

MARKET BULLETIN

REF: Y4500

Title	NRRA – U.S. Surplus/Excess Lines – Lloyd's market's transitional arrangements in response to Subtitle B, Title V of the Dodd-Frank Act, regarding state-based insurance reform, entitled the "Nonadmitted and Reinsurance Reform Act" (NRRA).
Purpose	This bulletin addresses the NRRA and considers specifically its provisions regarding surplus lines insurance, its implementation to date at state level and how this and remaining uncertainty impacts the Lloyd's Market.
Type	Annual
From	Rosemary Beaver, Head of International Regulatory Affairs
Date	23 June 2011
Deadline	Ongoing with effect from 21 July 2011
Related links	

Introduction

This bulletin is addressed to all Lloyd's market stakeholders dealing with the placement, underwriting, settlement and regulatory reporting of Lloyd's U.S. surplus lines business.

It sets out how the implementation of Subtitle B, Title V of the Dodd-Frank Act, regarding state-based insurance reform, entitled the "Nonadmitted and Reinsurance Reform Act" (NRRA) will impact the Lloyd's market. Exact details of requirements in the US are still developing and therefore the guidance in this bulletin is subject to future change.

This bulletin sets out:

- The key changes introduced under the NRRA and how they will impact the Lloyd's market.
- The actions to be taken by Lloyd's market stakeholders to ensure compliance.
- How we will engage with the market and keep stakeholders informed.
- The definitions in the NRRA of "Home State" and Exempt Commercial Purchaser (ECP) (See Appendix A).
- The impact on Lloyd's admitted business in Illinois, Kentucky and the USVI (See Appendix B).

Background

The NRRRA, which was signed into law on 21 July 2010, empowers U.S. states to create an equitable uniform method, by interstate compact or other procedure, to allocate and share taxes on multistate surplus lines risks. Its purpose is to simplify a multistate surplus lines transaction by imposing a single “Home State” jurisdiction in connection with surplus lines broker licensing, surplus lines tax payments and compliance filings. Lloyd’s supports the intent of the NRRRA provisions and has closely monitored its progress since enactment.

This is a new federal law which requires most states to change their laws for compliance purposes. A number of U.S. states are in the process of introducing legislation to enable them to respond to the NRRRA requirements outlined below by the 21 July 2011 deadline. At the time of issuing this bulletin, more than half of the states had passed legislation to this effect. As a result considerable uncertainty remains as to how states will resolve issues around the collection and potential reallocation of surplus lines tax and the need to continue state level insurer eligibility filings.

Lloyd’s objective is to ensure the market’s surplus lines eligibility is protected. Set out below are the key changes, how they impact Lloyd’s and the actions which brokers and underwriters need to take to ensure compliance with the new requirements.

Key Changes and Lloyd’s Proposed Approach

1. **The key changes introduced under the NRRRA and how they will impact the Lloyd’s market.**
 - i) **“Home State” jurisdiction** – The NRRRA provides the insured’s “Home State” with exclusive authority to regulate placement of surplus lines insurance. No state, other than an insured’s “Home State” (as defined in Appendix A), may require a surplus lines broker to be licensed in order to sell, solicit, or negotiate nonadmitted insurance with respect to such insured. The NRRRA explicitly provides for the preemption of laws, regulations, provisions, or actions of any state that applies to surplus lines insurance sold, solicited by, or negotiated with an insured whose “Home State” is another state.¹
 - **Lloyd’s position:** New or renewal multi state placements with an effective date (policy inception) on or after 21 July, 2011 will no longer require multiple surplus lines filings to be completed. Lloyd’s will collect information on the relevant “Home State” for each surplus lines transaction via an amendment to the Market Reform Contract (MRC) which will include a revised definition of “State of Filing” referring to “Home State”.
 - ii) **Exempt Commercial Purchasers (“ECP”)** – The NRRRA will also preempt any state laws or regulations requiring a surplus lines broker to satisfy surplus lines diligent search requirements to place surplus lines insurance for certain ECP.² In addition, other state exemptions may still be available.

¹ This pre-emption does not extend to excess insurance for self-funded workers’ compensation plans with a surplus lines insurer.

² See Appendix A.

- **Lloyd's position:** Changes to the slip (MRC) guidance will be progressed to include the necessary definition of this business within the U.S. surplus lines classification and Lloyd's will incorporate in changes to its surplus lines data processing.
- iii) **Surplus lines tax collection and allocation** – Under the NRRRA, only the insured's "Home State" will be permitted to collect premium taxes for surplus lines insurance. All other states are pre-empted from applying their surplus lines laws to such transactions.
- **Lloyd's position:** Currently, Lloyd's is required to complete surplus lines transactional filings (detailing the surplus lines broker and premium allocation across different states on a multistate surplus lines risk) in twenty-two states. To comply with the NRRRA, Lloyd's will collect information based on the "Home State" definition only and continue to monitor further guidance issued by individual states on an insurer's reporting requirements.
- iv) **NAIC Quarterly Listing of Alien Insurers ("White List")** – The NRRRA also provides that states cannot prohibit a surplus lines broker from placing business with a surplus lines insurer that is listed on the Quarterly Listing of Alien Insurers maintained by the International Insurers Department (IID) of the NAIC.
- **Lloyd's position:** Currently, Lloyd's is required to complete state level eligibility filings on behalf of the Lloyd's market with 35 U.S. states. As a result of the NRRRA, Lloyd's expects a single annual filing process for maintaining surplus lines eligibility. As of yet, the IID and state regulators have not issued any specific guidance regarding this change.
- v) **Any other changes**
- A revised definition of "State of Filing" will also be incorporated into the Lloyd's premium standard bordereaux to reflect the use of "Home State".
 - The market QA tool will also be updated to include the revised definition of "State of Filing".
 - All of the changes detailed above, and any subsequent changes at state level impacting the Lloyd's market, will be included on Lloyd's Crystal and, where required, a regulatory alert issued drawing attention to these changes.

2. Actions to be taken by Lloyd's market stakeholders.

Effective date of the legislation – The NRRRA requirements are effective from 21 July 2011. At this date the changes outlined above will apply to new and renewing policies with an effective date on or after 21 July 2011. These changes apply regardless of whether or not an individual state has enacted changes to its laws to bring them into conformance with the NRRRA.

In-force policies - In the absence of clear regulatory guidance concerning policies in-force prior to this date, any additional premiums, return premiums or endorsements, cancellations, and non-renewals will be subject to the laws and regulations of the state(s) where the surplus lines broker will have filed details of the risk at the time of placement.

The MRC guidance and premium standard bordereaux will be revised to recognise the “Home State” definition. Subject to agreement by all market associations, these changes should be defined by the end of August 2011 with a four month period for the amendment of slip templates to reflect the revised MRC guidance. In the intervening period, new and renewal surplus lines policies, with an effective date on or after 21 July, 2011, should show the “Home State” under the MRC “State of Filing”.

Lloyd’s anticipates that the capture of “Home State” data will transition through Q3 and Q4 2011, as pre-21 July, 2011 surplus lines placements work their way through the placement chain and brokers transition to submitting contract information on this basis. Lloyd’s recognises that the full year 2011 surplus lines transactional data will, inevitably, comprise data on a pre and post NRRRA basis.

- i) **Lloyd’s Underwriters** - should continue to ensure that surplus lines business is placed via a licensed surplus lines broker. The MRC should still include the details of the surplus lines broker³ and the “State of Filing”⁴ (see above), but in summary, for risks effective after 21 July 2011, this will be the “Home State”. Underwriters are advised to check, where new or renewal placements rely upon exemptions to the surplus lines laws, that these still apply (see “3. Keeping the market informed” below) in the relevant states.
- ii) **Lloyd’s Brokers** - Lloyd’s brokers should note that new or renewal multi state placements with an effective date on or after 21 July, 2011 will no longer require multiple surplus lines filings to be completed and then recorded for surplus lines business processing and reporting purposes). The “Home State” only should be included under “State of Filing” for MRC purposes.
- iii) **Lloyd’s Coverholders** - Lloyd’s coverholders should continue to ensure that premium bordereaux show the “State of Filing” and the name, address and surplus lines number of the surplus lines broker making the filing for each premium. New and renewal surplus lines policies declared under a binding authority, with an effective date on or after 21 July, 2011, should show the “Home State” under the “State of Filing”.
- iv) **Lloyd’s instructions to Xchanging** – Lloyd’s currently requires that documents presented to Xchanging for stage one signing in respect of U.S. surplus lines business must include the name, address and surplus lines licence number of the surplus lines broker handling the risk⁵ and the MRC must also show the “State of Filing”. For surplus lines policies which have an effective date on or after 21 July 2011 the MRC must instead show the “Home State”. In accordance with current instructions from Lloyd’s to Xchanging, a MRC

³ The MRC mandates the capture of the surplus lines broker name, address and license number.

⁴ The surplus lines broker will have filed details of the risk with a state insurance department or other authority

⁵ For further details see Lloyd’s Market Bulletin Y3889, dated 12 October 2006

presented to Xchanging that does not contain this information will not be processed until this information is provided.

3. Keeping the market informed

Lloyd's has closely monitored the progress of the NRRRA since its enactment. Lloyd's has issued updates to the market on current issues via market briefings and letters, keeping underwriters, brokers and market trade associations informed of developments.

State laws and regulations are still developing in a number of areas in response to the NRRRA requirements. Therefore, information in this market bulletin is likely to change. As updated information becomes available, Lloyd's will keep the market informed, issue further guidance as appropriate, and post relevant material on Crystal.

Lloyd's is closely monitoring state insurance laws with respect to the following: a.) implications of the NRRRA's and individual states' "Home State" definitions, b.) changes in state tax laws on surplus lines tax and direct procurement tax, c.) changes to, or possible effects upon, Group Schemes (see Appendix A), Industrial Insureds Exemptions, and MAT Exemptions. A market working group will be formed to ensure consultation on the surplus lines business placement, data capture and processing issues raised by the NRRRA as these issues develop through 2011 and beyond.

Further Contacts

Lloyds.com is a central point of reference for communications and guidance concerning Lloyd's and the NRRRA (there is a dedicated section covering "NRRRA – U.S surplus lines reform" under "Regulatory Projects". Further information can be found under the US section of Crystal. Managing agents who are unable to access the dedicated area of the Lloyds.com website should contact Lloyd's International Trading Advice (see contact details below):

Lloyd's International Trading Advice:
Tel: 020 7327 6677 or Email: lita@lloyds.com

For questions regarding Lloyd's US surplus lines eligibility, please contact:

Steve Yates, Manager, Lloyd's International Regulatory Affairs, Lloyd's
+44 20 7327 5351 or Email stephen.yates@lloyds.com , or:

Ameesh Shah, Executive, Lloyd's International Regulatory Affairs, Lloyd's
+44 20 7327 6051 or Email ameesh.shah@lloyds.com .

Appendix A**NRRA Definition of “Home State”****SEC. 521. REPORTING, PAYMENT, AND ALLOCATION OF PREMIUM TAXES.**

(a) HOME STATE’S EXCLUSIVE AUTHORITY.—No State other than the home State of an insured may require any premium tax payment for nonadmitted insurance.

SEC. 522. REGULATION OF NONADMITTED INSURANCE BY INSURED’S HOME STATE.

(a) HOME STATE AUTHORITY.—Except as otherwise provided in this section, the placement of nonadmitted insurance shall be subject to the statutory and regulatory requirements solely of the insured’s home State.

SEC. 527. DEFINITIONS.

(6) HOME STATE.—

(A) IN GENERAL.—Except as provided in subparagraph (B), the term “Home State” means, with respect to an insured—

(i) the State in which an insured maintains its principal place of business or, in the case of an individual, the individual’s principal residence; or

(ii) if 100 percent of the insured risk is located out of the State referred to in clause (i), the State to which the greatest percentage of the insured’s taxable premium

for that insurance contract is allocated.

(B) AFFILIATED GROUPS.—If more than 1 insured from an affiliated group are named insureds on a single nonadmitted insurance contract, the term “home State” means the home State, as determined pursuant to subparagraph (A), of the member of the affiliated group that has the largest percentage of premium attributed to it under such insurance contract.

Note on Group Schemes:

With respect to Group Schemes, the NRRA and state definitions of “Home State” will affect the recording of surplus lines premium tax. We understand that the NAIC and possibly the state departments of insurance are considering publishing guidance on “Home State” with respect to Group Schemes. Lloyd’s is monitoring promulgated state legislation and information concerning any changes to Lloyd’s current group schemes procedures will be presented in separate communications.

NRRA Definition of “Exempt Commercial Purchaser”

SEC. 525. STREAMLINED APPLICATION FOR COMMERCIAL PURCHASERS.

A surplus lines broker seeking to procure or place nonadmitted insurance in a State for an exempt commercial purchaser shall not be required to satisfy any State requirement to make a due diligence search to determine whether the full amount or type of insurance sought by such exempt commercial purchaser can be obtained from admitted insurers if—

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

(2) the exempt commercial purchaser has subsequently requested in writing the broker to procure or place such insurance from a nonadmitted insurer.

Sec. 527. DEFINITIONS.

(5) EXEMPT COMMERCIAL PURCHASER.

The term “exempt commercial purchaser” means any person purchasing commercial insurance that, at the time of placement, meets the following requirements:

(A) The person employs or retains a qualified risk manager to negotiate insurance coverage.

(B) The person has paid aggregate nationwide commercial property and casualty insurance premiums in excess of \$100,000 in the immediately preceding 12 months.

(C) (i) The person meets at least 1 of the following criteria:

(I) The person possesses a net worth in excess of \$20,000,000, as such amount is adjusted pursuant to clause (ii).

(II) The person generates annual revenues in excess of \$50,000,000, as such amount is adjusted pursuant to clause (ii).

(III) The person employs more than 500 full-time or full-time equivalent employees per individual insured or is a member of an affiliated group employing more than 1,000 employees in the aggregate.

(IV) The person is a not-for-profit organization or public entity generating annual budgeted expenditures of at least \$30,000,000, as such amount is adjusted pursuant to clause (ii).

(V) The person is a municipality with a population in excess of 50,000 persons.

(ii) Effective on the fifth January 1 occurring after the date of the enactment of this subtitle and each fifth January 1 occurring thereafter, the amounts in subclauses (I), (II), and (IV) of clause (i) shall be adjusted to reflect the percentage change for such 5-year period in the Consumer Price Index for All Urban Consumers published by the Bureau of Labor Statistics of the Department of Labor.

Appendix B

How these changes will impact Lloyd's admitted business in Illinois, Kentucky and the USVI.

Lloyd's is an eligible surplus lines insurer in all U.S. states with the exception of Kentucky and the USVI. Lloyd's is an admitted insurer in the states of Illinois⁶, Kentucky and in the USVI. The provisions of the NRRRA do not directly impact the admitted insurance market and Lloyd's will continue to accept admitted business from these states on the current basis. However, where this premium forms part of a multistate placement, and as is currently the case, the admitted Illinois, Kentucky or USVI portions of the total premium must be displayed on the schedule page of the contract, when premium is allocated on multistate risks. In addition, the admitted premium must be reported to Lloyd's attorney-in-fact for the particular jurisdiction so that the admitted tax(es) can be properly determined, collected, and paid.

The non-admitted (surplus lines) portions of these placements are subject to the guidance under "**2. Actions to be taken by Lloyd's market stakeholders.**" detailed in this market bulletin.

⁶ Underwriters at Lloyd's, Illinois is able to accept business on admitted basis in Illinois, or where the risk cannot be placed on this basis, export the risk on a surplus lines basis to Lloyd's.