

SB1279

Measure Title: RELATING TO INSURANCE.

Report Title: Insurance

Description: Adopts amendments to the insurance code to comply with the federal Nonadmitted and Reinsurance Reform Act of 2010 relating to surplus lines insurance and participate in a multi-state cooperative to collect surplus lines premium taxes and fees and distribute to the individual states the taxes and fees they assessed.

Companion: HB1052

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Current Referral: CPN



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COMMERCE AND CONSUMER PROTECTION

TWENTY-SIXTH LEGISLATURE
Regular Session of 2011

Friday, February 11, 2011
8:30 a.m.

TESTIMONY ON SENATE BILL NO. 1279 – RELATING TO INSURANCE.

TO THE HONORABLE ROSALYN BAKER, CHAIR, AND MEMBERS OF THE
COMMITTEE:

My name is Gordon Ito, State Insurance Commissioner ("Commissioner"),
testifying on behalf of the Department of Commerce and Consumer Affairs
("Department"). Thank you for hearing this bill. The Department strongly supports this
Administration bill.

The purpose of this bill is to adopt the National Association of Insurance
Commissioners' ("NAIC") recommendations relating to the states' implementation of the
provisions of the federal Nonadmitted and Reinsurance Reform Act of 2010 ("NRRA")
as they relate to the states' regulation and taxation of surplus lines insurance. NRRA's
effective date is July 21, 2011. Surplus lines or nonadmitted insurance are insurance
contracts that cover risks in states where the insurer is not an admitted or authorized
insurance company.

The first of two significant changes is the regulation of surplus lines policies that cover risks in multiple states. Presently, each state with a covered risk may regulate the insured and the insurer. NRRA limits the regulation of the surplus lines to solely the "home state" of the policyholder. The proposed legislation provides for the adoption of NAIC recommended definitions of "home state" and conforms to the NRRA limitation.

The second significant change is to authorize on the home state to collect premium taxes on multi-state surplus lines policies. The home state may collect taxes for all affected states and distribute to each state their share of the taxes.

Adoption of NAIC's recommendations are essential for the Insurance Division to participate in the multi-state effort to regulate companies and to collect and distribute the premium taxes. Presently, the Insurance Division collects and deposits into the General Fund \$10,000,000 of surplus lines taxes. The proposed legislation is intended to authorize the Insurance Division to join with other states in arrangements that are being developed to ensure the continued receipt of the surplus lines taxes.

NAIC's recommendations were recently issued, but modifications and adjustments continue to be made. We ask for your consideration and approval of the attached proposed S.D. 1 that (1) changes the definition of state to include the Northern Mariana Islands; (2) substitutes "insured" for "subject resident," "surplus lines insurance" for "unauthorized insurance," and "unauthorized insurer" for "nonadmitted insurer;" (3) describes the reporting requirements to the Commissioner; and (4) defines the tax reporting and payment due dates for the transition period and beyond.

We thank this Committee for the opportunity to present testimony on this matter and ask for your favorable consideration.

Report Title:

Insurance

Description:

Adopts amendments to the insurance code to comply with the federal Nonadmitted and Reinsurance Reform Act of 2010 relating to surplus lines insurance and participate in a multi-state cooperative to collect surplus lines premium taxes and fees and distribute to the individual states the taxes and fees they assessed.

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A BILL FOR AN ACT

RELATING TO INSURANCE.

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF HAWAII:

1 SECTION 1. The purpose of this act is to amend chapter
2 431, Hawaii Revised Statutes, to comply with the federal
3 Nonadmitted and Reinsurance Reform Act of 2010 relating to
4 surplus lines insurance and to participate in multi-state
5 cooperatives to collect surplus lines premium taxes and fees and
6 distribute to the individual states their taxes and fees.

7 SECTION 2. Section 431:1-213, Hawaii Revised Statutes, is
8 amended to read as follows:

9 "**§431:1-213 State defined.** State means any state of the
10 United States and the governments of Puerto Rico, American

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1 Samoa, Guam, Northern Mariana Islands, United States Virgin
2 Islands, and the District of Columbia."

3 SECTION 3. Section 431:1-214, Hawaii Revised Statutes, is
4 amended to read as follows:

5 "**§431:1-214 United States defined.** United States, when
6 used to signify a place, means the states of the United States
7 and the governments of Puerto Rico, American Samoa, Guam,
8 Northern Mariana Islands, United States Virgin Islands, and the
9 District of Columbia."

10 SECTION 4. Section 431:8-101, Hawaii Revised Statutes, is
11 amended to read as follows:

12 "**§431:8-101 Scope.** This article shall apply to the
13 placement of insurance [~~on any subject resident, located, or to~~
14 ~~be performed in this State,~~] in insurers not authorized to
15 transact insurance in [~~this State.~~] the state in which the
16 insured is located or in which the insurance contract will be
17 performed."

18 SECTION 5. Section 431:8-102, Hawaii Revised Statutes, is
19 amended as follows:

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1 (1) By amending the definitions of "authorized insurer",
2 "surplus lines insurance", and "unauthorized insurer" to read as
3 follows:

4 "Authorized insurer" means an insurer holding a valid
5 certificate of authority to transact an insurance business in
6 ~~[this State.]~~ the state in which the insured is located or in
7 which the insurance contract will be performed.

8 "Surplus lines insurance" means any property insurance or
9 casualty insurance, or both, on risks ~~[resident, located or to~~
10 ~~be performed in this State,]~~ procured from or placed with an
11 unauthorized insurer ~~[in accordance with part III of this~~
12 ~~article.]~~ under the laws of the insured's home state. Surplus
13 lines insurance when this State is the home state of the insured
14 shall be in accordance with part III of this article.

15 "Unauthorized insurer" means an insurer not holding a valid
16 certificate of authority to transact an insurance business in
17 ~~[this State.]~~ the state in which the insured is located or in
18 which the insurance contract will be performed."

19 (2) By adding definitions for "exempt commercial
20 purchaser", "home state", "home state of affiliated group",
21 "home state of group insurance", "independently procured

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1 insurance", "multi-state risk", "principal place of business",
2 "principal residence", and "single state risk" to read as
3 follows:

4 "Exempt commercial purchaser" means any person purchasing
5 commercial insurance which, at the time of placement, employs or
6 retains a qualified risk manager to negotiate insurance
7 coverage; and has paid aggregate nationwide commercial property
8 and casualty insurance premiums in excess of \$100,000 in the
9 immediately preceding twelve months. The person shall possess a
10 net worth in excess of \$20,000,000, or the person shall generate
11 annual revenues in excess of \$50,000,000, or the person shall
12 employ more than five hundred full time or full time equivalent
13 employees per individual insured or is a member of an affiliated
14 group employing more than one thousand employees in the
15 aggregate, or the person is a not-for-profit organization or
16 public entity generating annual budgeted expenditures of at
17 least \$30,000,000, or the person is a municipality with a
18 population in excess of fifty thousand persons. Effective on
19 January 1, 2015 and every five years thereafter, the amount of
20 net worth, annual revenues, and annual budgeted expenditures
21 shall be adjusted to reflect the percentage change for that

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1 five-year period in the Consumer Price Index for All Urban
2 Consumers published by the Bureau of Labor Statistics of the
3 federal Department of Labor.

4 "Home State", with respect to an insured, means the state in
5 which an insured maintains the insured's principal place of
6 business or, in the case of an individual, the state in which
7 the individual maintains the individual's principal residence;
8 except that if one hundred per cent of the insured risk is
9 located out of the state where the insured maintains the
10 insured's principal place of business or the state where the
11 individual maintains the principal residence, the home state
12 shall be the state where the greatest percentage of the insured's
13 taxable premium for that insurance contract is allocated.

14 "Home state of affiliated group" means the home state of the
15 member of the affiliated group that has the largest percentage
16 of premium attributed to it under an insurance contract, which
17 has more than one insured from the affiliated group listed as
18 named insureds on a single surplus lines insurance contract.

19 "Home state of group insurance" means the home state of the
20 group policyholder who pays one hundred per cent of the premium
21 from the policyholder's own funds. When the group policyholder

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1 does not pay one hundred per cent of the premium from the
2 policyholder's own funds, the term "home state" means the home
3 state of the group member.

4 "Independently procured insurance" means insurance obtained
5 by an insured directly from an unauthorized insurer as permitted
6 by the laws of the insured's home state.

7 "Multi-state risk" means a risk covered by an unauthorized
8 insurer with insured exposures in more than one state.

9 "Principal place of business" , with respect to determining
10 the home state of the insured, means (1) the state where the
11 insured maintains the insured's headquarters and where the
12 insured's high-level officers direct, control, and coordinate the
13 business activities; or (2) if the insured's high-level officers
14 direct, control, and coordinate the business activities in more
15 than one state, the state in which the greatest percentage of
16 the insured's taxable premium for that insurance contract is
17 allocated; or (3) if the insured maintains the insured's
18 headquarters or the insured's high-level officers direct,
19 control, and coordinate the business activities outside any
20 state, the state in which the greatest percentage of the

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1 insured's taxable premium for that insurance contract is
2 allocated.

3 "Principal residence", with respect to determining the home
4 state of the individual insured, means (1) the state where the
5 individual insured resides for the greatest number of days
6 during a calendar year; or (2) if the insured's principal
7 residence is
8 located outside any state, the state in which the greatest
9 percentage of the insured's taxable premium for that insurance
10 contract is allocated.

11 "Single state risk" means a risk with insured exposures in
12 only one state."

13 SECTION 6. Section 431:8-201, Hawaii Revised Statutes, is
14 amended to read as follows:

15 **"§431:8-201 Transacting insurance business without**
16 **certificate of authority prohibited.** It shall be unlawful for
17 any insurer to transact an insurance business in this State, as
18 defined in section 431:1-215, without a certificate of
19 authority, except that this section shall not apply to:

- 20 (1) The lawful transaction of surplus lines insurance;
21 (2) The lawful transaction of reinsurance by insurers;

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- 1 (3) Transactions in this State involving a policy lawfully
2 solicited, written, and delivered outside of this
3 State covering only subjects of insurance not
4 resident, located, or expressly to be performed in
5 this State at the time of issuance, and which
6 transactions are subsequent to the issuance of such
7 policy;
- 8 (4) Attorneys acting in the ordinary relation of attorney
9 and client in the adjustment of claims or losses;
- 10 (5) Transactions in this State involving group life and
11 group accident and health or sickness or blanket
12 accident and health or sickness insurance or group
13 annuities where the master policy of such groups was
14 lawfully issued and delivered in and pursuant to the
15 laws of a state in which the insurer was authorized to
16 do an insurance business;
- 17 (6) Transactions in this State involving any policy of
18 insurance or annuity contract issued prior to July 1,
19 1988; ~~and~~
- 20 (7) Transactions in this State involving ocean marine
21 insurance[-]; and

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1 (8) Transactions of contracts of insurance for property or
2 casualty, or both; multi-state risks; provided that
3 the producer is licensed to sell, solicit, or
4 negotiate that insurance in the home state of the
5 insured."

6 SECTION 7. Section 431:8-205, Hawaii Revised Statutes, is
7 amended to read as follows:

8 "**§431:8-205 Insurance independently procured; duty to**
9 **report and pay tax.** (a) Nothing in this part shall prohibit a
10 person from independently procuring, continuing, or renewing
11 insurance from an insurer which is not authorized to transact
12 insurance in this State.

13 (b) Each insured who in this State, before July 1, 2011,
14 procures [~~or~~] , continues, , or renews [~~insurance with an~~
15 ~~unauthorized insurer~~] surplus lines insurance on a risk located
16 or to be performed in whole or in part in this State, other than
17 insurance procured through a surplus lines broker pursuant to
18 part III of this article shall, within sixty days after the date
19 the insurance was [~~so~~] procured, continued, or renewed, file a
20 written report [~~of the same~~] with the commissioner [~~, upon forms~~
21 ~~prescribed by the commissioner, showing~~]. Each insured who in

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1 this State, after June 30, 2011, procures, continues, or renews
2 surplus lines insurance for which this State is the home state
3 of the insured, other than insurance procured through a surplus
4 lines broker pursuant to part III of this article shall, within
5 forty-five days after the end of the calendar quarter in which
6 the insurance was procured, continued, or renewed, file a
7 written report with the commissioner. The report shall be on
8 forms prescribed by the commissioner, showing:

- 9 (1) The name and address of the insured or insureds;
10 (2) The name and address of the insurer;
11 (3) The subject of the insurance;
12 (4) A general description of the coverage;
13 (5) ~~[The]~~ The itemized amount of [premium] premiums,
14 taxes, and fees currently charged [therefor,] for each
15 state; [and]
16 (6) Policy number, effective date of policy, home state;
17 and
18 (7) [Such] Other additional, pertinent information [as is
19 reasonably] requested by the commissioner.

20 (c) Gross premiums charged for the surplus lines
21 insurance[,] allocable to this State, less any return premiums,

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1 are subject to a tax at the rate of 4.68 per cent. At the time
2 of filing the report required in subsection (b) for insurance
3 procured, continued, or renewed before July 1, 2011, the insured
4 shall pay the tax to the commissioner. At the time of filing
5 the report required in subsection (b) for insurance procured,
6 continued, or renewed after June 30, 2011, when this State is
7 the home state of the insured, the insured shall pay the tax and
8 fees of this State and all other states to the director of
9 finance, through the commissioner. When this State is not the
10 home state of the insured, the insured shall pay the tax and
11 fees of this State to the home state of the insured.

12 As used in this subsection, "gross premiums" mean the
13 amount of the policy or coverage premium charged by the insurer
14 in consideration for the insurance contract. Any charges for
15 policy, survey, inspection, service, or similar fees or other
16 charges added by the broker shall not be considered part of
17 gross premiums.

18 (d) If an independently procured policy covers risks or
19 exposures only partially located or to be performed in this
20 State, the tax payable to this State shall be computed on the

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1 portion of the premium properly attributable to the risks or
2 exposures located or to be performed in this State.

3 (e) Delinquent taxes shall bear interest at the rate of
4 ten per cent per annum.

5 (f) This section does not abrogate or modify, and shall
6 not be construed or deemed to abrogate or modify, any provision
7 of section 431:8-202 or any other provision of this code.

8 (g) This section shall not apply to life insurance,
9 accident and health or sickness insurance, or annuities."

10 SECTION 8. Section 431:8-301, Hawaii Revised Statutes, is
11 amended to read as follows:

12 "**§431:8-301 Insurance placed with unauthorized insurer**
13 **permitted.** (a) In addition to section 431:8-205, insurance may
14 be procured from an unauthorized insurer provided:

15 (1) [~~The~~] That the insurance is procured through a
16 [~~licensed~~] surplus lines broker licensed in the
17 insured's home state;

18 (2) The full amount or kind of insurance cannot be
19 obtained from insurers who are authorized to do
20 business in this State; provided that a diligent
21 search is made among the insurers who are authorized

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1 to transact and are actually writing the particular
2 kind and class of insurance in this State each time
3 such insurance is placed or renewed;

4 (3) The surplus lines insurance procured is in addition to
5 or in excess of the amount and coverage which can be
6 procured from the authorized insurers; and

7 (4) The insurance is not procured at a rate lower than the
8 lowest rate which is generally acceptable to
9 authorized insurers transacting that kind of business
10 and providing insurance affording substantially the
11 same protection.

12 (b) A surplus lines broker is not required to make a due
13 diligence search to determine whether the full amount or type of
14 insurance can be obtained from admitted insurers when the broker
15 is seeking to procure or place surplus lines insurance for an
16 exempt commercial purchaser provided:

17 (1) The broker procuring or placing the surplus lines
18 insurance has disclosed to the exempt commercial
19 purchaser that such insurance may or may not be
20 available from the admitted market that may provide
21 greater protection with more regulatory oversight; and

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1 (2) The exempt commercial purchaser has subsequently
2 requested in writing for the broker to procure or place
3 the insurance from a unauthorized insurer."

4 SECTION 9. Section 431:8-302, Hawaii Revised Statutes, is
5 amended to read as follows:

6 "**§431:8-302 Surplus lines [in-solvent] insurers.** (a) No
7 surplus lines broker shall, either knowingly or without
8 reasonable investigation of the financial condition and general
9 reputation of the insurer, place insurance with a financially
10 unsound [insurers] insurer or with [insurers] an insurer
11 engaging in an unfair [practices] practice.

12 [~~(b) Before placing insurance with any unauthorized~~
13 ~~insurer, the broker shall ascertain the financial condition of~~
14 ~~the insurer and:~~

15 ~~(1) In the case of a foreign insurer, shall maintain in~~
16 ~~the broker's office a current certificate, in proper~~
17 ~~form, from the regulatory authority in the domicile of~~
18 ~~the unauthorized insurer, to the effect that the~~
19 ~~insurer has capital and surplus, or its equivalent~~
20 ~~under the laws of its domiciliary jurisdiction, which~~
21 ~~equals the minimum capital and surplus requirements of~~

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1 ~~this State for that kind of insurer as set out in~~
2 ~~article 3; or~~
3 ~~(2) In the case of an alien insurer, shall maintain in the~~
4 ~~broker's office evidence of the financial~~
5 ~~responsibility of the insurer. Evidence satisfactory~~
6 ~~to the commissioner that the insurer maintains in the~~
7 ~~United States an irrevocable trust fund in either a~~
8 ~~national bank or a member of the Federal Reserve~~
9 ~~System in an amount not less than \$5,400,000 for the~~
10 ~~protection of all its policyholders in the United~~
11 ~~States consisting of cash, securities, letters of~~
12 ~~credit, or of investments of substantially the same~~
13 ~~character and quality as those which are eligible~~
14 ~~investments for the capital and statutory reserves of~~
15 ~~authorized insurers writing like kinds of insurance in~~
16 ~~this State, shall constitute prima facie evidence of~~
17 ~~responsibility.~~
18 ~~Upon request by the commissioner, the broker shall immediately~~
19 ~~submit to the commissioner the items described in this~~
20 ~~subsection.~~

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1 ~~(c) The requirements of this section may be satisfied by~~
2 ~~an insurer possessing less than the capital and surplus set~~
3 ~~forth in subsection (b) upon an affirmative finding of~~
4 ~~acceptability by the commissioner. The finding shall be based~~
5 ~~upon such factors as quality of management, capital and surplus~~
6 ~~of parent company, company underwriting profit and investment~~
7 ~~income trends, and company record and reputation within the~~
8 ~~industry. In no event shall the commissioner make an~~
9 ~~affirmative finding of acceptability when the surplus lines~~
10 ~~insurer's capital and surplus is less than \$500,000.]~~

11 (b) A surplus lines broker may place surplus lines
12 insurance only with insurers who are authorized to write that
13 type of insurance in the insurer's domiciliary state.

14 (c) A surplus lines broker shall not place coverage with
15 an unauthorized insurer unless, at the time of placement, the
16 surplus lines broker has determined that the unauthorized
17 insurer has capital and surplus or its equivalent under the laws
18 of its domiciliary state that equal the greater of:

19 (1) The minimum capital requirement of this State or a
20 minimum of \$15,000,000. These requirements may be
21 satisfied by the insurer's possessing less than the

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1 minimum capital and surplus upon an affirmative
2 finding of acceptability by the commissioner. The
3 finding shall be based upon such factors as quality of
4 management, capital and surplus of any parent company,
5 company underwriting profit and investment income
6 trends, market availability, and company record and
7 reputation within the industry. In no event shall the
8 commissioner make an affirmative finding of
9 acceptability when the unauthorized insurer's capital
10 and surplus is less than \$4,500,000.

11 (2) For an insurer not domiciled in the United States or
12 its territories, the insurer shall be listed on the
13 Quarterly Listing of Alien Insurers maintained by the
14 National Association of Insurance Commissioners
15 International Insurers Department. In the case of an
16 alien insurer that is not in the Quarterly Listing of
17 Alien Insurers, the surplus lines broker shall
18 maintain in the broker's office evidence of the
19 financial responsibility of the insurer. Evidence
20 satisfactory to the commissioner that the insurer
21 maintains in the United States an irrevocable trust

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1 fund in either a national bank or a member of the
2 Federal Reserve System in an amount of not less than
3 \$5,400,000 for the protection of all its policyholders
4 in the United States, consisting of cash, securities,
5 letters of credit, or of investments of substantially
6 the same character and quality as those which are
7 eligible investments for the capital and statutory
8 reserves of authorized insurers writing like kinds of
9 insurance in this State, shall constitute prima facie
10 evidence of financial responsibility.

11 (d) The commissioner is authorized to enter into a
12 cooperative agreement or interstate agreement or compact to
13 establish additional and alternative nationwide uniform
14 eligibility requirements that shall be applicable to
15 unauthorized insurers domiciled in another state."

16 SECTION 10. Section 431:8-305, Hawaii Revised Statutes, is
17 amended by amending subsection (a) to read as follows:

18 "(a) Upon placing surplus lines insurance, the surplus
19 lines broker shall as soon as reasonably possible deliver to the
20 insured the policy, or if the policy is not available, the
21 surplus lines broker's certificate, cover note, binder or other

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1 evidence of insurance. Any confirmation of insurance shall be
2 executed by the surplus lines broker and shall show the
3 following:

- 4 (1) The policy number, effective date, home state, and the
5 description and location of the subject of the
6 insurance,
- 7 (2) A general description of the coverages, including any
8 material limitations other than those in standard
9 forms,
- 10 (3) The premium and rate charged itemized by each state,
- 11 (4) The taxes and fees to be collected from the insured
12 itemized by each state,
- 13 (5) The name and address of the insured,
- 14 (6) The name and address of the insurer,
- 15 (7) If the direct risk is assumed by more than one
16 insurer, the certificate shall state the name and
17 address and proportion of the entire direct risk
18 assumed by each insurer, and
- 19 (8) The name of the surplus lines broker and such broker's
20 license number."

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1 SECTION 11. Section 431:8-312, Hawaii Revised Statutes, is
2 amended by amending subsection (a) to read as follows:

3 "(a) Each licensed surplus lines broker shall keep in the
4 broker's office in this State a full and true record of each
5 surplus lines contract placed by the broker including a copy of
6 the policy, certificate, cover note, or other evidence of
7 insurance showing such of the following items as may be
8 applicable:

- 9 (1) Amount of the insurance and perils insured;
- 10 (2) Brief description of the property insured and its
11 location;
- 12 (3) Gross premium, taxes and fees charged itemized by each
13 state;
- 14 (4) Any return premium, taxes and fees paid itemized by
15 each state;
- 16 (5) Rate of premium charged upon the several items of
17 property;
- 18 (6) Effective date of the contract, and the terms thereof;
- 19 (7) Name [~~and~~] , address, and home state of the insured;
- 20 (8) Name and address of the insurer;

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1 (9) Amount of tax and other sums to be collected from the
2 insured itemized by each state; and

3 (10) Any additional information required by the
4 commissioner."

5 SECTION 12. Section 431:8-313, Hawaii Revised Statutes, is
6 amended to read as follows:

7 "§431:8-313 Surplus lines broker's [annual statement]
8 reports to commissioner. (a) Each surplus lines broker shall
9 file with the commissioner on or before March 15 [~~of each year~~]
10 , 2011 a verified statement of all surplus lines insurance
11 transacted during [the preceding calendar year] 2010. Each
12 surplus lines broker shall file with the commissioner on or
13 before September 15, 2011 a verified statement of all surplus
14 lines insurance transacted after December 31, 2010 and before
15 July 1, 2011. After June 30, 2011, each surplus lines broker
16 shall file with the commissioner within forty-five days of the
17 end of each calendar quarter a verified statement of all surplus
18 lines insurance transacted during the calendar quarter. The
19 statement for the quarter ending September 30 shall be filed
20 before or on November 15. The statement for the quarter ending
21 December 31 shall be filed before or on February 15. The

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1 statement for the quarter ending March 31 shall be filed before
2 or on May 15. The statement for the quarter ending June 30
3 shall be filed before or on August 15.

4 (b) The statement shall be on forms as prescribed and
5 furnished by the commissioner and shall show:

6 (1) Gross amount of premiums for each kind of insurance
7 transacted;

8 (2) Aggregate gross premiums charged[+] and itemized by
9 state;

10 (3) Aggregate of returned premiums paid to insureds[+] and
11 itemized by state;

12 (4) Aggregate of net premiums[+] and fees and itemized by
13 state;

14 (5) Amount of aggregate [~~tax~~] remitted[+] taxes and fees
15 and itemized by state; and

16 (6) Additional information as required by the
17 commissioner."

18 SECTION 13. Section 431:8-315, Hawaii Revised Statutes, is
19 amended to read as follows:

20 "**§431:8-315 Tax on surplus lines.** (a) [~~On or before~~
21 ~~March 15 of each year,~~] On or before March 15, 2011, each

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1 surplus lines broker shall pay to the director of finance,
2 through the commissioner, a premium tax on surplus lines
3 insurance transacted by [~~such~~] the broker during [~~the preceding~~
4 ~~calendar year.~~] 2010. On or before September 15, 2011, each
5 surplus lines broker shall pay to the director of finance,
6 through the commissioner, a premium tax on surplus lines
7 insurance transacted by the broker after December 31, 2010 and
8 before July 1, 2011. After June 30, 2011, within forty-five
9 days after the end of each calendar quarter, each surplus lines
10 broker shall pay to the director of finance, through the
11 commissioner, a premium tax on surplus lines insurance
12 transacted by the broker during the calendar quarter for
13 insurance for which this State is the home state of the
14 insured. The tax rate shall be in the amount of 4.68 per cent
15 of gross premiums, less return premiums, on [~~taxable~~] surplus
16 lines insurance[~~-~~] allocated to this State. The tax rate and
17 fees of other states shall be applied to the gross premiums,
18 less return premiums, allocated to those states.

19 (b) The commissioner shall collect the taxes and fees on
20 independently procured surplus lines insurance and from surplus
21 lines brokers and disburse to the other states the funds

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1 allocated to that state, provided that the other state has a
2 reciprocal allocation and disbursement procedure for the benefit
3 of this State. To the extent that other states, where portions
4 of the properties, risks, or exposures reside, have failed to
5 establish a reciprocal allocation and disbursement procedure
6 with this State, the net premium tax collected shall be retained
7 by this State.

8 As used in this subsection, "gross premiums" mean the
9 amount of the policy or coverage premium charged by the insurer
10 in consideration for the insurance contract. Any charges for
11 policy, survey, inspection, service, or similar fees or other
12 charges added by the broker shall not be considered part of
13 gross premiums.

14 ~~(b)~~ (c) If a surplus lines policy covers risks or
15 exposures only partially resident in this State, the tax so
16 payable shall be computed upon the proportion of the premium
17 which is properly allocable to the risks or exposures located in
18 this State. The taxes and fees payable to this State on
19 policies that cover risks and exposures only partially resident
20 in this State shall be remitted, on the quarterly schedule, to
21 the home state of the insured for disbursement to this State.

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1 ~~(e)~~ (d) The tax on any portion of the premium unearned
2 at the termination of the insurance contract shall be returned
3 to the policyholder.

4 (e) The commissioner may enter into a cooperative
5 agreement, reciprocal agreement, or compact with other states to
6 facilitate and provide for the collection, allocation, and
7 disbursement of premium taxes attributable to the placement of
8 surplus lines insurance; provide for uniform methods of
9 allocation and reporting among surplus lines insurance risk
10 classifications; conform to the requirements of the federal
11 Nonadmitted and Reinsurance Reform Act of 2010; and share
12 information among states relating to surplus lines insurance
13 premium taxes.

14 (1) The commissioner may establish a uniform statewide
15 rate of taxation applicable to surplus lines insurance
16 that shall be collected by other states. This rate
17 shall encompass all existing rates of taxation, fees,
18 and assessments imposed by this State and any of its
19 political subdivisions. The commissioner shall
20 document the method by which the statewide rate is
21 calculated.

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1 (2) The commissioner may utilize a method adopted in
2 cooperation with other states to allocate risk and
3 compute the tax due on the portion of premium
4 attributable to each risk classification and to each
5 state where properties, risks, or exposures are
6 located.

7 (3) The commissioner shall assess the insured for the cost
8 of the cooperative agreement, reciprocal agreement, or
9 compact to collect and distribute the premium taxes.

10 (4) Upon application of the insured, the commissioner
11 shall refund the insured for excess payments of taxes
12 received by the State that are the result of the
13 statewide tax rate."

14 SECTION 14. Section 431:8-316, Hawaii Revised Statutes, is
15 amended to read as follows:

16 "**§431:8-316 Penalty for failure to file statement or remit**

17 **tax.** (a) If any surplus lines broker fails to:

18 (1) File [~~an annual statement,~~] statements required by
19 section 431:8-313; or

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- 1 (2) Pay the premium tax required by section 431:8-315 when
2 the tax is due, the surplus lines broker may be liable
3 for a fine of up to \$25 for each day of delinquency.
- 4 (b) The commissioner may:
- 5 (1) Collect the premium tax required by section 431:8-315
6 by distraint;
- 7 (2) Recover the premium tax required by section 431:8-315
8 and fine for failure to pay the premium tax by
9 instituting an action in any court of competent
10 jurisdiction; or
- 11 (3) Recover the fine for failure to file the [~~annual~~]
12 statement by instituting an action in any court of
13 competent jurisdiction."

14 SECTION 15. Section 431:8-317, Hawaii Revised Statutes, is
15 amended by amending subsection (a) to read as follows:

16 "(a) The commissioner may suspend, revoke, or refuse to
17 extend any surplus lines broker's license for any cause
18 specified in any other provision of this chapter, or for any of
19 the following causes:

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- 1 (1) Failure to file [~~the annual statement~~] statements
2 required by section 431:8-313 or to pay the tax
3 required by section 431:8-315;
- 4 (2) Failure to keep records or to allow the commissioner
5 to examine the surplus lines broker's records as
6 provided in this article;
- 7 (3) Removal of office accounts and records from this State
8 during the period in which the accounts are required
9 to be maintained under this article;
- 10 (4) Any of the causes for which a producer's license may
11 be suspended or revoked under article 9A;
- 12 (5) Any cause for which issuance of the license could have
13 been refused had it then existed and been known to the
14 commissioner;
- 15 (6) If the licensee wilfully violates or knowingly
16 participates in the violation of any provision of this
17 code;
- 18 (7) If the licensee has obtained or attempted to obtain
19 the license through wilful misrepresentation or fraud,
20 or has failed to pass any examination required by
21 section 431:9A-105;

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- 1 (8) If the licensee has misappropriated, converted to the
2 licensee's own use, or illegally withheld moneys
3 required to be held in a fiduciary capacity;
- 4 (9) If the licensee, with intent to deceive, has
5 materially misrepresented the terms or effect of any
6 insurance contract, or has engaged or is about to
7 engage in any fraudulent transaction;
- 8 (10) If the licensee has been guilty of any unfair practice
9 or fraud as defined in article 13;
- 10 (11) If in the conduct of the licensee's affairs under the
11 license, the licensee has been a source of injury and
12 loss to the public;
- 13 (12) If the licensee issues or purports to issue any binder
14 as to any insurer named therein as to which the
15 licensee is not then authorized so to bind; or
- 16 (13) If the licensee has dealt with, or attempted to deal
17 with, insurance or to exercise powers relative to
18 insurance outside the scope of the licensee's
19 licenses."

20 SECTION 16. Statutory material to be repealed is bracketed
21 and stricken. New statutory material is underscored.

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1 SECTION 17. This Act shall take effect upon its approval.

2

3

INTRODUCED BY: _____

4

BY REQUEST



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Richard M. Bouhan
Executive Director

DATE: February 4, 2011

TO: The Honorable Robert Herkes
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The Honorable Rosalyn Baker
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FROM: Steven P. Stephan, J.D., CPCU, ARe
Director of Government Relations
steve@napslo.org

RE: HB1052/SB1279

The National Association of Professional Surplus Lines Offices (NAPSLO) represents surplus lines brokers and surplus lines insurance companies in all fifty states and the District of Columbia. NAPSLO would like to briefly comment about proposed legislation which amends the Hawaii surplus lines code. This proposal includes many of the provisions of the Nonadmitted and Reinsurance Reform Act (NRRRA). We support this effort, as does the National Conference of Insurance Legislators, the Council of State Governments, and the National Conference of State Legislators. NAPSLO would like to thank you for your efforts to keep the Hawaii surplus lines code current.

First, we believe the following language misconstrues the NRRA:

(b) The commissioner shall collect the taxes and fees on
8 independently procured surplus lines insurance and from
surplus
9 lines licensees and disburse to the other states the funds
10 earned by each state, provided that the other state has a
11 reciprocal allocation and disbursement procedure for the
benefit
12 of this State.

The tax revenue collected by Hawaii is Hawaii revenue and cannot be "earned by each state." Hawaii may elect to share some of its revenue with other states that reciprocate, but it is Hawaii tax revenue that is due on policyholders with a "home state" in Hawaii.

We are also writing to express our opposition to the language contained in HB1052/SB1279 granting the Insurance Commissioner the authority to participate in a multistate cooperative for taxes. The delegation of authority to the Commissioner was suggested to authorize the Commissioner to enter into an agreement known as the Nonadmitted Insurance Multistate Agreement or (NIMA). NAPLSO believes this proposal is a delegation of legislative authority to a state agency because it addresses tax issues that must be decided by the legislature. Any tax sharing agreement should be specifically set out in legislation and approved by the legislature. As a practical matter, this proposal is not adequate to apprise policyholders, brokers or legislators of how burdensome and expensive the NIMA proposal will be. A paper detailing our concerns about the NIMA proposal is attached.

NIMA would be an agreement between states that would result in a tax increase on some policyholders, would result Hawaii tax revenue being forwarded to another state, and would result in a surcharge on policyholders. All of these issues must be decided by the legislature after they are vetted through the legislative process. Decisions such as these cannot be delegated to an administrative agency.

If Hawaii is to impose additional taxes on policyholders and reporting requirements on brokers by entering an interstate tax agreement, the agreement should be transparently contained in legislation so the brokers, policyholders, and legislators know what is being proposed. We believe that for an interstate tax agreement to be effective it must be specifically spelled out in legislation and approved by the legislature. This proposal is inadequate legally and inadequate as a practical matter to notify the insurance community about the true burden and expense of the NIMA proposal.

We were advised by compact experts at the National Center for Interstate Compacts that it would not be legally adequate for a state to enter into an interstate agreement if the statute simply authorized a state agency, at its discretion to either enter or decide not to enter a tax allocation agreement. We were advised that the agreement language would need to be entered into the statute so the legislature has clearly decided whether or not to enter into a multi-state tax agreement. Another multi-state insurance agreement for life and health products, The Interstate Insurance Product Regulation Compact (IIPRC), has been adopted by 38 states and it was entered in its entirety into state statutes. It is not clear why something that is clearly a legislative issue such as taxes would be decided outside of the legislative process, while the IIPRC language was vetted through the legislative process.

The politics of tax allocation agreements are controversial. There are competing versions of surplus lines tax agreements. The National Conference of Insurance Legislators, the Council of State Governments and the National Conference of State Legislatures have all endorsed a version known as SLIMPACT. All three groups take the position that SLIMPACT should be included in its entirety in the state codes. We believe these groups have accurately assessed the necessity for including the terms of the multi-state tax allocation agreement in the state code.

We believe that this proposal imposes the tax rate of Hawaii upon those portions allocated to other states and support that view as further consistent with the intent of NRRRA. However, we are not certain of that. It is possible that the proposed legislation combined with the use of the Clearinghouse would impose tax rates of other states upon Hawaii policyholders. We would oppose any provision taxing Hawaii policyholders at tax rates of other states. The NRRRA would appear to envision the home state taxing its policyholders at its rates. If this issue is addressed at all, it should be addressed in connection with separate legislation authorizing a tax sharing agreement, if any is adopted.

We believe the non-tax NRRRA provisions in this proposal are generally consistent with NRRRA and should be included in the code even if the state is unable to adopt legislation implementing a tax allocation agreement. The definition of "home state," the modified eligibility language and the definition of an "exempt commercial purchaser" are examples of provisions that will be necessary regardless of whether the state adopts tax allocation legislation. We believe that this proposal needs language throughout more tightly focusing on Hawaii as the "home state" of the insured. We also see a need for the definition of qualified risk manager and the producer database language consistent with NRRRA. We have attached a marked up copy of the bill with some suggestions.

With the exception of the clause authorizing the Commissioner to enter into an unspecified tax agreement, we support adding these additional provisions and the provisions of this proposal to the insurance code. The state also has an interest in seeing this proposal pass without delay because it will need to tax the gross premium when it is the home state of the insured. We would urge you to consider addressing tax allocation agreements in detail in separate legislation so the other reforms in this proposal may advance through the legislative process.

Thank you for the opportunity to comment. We have included a copy of the proposed legislation in revision mode with our suggestions outlined above.

SPS/clr



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Richard M. Bouhan
Executive Director

WHY NAPSLO OPPOSES THE NAIC'S NONADMITTED INSURANCE MULTI-STATE AGREEMENT (NIMA)

The National Association of Insurance Commissioners is advocating that the states' enact the Nonadmitted Insurance Multistate Agreement or NIMA. NIMA is an agreement between states created by an NAIC committee and designed to allocate surplus lines premium tax money among the states on multi-state surplus lines policies. NIMA was developed after the passage of the Nonadmitted and Reinsurance Reform Act (NRRA) which allowed, but did not require, the states to enter into an agreement to allocate multi-state tax revenue among the states.

NAPSLO opposes NIMA because it requires brokers to use intricate allocations formulas for casualty lines, which have not been required in practice or by existing state law. As a result, the NIMA allocation formulas will be burdensome for brokers and for policyholders who will be required to create and report intricate data for the first time. A few of the largest brokers have attempted to allocate all casualty lines, but it has proven to be too burdensome to use as a nationwide tax collection system. Moreover, the NIMA allocation requirements violate the spirit and letter of the NRRA which was enacted to implement a single-state tax remittance system.

Legislation has recently been introduced in many states including South Dakota, North Dakota, Oregon, and Arizona, that would allow the state to join the NIMA agreement by authorizing the insurance Commissioner to enter into an agreement for the allocation of surplus lines tax. NAPSLO opposes such legislation. If a state intends to impose additional taxes and reporting requirements on brokers by entering an interstate agreement, the legislation should be transparently set out in the statutes so the brokers, policyholders, and legislators know what is being proposed. The burdensome reporting, the additional taxes, and the policyholder surcharges should not be imposed through vague legislation that is inadequate to notify the insurance community about the true expense of the NIMA proposal.

NAPSLO believes the NIMA agreement and the legislation authorizing the Insurance Commissioner to enter into a tax allocation agreement with other states should be opposed for the following reasons:

- 1. NIMA will create unnecessary and burdensome data reporting by brokers for the sole purpose of collecting taxes.**

The NIMA system will require detailed data reporting of dozens of data elements for every policy issued for the sole purpose of remitting taxes on surplus lines policies with exposures in multiple states. The burden imposed is completely disproportionate to any legitimate regulatory need. One large broker reported that the software system developed to remit surplus lines taxes involves more than 25,000 reporting rules. The IRS never requires this level of burdensome detailed reporting for the sole purpose of remitting taxes. This burdensome process could have been replaced with a uniform annual tax return.

2. NIMA requires novel allocation requirements for casualty lines

NIMA requires allocation of dozens of casualty lines when the vast majority of states have not sought to impose this intricate reporting system in the past. Many casualty lines do not generate state-specific data in the normal course of business. Products liability, D&O, E&O, completed operations and many other lines are frequently not rated based upon state-specific rating factors. For many lines there is simply no data available to comply with the casualty allocation data requirements of the NIMA system. NIMA will require the policyholders to attempt to generate or, if it is unavailable, estimate data for the broker to report through detailed software, for the sole purpose of remitting taxes. Again, taxes could have been collected with a uniform tax return.

3. State laws do not presently require allocation of casualty premium taxes.

The vast majority of state laws require allocation of taxes on premium that is “properly allocable” to a state. Most surplus lines brokers construed the term “properly allocable” to mean that taxes on casualty premium should be allocated to the home state of the insured because that is where the exposure resides for a casualty risk. The corporate headquarters is intuitively where a liability exposure resides. There is no other more appropriate method of allocating casualty premium. Allocating casualty premium to the home state is more intuitive for most brokers than using other criteria such as payroll, square footage, number of employees, revenue or some other method.

Eleven states tax the gross premium on a policy so there is no allocation required at all in those states. A few states explicitly require allocation of casualty premium, but it is not possible to fairly enforce these requirements because the other states do not agree on a casualty allocation methodology. A nationwide allocation system cannot work unless it is uniformly implemented from state to state.

4. NIMA fails to implement the efficient system or uniformity required by the Nonadmitted Reinsurance Reform Act (NRRA).

The clear intent of the Nonadmitted and Reinsurance Reform Act (NRRA) was to create a streamlined tax system that involved a payment to the home state of the insured using uniform requirements, forms and procedures. NIMA not only fails to establish uniform requirements, forms and procedures, but instead continues, by contract, the burdensome system that Congress sought to eliminate with the NRRA.

NIMA will perpetuate unnecessary, bureaucratic data reporting, with dozens of data elements and hundreds of state-specific tax nuances for every multi-state policy issued. NIMA will result in the creation of a software system that will require the broker to input anywhere from dozens of data elements to hundreds of data elements depending upon the multi-state policy issued. The reason the NRRA was adopted was to replace this dysfunctional system involving a vast number of state-specific nuances with a single-state payment system that included uniform requirements, forms and procedures. NIMA circumvents the NRRA and continues with the existing system through a contract between Insurance Commissioners.

5. NIMA violates the NRRA requirement that “no state other than the home state . . . may require any premium tax payments for nonadmitted insurance.”

The NRRA envisioned a single payment to the home state of the insured for a policy with multi-state exposures. The fact that the NRRA preempted any state other than the home state from using any “law, regulation, provision, or action” to collect its taxes, indicates that Congress intended the home state to use its tax rates. By adopting and signing NIMA a state is taking an “action” to collect its taxes in contravention of the NRRA. Instead of complying with the Congressional mandate, the NIMA proposal will require the collection of all surplus lines taxes, fees and assessments for every state where any portion of the exposure resides. Some states have several different fees and assessments tacked on to a surplus lines policy. The broker will be required to input data for all of these unique fees and assessments in direct contravention of the Congressional mandate that only the home state may require premium tax payments.

6. NIMA is not a transparent proposal

Legislation authorizing the Insurance Commissioner to enter into an agreement with other states fails to notify the insurance community that the NIMA proposal will impose numerous burdensome requirements and expenses on the broker and additional taxes and expenses on the insured. For many policyholders NIMA will result in a tax increase. NIMA will require policyholders with incidental exposures in the wind-exposed states to remit higher taxes to cover fees and assessments. The higher taxes will be necessary to fund state run facilities such as the hurricane catastrophe funds, and state-run insurance facilities. NIMA will also require Insurance Commissioners to impose a surcharge on policyholders to fund a clearinghouse. NIMA fails to indicate who will establish a clearinghouse, purchase computers, hire employees, set auditing standards, set accounting rules, purchase software, pay the expenses, rent office space, or open bank accounts. All of these issues should be more transparent because they impact the surcharge to be imposed upon policyholders. NIMA also fails to indicate how a contract signed by Commissioners can become law imposed upon insurance brokers or become the tax allocation law of the states. All of these issues should have been vetted through the legislative process because the NIMA agreement should have been introduced into legislation. Instead, some states have introduced legislation authorizing a Commissioner to enter into an agreement, which is inadequate to apprise the tax-paying brokers and policyholders of the burden and expense that will be imposed upon them by the NIMA system.

The legislation authorizing NIMA is not transparent and numerous objections to NIMA would be raised if NIMA were introduced as legislation. Legislation simply authorizing the Commissioner to enter into an agreement should be opposed because it not adequate to notify the insurance community that the intent is to implement the NIMA system and the added burden and expenses associated with it.