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DATE: April 16, 1997

**HOUSE OF REPRESENTATIVES
AS REVISED BY THE COMMITTEE ON
GOVERNMENTAL OPERATIONS
BILL RESEARCH & ECONOMIC IMPACT STATEMENT**

BILL #: CS/HB 269

RELATING TO: Surplus Lines Insurance

SPONSOR(S): Committee on Financial Services & Representative Bainter

STATUTE(S) AFFECTED: Amends ss. 626.918, .912, .931, .932 & .631.52; Creates s. 626.9325

COMPANION BILL(S): SB 908 (s) & SB 904 (c)

ORIGINATING COMMITTEE(S)/COMMITTEE(S) OF REFERENCE:

- (1) FINANCIAL SERVICES YEAS 11 NAYS 0
- (2) GOVERNMENTAL OPERATIONS YEAS 5 NAYS 0
- (3) FINANCE AND TAXATION
- (4)
- (5)

I. SUMMARY:

“Surplus lines insurance” is insurance coverage provided by an insurance company that is not licensed in Florida, but that is allowed to do business in the state because the particular coverage offered is not available from Florida-licensed companies.

This bill creates the Florida Surplus Lines Service Office (“service office”) as a private, nonprofit entity to supplement the regulatory functions of the Department of Insurance (“department”) with respect to surplus lines insurance. The service office is required to maintain files of surplus lines policy forms, maintain records of surplus lines transactions, and collect and remit to the department the existing 5% tax on surplus lines premiums.

The service office will be funded by a fee in the amount of up to 0.3% on surplus lines premiums, as determined by the department, which will generate up to \$1.9 million a year. It will operate subject to a plan of operation approved or adopted by the department, and will be governed by a board appointed by the department.

This bill also provides circumstances under which certain surplus lines insurers may be subject to the minimum surplus requirements applicable to admitted insurers, rather than the higher requirements applicable to surplus lines insurers.

This bill does not appear to have a fiscal impact on state or local governments. Furthermore, this bill does not reduce any current regulatory functions of the department, and is therefore not expected to have any fiscal impact on the department.

II. SUBSTANTIVE ANALYSIS:

A. PRESENT SITUATION:

“Surplus lines insurance” is insurance coverage provided by an insurance company that is not licensed in Florida, but that is allowed to do business in the state because the particular coverage offered is not available from Florida-licensed companies. Commercial general liability policies and similar policies typically exclude coverage for high-risk activities; a surplus lines policy provides a business with coverage for those activities. Hazardous materials transporters, day care centers, nuclear power plants, and taverns are among the kinds of businesses that usually need to obtain liability coverage in the surplus lines market. In 1995, Florida generated \$656 million in surplus lines premiums on approximately 175,000 policies.

When specific insurance coverages of subjects resident, located, or to be performed in Florida cannot be procured from authorized (i.e., Florida-licensed) insurers, the coverages are designated as “surplus lines.” Surplus lines coverage may be procured from unauthorized (i.e., not holding a Florida certificate of authority) insurers if the insurance is eligible for export (i.e., placement with a surplus lines insurer), the insurer is an eligible surplus lines insurer, the insurance is placed through a Florida-licensed surplus lines agent, and the other requirements of the surplus lines law, ss. 626.913-626.937, F.S., are met.

In general, insurance is eligible for export to surplus lines insurers if the full amount of insurance required cannot, after diligent effort by the agent, be procured from any admitted insurer (when some of the coverage can be procured from an admitted insurer, only the excess is eligible for export); if the premium is no lower than the rate actually in use by a majority of admitted insurers for the same coverage on a similar risk; if the policy form is no more favorable to the insured, as to coverage or rate, than the forms currently in use by a majority of admitted insurers; and if the policy contains no deductible other than those currently in use by any admitted insurer (except as to windstorm or as to extended coverage on a fire policy).

In order for an insurer to be an eligible surplus lines insurer, it must have been licensed in its state or country of domicile for at least three years (this requirement may be waived or shortened by the department), must have surplus (i.e., net worth) of at least \$15 million (this requirement is being phased in, with the 1997 surplus requirement equal to \$4.5 million), must have a good reputation, and must meet the trustworthiness and criminal history requirements that apply to admitted insurers under s. 624.404(3), F.S. By contrast, the required minimum surplus to maintain a certificate of authority as a property and casualty insurer is \$4 million (this requirement is also being phased in, and the 1997 requirement is \$1.95 million).

Surplus lines policies are subject to a 5% premium tax known as the “surplus lines tax,” which is collected by the surplus lines agent and remitted to the department on a quarterly basis. The Insurance Commissioner’s Regulatory Trust Fund, which is the source of Department of Insurance funding, receives 55% of the proceeds of the tax, and the General Revenue Fund receives the remaining 45%. The uses of the tax are not restricted to activities relating to surplus lines insurance.

Surplus lines agents currently play the key role in assuring compliance with the surplus lines laws. The agent must determine that the applicant qualifies for surplus lines coverage and that the surplus lines insurer is eligible. The agent must also file a quarterly report with the department which includes aggregate gross and net premiums and a listing of all policies issued. There is no automatic filing requirement for the policy forms themselves, but an agent must file a copy of a form upon request of the department. Agents are required to maintain certain records, which are subject to examination by the department.

Surplus lines policyholders are not protected by a guaranty association in the event of the insurer's insolvency; however, the surplus lines industry as a whole appears to be financially sound. According to a 1994 A. M. Best Co. solvency study, the annual average number of insolvencies among insurers as a whole from 1969 through 1993 was 0.87%, while the average number of surplus lines insolvencies was 0.80%.

Private, nonprofit "stamping offices" have been established in 10 states, including California, New York, Texas, and Illinois, to provide additional regulatory oversight of the surplus lines industry. The functions of these offices vary from state to state, but usually include the review of forms to determine whether they are in compliance with statutes that require enhanced data collection, tax calculation, and tax collection. In 1996, the California stamping office raised \$5,558,000 in revenues and had expenses of \$5,158,499; a fee of 0.35% of premium generated \$5,350,000 of the office's revenues. The Texas stamping office raised \$1,279,000 and spent \$2,024,600 in 1996; a fee of 0.1% of premium generated \$1,100,000 of revenues.

B. EFFECT OF PROPOSED CHANGES:

Under this bill, each surplus lines policyholder would pay a "surplus lines service fee" in the amount of up to 0.3% of the total gross premium of a filed surplus lines policy or document, as determined by the Department of Insurance ("department"). The fee would fund the Florida Surplus Lines Service Office ("service office"), which would be created to supplement the regulatory functions of the department with respect to surplus lines insurance.

The service office would be a nonprofit association of which all surplus lines agents would be members. Such agents would file with the service office a copy of, or information on, each surplus lines policy or other document required by the service office plan of operation. When the insurer or an adjuster representing the insurer received a claim notice under a policy subject to these filing requirements, the insurer or adjuster would notify the service office of the claim and the policy under which the claim was made. The service office would determine whether the policy was filed as required, and would report any unfiled policy to the department.

Subject to the Insurance Code and rules of the department, the service office would:

- ☞ Receive, record, and review all surplus lines insurance policies or documents.
- ☞ Maintain records of policies reported to the service office and provide monthly reports to the department.

- ☞ Prepare quarterly reports of each surplus lines agent's business, and collect and remit to the department the surplus lines tax.
- ☞ Reconcile reports from non-admitted insurers and surplus lines agents, and provide a report of the reconciliation to the department.
- ☞ Submit to the department for its approval an annual operating budget for the office.

The service office would operate under a board of governors appointed by the department, consisting of five members of the Florida Surplus Lines Association, a representative (who is a surplus lines agent) from each of the two major Florida associations of insurance agents, the Insurance Consumer Advocate, and a risk manager for a large domestic commercial enterprise.

The service office must submit a plan of operation to the department. If the service office fails to submit a suitable plan within 180 days after the effective date of the act, or if the service office subsequently fails to submit suitable amendments, the department must adopt a plan, amendments, or rules to effectuate the act.

The department is given the power to examine the service office as deemed necessary, at the service office's expense.

The service office, its governors, officers, agents, and employees, and the department and its officers, employees, and representatives would be immune from civil liability for actions taken by them in the performance of their powers and duties under s. 626.921, F.S., except in cases involving gross negligence, fraud, or bad faith.

Information furnished to the department under s. 626.923, F.S., or examined under s. 626.930, F.S., would continue to be confidential and exempt from the public records law. This exemption does not apply to any proceeding instituted by the department against an agent or insurer. This bill does not create any new public records exemption. It simply retains the public records exemption contained in s. 626.921, F.S. (see Comments).

This bill would also provide circumstances under which certain surplus lines insurers could be eligible to do business in Florida while maintaining the minimum surplus required of licensed insurers, rather than the higher minimum required of surplus lines insurers.

C. APPLICATION OF PRINCIPLES:

1. Less Government:

- a. Does the bill create, increase or reduce, either directly or indirectly:

- (1) any authority to make rules or adjudicate disputes?

Yes. The Department of Insurance is authorized to adopt rules to effectuate the provisions of s. 626.921, F.S.

- (2) any new responsibilities, obligations or work for other governmental or private organizations or individuals?

Yes. This bill creates a nonprofit association to perform oversight functions not currently required by law.

- (3) any entitlement to a government service or benefit?

No.

- b. If an agency or program is eliminated or reduced:

- (1) what responsibilities, costs and powers are passed on to another program, agency, level of government, or private entity?

None. This bill would create a Surplus Lines Service Office to perform functions not currently performed by the Department of Insurance.

- (2) what is the cost of such responsibility at the new level/agency?

Not applicable.

- (3) how is the new agency accountable to the people governed?

Not applicable.

2. Lower Taxes:

- a. Does the bill increase anyone's taxes?

No.

- b. Does the bill require or authorize an increase in any fees?

Yes. Surplus lines policyholders would pay a fee of up to of 0.3% of gross premiums on all surplus lines policies to fund the operations of the Surplus Lines Service Office.

c. Does the bill reduce total taxes, both rates and revenues?

No.

d. Does the bill reduce total fees, both rates and revenues?

No.

e. Does the bill authorize any fee or tax increase by any local government?

No.

3. Personal Responsibility:

a. Does the bill reduce or eliminate an entitlement to government services or subsidy?

Not applicable.

b. Do the beneficiaries of the legislation directly pay any portion of the cost of implementation and operation?

Policyholders, agents, and insurers all might benefit from the service office proposed in this bill. The fees to support the service office would be paid by policyholders.

4. Individual Freedom:

a. Does the bill increase the allowable options of individuals or private organizations/associations to conduct their own affairs?

No.

b. Does the bill prohibit, or create new government interference with, any presently lawful activity?

No.

5. Family Empowerment:

a. If the bill purports to provide services to families or children:

(1) Who evaluates the family's needs?

Not applicable.

(2) Who makes the decisions?

Not applicable.

(3) Are private alternatives permitted?

Not applicable.

(4) Are families required to participate in a program?

Not applicable.

(5) Are families penalized for not participating in a program?

Not applicable.

b. Does the bill directly affect the legal rights and obligations between family members?

Not applicable.

c. If the bill creates or changes a program providing services to families or children, in which of the following does the bill vest control of the program, either through direct participation or appointment authority:

(1) parents and guardians?

Not applicable.

(2) service providers?

Not applicable.

(3) government employees/agencies?

Not applicable.

D. SECTION-BY-SECTION ANALYSIS:

Section 1 provides that this bill may be cited as the Dana Roehrig Act.

Section 2 amends s. 626.921, F.S., relating to confidentiality of records of the surplus lines examining office; creates the Florida Surplus Lines Service Office ("service office"); provides the Legislative purpose for creating the service office; provides that all surplus

lines agents must be members of the service office and file certain information with the service office; provides that the service office must report to the department when any such information is not properly filed; provides that the service office will exercise its powers through a board of governors, and the service office will be regulated by the department; provides that the service office must conduct certain activities such as collecting a 0.3% service fee from surplus lines agents, preparing and delivering specified reports, and receiving, recording, and reviewing all surplus lines insurance policies, according to a plan of action created by the service office and submitted to the department; provides that if the service office fails to devise a plan of action, the department may adopt a plan for the service office; provides for occasional examinations of the service office by the department; provides limited immunity for the service office, its governors, officers, agents, or employees, or department employees and representatives for any action taken by them in performance of their powers or duties; retains the public records exemption contained in s. 626.921, F.S. (see Comments).

Section 3 amends s. 626.931, F.S., relating to quarterly reports. Currently, surplus lines agents must file with the department quarterly reports of their surplus lines business, foreign (i.e., non-Florida) insurers must file with the department quarterly reports of surplus lines business, and alien (i.e., non-U.S.) insurers must file with the department annual reports of surplus lines business. Effective January 1, 1998, this bill requires these reports to be filed instead with the Surplus Lines Service Office.

Section 4 amends s. 626.932, F.S., relating to the surplus lines tax. As described in "Present Situation," above, surplus lines agents currently collect from policyholders and remit to the Department of Insurance a 5% tax on surplus lines premiums. The proceeds of this tax are divided between the Insurance Commissioner's Regulatory Trust Fund (55%) and the General Revenue Fund (45%). Currently, the surplus lines agent must remit the tax to the department on a quarterly basis. Effective January 1, 1998, this bill requires agents to instead remit the tax to the Surplus Lines Service Office, which is required to forward amounts collected to the department. This bill also specifies that the new surplus lines service fee does not constitute a "premium" for purposes of the surplus lines tax.

Section 5 creates s. 626.9325, F.S., relating to the surplus lines service fee. This bill provides that surplus lines policies are subject to the service fee of up to 0.3% specified in s. 626.921, F.S., which must be collected along with the full amount of the premium at the time of delivery of the policy or other initial confirmation of issuance. The surplus lines agent may not absorb the service fee and may not rebate the fee or any portion of the commission as an inducement for insurance or for any other reason. Fees must be remitted to the service office monthly, and delinquencies are subject to a 9% interest charge. The fees must be used to fund the cost of operations of the service office.

If the surplus lines policy covers risks or exposures only partly within Florida, the fee applies only to the Florida risks or exposures. The fee does not apply to policies covering state or local government agencies.

For purposes of this section, the term "premium" is defined to include both the premium and any fees charged, including the per-policy fee under s. 626.916, F.S., (but excluding the up to 0.3% service fee).

Section 6 amends s. 626.918, F.S., relating to standards for eligibility of surplus lines insurers. In 1993, the Legislature raised the minimum surplus required both of admitted insurers and surplus lines insurers. These increases are currently being phased in; the 1997 minimum surplus requirement for admitted property and casualty insurers is \$1.95 million, and the 1997 minimum surplus requirement for surplus lines insurers is \$4.5 million. A surplus lines insurer could elect to be subject to the minimum surplus requirements applicable to insurers generally, rather than the higher requirements applicable to surplus lines insurers, if three requirements are met:

The insurer must be a member of a holding company which also owns a Florida-domiciled admitted insurer.

The insurer must comply with Chapter 625, F.S., which governs insurers' accounting and investments.

The insurer must be a member of the Florida Insurance Guaranty Association.

Compliance with these requirements would provide the department with greater regulatory authority than it has with respect to surplus lines insurers generally, and would provide protection for the surplus lines insurer's policyholders in the event of insolvency.

Section 7 amends s. 631.52, F.S., relating to the scope of the Florida Insurance Guaranty Association law, to conform this bill to the changes made by Section 6.

Section 8 provides that the act takes effect October 1, 1997.

III. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT:

A. FISCAL IMPACT ON STATE AGENCIES/STATE FUNDS:

1. Non-recurring Effects:

None.

2. Recurring Effects:

This bill is not expected to have any fiscal impact on the Department of Insurance, because the Surplus Lines Service Office created by this bill will perform some oversight and record collection functions that are not currently being performed by the department, and because the department will continue to perform its current regulatory functions.

3. Long Run Effects Other Than Normal Growth:

Indeterminate. There may be slight positive fiscal effects in the long run if the service office is able, through its regulatory oversight, to identify surplus lines agents or insurers that are not currently remitting the correct tax on surplus lines policies.

4. Total Revenues and Expenditures:

See above.

B. FISCAL IMPACT ON LOCAL GOVERNMENTS AS A WHOLE:

1. Non-recurring Effects:

None.

2. Recurring Effects:

None.

3. Long Run Effects Other Than Normal Growth:

None.

C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

1. Direct Private Sector Costs:

Surplus lines policyholders must pay, and surplus lines agents must remit to the Department of Insurance, a service fee of up to 0.3% on surplus lines premiums, as determined by the department, to fund the service office. The fee will generate up to \$1.9 million in annual revenues to support the private, nonprofit service office.

To the extent that reduced surplus requirements for certain surplus lines insurers increase the likelihood of insolvencies that would be covered by the Florida Insurance Guaranty Association, this bill could increase the potential for assessments by the guaranty association.

2. Direct Private Sector Benefits:

To the extent that the Surplus Lines Service Office will allow for better enforcement of the Surplus Lines Law, consumer protection may be improved.

3. Effects on Competition, Private Enterprise and Employment Markets:

See above.

D. FISCAL COMMENTS:

Based on 1995 surplus lines premiums, the service fee of up to 0.3% included in this bill will generate up to \$1.9 million in annual revenues to support the service office. Revenues for fiscal year 1997-98 would be substantially lower than this amount, because this bill takes effect on October 1, 1997, and is not expected to be fully implemented until about six months after the effective date.

IV. CONSEQUENCES OF ARTICLE VII, SECTION 18 OF THE FLORIDA CONSTITUTION:

A. APPLICABILITY OF THE MANDATES PROVISION:

This bill does not require counties or municipalities to spend funds or to take an action requiring the expenditure of funds.

B. REDUCTION OF REVENUE RAISING AUTHORITY:

This bill does not reduce the authority that counties and municipalities have to raise revenues in the aggregate.

C. REDUCTION OF STATE TAX SHARED WITH COUNTIES AND MUNICIPALITIES:

This bill does not reduce the percentage of a state tax shared with counties or municipalities.

V. COMMENTS:

CS/HB 269 substantially retains the public records exemption in s. 626.921, F.S., for certain records held by the department, except that this bill makes the exemption subject to the Open Government Sunset Review Act of 1995. This means the exemption will stand repealed on October 2, 2001, unless reviewed and reenacted by the Legislature. No provision in this bill makes records of the service office confidential or exempt from public records laws.

In 1996, the sponsor of this bill sponsored HB 1845, which also attempted to create a Surplus Lines Service Office. HB 1845 passed the Committee on Insurance and the Committee on Finance and Taxation, and was withdrawn from the Committee on Appropriations. It passed the House by a vote of 117 to 0 on May 3, 1996. HB 1845 died in Senate messages on May 4, 1996. This bill substantially reflects the provisions contained in HB 1845.

Note: All uncited references in this bill analysis may be verified with staff of the Committee on Financial Services.

VI. AMENDMENTS OR COMMITTEE SUBSTITUTE CHANGES:

CS/HB 269 is substantially the same as HB 269 as originally filed, except that the committee substitute:

- includes a short title for this bill;
- changes the amount of the service fee from 0.3% of premium to *up to* 0.3% of premium, as determined by the Department of Insurance;

- provides a January 1, 1998, effective date for provisions relating to surplus lines agents' duty to file quarterly reports and to remit taxes to the Surplus Lines Service Office rather than the Department of Insurance; and
- provides circumstances under which certain surplus lines insurers may be subject to the minimum surplus requirements applicable to admitted insurers, rather than the higher requirements applicable to surplus lines insurers.

On April 15, 1997, the Committee on Governmental Operations adopted 5 amendments to CS/HB 269. These amendments do the following:

Amendment #1

- ⊗ removes the requirement that, in order to be permitted to maintain the same surplus requirements as Florida insurers, a surplus lines insurer affiliated with a Florida domestic insurer must also be a member of the Florida Insurance Guaranty Association;

Amendment #2

- amends s. 626.918(2)(d), F.S.;
- adds the requirement that, in order to become an eligible surplus lines insurer, an alien surplus lines insurer must maintain both a \$15 million surplus as to policyholders and a United States trust fund of not less than \$5.4 million for the protection of the policyholders;
- provides that the above mentioned surplus requirement and trust fund must be represented by eligible investments identical to those required of domestic insurers in ch. 625, F.S., except that an alien surplus lines insurer's surplus as to policyholders may be such investments permitted by their own domestic regulators if the investments are substantially similar to those types of investments permitted in Florida;

Amendment #3

- provides for severability of CS/HB 269, so that if one portion of the bill is found invalid, the other provisions or applications of the bill will not be affected if they can be given effect without the invalid portion;

Amendment #4

- ⊗ removes a provision which exempted from the scope of s. 631.52, F.S., any surplus lines insurance where the insurer elected to participate as a member insurer of the Florida Insurance Guarantee Association;

Amendment #5

- ⊗ removes a provision granting qualified immunity from liability or suit to the Service Office itself;
- grants immunity from liability or suit to the following:
 - any member¹ or the member's agents or employees,
 - agents or employees of the association,
 - members of the association's board of governors, or
 - the department or its representativesfor any action taken in furtherance of their official duties under this bill;
- ⊗ removes any such immunity from liability or suit against the above mentioned parties for an action omitted by them in performance of their powers and duties under this bill; and
- provides that such immunity does not apply in cases involving
 - breach of contracts or agreements pertaining to insurance; or
 - willful torts².

VII. SIGNATURES:

COMMITTEE ON FINANCIAL SERVICES:

Prepared by:

Legislative Research Director:

Leonard Schulte

Stephen Hogge

AS REVISED BY THE COMMITTEE ON GOVERNMENTAL OPERATIONS:

Prepared by:

Legislative Research Director:

Jason W. Owsley

Jimmy O. Helms

¹ The amendment does not specify that the term "member" means "**member of the association**," although this appears to be the intent of the amendment.

² Torts are traditionally divided into intentional and unintentional (negligence) torts. If the term "willful" equates to "intentional," it appears that this immunity provision principally covers suits involving negligent actions, rather than intentional torts or negligent omissions.