SURPLUS LINES (C) TASK FORCE

Surplus Lines (C) Task Force, Aug. 3, 2019, Minutes
2020 Proposed Charges (Attachment One)
Surplus Lines (C) Working Group, June 27, 2019 Minutes (Attachment Two)

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Surplus Lines (C) Task Force
New York, New York
August 3, 2019

The Surplus Lines (C) Task Force met in New York, NY, Aug. 3, 2019. The following Task Force members participated: James J. Donelon, Chair, Stewart Guerin and Warren Byrd (LA); Al Redmer Jr., Vice Chair (MD); Lori K. Wing-Heier, represented by Joanne Bennett (AK); Ricardo Lara represented by Susan Stapp and Emma Hirschhorn (CA); Michael Conway represented by Rolf Kaumann (CO); Stephen C. Taylor represented by David Christhilf (DC); Colin M. Hayashida represented by Paul Yuen (HA); Robert H. Muriel represented by Patrick Hyde (IL); Vicki Schmidt represented by Tat Flott (KS); Nancy G. Atkins represented by Russell Hamblen (KY); Mike Causey represented by Fred Fuller (NC); Marlene Caride represented by Shail Mankad (NJ); John G. Franchini represented by Victoria Baca (NM); Barbara D. Richardson (NV); Elizabeth Kelleher Dwyer represented by Beth Vollucci (RI); Raymond G. Farmer represented by Lee Hill (SC); Larry Deiter (SD); Kent Sullivan represented by Jamie Walker (TX); Mike Kreidler represented by Mel Anderson (WA); and Jeff Rude represented by Donna Stewart (WY).

1. **Adopted its Spring National Meeting Minutes**

   Mr. Hamblen made a motion, seconded by Mr. Hill, to adopt the Task Force’s April 6 minutes (see NAIC Proceedings – Spring 2019, Surplus Lines (C) Task Force). The motion passed unanimously.

2. **Adopted its 2020 Proposed Charges**

   Commissioner Donelon said the Task Force’s 2020 proposed charges (Attachment One) have been updated to provide a more accurate and complete description of the focus area for the Task Force and its supporting Surplus Lines (C) Working Group. He said a new charge describes the Task Force’s responsibility to develop or amend relevant NAIC model laws, regulations and/or guidelines. David Kodama (American Property Casualty Insurance Association—APCIA) asked whether the new charge was drafted with any specific topic in mind. Andy Daleo (NAIC) said the primary reason for the new charge was to consider revision of the Nonadmitted Insurance Model Act (#870). He indicated that Model #870 had not been updated since 2002, and staff had identified several areas within the model that require revision. Commissioner Donelon added that the Guideline on Nonadmitted Accident and Health Coverages (#1860) is a recent example of an effort by the Task Force to address Model #870. Mr. Kodama asked if any additional coverages, like accident and health, were anticipated by the charge. Mr. Daleo said none were under current consideration.

   Mr. Hill made a motion, seconded by Ms. Anderson, to adopt its 2020 proposed charges. The motion passed unanimously.

3. **Adopted the Report of the Surplus Lines (C) Working Group**

   Mr. Guerin reported that the Surplus Lines (C) Working Group met via conference call May 13 in regulator-to-regulator session, pursuant to paragraph 3 (specific companies, entities or individuals) of the NAIC Policy Statement on Open Meetings; and June 27, once in open session and once in regulator-to-regulator session, pursuant to paragraph 3 (specific companies, entities or individuals) of the NAIC Policy Statement on Open Meetings.

   During the May 13 conference call, the Working Group discussed draft enhancements and edits to the International Insurer Department (IID) Plan of Operation, which guides alien insurers on filing and compliance requirements to become and remain listed on the Quarterly Listing of Alien Insurers. Proposed changes to the Plan of Operation included a clarification of the role of the Property and Casualty Insurance (C) Committee, a flow chart that describes the IID process, a requirement for insurers to submit updated biographical affidavits when a material change in an individual’s personal record has occurred, and language describing required attestations for Lloyd’s syndicates and managing agencies that are partially or wholly owned, directly or indirectly, by a sovereign government.

   During the June 27 open call (Attachment Two), three comments related to the exposure of the IID Plan of Operation were discussed. Following a couple of friendly amendments, the IID Plan of Operation was unanimously adopted. A comment letter was also received regarding the exposure of the private flood data collection form. Following a brief discussion, the private flood data collection form was adopted, and it will be implemented beginning with the financial YE 2019 filing. The Working Group also discussed revisions to be considered for the YE 2020 filing which included: 1) separation of first dollar and excess premium for residential private flood; and 2) collection of the number of policies in-force and endorsements at the beginning
and ending of the reporting period. Birny Birnbaum (Center for Economic Justice—CEJ) asked whether those revisions will be made or merely considered for the 2020 reporting year. Mr. Guerin said the two enhancements would be exposed in the summer of 2020 for comment and voted on by the Working Group before implementing.

During the June 27 regulator-only call, the Working Group heard a summary of two applications for admission to the Quarterly Listing of Alien Insurers. Following a brief discussion, both applications were admitted to the July 1 addition of the listing. The Working Group also discussed the results of a Surplus Lines Tax Reconciliation Survey.

Mr. Kaumann made a motion, seconded by Ms. Bennett, to adopt the report of the Surplus Lines (C) Working Group. The motion passed unanimously.

4. Exposed a Blanks Proposal Regarding Home State Direct Premiums Written

Mr. Guerin indicated that during the June 27 regulator-only call, the Working Group discussed the results of a Surplus Lines Tax Reconciliation Survey. The survey resulted from discussions with NAIC staff, and it was based on numerous inquiries from the states regarding resources for help in the reconciliation of surplus lines premium tax. The survey consisted of five questions, and 33 states responded. Mr. Guerin said the survey addressed the extent to which the states perform premium tax reconciliation and the frequency. A question was posed to the states regarding the benefit of either: 1) a new part 3 to Schedule T – Exhibit of Premiums Written to address home state direct premiums written; or 2) an entirely new schedule that would provide allocation of surplus lines premiums by line of business and home state direct premiums written. Mr. Guerin said a majority of the responses were in favor of the Schedule T proposals. The Working Group decided on a new part to Schedule T.

Mr. Kodama asked if Schedule T is used for solvency regulation. Mr. Guerin said it is. Mr. Kodama then asked how the proposed enhancement to Schedule T related to solvency regulation. Mr. Daleo said not all information contained within the financial statements relates strictly to solvency regulation. He said the home state premium information would provide state insurance regulators with a starting point in determining whether the correct amount of surplus lines premium tax was collected. Mr. Guerin added that in Louisiana, reconciliation of premium taxes for admitted carriers already occurs. He said by obtaining home state direct premium written, state insurance regulators would be able to do the same for nonadmitted carriers.

Commissioner Donelon asked Mr. Kodama whether he thought this new information would pose an additional burden on the nonadmitted carriers. Mr. Kodama said he hoped the exposure period would be long enough to allow the impacted companies to determine whether the information is readily available, determine any required changes to systems, and determine if the companies would need to coordinate this information with the brokers. At the request of Mr. Kodama, Commissioner Donelon indicated that the exposure period would be extended to a 60-day comment period.

5. Heard an Update on its Referral to the Producer Licensing (D) Task Force

Commissioner Donelon said the referral to the Producer Licensing (D) Task Force suggested modifications to the State Licensing Handbook to accommodate the newly adopted Guideline #1806. Director Deiter, chair of the Producer Licensing (D) Task Force, said the referral was discussed at its Spring National Meeting. Following the discussion, a draft amendment to the Uniform Licensing Standards for Surplus Lines, and the State Licensing Handbook was circulated for comment to the Producer Licensing (D) Task Force members, state licensing directors, and interested parties. Consistent with the Surplus Lines (C) Task Force request, the draft proposal to the Producer Licensing (D) Task Force is to expand the underlying licensure requirements to qualify for a surplus lines license to include the accident and health line of authority. The Producer Licensing (D) Task Force will discuss the proposal and comments during its meeting later that day. Director Deiter said the Task Force may possibly adopt the proposal at that time. However, he said it is likely that there may be additional discussion and comments at the meeting, and he will look for some action on the proposal in the near future.

Commissioner Donelon asked Director Deiter to provide an update for the Surplus Lines (C) Task Force at the Fall National Meeting.

6. Heard a Financial Summary of the 2018 Surplus Lines Market

Mr. Daleo indicated that 151 entities, 62 companies, and 89 Lloyd’s syndicates were on the Quarterly Listing of Alien Insurers at year-end 2018. He said alien entities, or those insurers domiciled outside the U.S., collectively wrote $15.3 billion in direct surplus lines premiums in the U.S., a 12.4% increase from the prior year. Further, he indicated that U.S. domestic insurers wrote $34.7 billion in surplus lines premiums in 2018, a 10.3% increase from 2017. He said in 2018, alien insurer surplus lines
premiums accounted for 30.6% of total U.S. surplus lines exposure, up from 30.2% and 29.8% in 2017 and 2016, respectively. He said on Dec. 31, 2018, the 151 alien insurers reported an aggregate $25.2 billion in gross loss, loss adjustment expense (LAE), and incurred but not reported (IBNR) reserves. As of March 31, 2019, the gross reserves were partially secured by nearly $6.8 billion, or about 27%, in individual U.S. trust fund assets.

Mr. Daleo indicated that cybersecurity coverage written by alien insurers is in its third year of collection, and 72 entities reported exposure in 2018, virtually unchanged from the 71 reported in 2017. He said 14 insurers reported only stand-alone policies, 26 wrote only package policies, and 32 wrote both stand-alone and package policies. He said cyber direct premiums written increased by 53% in 2018 to $1.8 billion versus $1.2 billion in 2017. He commented that the growth in premiums was driven by a 91% jump in stand-alone policies written to $1.5 billion, while package policy direct premiums written were down 14% to $370 million. Further, he indicated that direct losses incurred increased by 87% from the previous year to $346 million, which equates to a direct loss ratio of 28.1%, up from about 20% in 2017. Lastly, he said there were close to 207,000 alien cyber policies in force reported for 2018, representing a 33% increase over the previous year.

Mr. Daleo also provided an update on domestic surplus lines insurers (DSLI), a type of insurer authorized to write surplus lines coverage in its state of domicile. Legislation authorizing DSLIs has been enacted in 21 states: AR, AZ, CT, DE, GA, IA, IL, LA, MO, NC, ND, NE, NH, NJ, NV, OH, OK, TX, VA, VT and WI. Currently, there are 76 DSLIs authorized in 14 states that in 2018 collectively wrote $10.2 billion in surplus lines premiums, of which nearly $353 million was written in their states of domicile.

Commissioner Donelon said for anyone interested in additional review of these results, they would be posted to the Task Force webpage.

Having no further business, the Surplus Lines (C) Task Force adjourned.
2020 PROPOSED CHARGES
SURPLUS LINES (C) TASK FORCE

Mission

The mission of the Surplus Lines (C) Task Force is to monitor the surplus lines market and regulation, including the activity and financial condition of U.S. and alien surplus lines insurers by providing a forum for discussion of issues and to develop or amend relevant NAIC model laws, regulations and/or guidelines.

Ongoing Support of NAIC Programs, Products or Services

The Surplus Lines (C) Task Force will:

1. Provide a forum for discussion of current and emerging surplus lines-related issues and topics of public policy and determine appropriate regulatory response and action.
2. Review and analyze quantitative and qualitative data on U.S. domestic and alien surplus lines industry results and trends.
3. Monitor federal legislation related to the surplus lines market and ensure all interested parties remain apprised.
4. Develop or amend relevant NAIC model laws, regulations and/or guidelines.
5. Oversee the activities of the Surplus Lines (C) Working Group.

The Surplus Lines (C) Working Group will:

A. Operate in regulator-to-regulator session pursuant to paragraph 3 (specific companies, entities or individuals) of the NAIC Policy Statement on Open Meetings and operate in open session when discussing surplus lines topics and policy issues, such as amendments to the International Insurers Department (IID) Plan of Operation.
B. Maintain and draft new guidance within the IID Plan of Operation regarding standards for admittance and continued inclusion on the NAIC Quarterly Listing of Alien Insurers.
C. Review and consider appropriate decisions regarding applications for admittance to the NAIC Quarterly Listing of Alien Insurers.
D. Analyze renewal applications of alien surplus lines insurers on the NAIC Quarterly Listing of Alien Insurers and ensure solvency and compliance per the IID Plan of Operation guidelines for continued listing.
E. Provide a forum for surplus lines-related discussion among jurisdictions.

NAIC Support Staff: Andy Daleo/Robert Schump
Surplus Lines (C) Working Group
Conference Call
June 27, 2019

The Surplus Lines (C) Working Group of the Surplus Lines (C) Task Force met via conference call June 27, 2019. The following Working Group members participated: Stewart Guerin, Chair (LA); David Phifer (AK); Michelle Lo (CA); Rolf Kaumann (CO); Robert Ballard (FL); James A. McCarthy (MA); Jose Joseph (NY); and Lee Hill (SC).

1. **Adopted its May 13 Minutes**

Mr. Kaumann made a motion, seconded by Mr. Joseph, to adopt the Working Group’s May 13 minutes (Attachment One). The motion passed unanimously.

2. **Reviewed IID Plan of Operation Comment Letters**

Robert F. Schump (NAIC) summarized the comments submitted by Thomas M. Dawson (Drinker Biddle & Reath). Mr. Dawson’s comments said the 30-day time requirement for submission of an updated biographical affidavit following a material change may be a challenge, and he suggested the addition of the following language: “Or where available within 30 days, approval of a new director or officer by the insured’s domestic regulator, whichever is later.” The recommended language was due to delays in the approval of individuals by the United Kingdom’s (UK) Prudential Regulation Authority. Mr. Schump said NAIC staff supports the addition of the submitted language.

Mr. Kaumann suggested identifying the members of the International Insurers Department (IID) Internal Review Committee for transparency purposes. He also suggested changing the language related to the sharing of confidential documents from “may share” to “will share” since the NAIC would not withhold information from state insurance regulators if requested. Mr. Schump said listing the actual names of the Committee members would require frequent updates to the IID Plan of Operation (Plan). He suggested that instead, all IID Committee members could be identified during Working Group conference calls. Mr. Kaumann agreed with that proposal, and he said providing the Working Group with a list of the Committee members is what he had intended.

Timothy Grant (Lloyds) suggested modifying the language related to the assessment of syndicate applicant member funds at Lloyds. The current “assessment” language may be interpreted as implying a financial penalty or levy. The suggested language would be a “review” of member funds at Lloyd’s. This serves to solidify the ongoing practice where the Working Group can ask for an applying syndicates member funds at Lloyd’s.

Mr. Guerin suggested that the proposed changes be incorporated into the Plan, as there were more clean-up, rather than substantive, changes.

Mr. Hill made a motion, seconded by Mr. Kaumann, to adopt the proposed IID Plan of Operation revisions. The motion passed unanimously.

3. **Reviewed Alien Insurer Private Flood Data Collection Form Comment Letters**

Mr. Schump summarized the comments submitted by Mr. Dawson, covering the difficulty for alien insurers to collect accurate information, specifically referring to commercial flood policies where flood coverage may be built into a package policy or where the premium for a separately invoiced coverage may not be easily obtainable. Mr. Dawson included comments from the International Underwriting Association (IUA), providing that virtually none of their members were currently writing U.S. residential flood coverage. Therefore, the IUA suggested adopting the original one-page flood statement with the expectation that if individual insurers were found to be writing flood insurance, then those insurers could be targeted for further information requests. Birny Birnbaum (Center for Economic Justice—CEJ) said if a company does not write residential flood coverage, it has nothing to report, so there is no burden on it to report. He said if the information is not asked for, then you do not know whether companies are writing residential flood coverage. Mr. Guerin said most companies have not written residential flood coverage in the past, primarily because they were not allowed to due to regulation in place at that time that prohibited them from doing so. Recent changes to regulations may alter that, and companies may start writing this coverage in the future. Therefore, Mr. Guerin does not see an issue with collecting residential flood coverage information.

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Mr. Birnbaum provided three recommendations related to the collection of data on flood insurance coverage provided by alien surplus lines insurers. The first recommendation was to separate data collection into two reporting categories: first dollar coverage and excess coverage. This is because these are significantly different coverages in terms of both sales/pricing and reserving. The second had to do with the data item on the form asking for the number of policies enforced. Mr. Birnbaum suggested collecting data on the number of policies in force at the beginning of the period, as well as at the end of the period, to give an idea of the growth the company experienced. He said this information would be useful for financial examination and market analysis. The number of policies in force at the beginning of the reporting period should equal those reported at the end of the prior reporting period. If not, this presents an opportunity to trigger an inquiry to the reporting company. Mr. Birnbaum said policies can be sold on a stand-alone basis or as endorsements to existing property insurance coverage, whether commercial or residential. He went on to state the importance of collecting data on products written in the marketplace that are written as both policies and endorsements. The third recommendation was to incorporate the Market Conduct Annual Statement (MCAS) into the reporting requirements of the IID. Mr. Guerin said collecting data while distinguishing first dollar from excess of loss policies would be useful; although, it is unknown whether alien surplus lines insurers have systems in place to easily identify that information within a short timeframe. However, he acknowledged that reporting would be more accurate over time as companies develop those reporting systems. As for the second comment, Mr. Guerin said collecting data on beginning of period and end of period policies in force made sense, and it would not be unduly burdensome on insurers. He said including endorsements would provide useful information, as it may be a major source for these kinds of coverage. With regards to the third comments related to MCAS, he said that may be outside of the scope of the Working Group, which is focused on financial aspects, such as the adequacy of surplus lines insurer’s shareholders’ equity in relation to their operations, asset quality, business mix, leverage, etc. The Working Group is also monitoring trust fund levels for adequacy based on the liabilities that companies hold. That may be an overreach for the Working Group, as well as the fact that similar data is not requested of surplus lines insurers writing other lines of business, so it would be outside the normal scope of how the Working Group operates. Mr. Hill and Mr. Joseph agreed with Mr. Guerin that market conduct is outside the Working Group’s responsibility and expertise; however, they both agreed with Mr. Birnbaum’s other two recommendations.

Mr. Dawson commented that alien surplus lines insurers account for 30% of surplus lines premiums written within the U.S., with Lloyd’s accounting for roughly 20%, while companies make up 5–10% of the total. He said after talking with IUA members in London, there is not much involvement by alien surplus lines insurers in the U.S. private flood insurance market. Most of the members are involved in writing commercial lines coverage. In terms of data collection and understanding the political implications of the flood insurance market, alien surplus lines insurers will find it burdensome to collect data on private flood insurance written within the U.S. due to the way the marketplace is structured. Mr. Dawson said asking for this data is a real departure from previous data collection efforts. Mr. Guerin said because alien insurers have not written private flood insurance in the past, that does not mean they will not in the future due to the loosening of regulations at the federal level. The odds are that flood collection will stay in the IID forms even if the data collected are zeros. With regard to MCAS, Mr. Guerin said it is outside the scope of the Working Group, which deals primarily with financial matters. Mr. Birnbaum asked Mr. Dawson if he was rejecting all three CEJ proposals or just focusing on an objection to the MCAS. Mr. Dawson said they were objecting to all three. Mr. Birnbaum said if companies are writing first-dollar or excess coverage, they need to report that information. In terms of policies in force at the beginning and end of a period, those are known items and are a minor addition to ensure data quality. Mr. Birnbaum also said companies should be given lead time to collect the data if they are not already collecting it. He said the first two data elements are not critical, and it is hard to imagine that companies do not already actively collect these on a regular basis. If companies can show that it would be burdensome to collect the data and that they need more time, then it would be reasonable to consider such requests at that point in time. As for the issue of MCAS, the CEJ intends to bring this issue up with the Property and Casualty Insurance (C) Committee, as this committee has a broader context than the Working Group.

Sabrina Miesowitz (Lloyd’s) said companies operating in the London marketplace do not collect data at the same level of granularity as U.S. companies, and adding additional data elements for the IID forms will make it more difficult for the underwriters. Lloyd’s would prefer that the Working Group use the original flood form that was exposed for comment and, if planning on adding additional elements, understand that this data may not be available, or may need to be manually collected, as many Lloyd’s underwriters do not collect this information.

Mr. Guerin inquired with NAIC staff as to when the flood data collection would begin. Mr. Schump said the intention was that the flood form collection would begin in July 2020 for 2019 year-end results.

Mr. Birnbaum said it is implausible that companies would be unable to obtain information on how many policies were in force at the beginning of a period versus the end of the period. Similarly, it is difficult to understand how companies would not have
access to information about whether products are providing first-dollar or excess coverage. He said when a claim comes in, the insurer has to know whether they are providing first-dollar or excess coverage.

Mr. Dawson said he is unaware of anywhere that flood coverage data is currently being collected, and until now, it was not even collected by the IID. When a claim is submitted, this data can be accessed through a manual, reactive process. There may be some insurers in London that do write flood insurance on the commercial side, but they may not write it on a stand-alone basis. Mr. Dawson said it is probably packaged with other coverages, and there may not be separate premiums charged for the flood coverage. Getting that information would be a manual process.

Mr. Birnbaum said the requirement to include beginning and ending period policy-in-force data does not require more granularity, and he said the proposal requires a distinction between the residential first dollar and excess policy data. He suggested that the Working Group adopt the current form for 2019, but for 2020 and beyond, the Working Group should require companies to separate residential flood data into these two categories.

Mr. Kaumann made a motion, seconded by Mr. Hill, to adopt the Alien Insurer Private Flood Data Collection Form as originally exposed and to re-evaluate the form in 2020 with the intention of adding additional reporting criteria in order to capture data at a more granular level. The motion passed unanimously.

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