National Association of Professional Surplus Lines Offices, Ltd.

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May 1, 2014

Dear Commissioner:

On behalf of the National Association of Professional Surplus Lines Offices (NAPSLO)[1], we appreciate the opportunity to share our updated analysis on the implementation of the Nonadmitted and Reinsurance Reform Act (NRRA). We also write to share our views on several important national issues on the 2014 Congressional agenda.

NRRA

The changes brought about by the states through the NRRA's implementation continue to promote administrative efficiency for the surplus lines industry. By providing a national framework for efficiency, clarity and uniformity in the regulation and taxation of surplus lines insurance nationwide, states' implementation of the NRRA has dramatically simplified compliance for multistate risks. Instead of trying to comply with as many sets of rules, disclosures and requirements as there are states, and the filings to document compliance with them, there is now one state, the home state of the insured, with the sole and exclusive authority to tax and regulate a surplus lines transaction.

NAPSLO strongly supports the home state approach facilitated by the NRRA. This approach benefits surplus lines brokers, carriers and consumers, and our members are very appreciative of its impact, which is focused in the areas of taxation and insurer eligibility.

Surplus Lines Taxation

We strongly support home state taxation where the home state of the insured assesses and retains 100% of the tax on a multistate risk at the home state rate in accordance with their laws and regulations. This approach is currently implemented and working well in 46 states representing more than 80% of nationwide surplus lines premium. We firmly believe the home state approach is the only viable and uniform national solution to Section 521 of the NRRA.

[1] NAPSLO is the national trade association representing the surplus lines industry and the wholesale insurance distribution system. NAPSLO's membership consists of approximately 400 brokerage member firms, 100 company member firms and 200 associate member firms, all of whom operate over 1,500 offices representing approximately 15,000 to 20,000 individual brokers, insurance company professionals, underwriters and other insurance professionals in the 50 states and the District of Columbia. NAPSLO is unique in that both surplus lines brokers and surplus lines companies are full members of the association; thus NAPSLO represents and speaks for the surplus lines wholesale marketplace.

On August 9, 2013, we shared our initial analysis of the data available at that time regarding tax sharing and advised you that we would continue to provide updated information as it developed. The Council of Insurance Agents & Brokers and NAPSLO recently obtained data from certain states participating in the Nonadmitted Insurance Multi-State Agreement (NIMA) regarding their first fifteen months of operation. Together, we updated our analysis with this new data and shared it with all states participating in NIMA as well as those states who adopted the Surplus Lines Insurance Multi-State Compliance Compact (SLIMPACT), which we have attached for your review as Exhibit I.

In summary, the new data received from Florida, Louisiana, Utah and Wyoming indicates that, during the first five quarters of operation, NIMA jurisdictions shared approximately $1.1 million tax dollars. According to data published by the Surplus Lines Clearinghouse (SLC), $533.2 million of premium reported through the SLC to NIMA jurisdictions resulting in filing fees of $1.6 million in the SLC's first year of operation. As a result, $1.1 million in SLC taxes shared over 15 months is far less than SLC filing fees of $1.6 over 12 months of operation. We believe these facts clearly illustrate the reality of insignificant tax allocations in relation to the cost to the industry and insureds to support the tax allocation process. While we recognize this comparison excludes the state data missing from some of the NIMA jurisdictions in certain quarters, and we look forward to incorporating that data should we receive it. We do not believe that will change the cost/benefit scenario.

Our analysis also indicates the $1.1 million of allocated taxes had the following net impact on the NIMA jurisdictions from July 1, 2012 to September 30, 2013.

	Taxes Collected By:						Total	
	FL	LA	PR	SD	UT	WY	Tax Sharing	
Tax Distributions To:								**Net In/(Out)**
Florida		$ -	$ -	$ -	$ -	$ -	$ -	$ (959,178)
Louisiana	$ 444,736		-	977	21,558	188	467,459	453,784
Puerto Rico	468,263	-		-	-	-	468,263	468,263
South Dakota	5,222	-	-		3	7	5,233	2,164
Utah	27,811	1,524	-	-		3,629	32,964	(108,432)
Wyoming	13,146	12,151	-	2,091	119,835		147,224	143,399
	$ 959,178	$ 13,675	$ -	$ 3,068	$ 141,396	$ 3,825	$ 1,121,143	$ -

A few additional highlights of our analysis in Attachment B of Exhibit I include:

1. There are 47 instances where individual NIMA jurisdictions shared $0 tax dollars;
2. There are 3 instances where individual NIMA jurisdictions shared less than $10 in tax dollars (e.g., South Dakota received $2.91 from Utah in 1st Quarter 2013, South Dakota received $7.36 from Wyoming in 3rd Quarter 2013 and Utah received $9.56 from Louisiana in 2nd Quarter 2013);
3. There are 15 instances where individual NIMA jurisdictions shared less than $1,000 in tax dollars;
4. There are 26 instances where individual NIMA jurisdictions shared less than $5,000 in tax dollars;
5. There are 60 instances where we don't yet have the data to complete the analysis.

This data and our analysis indicate the cost of tax allocation exceeds the actual amount of taxes shared among participating states. As a result, we strongly believe the only viable national solution to uniform surplus lines taxation is 100% implementation of home state taxation. We further believe the attached data strongly supports this conclusion, and we ask that all states carefully consider these economics before considering any participation in NIMA's Associate Membership or any tax sharing mechanism.

It is also important to note that NAPSLO's opposition to tax sharing does not represent opposition to the automation of surplus lines regulatory transactions. In general, NAPSLO members appreciate the automation and uniformity facilitated by web-based systems supporting surplus lines transactions. Where NAPSLO members have concerns is when such systems include the tax sharing component and functionality.

We continue to ask NIMA, members of SLIMPACT and all other states to carefully consider these economic realities, including specific review of the amount of taxes that have actually been allocated among the NIMA jurisdictions as illustrated herein, as the basis for abandoning all tax sharing efforts in favor of 100% home state taxation nationwide. While we understand and recognize the states have worked hard and diligently to make the SLC work, the data now illustrates the cost of tax sharing far exceeds very insignificant tax shifts among a small number of states. For this reason, we respectfully request that all states conclude all tax sharing efforts and join the 45 states and District of Columbia to achieve the national uniform home state system of taxation we all desire.

Insurer Eligibility

Our work continues to promote the uniform implementation of the NRRA's insurer eligibility standards nationwide. The NRRA provided clear criteria for determining an insurer's eligibility to provide surplus lines insurance in each state. The NRRA's intent was to make it easier for a nonadmitted insurer that meets the NRRA eligibility criteria to become eligible to conduct surplus lines business in all states where it wishes to write surplus lines insurance. While some states have eliminated many pre-NRRA eligibility requirements, such as "white lists," a number of states continue to impose eligibility requirements beyond those outlined in the NRRA.

We are encouraged by the work that was completed last year by the NAIC's Surplus Lines Requirements (C) Subgroup. In August 2013, the NAIC's Surplus Lines (C) Task Force accepted the recommendation of the Subgroup to adopt "Suggestions for Improving Information Access for Regulators, Brokers and Insureds." The Suggestions are intended to help states move towards the uniform treatment of the insurer eligibility provisions from the NRRA, focusing on reducing unnecessary requests for supporting documentation and providing suggestions for states to access and review existing information. We hope your office has had a chance to review these suggestions and we offer any assistance you may need to fully implement them in your jurisdiction.

Government Accountability Office Study of the NRRA

On January 16, 2014 the GAO released its study "Effects of the Nonadmitted and Reinsurance Reform Act of 2010." As mandated by the NRRA, the purpose of the GAO's study was to (1) examine the effects, if any, on the price and availability of insurance coverage in the surplus lines market and (2) examine actions states have taken to implement the NRRA.

The GAO found that the NRRA has had little, if any, effect on the prices or availability of coverage, as the NRRA was not intended to affect these areas. The report also notes the NRRA and resulting changes in states' laws have simplified the compliance process for brokers and insurers writing multistate risks. The

GAO noted the need for additional work toward (1) the uniform treatment of surplus lines premium tax post-NRRA; and (2) the uniform implementation of the NRRA's insurer eligibility provisions.

Other National Issues

Next week, NAPSLO members will be meeting with a number of federal lawmakers in Washington D.C. regarding several important national issues impacting the surplus lines industry and NAPSLO members. Our most important message will be NAPSLO's strong support for the state-based system of insurance regulation. We will also be discussing NAPSLO's support for the reauthorization of the Terrorism Risk and Insurance Act, the adoption and implementation of the National Association of Registered Agents and Brokers, and necessary revisions to the current definition of private flood insurance to ensure surplus lines insurers are eligible to offer private market solutions and alternatives to consumers with unique and complex flood risks. These key messages are summarized for your reference in Exhibit II.

A.M. Best Surplus Lines Market Review

Since 1994, the Derek Hughes/NAPSLO Educational Foundation has provided a grant to the A.M. Best Company to study and publish a special report on the surplus lines market. We are pleased to present you with a copy of A.M. Best's 2013 Report, noting that, for the ninth year in a row, the surplus lines industry reported no financially impaired companies, in contrast to the admitted property/casualty industry's 21 disclosed financial impairments, and domestic professional surplus lines insurers continue to maintain a higher proportion of secure ratings than the overall property/casualty industry. We hope you find the report useful and informative, and we look forward to sharing A.M. Best's 2014 report at the end of this year.

We always appreciate the opportunity to discuss these important issues with you and your staff. Please do not hesitate to contact us should you have questions or if we can assist you in any way. Thank you in advance for your consideration.

Sincerely,

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Exhibit I

NIMA Tax Sharing Data
July 1, 2012 to September 30, 2013

Data by Quarter

		Taxes Collected By:						Total	Home State	Total Distribution
	Tax Distributions To:	FL	LA	PR	SD	UT	WY	Tax Sharing	Allocations Kept	from Clearinghouse
3rd Quarter 2012	Florida							$ -		$ -
	Louisiana	14,447.42		-	-	14,747.23	188.40	29,383.05	135,379.38	164,762.43
	Puerto Rico							-		-
	South Dakota							-		-
	Utah							-		-
	Wyoming	1,438.50	862.43	-	-	286.17		2,587.10	3,029.68	5,616.78
4th Quarter 2012	Florida							-		-
	Louisiana	43,155.32		-	-	944.55	-	44,099.87	442,911.90	487,011.77
	Puerto Rico							-		-
	South Dakota							-		-
	Utah							-		-
	Wyoming	58.12	2,841.56	-	507.88	102,543.76		105,951.32	139,118.17	245,069.49
1st Quarter 2013	Florida							-		-
	Louisiana	62,856.93		-	-	-	-	62,856.93	428,063.20	490,920.13
	Puerto Rico	1,730.02	-		-	-	-	1,730.02	-	1,730.02
	South Dakota	696.92	-	-		2.91	-	699.83	62,720.25	63,420.08
	Utah	6,301.18	-	-	-		2,007.73	8,308.91	241,598.27	249,907.18
	Wyoming	1,215.28	206.49	-	123.03	5,663.66		7,208.46	172,535.63	179,744.09
2nd Quarter 2013	Florida							-		-
	Louisiana	156,114.55		-	976.97	5,698.51	-	162,790.03	1,825,214.96	1,988,004.99
	Puerto Rico	459,507.14	-		-	-	-	459,507.14	-	459,507.14
	South Dakota							-		-
	Utah	15,253.50	9.56	-	-		1,621.44	16,884.50	112,513.49	129,397.99
	Wyoming	1,731.20	6,685.44	-	1,460.55	10,346.29		20,223.48	19,249.47	39,472.95
3rd Quarter 2013	Florida							-		-
	Louisiana	168,161.82		-	-	167.43	-	168,329.25	1,155,201.11	1,323,530.36
	Puerto Rico	7,025.74	-		-	-	-	7,025.74	-	7,025.74
	South Dakota	4,525.50	-	-		-	7.36	4,532.86	3,765.37	8,298.23
	Utah	6,256.05	1,514.41	-	-		-	7,770.46	137,869.93	145,640.39
	Wyoming	8,702.96	1,555.15	-	-	995.59		11,253.70	16,344.54	27,598.24
		$ 959,178.15	$ 13,675.04	$ -	$ 3,068.43	$ 141,396.10	$ 3,824.93	$ 1,121,142.65	$ 4,895,515.35	$ 6,016,658.00

Still awaiting state report for applicable Quarter.

Totals Over Five Quarters

	Taxes Collected By:						Total	
Tax Distributions To:	FL	LA	PR	SD	UT	WY	Tax Sharing	Net In/(Out)
Florida		$ -	$ -	$ -	$ -	$ -	$ -	$ (959,178)
Louisiana	$ 444,736		-	977	21,558	188	467,459	453,784
Puerto Rico	468,263	-		-	-	-	468,263	468,263
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NAPSLO

National Association of Professional Surplus Lines Offices

About NAPSLO

The National Association of Professional Surplus Lines Offices (NAPSLO) is a professional trade association representing the surplus lines industry and the wholesale distribution system. Since its incorporation in 1975, NAPSLO has become the authoritative voice of the surplus lines industry, advocating for the industry's vital role in the insurance marketplace by insuring those risks that cannot be covered in the standard market.

NAPSLO's membership consists of approximately 400 brokerage member firms, 100 company member firms and 200 associate member firms, who together operate more than 1,500 offices representing approximately 15,000 to 20,000 individual brokers, insurance company professionals, underwriters and other insurance professionals. NAPSLO is unique in that both surplus lines brokers and insurance companies are voting members of the Association; thus NAPSLO represents and speaks for the surplus lines wholesale marketplace.

Current Surplus Lines Issues

- **TRIA (Terrorism Risk Insurance Act)**
  NAPSLO **strongly supports** the **reauthorization of the TRIA**. Congress should act quickly and well in advance of the December 31, 2014 expiration date. Immediate resolution is critical in order to provide certainty for insureds and the insurance marketplace with coverage periods for 2014 and beyond.

  TRIA's caps on insurer liability provide some level of certainty and help insurers better manage the risk; increasing these caps would reduce the level of certainty in terrorism risk management, will place smaller insurers at greater risk, and may unintentionally constrain the availability of private capital solutions for terrorism risks.

- **NARAB II (National Association of Registered Agents and Brokers)**
  NAPSLO **strongly supports NARAB II**, which will streamline agent and broker licensing for those operating on a multi-state basis. Congress should pass this legislation during this Congressional Session.

- **Private Flood Insurance Definition**
  Congress should revise the current definition of private flood insurance under 42 USC §4012a(b)(7) to ensure surplus lines insurers are eligible to offer private market solutions and alternatives to consumers in need of unique and complex flood risks. Congress should pass language similar to the amendment offered by Senators Heller and Lee during the debate of S. 1296, the Homeowner Flood Insurance Affordability Act.

About Surplus Lines

Often called the "safety valve" of the insurance industry, surplus lines insurers fill the need for coverage in the marketplace by insuring those risks that are declined by the standard underwriting and pricing processes of admitted insurance carriers. The surplus lines market plays an important role in providing insurance for hard-to-place, unique or high capacity risks.

With the ability to accommodate a wide variety of risks, the surplus lines market acts as an effective supplement to the admitted market. Surplus lines insurers are able to cover unique and hard-to-place risks because, as nonadmitted insurers, they are able to react to market changes and accommodate the unique needs of insureds that are unable to obtain coverage from admitted carriers. This results in cost-effective solutions for consumers that are not "one size fits all," but are instead skillfully-tailored to meet specific needs for non-standard risks.

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NAPSLO Regulatory Principles

The NAPSLO Legislative Committee has prepared the following Regulatory Principles as a "roadmap" for current and future positions on various legislative and regulatory issues.

I. Freedom From Regulation of Surplus Lines Rates and Forms
Freedom from regulation of rates and forms is what distinguishes the surplus lines market from the admitted market and is the essential feature that allows the surplus lines industry to serve the consumer and function as a market for hard to place risks. It should be defended at all times in all states, even for seemingly minor infringements.

II. The Principle of Export
The principle of export means that surplus lines transactions involve state regulated surplus lines brokers, exporting business to nonadmitted companies not regulated by the state. This principle forms the regulatory framework of the surplus lines market. It defines the role of the surplus lines broker in the transaction as the regulated entity. It separates the company from direct 50 state regulation – including rates and forms. It establishes context of the taxation of the transaction.

III. Primacy of Surplus Lines
State based residual market mechanisms should not be given risk placement preference before surplus lines. The sequence of risk placement should be as follows: admitted market → surplus lines market → state based residual market.

IV. Uniform and Reciprocal Licensing of Surplus Lines Brokers Between the States
NAPSLO's goal is a simple and conflict free single payment system for remitting surplus lines taxes on multi-state risks.

V. Standardization of Taxation of Multi-State Surplus Lines Brokers Between the States
NAPSLO's goal is a uniform and reciprocal 50 state system.

VI. Guaranty Funds
NAPSLO is opposed to surplus lines guaranty funds for the following reasons:

- They promote a false security because the coverage is typically inadequate for commercial lines;
- They promote the use of financially weak companies;
- Potential premium assessments are an unfair burden on surplus lines consumers; and
- The surplus lines marketplace is financially secure and domi nated by companies with average ratings significantly higher than the overall market.

VII. Commercial Lines Deregulation – Automatic Export
Transactions involving commercial policyholders under state commercial lines deregulation laws should automatically qualify for export to the surplus lines market without conducting a diligent search.

VIII. State Regulation
The surplus lines marketplace has proven to be an essential part of the national insurance market. It operates successfully in the state-based regulatory system where business is exported from one state to another.

NAPSLO favors the continuation of a state-based regulatory system for insurance over a federal system. However, the current state-based system must become more uniform and efficient.

Federal Standards for State Regulation
Uniformity and reciprocity among and between the states in areas of producer licensing and taxation are desirable. The adoption of such truly national standards could be a positive step in improving the efficiency and effectiveness of the state regulatory system.

However, no federal standard should be enacted that curtails, hinders or otherwise prevents the surplus lines market from performing its vital role as a supplemental market for insurance consumers.

IX. Federal Regulation
NAPSLO does not believe that a federal based system of regulation can be effective in the oversight of an industry established to address a state based system of reparations.

Optional Federal Charter
Proponents of creating optional federal charters believe that regulation of rates and forms will be eliminated by securing such charters. If a system of optional federal charters is created, it will be an unproven regulatory system. Under a system of federal charters, it will be essential, for surplus lines underwriters that the regulatory structure permit a holding company to simultaneously hold federal and state charters so that the insurance can be placed under the regulatory system that offers rates, terms and conditions most consistent with the policyholder's needs.

Federal Insurance Office (FIO)
NAPSLO supports the role of the FIO in studying and overseeing the efficiency and modernization of the system of insurance regulation in the United States, and believes any federal policy regarding insurance regulation continue a course aimed at strengthening state insurance regulation and coordinating the efforts of federal agencies with state regulatory systems. NAPSLO supports the elimination of Federal subpoena authority as it relates to insurance data and recommends that any Federal entity secure such date through the appropriate state insurance regulator. Protecting our industry from such subpoena authority prevents insurance companies from unnecessary and costly reporting requirements that would ultimately add little value while increasing the costs of doing business. As in any business, these costs would ultimately be felt by the consumers of our services.

X. Nonadmitted and Reinsurance Act
NAPSLO strongly supports the uniform implementation of the NRRA by the states. Properly implemented as consistent with the letter of the law and Congressional intent, the NRRA will significantly improve the surplus lines market. NAPSLO will continue to revisit these Regulatory Principles as the NRRA is implemented.

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