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Date Posted: July, 2011

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## **Surplus Lines Sea Change: Calif.'s AB 315 By Richard Brown | June 17, 2011**

California is expected to pass surplus lines regulations before July 21, 2011. On that date, the Nonadmitted and Reinsurance Reform Act of 2010 (NRRA) becomes effective, and only the “insured’s home state” may tax surplus lines premium and regulate surplus lines transactions.

Assembly Bill 315 (AB 315) is the California Department of Insurance’s legislative proposal to implement the NRRA. The bill already has cleared the Assembly, is under consideration by the Senate, and is supported by the California Insurance Wholesaler’s Association (CIWA), the National Association of Professional Surplus Lines Offices (NAPSLO), the American Association of Managing General Agents (AAMGA), IBA West, the SLA, and all presidential candidates. There is no opposition.

Expect it to be signed by Governor Brown before July 21, 2011.

### High Points

Transition Rule – Surplus lines policies issued or renewed prior to July 21, 2011, will be governed through expiration, including endorsements and cancellations, by the law in effect prior to July 21, 2011. The transition rule expires Oct. 18, 2012. §1774(3).

New York has adopted the same transition rule. There is a general industry expectation that the other states will follow suit in some fashion given the transition rule’s common-sense practicality.

Policies incepting on and after July 21, 2011, should be treated the same way for the same common-sense reasons: The Home State as of the policy effective date should remain the Home State through policy expiration

LES LI/LAS LI – All surplus line insurers listed on the LES LI (List of *Eligible* Surplus Line Insurers) are automatically grandfathered as of July 21, 2011, on LAS LI (List of *Approved* Surplus Line Insurers) through expiration of all policies in effect as of July 21, 2011. For more detailed information about surplus line insurer eligibility under AB 315, see “How the California Bill Implements Federal NRRA Surplus Lines Reform” ([http://www.insuregulatory.com/pdf/2011-03-21\\_WEST18-20.pdf](http://www.insuregulatory.com/pdf/2011-03-21_WEST18-20.pdf)).

Any insurer that appears on LAS LI or on the NAIC’s Quarterly List of Alien Insurers is eligible to accept surplus lines placements. If the nonadmitted insurer appears on neither list, there is another option under § 1765.1, but proceed with caution.

Diligent Search Exemption For “Commercial Purchaser” – AB 315 adopts the NRRA definition of Exempt Commercial Purchaser, which waives the diligent search requirement for large accounts as defined (§ 1760.1(b)), and incorporates the NRRA disclosure requirements (§1763(h)).



Home State Insured – Surplus line brokers are responsible for determining “whether an applicant for nonadmitted insurance is a California home state insured.” The surplus line broker may reasonably rely on information provided in good faith by the applicant. (§1760.2).

Recordkeeping — The surplus line broker must maintain records “for California home state insureds” that include defined documentation: *verification* that (a) the insured is a California home state insured, (b) the commercial insured or industrial insured meet the requisite statutory criteria, (c) the policy is a single-state or multistate policy, and (d) “where allocation of premium to the states is required, [collect and maintain] data as necessary to make that allocation.” (§1768).

The Commissioner may waive or modify the § 1768 requirements to accommodate the realities of transition to the NRRA Home State taxation and regulatory environment.

Premium Allocation Reporting – The annual statement of business transacted “shall include (A) the total amount of gross premium; (B) the total gross premium for *single state risks* where 100 percent of the premium is attributable to risks in California; and (C) for *multistate risks*, the percentage of gross premium allocated to California and *each other state*. §1774(a).

As with §1768, the Commissioner may waive or modify the §1774(a) data reporting requirements to accommodate the transition to NRRA Home State taxation and regulation.

GAP Exemption – The limited use of non-LES LI/LASLI nonadmitted insurers to round out gaps in coverage remains unaffected, slightly renumbered from § 1765.1(k) to § 1765.1(h).

SLIMPACT/NIMA – AB 315 leaves to the future whether California will participate in SLIMPACT (Surplus Lines Insurance Multistate Compact) or NIMA (Nonadmitted Insurance Multistate Agreement).

#### Uncharted Waters

The NRRA represents the first express federal intervention into state regulation and taxation of insurance since the passage of the McCarran-Ferguson Act in 1945.

Whether and to what extent the States comply with NRRA federal preemption involves unprecedented Constitutional and state law issues. These issues ultimately must be resolved (a) by the courts or (b), more likely, through cooperative discourse between industry and regulators.

The next year or so under the NRRA is a shakedown cruise for surplus lines brokers and regulators alike. Fair winds should prevail through a reasonable transition period. Keep foul weather gear handy for future premium audits.

#### NRRA Information

Extensive, current, and truly useful information about the NRRA, state implementing legislation, and NRRA compliance is available on the Web sites of the Insurance Journal, NAPSLO, CIWA, AAMGA, CIAB, and the major state stamping offices (e.g., California SLA, SLSOT, ELANY, FLSO), as well as InsuRegulatory.com. *Brown is an insurance regulatory attorney who regularly represents surplus lines insurers, surplus lines brokers, and industry organizations in a variety of regulatory and other surplus lines matters. He has authored multiple articles about the NRRA and its implementation and can be contacted at [RAB@InsuRegulatory.com](mailto:RAB@InsuRegulatory.com). Copies of his other NRRA articles are available at: [www.InsuRegulatory.com](http://www.InsuRegulatory.com).*