million*)*, or
 - prohibit insurance from being placed with alien company on NAIC International Insurers Department Quarterly Listing of Alien Insurers.

*Unless that state has adopted "nationwide uniform requirements, forms and procedures"

Other Provisions

- Streamlined procedures for “Exempt Commercial Purchaser” – avoid declinations, even in home state.
- Pushes states to adopt laws or regulations providing for participation in NAIC national producer database (otherwise state can’t collect licensing fees).
- GAO study of surplus lines market.

NRRA – Model for Other Federal Regulation of Insurance?

- Federal government can take over regulation of insurance.
- Federal government cannot mandate states adopt a law or regulation (*New York v. U.S.*, 505 U.S. 144 (1992)).
- Federal government cannot mandate states enforce a federal law (*Printz v. U.S.*, 521 U.S. 898 (1997)).
- Federal government can threaten (\$), cajole, etc.
- Federal government can prohibit states from regulating interstate commerce – or from regulating it other than in a certain manner; “channeling”.

Interstate Compact

“States may enter into a compact or otherwise establish procedures to allocate among the States the premium taxes paid to an insured’s home state”

Insured’s home state may require annual tax allocation reports.

“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 for nonadmitted insurance consistent with this section.”

Competing Compacts

1. SLIMPACT/SlimPact Light (NCOIL)
 - Allows industry input to development of uniform standards
 - Clearinghouse for tax payment/allocation
2. NIMA (Nonadmitted Insurance Multistate Agreement) (NAIC)
 - Clearinghouse for tax payment/allocation
 - Proposes allocation schedule based on information/factors that brokers do not currently collect.
3. Nothing

Past Experience with Insurance Compacts

Insurance Receivership Compact

- A solution looking for a problem
- Non-legislative attempt to revise liquidation laws

Life and Health Product Approval Compact

- Works well enough
- Not adopted in some key states, e.g., NY

DEWEY & LeBOEUF

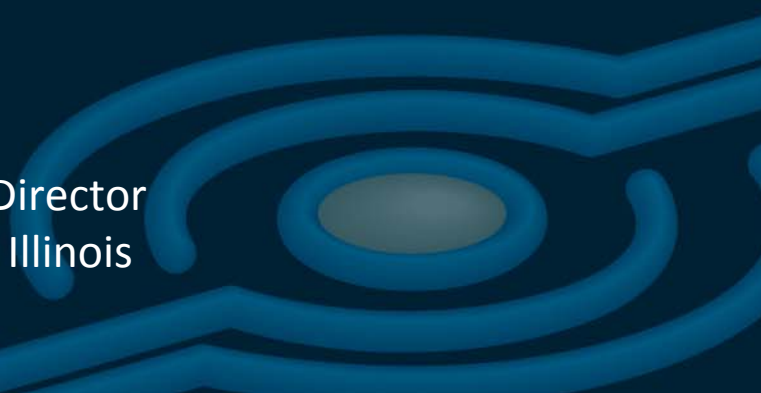
Questions?

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And Now For Something Completely Different*

David L. Ocasek, Executive Director
Surplus Line Association of Illinois
www.slai.org







* ... or ...

How I Learned To Stop Worrying and Love the NRRA

Outline



- ♥ What is Illinois' Position?
- ♥ Can You Translate That To English, Please?
- ♥ How Will My Life Change?
- ♥ Anything Weird I Need to Know About?
- ♥ Can I Get a Hug?

Illinois' Position



♥ No Legislation Passed

♥ Company Bulletin #2011-09

English, Please



- ♥ What is Illinois' Position?
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English, Please



- ♥ Reiterates federal definition of “Home State”
- ♥ Policy effective date rules
- ♥ IL will tax 100% on multistate policies
- ♥ IL anticipates participation in NIPR by 7/21/2012
- ♥ Reiterates federal exempt commercial purchaser provisions
- ♥ Reiterates federal nonadmitted insurer eligibility provisions
- ♥ Reiterates the rest of the federal definitions

English, Please



♥ Policy effective date rules

For a policy effective before 7/21/2011, and any endorsements to that policy, the old rules apply.
For a policy effective 7/21/2011 or later, the new rules apply.

English, Please



- ♥ IL will tax 100% on multistate policies

If IL is the home state, surplus line tax, fire marshal tax and stamping fee apply to the entire policy premium (Illinois and non-Illinois portions).

The fire marshal tax schedule in the SLA Procedures Manual still applies.

English, Please



- ♥ IL anticipates participation in NIPR by 7/21/2012

This will allow for online surplus line license applications and renewals. If they fail to participate by that date, they will no longer be able to collect license fees.

Outline



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Change



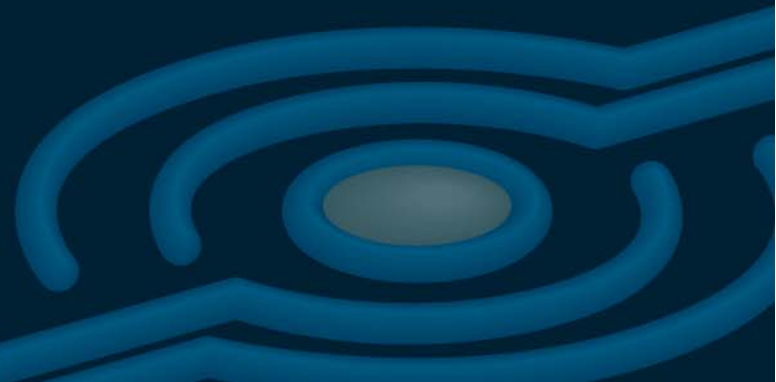
The new “NRRRA Two-Step”



Determine the Home State



Follow That State’s Rules



Change



- ♥ Determine the Home State
 - Principal Place of Business / Principal Residence
 - If 100% not in that state, state with most taxable premium
 - Affiliated Groups
 - Document This Determination!!

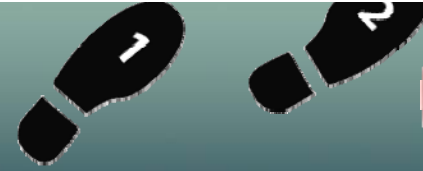
Change



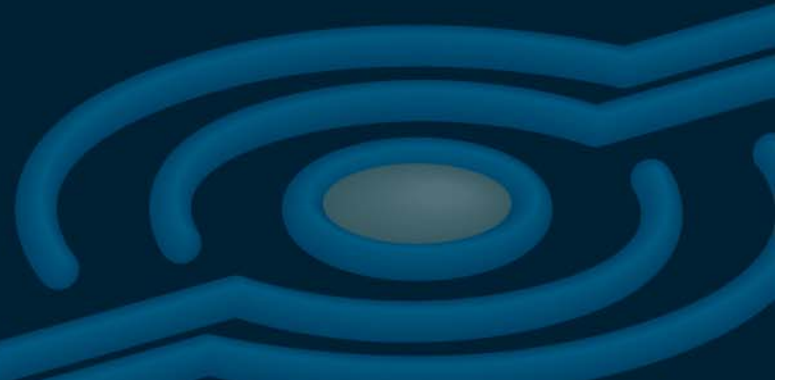
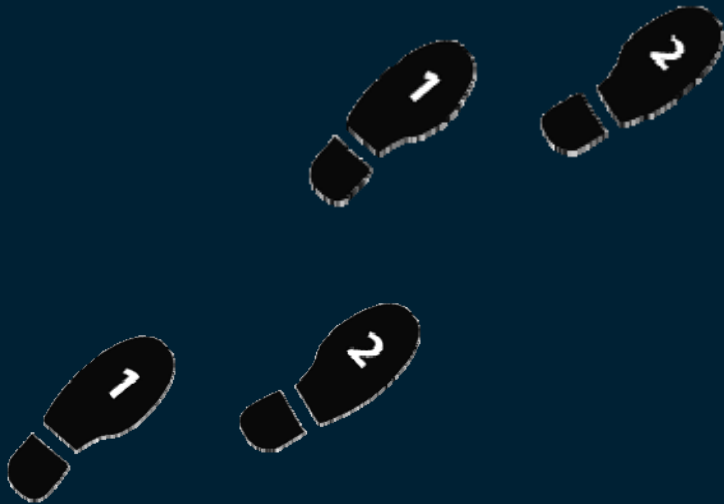
♥ Follow That State's Rules

- Most States Are Non-Allocation – File 100%
- SLIMPACT / NIMA Clearinghouses Are Not Yet Established – Pay Attention To State Bulletins
- A Few States Are Pro-Rata
- Some States Tax Entire Risk At Their Own Rate, Some Use Rates From Other States Also
- Some Data Requirements Are Changing

Change



- ♥ Will This Have An Impact on Lloyd's Business?
 - Same New 2-Step
 - Same Lloyd's Filing Process
 - File 100% of Premium on Multistate Policy



Outline



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Weird



♥ Home State Definition

- Many States Have Added Principal Place of Business / Principal Residence Definitions
- CA / NY Have Expanded “Nerve Center” Definition

Weird



♥ Affiliated Group Definition

- MO Has Expanded Affiliated Group Definition to Say All States In Group Must Be Named Insureds

Weird



♥ Tax Rates / Assessments

- FL Requires Calculation of Taxes on Multistate Risks Using Each State's Rate
- Assessments Apply to 100% of Premium

Weird



♥ Allocation Information Collection

- NRRRA Interpretation: Annual Reporting?
- OR (Others?) Collection Allocation Information, But Not Allocating!

Outline



- ♥ What is Illinois' Position?
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Hug



- ♥ H is for Home State
- ♥ U is for Understand the Rules
- ♥ G is for Get Updates