

San Francisco

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Los Angeles

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SLA Annual Meeting Presentation

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Overview

- Silvers v. Lexington
- New California Legislative Requirements
 - AB 2956
 - AB 1699
- Governor's Energy Response Initiative (Fire Surcharge)
- LESLI White Paper
- New York Insurance Exchange
- The Federalization of Insurance?

Silvers v. Lexington

Silvers v. Lexington et al.

- Plaintiffs seek a judicial declaration that the State Board of Equalization ("SBE") has a duty to assess taxes against Lexington Insurance Company under Cal. Const.
 - Essentially seek a determination that Lexington and other surplus insurers are **doing business in CA** and subject to the state's premium tax (2.35%).
- **SLA** filed an **amicus brief** arguing: tax and regulatory obligations and legislative history do not support taxation of surplus line insurers.
 - Ins. Code § 1776 clearly states coverage written by surplus line insurers and placed by surplus line brokers "**shall not be deemed to be business done by the insurer in this state.**"
 - **Cal. Constitution only applies to insurers doing business in this state.**
 - Instead, Ins. Code § 1775.5 imposes a 3% tax on gross premiums written by surplus line insurers.

Silvers v. Lexington et al. *continued*

- Demurrers filed by the SBE and Lexington were denied.
- CDI has intervened in the action.
 - CDI position is aligned with the SLA/industry position.
- Motions for summary judgment are to be heard in March.

New California Legislative Requirements

AB 2956

AB 1699

AB 2956

IT'S ALL ABOUT DA FEES!

- Clarifies distinction between an **agent and a broker** in the admitted market.
- Does not apply to **surplus line brokers**; however, members also acting as admitted market brokers should become familiar with new terms in Cal. Ins. Code § 1623.
- Identifies characteristics and disclosures that create a **presumption** that a producer is acting **as a broker**.
 - Presumption is created if the broker provides and the customer signs a written disclosure that includes:
 - ❖ That it is **acting as a broker**;
 - ❖ The **services** it will provide;
 - ❖ The **broker fees** it will charge; and
 - ❖ If applicable, that it may be entitled to **compensation from the insurer**.

AB 2956 *continued*

- A **wholesale broker** should make this disclosure to the retail broker.
- **Disclosures** must be **signed** by the client.
- Also, identifies **characteristics that rebut the broker presumption**.
 - The characteristics are:
 - ❖ An **appointment by the insurer** for the classes of insurance being transacted;
 - ❖ A **written agreement** with an insurer authorizing the licensee **to obligate the insurer** without first obtaining notification from the insurer that the insurer has accepted, conditionally or unconditionally, the submitted risk;
 - ❖ **Authorization to appoint other licensees** as agents of the insurer; and
 - ❖ **Authorization to pay claims** on behalf of the insurer.
 - If such characteristics are present, the brokerage **presumption is rebutted** and the **producer is deemed** to be acting as an **agent of the insurer**.

AB 2956 *continued*

- Nevertheless, the following functions **do not constitute agency acts**:
 - **Collection and transmission of premium/return premium.**
 - **Delivery of policies and evidence of insurance.**
- Otherwise, whether a producer is acting as an agent or broker will be determined by the **totality of the circumstances**.

AB 1699

- **Amends licensing requirements for surplus lines brokers.**
- **Individuals** who:
 - **Transact insurance with the public** under an entity's surplus lines broker license must also have an individual license.
 - **Maintain more than one surplus line office** must also have an individual license.
- Prior law allowed individual fire and casualty broker agent licensees to transact surplus lines business under an employer entity's license.
- Fees and bonding requirement half the price for individual licensee transacting on behalf of a licensed entity and those transacting independently (\$250 vs. \$500 per year).
- Licensed entities are required to provide 2 hours of training every five years to individuals who transact on their behalf.
- The SLA has developed a curriculum for that training.

Governor's Energy Response Initiative (Fire Surcharge)

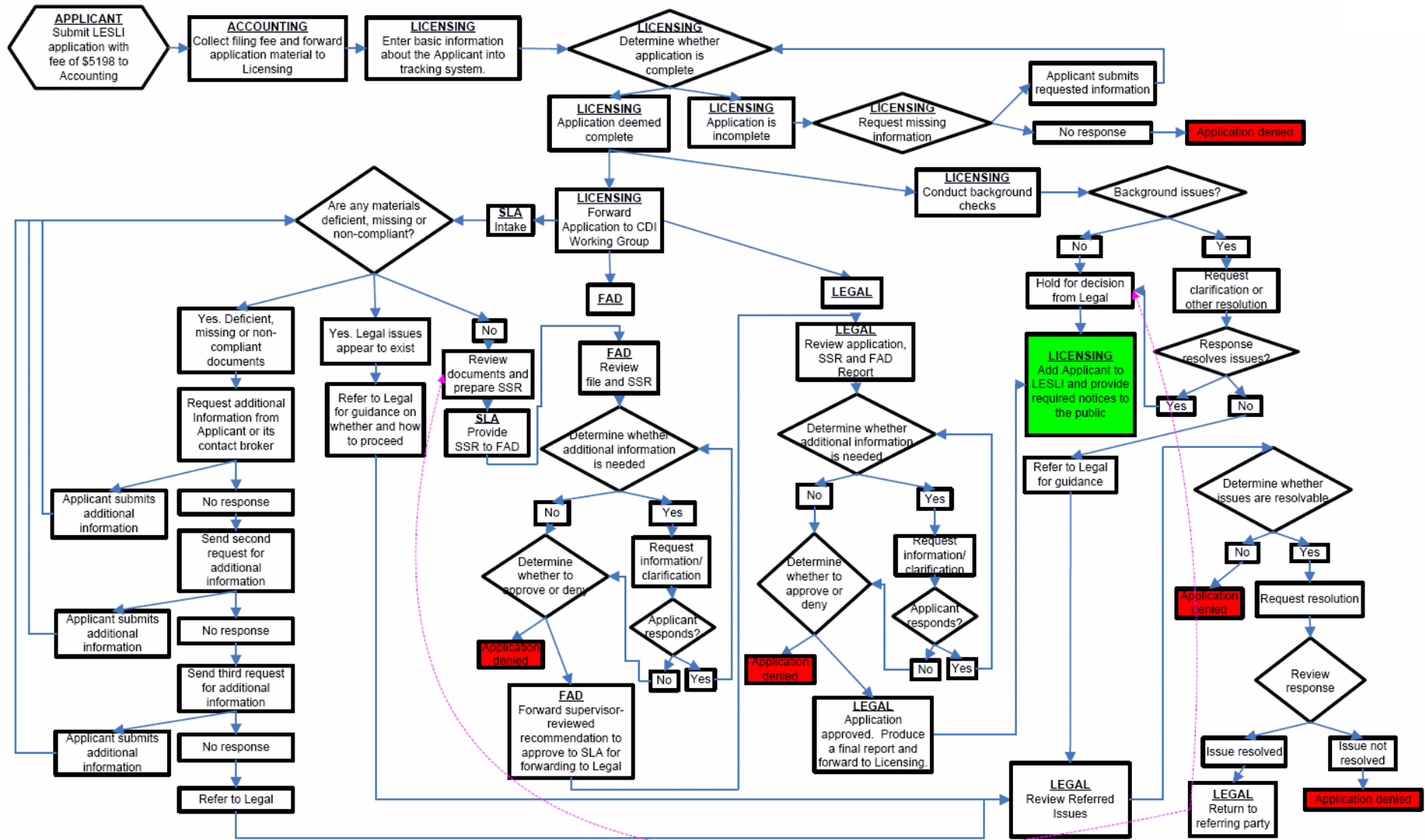
Governor's Emergency Response Initiative

- The Governor has **proposed a surcharge on property insurance** to fund emergency response measures (i.e., a 2.8% fire surcharge).
 - Although not included as part of the budget adopted in 2008, the surcharge proposal has reemerged in connection with the recent budget negotiations.
- Surcharge would apply to property coverages in surplus lines.
 - Collected by surplus lines brokers and submitted to the SLA in the same manner as the stamping fee.

LES LI White Paper

LESLI White Paper

- SLA is working with the CDI to gain a better understanding of the LESLI approval process.
- In December, the SLA presented an overview of the surplus line market and related issues to the CDI, including a discussion about the LESLI process.
- SLA is looking to identify actions that the SLA, the CDI, and the applicants may take to facilitate the smooth functioning of the LESLI process.



New York Insurance Exchange

Insurance Exchange

- At the recent annual meeting of the I.I.I. in NY, Superintendent Dinallo announced his **intent to revive the defunct New York Insurance Exchange**.
 - Recall the creation and failure of three Insurance Exchanges in the early 1980's: New York, Illinois and Florida.
 - Presumably, the NY Exchange would draw business away from Bermuda.
 - The NY Exchange could be similar to a Lloyd's Model (a central insurer location where brokers could access markets across state lines).
 - **Bermuda** continues to be attractive due to low corporate tax rates and a preemption of regulation that is less onerous than in the US.
 - **A California Exchange?**

The Federalization of Insurance?

Federalization of Insurance?

- There are moves in **Congress to pursue some form of federal regulation** as part of a reform package for the financial services industry.
 - Members of the House Financial Services Committee intend to ask the Treasury Secretary to create an Office of Insurance Information within Treasury.
- **State regulators are fighting back.**
 - Dinallo, Sullivan, and Sevigny have issued strong statements opposing federalization.
 - They note the success of state system in protecting solvency of insurers and avoiding troubles of the federally regulated banks.
- **AIG's problems not with state regulated insurers but with other entities in the holding company.**

Federalization of Insurance? *continued*

- **The GAO Report:**

- Entitled: “Financial Regulation: A Framework for Crafting and Assessing Proposals to Modernize the Outdated U.S. Financial Regulatory System” in January 2009.
- Notes that the “US regulatory system is a **fragmented** and complete system of federal and state regulators – put into place over the past **150 years** – that has not kept pace with the major developments that have occurred in the financial markets and products in recent decades.”
- Identifies the **risk of complex holding companies** with a variety of different financial entities, one of the challenges that the current scheme of decentralized financial regulation is inadequately equipped to address.

Federalization of Insurance? *continued*

- Also notes that a lack of a centralized US authority on insurance issues has complicated regulatory decision-making in the **international arena**.
- Includes suggestions that “Congress could consider the advantages and disadvantages of providing a **federal charter option** for insurance and creating a federal insurance regulatory entity.”
 - ❖ Washington Post article highlights issues related to the **regulated choosing the regulator** (30 banks since 2000 have chosen to convert to state regulation).

Federalization of Insurance? *continued*

- **The Group of Thirty:**

- A private, nonprofit, international body composed of very senior representatives of the private and public sectors and academia. Paul Volcker and Timothy Geithner are members.
- Published “Financial Reform: A Framework for Financial Stability” in January 2009.
- The report explicitly endorses national-level consolidated prudential regulation of large, internationally active insurance companies.