

# MYTHS VS. FACTS ON THE NON-ADMITTED REINSURANCE REFORM ACT (NRRA)

## IMPLEMENTATION LEGISLATION

- I. INTERSTATE COMPACT/AGREEMENT MYTHS** - Many states have introduced legislation that would create or enable insurance commissioners to enter interstate compacts or agreements for tax sharing purposes. NAPSLO is not opposed to a compact that increases uniformity and efficiency of surplus lines tax regulation; however, believes it important to dispel the myth that interstate compacts or agreements are a requirement of the NRRA, and that such compacts will result in tax revenue windfalls for participating states.
- ❖ **MYTH #1:** States must enter into an interstate compact or agreement in order comply with the provisions of the NRRA.
  - ❖ **FACT:** The NRRA acknowledges that states may enter into a compact or agreement with other states in order to allocate premium taxes for multi-state surplus lines risks. However, participation in a compact or agreement is not required by the NRRA.
    - A state may pass legislation to conform its codes with the NRRA without contemplating a tax sharing compact or agreement.
    - A state that does not enter into a tax compact or agreement nonetheless maintains its ability to collect taxes on multi-state risks where it is the "home state" of the insured, and to retain those tax dollars.
    - A state will not be penalized – legally, politically, or monetarily – for opting not to enter into an interstate compact or agreement.
    - A state does not have to enter into a compact in order to tax 100% of the premium on multi-state risks where it is the “home state” of the insured.
  - ❖ **MYTH #2:** All states that enter interstate compacts or agreements will receive a windfall of additional tax revenue.
  - ❖ **FACT:** A compact or agreement does not guarantee additional revenue for a state; while some states may receive additional tax revenue by participating in interstate compacts or agreements, others will lose tax revenue by allocating more tax revenue to other states than they will receive.
    - Interstate tax compacts or agreements are not a fund or a grant. There is no "pot of gold" at the end of the interstate compact rainbow.
    - An interstate compact or agreement must be successfully established and implemented in order for a state to receive its allocated share of multi-state tax revenue. No multi-state premium tax compact or agreement currently exists.
    - Certain states will benefit from participation in an interstate compact or agreement, while other states will take a loss.
    - A state's status as a ”winner” or a “loser” hinges on the amount of multi-state tax premium that is designated to it as the “home state” of an insured on a multi-state surplus lines risk.
    - A state's status as a "winner” or “loser” could change from year to year.
  - ❖ **MYTH #3:** The NRRA imposes a deadline on the states to act.
  - ❖ **FACT:** As noted, the NRRA does not require action by the states, and there is no deadline for the states to take action.
    - If a state *chooses* to adopt a compact or other procedure on or before June 16, 2011 (330 days after the enactment of the NRRA), then any nonadmitted insurance premium tax owed to that state in 2011 shall be subject to the compact or other procedures.

- If a state chooses to adopt a compact at any time after June 16, 2011, then the compact applies to premium taxes that are owed in 2012 and later.
- The 330 day period is not a deadline for state action, rather it simply defines what rules apply to 2011 premium taxes should a state choose to adopt a compact.
- ❖ **MYTH #4** The NRRA allows states to require brokers or insureds to submit multi-state allocation reports quarterly or semi-annually.
- ❖ **FACT:** The NRRA permits a state (when it is the home state) to require brokers or insureds to submit multi-state allocation reports only annually. Requiring brokers or insureds to submit such reports quarterly, semiannually, or otherwise more often than annually, would violate the NRRA.

**II. NIMA MYTHS:** In those states that have introduced legislation that enables the insurance commissioner to enter a tax compact or agreement, commissioners will be faced with the choice of two competing interstate compact options: NIMA or SLIMPACT-lite.

- \* SLIMPACT-lite was developed based on extensive industry input and is supported by the National Conference of Insurance Legislators (NCOIL), the Council of State Governments (CSG), and the National Conference of State Legislatures (NCSL). It is the only interstate proposal that provides a mechanism to improve regulatory efficiency and uniformity as intended by the NRRA.
- \* NIMA, on the other hand, would create inefficiencies, constitute an unlawful delegation of authority, and create an unstable interstate system.
- ❖ **MYTH #1:** NIMA represents the spirit and letter of the NRRA.
- ❖ **FACT:** The clear intent of the NRRA was to create a streamlined, efficient tax system where brokers would follow uniform requirements, forms, and procedures to pay taxes on multi-state risks to the “home state” of the insured. NIMA fails to accomplish either uniformity or efficiency.
  - NIMA perpetuates unnecessary, bureaucratic data reporting, with dozens of data elements and hundreds of state-specific tax nuances for every multi-state policy issued.
  - NIMA would require the allocation of certain multi-state risks, including dozens of casualty lines, when most states currently do not require that these risks be allocated.
  - NIMA's complex and untested allocation requirements will force policyholders to attempt to create or estimate data for the broker to report.
- ❖ **MYTH #2:** Legislation authorizing insurance commissioners to enter NIMA is constitutional.
- ❖ **FACT:** By authorizing insurance commissioners to enter NIMA, legislatures are enabling insurance departments to send tax revenues to other states in contravention of state constitutional principles.
  - NIMA provides insurance commissioners the discretion to send state tax revenues to other states, which constitutes an unconstitutional delegation of policymaking and/or taxing authority to a state agency.
  - Any tax sharing agreement should be specifically set out in legislation, approved by the state legislature and signed by the Governor.
  - NIMA fails to put brokers, insureds, and other stakeholders on notice of changes to the regulatory regime with which they must comply.
- ❖ **MYTH #3:** NIMA will provide stability and administrative simplicity.

- ❖ **FACT:** NIMA enables states to withdraw from the agreement upon 60 days notice, which will cause instability and uncertainty within the industry.
  - The ability of states to withdrawal from NIMA on short notice could result in constant confusion about the operation of the agreement.
  - This instability will be an administrative nightmare for both insurance departments and industry alike:
    - Withdrawing states will have expended unnecessary time and resources creating a system they abandoned.
    - Remaining participating states will have wasted resources creating new tax sharing systems and procedures, to cooperate with former participating states.
    - No participating state will be able to accurately predict its allocated revenues given the systemic instability of the agreement.
    - Brokers will have needlessly devoted time and energy to learn a reporting system that could be defunct at the whim of a regulator.
  
- ❖ **MYTH #4:** States will quickly obtain the necessary legislative authority to participate in NIMA, and the system will be operational very soon.
  
- ❖ **FACT:** The NIMA proposal has become incredibly controversial, states are increasingly reluctant to provide insurance regulators with the necessary authority to participate, and the system is unlikely to be operational for many months.
  - Few states have enacted legislation that would empower their respective state insurance regulators to participate in NIMA.
    - Only a handful states have passed such legislation in the 2011 session, and these are mainly very small jurisdictions with relatively modest surplus lines business (e.g. West Virginia and Wyoming).
    - The largest states have been especially reluctant to pass open-ended legislation of this nature.
  - NIMA is universally opposed by the state legislator organizations, the insurer and insurance producer communities, and insurance purchaser groups.
    - The NIMA system expands the burdens currently imposed on the surplus lines community, and the private sector remains steadfastly opposed.
  - Despite assurances made last year to the contrary, the complex NIMA system will not be operational by July 2011 and is unlikely to be completed in the foreseeable future.