

# SENATE STAFF ANALYSIS AND ECONOMIC IMPACT STATEMENT

(This document is based on the provisions contained in the legislation as of the latest date listed below.)

BILL: CS/SB 658

SPONSOR: Banking and Insurance Committee and Senator Holzendorf

SUBJECT: Surplus Lines Insurance

DATE: March 19, 2001      REVISED: \_\_\_\_\_

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	<u>Deffenbaugh</u>	<u>Deffenbaugh</u>	<u>BI</u>	<u>Favorable/CS</u>
2.	<u>Keating</u>	<u>Johansen</u>	<u>FT</u>	<u>Favorable</u>
3.	_____	_____	<u>AGG</u>	_____
4.	_____	_____	<u>AP</u>	_____
5.	_____	_____	_____	_____
6.	_____	_____	_____	_____

## I. Summary:

This bill authorizes the Florida Surplus Lines Service Office (“Service Office”) to have access to records of surplus lines insurance agents related to the surplus lines insurance policies they write, as currently authorized for the Department of Insurance. The bill also requires surplus lines agents to report certain information on policies written to the Service Office, that in most respects codifies the current practice of the Service Office pursuant to operational procedures approved by the Department of Insurance. Similarly, the bill clarifies the responsibilities of the Service Office relative to those of the department with regard to monitoring the surplus lines business and collecting the 5 percent premium tax imposed on surplus lines policies and the 0.3 percent service fee that funds the operations of the Service Office. Current fines and penalties that apply to late payment of the premium tax would also apply to late payment of the service fee. The bill also deletes the requirement that insurers and adjusters notify the Service Office of each claim that is filed.

The bill increases maximum per-policy fee that may be charged by a surplus lines agent to a policyholder from \$25 to \$35.

The bill requires persons who independently obtain coverage from a surplus lines insurer (rather than through a surplus lines agent) to report and pay the 5 percent premium tax to the Service Office, rather than to the department, as currently required. The bill would also impose the 0.3 percent service fee on independently procured coverage, payable to the Service Office, which currently does not apply.

The bill provides that the Service Office, rather than a surplus lines agent, must request eligibility of a surplus lines insurer, as a condition of department approval of an eligible surplus lines insurer.

This bill substantially amends the following sections of the Florida Statutes: 626.916, 626.918, 626.921, 626.923, 626.930, 626.931, 626.932, 626.933, 626.935, 626.936, 626.9361, and 626.938.

## **II. Present Situation:**

### **Surplus Lines Insurance**

The Florida Insurance Code contains the Surplus Lines Law in ss. 626.913-626.937, F.S. The purpose of this law is to provide access to insurance coverage that cannot be obtained from insurers authorized to sell insurance in Florida. The law establishes requirements for approval of eligible surplus lines insurers and licensure of surplus lines agents by the Department of Insurance. One of the conditions for department approval of an eligible surplus lines insurer is that a licensed surplus lines agent makes a request for such approval. (s. 626.918, F.S.) The law also specifies the conditions that must be met before insurance coverage may be exported to an eligible surplus lines insurer, also referred to as a nonadmitted insurer. Surplus lines insurance is not subject to Florida regulation of rates or forms and there is no insurance guaranty fund protection if the insurer becomes insolvent.

### **Taxes and Fees for Surplus Lines Insurance**

A surplus lines agent is authorized to charge each policyholder a reasonable per-policy fee, not to exceed \$25 (in addition to the commission paid by the insurer). (s. 626.923, F.S.)

Surplus lines insurance policies are subject to a 5 percent premium tax paid by the policyholder. (s. 626.932, F.S.) In addition, surplus lines policies issued through surplus lines agents are subject to a service fee of 0.3 percent of premium to fund the operations of the Florida Surplus Lines Service Office, described below. (s. 626.9325, F.S.). Failure to pay the 5 percent premium tax is grounds for mandatory suspension or revocation of an agent's license. Late payment of the tax is subject to a 9 percent annual interest rate and a fine of up to \$50 per day. These penalties and fines do not apply to failure to pay, or late payment of, the 0.3 percent service fee.

### **The Florida Surplus Lines Service Office**

Legislation in 1997 created the Florida Surplus Lines Service Office, a nonprofit association to act as a "self-regulating organization" to permit better access by consumers to approved surplus lines insurers. (Ch. 97-196, L.O.F.; s. 626.921, F.S.) The Insurance Commissioner appoints a board to operate the association and the department must approve its plan of operation. All surplus lines agents are required to be members of the association, which employs a full-time staff and maintains its office in Tallahassee.

The Florida Surplus Lines Service Office is required to receive, record, and review all surplus lines insurance policies; maintain records of the reported policies; prepare monthly reports for the department; prepare and deliver to each surplus lines agent quarterly reports of the agent's business and collect and remit to the department the surplus lines tax; and report to the

department a reconciliation of the policies written in the surplus lines market, as reported by surplus lines insurers and surplus lines agents.

The 0.3 percent service fee on surplus lines policies generates about \$3 million annually, which funds the operations of the Service Office which has an annual budget of about \$2.8 billion.

#### **Filing Requirements for Surplus Lines Agents; Access to Records**

Surplus lines agents are required to report and file with the Florida Surplus Lines Service Office such information on each surplus lines insurance policy as required in the plan of operation. [s. 626.921(2), F.S.] The plan of operation specifies that information on policies shall be submitted in a format approved by the department. The Service Office developed the *Agents Procedures Manual*, which was adopted by order of the department, which requires agents to submit specific information to the Service Office within 21 days of the effective date of coverage on each policy, including the name and address of the insured and insurer, the type of coverage, amount of coverage, the premium, effective date, fees charged, deductibles, and other information.

Surplus lines agents are also required by statute to submit a quarterly report to the Service Office that includes aggregate gross and net premiums and a listing of all policies issued, including an affidavit as to efforts made to place coverages with authorized insurers. (s. 626.931, F.S.) In practice, however, the quarterly report of aggregate data is no longer required, because agents must report detailed information on each policy, as described above. But, the quarterly affidavit of efforts to place the coverage is still required.

If requested by the *department*, surplus lines agents are required to submit copies of policies, applications, certificates, confirmation of coverage, memoranda, and any changes or endorsements. (s. 626.923, F.S.) Similarly, surplus lines agents are required to maintain in their office for 5 years, open to examination by the *department*, each surplus lines contract, including applications and certificates, confirmation of coverage, memoranda, any substitutions or endorsements, the amount of the insurance and perils insured against, brief description and location of property insured, premium charged, return premium paid, effective date and terms of the contract, name and address of the insured and the insurer, amount collected from the insured, and other information as may be required by the department. (s. 626.930, F.S.) The department typically requests such information only if it is investigating an agent for a suspected violation, such as non-payment of the surplus lines tax, misappropriation of funds, or improper placement of business in the surplus lines market.

The current law does not expressly provide the Florida Surplus Lines Service Office with the same right of access to records that is provided to the department. But, the *Agents Procedure Manual*, adopted by the Service Office and by department order, requires that the surplus lines insurance agents' records specified above also be open to examination by the Service Office.

#### **Filing Requirements for Surplus Lines Insurers**

Each foreign insurer (formed under the laws of another state) is required to file a quarterly report with the Service Office of all surplus lines insurance transacted in Florida during the quarter. Similarly, each alien insurer (formed under the laws of another country) must file a report with the Service Office of all surplus lines insurance transacted, but reported annually, rather than quarterly. [s. 626.931(4) and (5), F.S.] The statute applies these reporting requirements to those

foreign and alien insurers accepting premiums “which are subject to taxes.” The 5 percent premium tax does not apply to coverage for specified risks such as vessels, cargo, aircraft, and governmental entities, as specified in s. 626.932(4), F.S. But, the quarterly and annual reports of foreign and alien insurers, includes all surplus lines business written and the Service Office determines which coverages are subject to the premium tax.

Surplus lines insurers and adjusters are currently required to notify the Service Office upon receipt of any claim notice reported under a surplus lines policy. The Service Office is required to determine whether the policy has been filed as required by this section. The Service Office states that this report is not providing any useful information that is not otherwise required to be reported to the Service Office by agents and insurers related to each surplus lines policy written.

### **Independently Procured Coverage**

*Independently procured coverage* is insurance coverage that an insured, typically a business, obtains by directly contacting a surplus lines insurer without using a surplus lines agent. The insured must file specific information about the policy with the Department of Insurance and must pay the 5 percent surplus lines premium tax to the department. Unlike coverage written through surplus lines agents, this report and tax is not submitted to the Service Office. The 0.3 percent service fee does not currently apply to independently procured coverage. (s. 626.938, F.S.)

## **III. Effect of Proposed Changes:**

**Section 1** amends s. 626.916, F.S., to increase the limit from \$25 to \$35 on the per-policy fee that a surplus lines agent may charge a policyholder for each surplus lines policy written.

**Section 2** amends s. 626.918, F.S., to provide that the Florida Surplus Lines Service Office, rather than a surplus lines agent, must request eligibility of a surplus lines insurer, as a condition of department approval of an eligible surplus lines insurer.

**Section 3** amends s. 626.921, F.S., to delete the requirement that insurers and adjusters notify the Service Office upon receipt of any claim notice reported under a surplus lines policy, and the requirement that the Service Office determine whether the policy has been filed as required by this section. The Service Office states that this report is not providing any useful information that is not otherwise required to be reported to the Service Office by agents and insurers related to each surplus lines policy written.

**Section 4** amends s. 626.923, F.S., to provide the same authority to the Florida Surplus Lines Service Office, as currently provided to the department, to require a surplus lines agent to submit, within 30 days of a request, copies of policies, applications, certificates, confirmation of coverage, memoranda, and any changes or endorsements.

**Section 5** amends s. 626.903, F.S., to provide the same authority to the Florida Surplus Lines Service Office, as currently provided to the department, to have access to examine, without notice, the surplus lines records that surplus lines agents are currently required to maintain for five years, including applications and certificates, confirmation of coverage, memoranda, any substitutions or endorsements, the amount of the insurance and perils insured against, brief

description and location of property insured, premium charged, return premium paid, effective date and terms of the contract, name and address of the insured and the insurer, amount collected from the insured, and other information as may be required by the department.

This change may be viewed as clarifying current law because even though the statute does not expressly authorize the Service Office to have access to an agent's records, the *Agents Procedure Manual* adopted by the Service Office and by department order, requires that such records of surplus lines agents be open to examination by both the department and the Service Office.

**Section 6** amends s. 626.931, F.S., to revise the reporting requirements for surplus lines insurance agents. The bill strikes the requirement that surplus lines agents submit quarterly reports containing aggregate data of surplus lines policies written during the quarter. In practice, this report is not currently required, since it has been replaced with the requirement in the *Agents Procedure Manual* that specific information on each surplus lines policy written be submitted to the Service Office within 21 days of the effective date. The bill retains the requirement that agents submit a quarterly affidavit as to efforts made to place coverages with authorized insurers and adds that the affidavit must state that the agent has submitted to the Service Office all surplus lines insurance transacted during the quarter as required.

With regard to the reporting requirements for surplus lines insurers, the bill deletes the reference to policies which are subject to taxes, since the reporting, in practice, includes all surplus lines insurance transacted in Florida, including risks exempt from the premium tax. The bill also specifies that the Service Office, rather than the department, prescribe the forms or computer format for each report. The bill authorizes the Service Office, in addition to the department, to require surplus lines insurers to submit any additional information.

**Section 7** amends s. 626.932, F.S., related to the surplus lines tax that must be collected and paid by surplus lines agents. The bill clarifies that the tax remitted by the agent to the Service Office must be "payable to the Department of Insurance." That is, a check must be payable to the department, which is the current practice that the Service Office instructs agents to follow, but if a check is made payable to the Service Office, it deposits and transfers the funds to the department.

**Section 8** amends s. 626.933, F.S., related to collection of the premium tax and service fee. The current law provides that if an agent does not pay the premium tax within the time prescribed, the department may file suit against the agent to recover the amount due. As amended this would also apply to the 0.3 percent service fee that agents must pay to fund the Service Office.

**Section 9** amends s. 626.935, F.S., related to suspension or revocation of a surplus lines agent's license by the department. The bill specifies that failure to pay the service fee (as current law provides for failure to pay the premium tax) is grounds for mandatory suspension or revocation of the license of a surplus lines agent and all other insurance licenses held by the agent. Similarly, the bill adds as a mandatory ground for suspension or revocation the failure of an agent to file the required affidavit, in addition to failure to file reports, when due as required by s. 626.931, F.S.

**Section 10** amends s. 626.936, F.S., related to failure of surplus lines agents to file reports or pay taxes or service fees. The current law provides for a fine of up to \$50 per day for each day a surplus lines agent fails to file a “quarterly” report within the time required, to be deposited into the Insurance Commissioner’s Regulatory Trust Fund. The bill provides that this fine applies to late filing of “a report or an affidavit” as required by the Florida Surplus Lines Law. This would capture all reporting requirements, including as those in the *Agent Procedure Manual*, adopted pursuant to s. 626.921, F.S., and the quarterly affidavit required by s. 626.931, F.S., as amended.

The bill applies the same penalty for failure of an agent to timely pay to the Service Office the 0.3 percent service fee, as current law applies to an agent who fails to timely pay the 5 percent premium tax. The penalty is a fine of up to \$50 per day for each day the payment is late, plus interest at the rate of 9 percent per year, deposited into the Insurance Commissioner’s Regulatory Trust Fund.

**Section 11** amends s. 626.9361, F.S., related to failure of eligible surplus lines insurers to file reports. The current penalty of a maximum \$500 per day fine for each day a required *quarterly report* is late, is revised to apply to each day a required *report* is late. This would clearly apply the fine to the annual report that alien insurers are required to file under s. 626.631(4), as amended, in addition to the quarterly report that foreign insurers are required to file under s. 626.631(3), as amended. The bill also strikes the reference to the reports being received *by the department* to conform to the requirement in s. 626.631, F.S. that the reports be submitted to the Service Office.

**Section 12** amends s. 626.938, F.S., related to reporting and taxation of *independently procured coverage*, which is coverage obtained by an insured directly from a surplus lines insurer without using a surplus lines agent. The bill provides that the required report of the transaction and the 5 percent surplus lines premium tax, which currently must be reported and paid by the insured to the Department of Insurance, would instead be reported and paid to the Service Office (payable to the department), as currently done by surplus lines agents. The bill also imposes the 0.3 percent service fee on independently procured coverage, which currently does not apply.

**Section 13** provides that the act shall take effect upon becoming a law.

#### IV. Constitutional Issues:

##### A. Municipality/County Mandates Restrictions:

None.

##### B. Public Records/Open Meetings Issues:

See, Related Issues, below.

##### C. Trust Funds Restrictions:

None.

**V. Economic Impact and Fiscal Note:****A. Tax/Fee Issues:**

Section 1 increases the maximum per-policy fee that may be charged by a surplus lines agent to a policyholder from \$25 to \$35.

Section 10 of the bill imposes the 0.3 percent of premium service fee on independently procured surplus lines coverage, which currently is not subject to this fee. The 0.3 percent service fee is paid to the Florida Surplus Lines Service Office. The Service Office estimates that the fee will add about \$240,000 in annual revenue to the current \$3 million annual revenue to fund the operations of the Service Office. The additional revenue will support the additional responsibilities of the Service Office to receive and record reports, taxes, and fees for independently procured coverage.

**B. Private Sector Impact:**

Surplus lines policyholders may be required to pay an additional \$10 policy fee (because the maximum fee is increased from \$25 to \$35). Surplus lines agents would receive this increased revenue, assuming the commission paid by the insurer is unchanged.

Insureds (typically, businesses) that independently procure surplus lines coverage will be subject to the 0.3 percent service fee that is paid to the Florida Surplus Lines Service Office.

Surplus lines insurers and adjusters would be relieved of the costs of notifying the Service Office of each claim that is filed and the Service Office would be relieved of the administrative duty of processing such notices.

**C. Government Sector Impact:**

None

**VI. Technical Deficiencies:**

None

**VII. Related Issues:**

The Banking and Insurance Committee has introduced Senate Bill 1026, a public records exemption bill, that reenacts and expands the current exemption that applies to certain surplus lines insurance records obtained by the department. The bill expands the exemption to apply to certain surplus lines insurance records obtained by the Florida Surplus Lines Service Office. That bill will need to be amended to conform to the provisions of this bill (if both are passed), in order to make the correct cites to the statutes that would authorize the Service Office to obtain records, which are revised by this bill. This bill, CS/SB 658, provides authority for the Service Office to obtain records in ss. 626.923, 626.930, and 626.931, F.S. However, Senate Bill 1026 refers only to the authority currently provided by s. 626.921.

**VIII. Amendments:**

None.

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This Senate staff analysis does not reflect the intent or official position of the bill's sponsor or the Florida Senate.

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