HB
71

HOUSE OF REPRESENTATIVES
THIRTIETH LEGISLATURE, 2019
STATE OF HAWAII

H.B. NO. 71

A BILL FOR AN ACT

RELATING TO SURPLUS LINES.

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF HAWAII:

SECTION 1. Section 431:8-302, Hawaii Revised Statutes, is amended to read as follows:

"**§431:8-302 Surplus lines insurers.** (a) No surplus lines broker shall, either knowingly or without reasonable investigation of the financial condition and general reputation of the insurer, place insurance with a financially unsound insurer or with an insurer engaging in an unfair practice.

(b) A surplus lines broker may place surplus lines insurance only with insurers who are authorized to write that type of insurance in the insurer's domiciliary state.

(c) A surplus lines broker shall not place coverage with an unauthorized insurer unless, at the time of placement, the surplus lines broker has determined that:

(1) The unauthorized insurer has capital and surplus or its equivalent under the laws of its domiciliary state that equal the greater of the minimum capital

requirement of this State or a minimum of $15,000,000; provided that:

(A) Minimum capital requirements may be satisfied by the insurer's possessing less than the minimum capital and surplus upon an affirmative finding of acceptability by the commissioner;

(B) A finding of acceptability pursuant to subparagraph (A) shall be based upon factors such as quality of management, capital and surplus of any parent company, company underwriting profit and investment income trends, market availability, and company record and reputation within the industry; and

(C) The commissioner shall not make an affirmative finding of acceptability pursuant to subparagraph (A) if the unauthorized insurer's capital and surplus is less than $4,500,000; or

(2) For an insurer not domiciled in the United States or its territories, the insurer shall be listed on the Quarterly Listing of Alien Insurers maintained by the

National Association of Insurance Commissioners International Insurers Department; provided that:

(A) If an alien insurer is not in the Quarterly Listing of Alien Insurers, the surplus lines broker shall maintain in the broker's office evidence of the financial responsibility of the insurer; and

(B) Evidence satisfactory to the commissioner that the insurer maintains in the United States an irrevocable trust fund in either a national bank or a member of the Federal Reserve System in an amount of not less than $5,400,000 consisting of cash, securities, letters of credit, or of investments of substantially the same character and quality as those which are eligible investments for the capital and statutory reserves of authorized insurers writing like kinds of insurance in this State, for the protection of all its policyholders in the United States, shall constitute prima facie evidence of the financial responsibility of the insurer.

[~~(d) The commissioner is authorized to enter into a cooperative agreement or interstate agreement or compact to establish additional and alternative nationwide uniform eligibility requirements that shall be applicable to unauthorized insurers domiciled in another state.~~]"

SECTION 2. Section 431:8-305, Hawaii Revised Statutes, is amended by amending subsection (a) to read as follows:

"(a) Upon placing surplus lines insurance, the surplus lines broker shall as soon as reasonably possible deliver to the insured the policy or, if the policy is not available, the surplus lines broker's certificate, cover note, binder, or other evidence of insurance. Any confirmation of insurance shall be executed by the surplus lines broker and shall show:

(1) The policy number, effective date, home state, and a description and location of the subject of the insurance;

(2) A general description of the coverages, including any material limitations other than those in standard forms;

(3) The premium and rate charged[~~, itemized by each state~~];

(4) The taxes and fees to be collected from the insured[~~, itemized by each state~~];

(5) The name and address of the insured;

(6) The name and address of the insurer;

(7) If the direct risk is assumed by more than one insurer, the certificate shall state the name and address and proportion of the entire direct risk assumed by each insurer; and

(8) The name of the surplus lines broker and such broker's license number."

SECTION 3. Section 431:8-312, Hawaii Revised Statutes, is amended by amending subsection (a) to read as follows:

"(a) Each licensed surplus lines broker shall keep in the broker's office in this State a full and true record of each surplus lines contract placed by the broker including a copy of the policy, certificate, cover note, or other evidence of insurance including, as applicable:

(1) Amount of the insurance and perils insured;

(2) Brief description of the property insured and its location;

(3) Gross premium, taxes, and fees charged[~~, itemized by each state~~];

(4) Any return premium, taxes, and fees paid[~~, itemized by each state~~];

(5) Rate of premium charged upon the several items of property;

(6) Effective date of the contract and its terms;

(7) Name, address, and home state of the insured;

(8) Name and address of the insurer;

(9) Amount of tax and other sums to be collected from the insured[~~, itemized by each state~~]; and

(10) Any additional information required by the commissioner."

SECTION 4. Section 431:8-313, Hawaii Revised Statutes, is amended by amending subsection (b) to read as follows:

"(b) The statement shall be on forms as prescribed and furnished by the commissioner and shall show:

(1) Gross amount of premiums for each kind of insurance transacted;

(2) [~~Aggregate gross~~] <u>Gross</u> premiums charged[~~, itemized by each state~~];

(3) [~~Aggregate of returned~~] Returned premiums paid to insureds[~~, itemized by each state~~];

(4) [~~Aggregate of net~~] Net premiums and fees[~~, itemized by each state~~];

(5) Amount of [~~aggregate~~] remitted taxes and fees[~~, itemized by each state~~]; and

(6) Additional information as required by the commissioner."

SECTION 5. Section 431:8-315, Hawaii Revised Statutes, is amended to read as follows:

"**§431:8-315 Tax on surplus lines.** (a) On or before March 15, 2011, each surplus lines broker shall pay to the director of finance, through the commissioner, a premium tax on surplus lines insurance transacted by the broker during 2010. On or before September 15, 2011, each surplus lines broker shall pay to the director of finance, through the commissioner, a premium tax on surplus lines insurance transacted by the broker after December 31, 2010, and before July 1, 2011. After June 30, 2011, within forty-five days after the end of each calendar quarter, each surplus lines broker shall pay to the director of finance, through the commissioner, a premium tax on surplus lines insurance transacted by the broker during the calendar quarter for insurance for which this State is the home state of the insured. The tax rate shall be in the amount of 4.68 per cent of gross premiums, less return premiums, on surplus lines insurance [~~allocated to~~] for which the home state is this State. [~~The tax rate and fees of other states shall be applied to the gross premiums, less return premiums, allocated to those states.~~]

As used in this subsection, "gross premiums" means the amount of the policy or coverage premium charged by the insurer in consideration for the insurance contract. Any charges for policy, survey, inspection, service, or similar fees or other charges added by the broker shall not be considered part of gross premiums.

[~~(b) The commissioner shall collect the taxes and fees on independently procured surplus lines insurance and from surplus lines licensees and disburse to the other states the funds earned by each state; provided that the other state has a reciprocal allocation and disbursement procedure for the benefit of this State. To the extent that other states, where portions of the properties, risks, or exposures reside, have failed to~~

~~establish a reciprocal allocation and disbursement procedure with this State, the net premium tax collected shall be retained by this State.~~

~~(c) If a surplus lines policy covers risks or exposures only partially resident in this State, the tax payable shall be computed upon the proportion of the premium which is properly allocable to the risks or exposures located in this State. The taxes and fees payable to this State on policies that cover risks and exposures only partially resident in this State shall be remitted on the quarterly schedule established by subsection (a) to the home state of the insured for disbursement to this State.~~

~~(d)~~] (b) The tax on any portion of the premium unearned at the termination of the insurance contract shall be returned to the policyholder.

[~~(e) The commissioner may:~~

~~(1) Enter into a cooperative agreement, reciprocal agreement, or compact with other states to facilitate and provide for the collection, allocation, and disbursement of premium taxes attributable to the placement of surplus lines insurance;~~

~~(2) Provide for uniform methods of allocation and reporting among surplus lines insurance risk classifications;~~

~~(3) Conform to the requirements of the federal Nonadmitted and Reinsurance Reform Act of 2010;~~

~~(4) Share information among states relating to surplus lines insurance premium taxes; and~~

~~(5) Utilize a method adopted in cooperation with other states to allocate risk and compute the tax due on the portion of premium attributable to each risk classification and to each state where properties, risks, or exposures are located.~~

~~The commissioner shall assess the insured for the cost of the cooperative agreement, reciprocal agreement, or compact to collect and distribute the premium taxes. Upon application of the insured, the commissioner shall refund the insured for excess payments of taxes received by the State that are the result of the statewide tax rate.~~]"

SECTION 6. Statutory material to be repealed is bracketed and stricken. New statutory material is underscored.

SECTION 7. This Act shall take effect upon its approval.

INTRODUCED BY: ______________________________

JAN 17 2019

H.B. NO. 71

Report Title:
Surplus Lines Premium Tax; Insurance

Description:
Amends the calculation of surplus lines insurance premium tax to tax the entirety of the premium using the rate established by Hawaii statute regardless of location of risk.

The summary description of legislation appearing on this page is for informational purposes only and is not legislation or evidence of legislative intent.

DAVID Y. IGE
GOVERNOR

JOSH GREEN
LT. GOVERNOR

STATE OF HAWAII
OFFICE OF THE DIRECTOR
DEPARTMENT OF COMMERCE AND CONSUMER AFFAIRS
335 MERCHANT STREET, ROOM 310
P.O. BOX 541
HONOLULU, HAWAII 96809
Phone Number: 586-2850
Fax Number: 586-2856
cca.hawaii.gov

CATHERINE P. AWAKUNI COLÓN
DIRECTOR

JO ANN M. UCHIDA TAKEUCHI
DEPUTY DIRECTOR

Testimony of the Department of Commerce and Consumer Affairs

Before the
House Committee on Consumer Protection and Commerce
Wednesday, February 6, 2019
2:00 p.m.
State Capitol, Conference Room 329

On the following measure:
H.B. 71, RELATING TO SURPLUS LINES

Chair Takumi and Members of the Committee:

My name is Colin Hayashida, and I am the Insurance Commissioner of the Department of Commerce and Consumer Affairs' (Department) Insurance Division. The Department offers the following comments.

The purpose of this bill is to amend the calculation of surplus lines insurance premium tax to tax the entirety of the premium using the rate established by Hawaii statute, regardless of location of risk.

This bill would repeal language authorizing the Insurance Commissioner to enter an interstate compact to collect surplus lines premium taxes. Under current law, the interstate compact requires the State to, among other things, use a method in cooperation with other states in allocating risk and computing taxes due on premium to each state where properties, risks, or exposures are located. A very small minority of states have signed onto this interstate compact, and it is more beneficial for the State to use a system where surplus lines brokers make direct payments to the Director of Finance.

Thank you for the opportunity to testify on this bill.

To: The Honorable Roy Takumi, Chair
The Honorable Linda Ichiyama, Vice Chair
House Committee on Consumer Protection & Commerce

FROM: John Meetz, State Relations Manager
Wholesale and Specialty Insurance Association (WSIA)

Re: HB 71 - Relating to Surplus Lines
Position: SUPPORT with amendment

Date: Wednesday, February 6, 2019
2:00 p.m., Conference Room 329

Aloha Chair Takumi, Vice Chair Ichiyama and Members of the Committee:

The Wholesale & Specialty Insurance Association (WSIA)[1] appreciates the opportunity to provide testimony in strong support of HB 71, regarding surplus lines insurance premium taxes. We respectfully request a technical amendment that would delay the implementation of the bill by 90 days after signing so that our members have time to adjust IT programs for pending business.

We would like to provide some background on surplus lines insurance and the unique process for collecting surplus lines tax. Surplus lines insurance premium tax is collected differently than standard insurance premium tax for admitted lines. It is the responsibility of the insurance broker to collect the tax from the consumer and pay the tax to the state. This differs from a standard insurance transaction where the tax is included as part of the consumer's insurance premium and paid by the insurance company to the state.

In 2010, Congress passed the Nonadmitted and Reinsurance Reform Act (NRRA) as part of the Dodd Frank Act. The purpose of the NRRA was to achieve a simpler and more efficient system of regulation and taxation of the surplus lines industry by establishing the insured's (the consumer's) "home state" as the one and only jurisdiction to regulate and tax surplus lines transactions. Because of the NRRA, surplus lines insurance transactions are now regulated solely by the "home state" of the consumer. Therefore, if a consumer, whether an individual or a business, is principally located in Hawaii, then Hawaii regulates the entire transaction, even when parts of the risk are located in other states.

[1] Effective August 1, 2017, the National Association of Professional Surplus Lines Offices (NAPSLO) and the American Association of Managing General Agents (AAMGA) merged to form the WSIA. WSIA is the U.S. professional trade association representing the wholesale and specialty insurance market and the wholesale distribution system. WSIA presents approximately 400 wholesale broker member firms, 100 surplus lines insurance companies, and 200 associates and service providers to the surplus lines market, our membership operates in more than 1,500 offices representing tens of thousands of individual brokers, insurance company professionals, underwriters and other insurance professionals worldwide – all of whom are committed to the wholesale distribution system and U.S. surplus lines market.

As part of the implementation of the NRRA, Congress allowed states to voluntarily enter into tax sharing agreements, and for a short time, several states pursued agreements to enact reciprocal allocation procedures. The current law governing Hawaii surplus lines taxation passed in 2011 in anticipation of joining one of these reciprocal allocation procedures as soon as it became viable. Evidence ultimately emerged showing that the reciprocal allocation procedures resulted in an inefficient tax structure and each of the agreements eventually dissolved. In their place, states embraced the "home state" approach of taxing and retaining 100% of the premiums at the home state rate.

Although Hawaii retains 100% of the tax that is remitted to the state, risks that are located outside Hawaii are taxed based on where the risk resides, rather than exclusively at the Hawaii rate (4.68%). This results in unnecessary regulatory burdens for the broker, requires a difficult allocation of risk when it resides in multiple states, results in additional costs of compliance which ultimately impacts the consumer, and in some cases, collects less tax for the state than the amount to which it is legally entitled. HB 71 would amend Hawaii law to tax all surplus lines premiums, for which Hawaii is the home state, entirely at the home state rate of 4.68%, just as 46 states plus the District of Columbia and Puerto Rico do today (legislation is pending in all four remaining states).

In addition to easing the regulatory burden for surplus lines brokers, another beneficial effect of this legislation will likely be increased premium tax revenue. Hawaii's tax rate of 4.68% exceeds the average U.S. surplus lines premium tax rate of 3.53%. Because of this, most insurance policies that contain multi-state premium are currently being taxed at a rate below the 4.68% Hawaii rate and below the states authority under the NRRA. For surplus lines insurance policies where Hawaii is the "home state," HB 71 would amend the law to tax all surplus lines premium at 4.68% regardless of the location of that risk.

HB 71 would codify the "home state" approach in Hawaii as it has been done in most of the U.S. and is being pursued in the remaining states. In passing HB 71, Hawaii will reduce the regulatory burden for local surplus lines brokers, simplify compliance procedures for brokers and regulators, increase nationwide uniformity in surplus lines taxation and very likely increase premium tax revenue for the state.

WSIA strongly supports the measure and asks the committee for its consideration of an amendment to delay the effective date of the bill to 90 days following the enactment of the legislation to allow surplus lines brokers to accurately tax any transactions that are pending in proximity to the date of signing.

Sincerely,

John H. Meetz
State Relations Manager
john@wsia.org
816.799.0863

Keri A. Kish
Director of Government Relations
keri@wsia.org
816.799.0855

American Property Casualty Insurance Association

To: The Honorable Representative Roy M. Takumi, Chair
The Honorable Representative Linda Ichiyama, Vice Chair
House Committee on Consumer Protection & Commerce

From: Mark Sektnan, Vice President

Re: **HB 71 – Relating to Surplus Lines**
APCIA Position: Support

Date: Wednesday, February 6, 2019
2:00 p.m., Conference Room 329

Aloha Chair Takumi, Vice Chair Ichiyama and Members of the Committee:

The American Property Casualty Insurers Association of America (APCIA) is pleased to support HB 71 which would amend the calculation of surplus lines insurance premium tax to tax the entirety of the premium using the rate established by Hawaii statute regardless of location of risk. Representing nearly 60 percent of the U.S. property casualty insurance market, the American Property Casualty Insurance Association (APCIA) promotes and protects the viability of private competition for the benefit of consumers and insurers. APCIA represents the broadest cross-section of home, auto, and business insurers of any national trade association. APCIA members represent all sizes, structures, and regions, which protect families, communities, and businesses in the U.S. and across the globe. APCIA also includes member insurance companies that write over 70% of the surplus lines' premiums reported by U.S. insurers.

The APCIA has been a strong advocate for states to adopt the provisions of the Nonadmitted and Reinsurance Reform Act (NRRA), enacted within the Dodd-Frank Act of 2010 (DFA), which calls for greater uniformity and consistency across the states on the regulation and taxation of nonadmitted insurance, commonly known as surplus lines.

Since the effective date of the NRRA on July 21, 2011, 46 states have correspondingly amended their laws to streamline the taxation of surplus lines premiums on multi-state policies. In those states, the taxation rules of the home state of the insured[1] requires that 100% of the gross premiums of the multi-state policy be solely subject to the tax rate of

[1] 15 U.S.C. § 8206. 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.

the home state. This subsequently eliminates the time-consuming computation, reporting, allocation, and reconciliation of state-by-state tax monies that ultimately are all retained by the home state.

So, as provided under the NRRA, HB 71 would likewise amend the calculation of surplus lines insurance premium tax where Hawaii is the home state of the insured to tax the entirety of the policy premium using the rate established by Hawaii statute regardless of where other parts of the insured's risks are located.

The surplus lines market represents only around 7% of the premium writings in the property & casualty insurance industry. However, it responds to critical insurance needs for commercial and individual consumers who cannot otherwise find their necessary insurance coverage in the standard admitted market. The APCIA believes HB 71 not only appropriately addresses the Congressional call under the NRRA, it further enables this efficient and effective response to the benefit of the Hawaii marketplace.

For these reasons, APCIA asks for your support of HB 71.