

MARKET BULLETIN

From	Director Worldwide Markets (extn 6677)
Date	12 October 2006
Reference	Y3889
Subject	US surplus lines: requirements for documents presented to Xchanging for signing
Subject areas	US surplus lines insurance
Attachments	None
Action points	Lloyd's brokers and managing agents to ensure compliance with the requirements set out in this bulletin
Deadlines	Immediate

1. Purpose of bulletin

To remind managing agents and Lloyd's brokers of the requirement for US surplus lines information to be shown on documents presented to Xchanging for stage one signing.

If these requirements are not met, the processing of premiums can be delayed. It is therefore important that underwriters, managing agent staff and Lloyd's brokers dealing with US surplus lines business familiarise themselves with these requirements and ensure that they are complied with.

2. Background

This bulletin follows the introduction of Lloyd's requirement that, from 1 August 2006, US documents presented to Xchanging for stage one signing in respect of US surplus lines business must include the **licence number of the surplus lines broker** handling the regulatory and fiscal filings associated with the premium.

It was already a requirement that such documents contain the **name and address of the surplus lines broker** and **the state(s) in which filing takes place**.

Lloyd's has instructed Xchanging to check relevant documents to ensure that these requirements are complied with and to take the action detailed in the event of non-compliance.

These requirements were the subject of market bulletins [Y3768.pdf](#) (issued 16 March 2006) and [Y3858.pdf](#) (issued 10 August 2006). The reasons why Lloyd's has made provision of this information mandatory are set out in appendix 1.

3. Action required

Lloyd's requirements for the documentation of US surplus lines business are set out below.

Open market risks

The slip must include the name, address and surplus lines licence number of the surplus lines broker handling the risk. This surplus lines broker will have filed details of the risk with a state insurance department or other authority. For most contracts it will also have arranged payment of the surplus lines tax.

Further details of the completion of the "fiscal and regulatory" section of the Market Reform Slip for US surplus lines business are set out in appendix 2.

Open market risks – multi-state placements

The slip must include a split of premium, showing the states in which filings have been made, the amounts of premium recorded in each filing and the name, address and surplus lines licence number of the broker making each filing.

If there is insufficient room on the slip for this information, it should be provided on a separate spreadsheet or bordereau. Any such attachment should make it clear who the broker is making each filing. The surplus lines licence number provided for a particular state should be the number of the licence held for that state. Some surplus lines brokers are licensed in more than one state, so it is important that the correct licence number is given.

Lloyd's is not seeking to second-guess decisions made about the filing of premiums. It simply wants the slip to record details of the filings that have actually been made. At the same time, if a slip records premium for a particular state, it will expect a filing to have been made in that state, and so details of the surplus lines broker concerned are to be provided. An exception to this is discussed in section 4 below.

Binding authorities

Bordereaux containing details of US surplus lines premiums must show the state of filing and the name, address and surplus lines licence number of the surplus lines broker making the filing for each premium.

The precise way in which this information is presented is up to the broker preparing the bordereau. It should be clear who has made the filings and where they have been made. If one surplus lines broker has made several filings those filings may be grouped under the details of the one broker.

4. Particular issues arising

Types of surplus lines brokers

Licensed surplus lines brokers (sometimes referred to as “surplus lines producers” or “surplus lines agents”) may be firms or individuals. Most states issue surplus lines licences to both, although some, such as Georgia, will only licence individuals.

When providing details of the surplus lines broker who has made a filing, it is important to establish who precisely made the filing, and whether it was done by a firm or by a licensed individual employed by the firm.

Social security numbers (SSN) or FEIN numbers used as licence numbers

In some states either the SSN or FEIN number of the surplus lines broker or surplus lines agency is used as the surplus lines licence number.

For such brokers, rather than provide the full SSN or FEIN number, the slip (or other documentation) should state the initials “SSN” or “FEIN” rather than the licence number. Lloyd’s is aware that this is the case in the following states:

- a) North Carolina
- b) South Carolina
- c) North Dakota
- d) Virginia

Surplus lines brokers’ addresses

It is desirable that the fullest details of a surplus lines broker are given, to enable a correct identification to be made. However, to avoid the need for a Lloyd’s broker to enter full addresses several times, Lloyd’s has instructed Xchanging not to query slips that show just the state in which a surplus lines broker is situated, without giving the full address. This is intended particularly for documentation which gives details of several surplus lines brokers, such as binding authority bordereaux and multi-state placements.

Multi-state placements – “insured’s responsibility” and “no filing due”.

Lloyd’s brokers have represented to Lloyd’s that on multi-state placements, some US states permit the insured to take responsibility for filing and the payment of taxes or do not require filing and payment of tax if the amount of premium allocated to a state is de minimis or reflects incidental exposure. Lloyd’s has therefore agreed that, to facilitate processing, the information presented with a slip can show “insured’s responsibility” or, as the case may be “no filing due” against the relevant premium amounts from individual states.

Xchanging will query the use of these explanations if they are clearly wrong – for example if they are used on a single state placement. Otherwise they will accept in good faith the information presented to them by the Lloyd's broker. It is therefore important that these categorisations are used correctly and only in compliance with local laws.

Compliance with local state laws may mean that Lloyd's has to report the premiums concerned to the appropriate state authorities, with explanations that the insured was responsible for paying the tax or that it has not been paid as no filing was due. The state authorities may query these explanations and, if this placement is not compliant, the underwriter(s) of the business will be held responsible for the consequences of the breach.

"Insured's responsibility" and "No filing due" are the only terms that should be used to describe premiums where no surplus lines broker has made a filing. Other comments such as "silent state" or "IP" may be queried by Xchanging.

5. Lloyd's instructions to Xchanging

A slip presented to Xchanging for signing that does not include the name, address (other than as described above) and licence number of the surplus lines broker will be queried by Xchanging, so the premium will not be processed until this information is provided.

Xchanging has a database of US surplus lines brokers, populated by Lloyd's from information provided by state insurance departments and by Lloyd's brokers. If the name, address and licence number of the surplus lines broker on the slip does not match any details on Xchanging's database, Xchanging will ask the Lloyd's broker to check the details and to confirm in writing that they are correct. Lloyd's has provided Xchanging with a list of entities and organisations which are not surplus lines brokers, and for which Xchanging cannot accept a Lloyd's broker's confirmation that the details are correct.

For the time being, processing of the premium is not held up by a query when details are provided, but cannot be matched. This puts the onus on the Lloyd's broker to come back to Xchanging with the requested details in a reasonable period. This approach will be reconsidered – possibly on a firm-by-firm basis - if it appears that Lloyd's brokers are not making reasonable efforts to provide timely confirmation to Xchanging.

Lloyd's brokers sometimes respond to a request from Xchanging for confirmation that a broker is a properly-licensed surplus lines broker by providing a copy of the relevant surplus lines licence. This is helpful, definitive confirmation but it is important to ensure that the document provided is a surplus lines licence and not any other intermediary licence that the broker may hold. Lloyd's has not instructed Xchanging to require copies of surplus lines licences, as it is appreciated that obtaining them can be time consuming. However, if a query arises on details provided, Xchanging or Lloyd's may agree with the Lloyd's broker that the query can best be resolved by provision of a copy of a licence.

6. Further information

If you have any queries about this market bulletin, please contact Lloyd's Worldwide Market Services:

Lloyd's Worldwide Market Services
Tel: 020 7327 6677
Email: market.services@lloyds.com
Box 190b, Gallery 1

This market bulletin has been sent to active underwriters and to the compliance officers of managing agents and Lloyd's brokers.

Julian James
Director,
Worldwide Markets

Lloyd's and US surplus lines regulation

The reasons why it requires details of surplus lines brokers and filings

Summary

Lloyd's requires details of surplus lines brokers and filings because:

1. Lloyd's syndicates, as eligible surplus lines insurers, are responsible for ensuring that every surplus lines transaction is placed via a licensed surplus lines broker.
2. Lloyd's submits financial filings to US state insurance departments, as state insurance laws require surplus lines insurers to do. In many states these include transactional reports, listing surplus lines transactions from the state by the surplus lines broker who handled them.

Details of these requirements and of surplus lines insurance regulation are set out below.

Basic requirements

Insurance in the US is regulated by state, meaning that each state (and most US territories) has its own legislative body, insurance department responsible for regulating insurance business in the state (usually headed by a commissioner, a superintendent or a director) and a set of insurance laws and regulations.

US surplus lines insurance is coverage that is not available from a licensed (or admitted) insurer and that can therefore be placed with an eligible non-admitted insurer in compliance with state surplus lines laws. All surplus lines contracts must be placed via a surplus lines broker licensed in the state whose laws govern placement of the risk. If a contract covers insureds located in several different states, the placement should involve a surplus lines broker licensed in each of the states where an insured is located.

Surplus lines brokers are regulated by the states for which they hold a licence. A surplus lines broker must ensure that a risk is placed in accordance with state surplus lines laws. It must file details of the risk with the local state insurance department and collect and pay the surplus lines taxes due on the premium.

A contract must be eligible for export to the surplus lines market under the surplus lines laws of the state governing the transaction. The rules governing export to the surplus lines market vary from state to state. States may prohibit the export of particular lines of business and may also have "export lists" of lines of business that are automatically exportable without evidence of diligent effort to place the risk in the admitted market. In most states, a surplus lines broker must offer a risk that is eligible for export to licensed insurers authorised to write that type of risk. Only if a defined number of authorised insurers (often three or five) decline the risk can it be placed with a surplus lines (or non-admitted) insurer.

The surplus lines (or non-admitted) insurer with whom the business is placed must meet the criteria of “eligibility”. Most Lloyd’s syndicates are eligible to transact surplus lines insurance in all US states and territories other than Kentucky and the US Virgin Islands¹.

Lloyd’s publishes [a list of syndicates.pdf](#) who appear on the National Association of Insurance Commissioner’s quarterly listing of alien insurers, and who are therefore eligible to write surplus lines insurance.

Requirement for a surplus lines broker in every surplus lines placement

Acceptance of a surplus lines placement is unlawful if the risk has not been exported by a surplus lines broker licensed in the state from which the placement originates. **Lloyd’s underwriters are responsible for ensuring that every US surplus lines risk that they write is placed via a broker who possesses a current surplus lines licence for the relevant US state.** This responsibility exists whether the risk is written via a binding authority, another form of delegated underwriting or on an open market basis.

If Lloyd’s syndicates write business in breach of this responsibility they run the risk of incurring fines or other penalties and also of damaging the name and trading position of Lloyd’s in the US.

This responsibility means that underwriters and their managing agents require information about the surplus lines broker for every surplus lines contract that they enter into. Lloyd’s instructions that surplus lines slips contain the name, address and licence number of the surplus lines broker help ensure that underwriters have the information necessary to comply with this requirement.

Although the way that business is processed at Lloyd’s and in the London market means that information has to be provided by the Lloyd’s broker, ultimate responsibility for complying with the requirement that surplus lines risks be handled by surplus lines brokers rests with the insurer/underwriter and cannot be delegated to a Lloyd’s broker, a coverholder or any other entity in the distribution chain.

Lloyd’s surplus lines transactional reporting

The insurance laws of most states require Lloyd’s, as an eligible alien surplus lines insurer, to file financial reports with the state insurance department on an annual or quarterly basis. Detailed reporting requirements vary from state to state. In several states these financial reports include transactional reports, detailing, among other items, premium written by licence number, name and address of the surplus lines broker. Again, the precise format of the transactional report is different in different states.

¹ In Kentucky and the US Virgin Islands Lloyd’s underwriters can transact insurance in accordance with Lloyd’s licences. Lloyd’s has a “dual status” in Illinois, meaning that it can transact insurance on a licensed basis and, provided applicable legal requirements are met, on a surplus lines basis.

These reports are filed as part of a surplus lines insurer's continued eligibility to do business in a particular state. They can be used by a state to verify the amount of surplus lines taxes receivable from their surplus lines brokers.

Lloyd's complies with these reporting requirements centrally, on behalf of all syndicates doing business in a particular US state or territory, thereby relieving individual managing agents of what could be an onerous reporting burden. When Lloyd's is preparing transactional reports it relies on transactional data provided by Xchanging, of transactions processed through central accounting in a particular calendar period.

Lloyd's surplus lines reporting has been deficient, as the transactional reports it had filed have not included all the data required by states. In part, this is because the states require data that is not easily available, such as the names and addresses of individual insureds. However, a major issue has been the poor quality of information held centrally about the surplus lines brokers who have handled business, reflecting deficiencies in information provided on slips and other documents presented to Xchanging.

Until recently Lloyd's instructed Xchanging to accept the details of surplus lines brokers provided by Lloyd's brokers as they were presented. In some cases these details were inaccurate: the information provided to Lloyd's for reporting to state insurance departments was therefore not correct.

In recent years, individual states have raised issues of reporting accuracy with Lloyd's on several occasions. Lloyd's has, in response, agreed to improve its reporting systems and has made some incremental changes. As the pressure from states has increased, it is now moving to deal with the fundamental issue of accuracy of surplus line broker details. Its objective is to be in a position to report all Lloyd's surplus lines premiums by the surplus lines broker who has filed details of the transaction and arranged payment of the surplus lines tax.

Definition of "United States of America"

The United States of America (US) includes the 50 US states and the following dependent territories: American Samoa, Guam, Northern Mariana Islands, Puerto Rico, the US Virgin Islands, Midway Islands, Wake Island, Johnston Atoll, Baker, Howland & Jarvis Islands, Kingman Reef, Navassa Island and Palmyra Atoll.

This list of territories include places from which a surplus lines risk is unlikely to originate, but it is important to note that insurance risks coming from places such as Puerto Rico should be treated in the same way as risks from US states.

Completion of Market Reform Slips for US surplus lines business

For US surplus lines open market placements, the **Fiscal & Regulatory section** of the slip must include the following information:

Slip heading	Notes
TAX PAYABLE BY UNDERWRITER(S)	<i>“Not applicable”</i>
COUNTRY OF ORIGIN	<i>“The US”</i> (or equivalent wording)
OVERSEAS BROKER	<p>If no broker is involved in the placement other than the surplus lines broker (and the Lloyd’s broker) this should be completed <i>“Not applicable”</i> or <i>“See below”</i>.</p> <p>If the placement involved another broker who is next to the Lloyd’s broker in the placing chain, its name and address should be put in this section.</p>
SURPLUS LINES BROKER	<p>The name, address and licence number of the US surplus lines broker involved in the placing of this risk.</p> <p>If taxes and filings are due in more than one state/territory, details must be provided of all the surplus lines brokers who paid taxes and made filings. The licence number provided must be the surplus lines licence number for the state in which the filing was made.</p> <p>For New Jersey surplus lines risks, this section must contain the transaction number.</p>
STATE OF FILING	<p>The US state or territory in which taxes are due and a filing has been made, or will be made, by the surplus lines broker(s) mentioned in the above heading.</p> <p>If taxes and filings are due in more than one state/territory, each state/territory must be given, specifying the amount of premium filed in each state. It must be clear from this and the preceding heading precisely which surplus lines broker has paid taxes/ filed in which state. If appropriate this information may be provided on an attachment such as a spreadsheet.</p>
LICENCE INFORMATION	<i>“The US”</i> or equivalent wording

US CLASSIFICATION	<i>"US surplus lines"</i>
NAIC CODES	<i>"Not applicable"</i>
ALLOCATION OF PREMIUM TO CODING	The Lloyd's risk code allocated and the split of premium for signing purposes.
ALLOCATION OF PREMIUM TO YEAR OF ACCOUNT	Only required where the policy period exceeds 18 months.
FSA CLIENT CLASSIFICATION	Complete in accordance with instructions provided by the Market Reform Group in the document entitled "The Market Reform Slip" dated June 2006.
IS THE BUSINESS SUBJECT TO THE DISTANCE MARKETING DIRECTIVE?	Complete in accordance with instructions provided by the Market Reform Group in the document entitled "The Market Reform Slip" dated June 2006.