Ohio Legislative Service Commission

Bill Analysis

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S.B. 102

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(As Introduced)

Sen. Bacon

BILL SUMMARY

- Conforms Ohio's law regulating surplus lines products with the federal Nonadmitted and Reinsurance Reform Act.
- Specifies that Ohio's law regarding unauthorized insurance and surplus lines brokers applies only when Ohio is the home state of the insured.
- Allows the Superintendent of Insurance to enter into a multi-state agreement or compact concerning unauthorized insurance.
- Makes changes to the surplus lines broker, individual procurement, and unauthorized insurer taxes while maintaining current law's 5% tax on gross premiums.
- Allows the Superintendent to waive the tax late penalty in certain situations.
- Exempts from the tax requirements insureds that are otherwise exempt from the payment of premium or franchise taxes under state or federal law and political subdivisions.
- Revises the surplus lines broker record filing requirements.
- Allows only licensed property and casualty insurance agents to perform due diligence requirements.
- Exempts insurance agents and surplus lines brokers from due diligence requirements for an exempt commercial purchaser.
- Removes from service of process requirements for unauthorized insurance transactions an exemption for contracts of insurance issued to an employer insured.

- Makes other conforming and clarifying changes.

CONTENT AND OPERATION

Application of the law

The bill conforms Ohio's law regulating surplus lines products with federal law. The federal Nonadmitted and Reinsurance Reform Act[1] (federal Act) was enacted July 21, 2010, as part of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010. Under the federal Act, states are prohibited from regulating, requiring a premium tax for, or requiring a surplus lines broker to be licensed in order to sell, unauthorized insurance when that state is not the insured's home state.[2] "Unauthorized insurance" (also called "nonadmitted insurance" and "surplus lines insurance") is insurance sold by an insurer that is not licensed to do business in the state. A "surplus lines broker" is a person who negotiates for and obtains insurance, other than life insurance, on property or persons in the state from unauthorized insurers.

The bill conforms Ohio's law to this prohibition by specifying that Ohio's law regarding unauthorized insurance and surplus lines brokers applies only when Ohio is the home state of the insured. The bill also separately specifies that current law's surplus lines broker licensure requirement does not apply to any selling, soliciting, or negotiating of unauthorized insurance that takes place in an insured's home state if the home state of the insured is not Ohio.[3]

Home state

Under both the bill and federal Act, the home state of the insured is the state in which an insured maintains its principal place of business or, in the case of an individual, the individual's principal residence. However, if 100% of the insured risk is located out of the state in which an insured maintains its principal place of business or principal residence, the home state of the insured is the state to which the greatest percentage of the insured's taxable premium for that insurance contract is allocated. If more than one insured from an affiliated group are named insureds on a single unauthorized insurance contract, the home state of the insured is the state in which the member of the affiliated group that has the largest percentage of premium attributed to it under such insurance contract. An insured's principal place of business is the state

[1] 15 U.S.C. 8201 *et seq*.

[2] 15 U.S.C. 8201 *et seq*.

[3] R.C. 3905.31 and 3905.38.

where the insured maintains the insured's headquarters and where the insured's high-level officers direct, control, and coordinate the business activities of the insured.[4]

Multi-state compact for the allocation of premium taxes

The federal Act allows states to enter into a multi-state compact to allocate premium taxes paid for unauthorized insurance. If a state does not adopt the multi-state compact prior to 330 days after the effective date of the act (June 16, 2011), the premium tax allocation under the multi-state contract will not be effective for that state until January 1, 2012.[5]

The bill complies with the federal Act by allowing the Superintendent of Insurance to enter into a multi-state agreement or compact for determining eligibility for placement of unauthorized insurance and for payment, reporting, collection, and allocation of the tax on unauthorized insurance. The multi-state agreement or compact also may include eligibility for placement of unauthorized insurance and payment, reporting, collection, and allocation of the tax on unauthorized insurance for risks that are not multi-state, and for independently procured insurance in the unauthorized market.[6]

Taxes

Surplus lines brokers tax

Continuing law requires licensed surplus lines brokers to pay a 5% tax on gross premiums paid for unauthorized insurance after a deduction for return premiums. Under current law, the form used for calculating the tax is prescribed by the Treasurer of State.[7]

The bill removes the specification that the Treasurer of State prescribes the form for calculating that tax. Under the bill, persons must use the prescribed format to calculate the tax or calculate the tax in compliance with any requirements of the multi-state agreement or compact that the Superintendent enters into under the bill. The bill does not specify who prescribes the form.[8]

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[4] R.C. 3905.30(A) and 15 U.S.C. 8206(6).

[5] 15 U.S.C. 8201.

[6] R.C. 3905.33(E).

[7] R.C. 3905.36(C).

[8] R.C. 3905.36(C).

Independent procurement tax

Continuing law also requires persons that independently procure unauthorized insurance (also called direct placement) to pay a 5% tax on gross premiums paid for unauthorized insurance after a deduction for return premiums. The bill removes the tax for items other than the gross premium, including membership fees, assessments, dues, and other consideration charges collected. The bill also changes the way the tax is calculated, requiring persons to use the prescribed format to calculate the tax or to calculate the tax in compliance with any requirements of the multi-state agreement or compact entered into by the Superintendent under the bill. The bill does not specify a form. Under current law, the form used for calculating the tax is prescribed by the Treasurer of State.

Persons that independently procure unauthorized insurance must file transaction details, but the bill does not prescribe who the person must file those details with or further specify what the filing must include. This replaces the current law requirement under which a person who is filing the independent procurement tax also must file with the Superintendent a statement under oath showing the name and address of the insured, name and address of the insurer, subject of the insurance, general description of the coverage, and amount of gross premium, fee, assessment, dues, or other consideration for the insurance for the preceding calendar year.[9]

The bill allows insurers to submit the required transaction details and remit the tax payment on behalf of an insured.[10]

Unauthorized insurer tax

Continuing law requires unauthorized insurers to pay a 5% tax on gross premiums paid for unauthorized insurance after a deduction for return premiums. As with the independent procurement tax, the bill removes the tax for membership fees, assessments, dues, and other consideration charges collected. The bill requires the tax to be paid as required for the above surplus lines broker and independent procurement taxes and similarly changes the date the tax is due from July 1 to March 31.[11]

Tax late penalty

Continuing law prescribes a penalty of 25% for the above surplus lines broker, independent procurement, and unauthorized insurer taxes that are not paid when due,

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[9] R.C. 3905.36(A).

[10] R.C. 3905.36(A).

[11] R.C. 3901.17(G).

and adds interest charges to that sum. The bill allows the Superintendent to waive the 25% penalty and interest charge for a first-time, inadvertent nonpayment of the tax when due if the nonpayment is reported immediately upon discovery and the outstanding tax is immediately paid to the Superintendent.[12]

Tax exemptions

The bill exempts from the above tax requirements:

- Insureds that are otherwise exempt from the payment of premium or franchise taxes under state or federal law;

- All of the following political subdivisions or a combination or consortium of the following subdivisions: any county; municipal corporation; township; township police district; township fire district; joint fire district; joint ambulance district; joint emergency medical services district; fire and ambulance district; joint recreation district; township waste disposal district; township road district; community college district; technical college district; detention facility district; a district for county-run juvenile facilities for training, treatment, and rehabilitation, including when combined with a juvenile detention facility; a joint-county alcohol, drug addiction, and mental health service district; a drainage improvement district; a union cemetery district; a county school financing district; a city, local, exempted village, cooperative education, or joint vocational school district; or a regional student education district, any public division, district, commission, authority, department, board, officer, or institution of any one or more of those subdivisions, that is entirely or substantially supported by public tax moneys.[13]

Surplus lines broker record filing

Under continuing law, every licensed surplus lines broker must keep a separate account of the business done under the person's license. Current law requires the brokers to file the portion of that account that details business done during the preceding calendar year with the Superintendent on or before the last day of January. Current law also details the information that must be contained in the account: the amount of the insurance, the name of the insured, a brief description of the type of insurance, the location of the property, the gross premium charged, the name of the

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[12] R.C. 3905.17(G) and 3905.36(A) and (C).

[13] R.C. 3905.36(B)(1), (B)(7), and (D).

insurer, the date and term of the policy, and a report in the same detail of all the policies canceled and the gross return premiums on those canceled policies.[14]

The bill changes the due date for filing account details. Under the bill, that filing is due the last day of March or when required under a multi-state agreement or compact that the Superintendent enters into under the bill. (March 31 is the same date as the surplus lines broker tax deadline.) Additionally, the bill requires brokers to file the details in the format prescribed by the Superintendent, but it removes any specification about who the brokers must file those details with and the specific information that must be included in the filing.[15]

Unauthorized insurer eligibility

Under current law, the Superintendent may establish the eligibility of an unauthorized insurer to sell policies on a surplus lines basis in Ohio by requesting certain documents. The bill removes one of the documents the Superintendent may request to make that determination: biographies of the owners and managers of the insurer. The bill also removes the Superintendent's duty to establish the eligibility of an unauthorized insurer if the Superintendent enters into a multi-state agreement under the bill.[16]

Due diligence

Under continuing law, a surplus lines broker is prohibited from selling, soliciting, procuring, placing, or renewing insurance with an unauthorized insurer unless an insurance agent or broker complies with due diligence requirements. (Current law also applies this prohibition to insurance agents, which does not appear to be something agents may do under current law. The bill removes this apparently erroneous reference.) To complete due diligence requirements the agent or broker must contact at least five of the authorized insurers the agent or broker represents that customarily write the kind of insurance required. If the agent or broker does not represent five insurers that customarily write that kind of insurance, the agent or broker must contact as many as the agent or broker represents. Due diligence is presumed if every insurer contacted either declines to cover the risk or fails to respond within ten days.[17]

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[14] R.C. 3905.34.

[15] R.C. 3905.34.

[16] R.C. 3905.33(A).

[17] R.C. 3905.33(B)(1).

Under the bill, due diligence only may be performed by an agent licensed in Ohio as a property and casualty insurance agent.[18]

Exempt commercial purchaser

Additionally, as required under the federal Act, the bill exempts insurance agents and surplus lines brokers from due diligence requirements if the agent or broker is seeking to procure or place unauthorized insurance for an exempt commercial purchaser if: (1) the surplus lines broker has disclosed to the exempt commercial purchaser that the insurance may or may not be available from the authorized market that may provide greater protection with more regulatory oversight, and (2) after receiving the disclosure, the exempt commercial purchaser has requested in writing that the insurance agent or broker procure or place the insurance from an unauthorized insurer. In order to qualify for this exemption, an exempt commercial purchaser must satisfy both of the following requirements:

- The purchaser must employ or retain a qualified risk manager to negotiate insurance coverage.
- The purchaser must have paid aggregate nationwide commercial property and casualty insurance premiums in excess of $100,000 in the immediately preceding 12 months.

Additionally, the purchaser must satisfy at least one of the following criteria:

- The person possesses a net worth in excess of $20 million.
- The person generates annual revenues in excess of $50 million.
- 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.
- The person is a not-for-profit organization or public entity generating annual budgeted expenditures of at least $30 million.
- The person is a municipality with a population in excess of 50,000 persons.

Under the bill, beginning January 1, 2015, and every five years thereafter, the Superintendent of Insurance must adjust the above dollar amounts to reflect the

[18] R.C. 3905.33(B)(1) and (2).

percentage change for that five-year period in the Consumer Price Index for All Urban Consumers.[19]

Qualified risk manager

As required under the federal Act, the bill requires that a qualified risk manager employed or retained to negotiate insurance by an exempt commercial purchaser to satisfy both of the following requirements:

- The person is an employee of, or third-party consultant retained by, the commercial policyholder.
- The person provides skilled services in loss prevention, loss reduction, or risk and insurance coverage analysis and the purchase of insurance.

Additionally, the qualified risk manager must satisfy one of the following:

- The person has obtained a bachelor's degree or a higher degree from an accredited college or university in risk management, business administration, finance, economics, or any other field determined by a state insurance commissioner or other state regulatory official or entity to demonstrate minimum competence in risk management, and either has approved designation or three years of experience in risk financing, claims administration, loss prevention and insurance analysis, or purchasing commercial lines of insurance;
- The person has at least seven years of experience in risk financing, claims administration, loss prevention, risk and insurance coverage analysis, or purchasing commercial lines of insurance; and has an approved designation;
- The person has at least ten years of experience in risk financing, claims administration, loss prevention, risk and insurance coverage analysis, or purchasing commercial lines of insurance;
- The person has a graduate degree from an accredited college or university in risk management, business administration, finance, economics, or any other field determined by the Superintendent to demonstrate minimum competence in risk management.

[19] R.C. 3905.33(B)(4) and 3905.331(A) and (B) and 15 U.S.C. 8205 and 8206.

All of the following are approved designations under the bill:

- A designation as a chartered property and casualty underwriter issued by the American Institute for CPCU and the Insurance Institute of America;
- A designation as an associate in risk management issued by the American Institute for CPCU and the Insurance Institute of America;
- A designation as certified risk manager issued by the National Alliance for Insurance Education and Research;
- A designation as a RIMS fellow issued by the Global Risk Management Institute;
- Any other designation, certification, or license determined by the Superintendent to demonstrate minimum competency in risk management.[20]

Due diligence notice requirement

Under continuing law, an agent who procures or places insurance through a surplus lines broker must obtain an affidavit from the insured acknowledging that the insurance policy is to be placed with a company or insurer not authorized to do business in Ohio and acknowledging that, in the event of the insolvency of the insurer, the insured is not entitled to any benefits or proceeds from the Ohio Insurance Guaranty Association.

Under the bill, if the agent or broker is exempt from the due diligence requirements as described above, or if the agent or broker is exempt under the law's current exemption for insurance procured from a risk purchasing group or risk retention group, the agent is also exempt from the affidavit requirements.

Additionally, current law requires surplus lines brokers to keep the original affidavit for at least five years, but the bill allows the broker to keep a copy.[21]

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[20] R.C. 3905.331(C) and 15 U.S.C. 8206.

[21] R.C. 3905.33(C).

Other changes

Service of process

The bill removes an exemption from Ohio's requirements for services of process for unauthorized insurance transaction requirements. The exemption was for contracts of insurance issued to an employer insured. Under current law, employer insureds qualify for the exemption if all of the following apply:

- The employer insured procures the insurance of any risk or risks by use of the services of a full-time employee acting as an insurance manager or buyer or the services of a regularly and continuously qualified insurance consultant who is not including a licensed insurance agent.
- The employer insured's aggregate annual premiums for insurance on all risks total at least $25,000.
- The insured has at least 25 full-time employees.[22]

Conforming changes

The bill makes other conforming and clarifying changes.

HISTORY

ACTION	DATE
Introduced	03-01-11

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[22] R.C. 3901.17(I)(7).