



**December 5, 1994**

**BULLETIN #672**

**RE: CALIFORNIA DEPARTMENT OF INSURANCE BULLETIN #94-13 REGARDING  
SENATE BILL 959**

Attached is the above referenced Bulletin #94-13 regarding Senate Bill 959. As this bill will become effective January 1, 1995, it is recommended Members thoroughly familiarize themselves with the contents of Bulletin #94-13 and its immediate impact on current filing requirements and procedures.

Should you have questions or concerns, please contact the SLA office at 415-434-4900. Thank you.

James S. Pugh  
Assistant Manager  
JSP/ljl

**Attachments**

STATE OF CALIFORNIA  
DEPARTMENT OF INSURANCE  
45 FREMONT STREET  
SAN FRANCISCO, CA 94105

December 2, 1994

**Bulletin No. 94-13**

**TO:** All Surplus Line Brokers, Insurance Producers & Other Interested Persons **SUBJECT:** New Surplus Line Insurance Law

Senate Bill 959, the latest in a series of legislative changes intended to curb fraud and abuse in the surplus line market, has been approved by the Governor and will take effect on January 1, 1995. The purpose of this bulletin is to highlight the significant provisions of this new legislation and to give guidance to the surplus line industry on how to comply with this new law.

**Consumer Disclosure Statement Revisions**

Existing law, as set forth in §1764.1 of the California Insurance Code, requires every policy issued by nonadmitted insurer to contain a specified disclosure statement in bold face, 16-point type on the front page of the policy. Additionally, every surplus line broker must ensure that the signature of the applicant is obtained on a free-standing disclosure statement containing the same mandatory language as is required on the front page of the policy.

SB 959 changes the Consumer Disclosure requirements as follows. First, the text of the mandatory disclosure statement has been slightly modified to require the insertion of a toll-free telephone number for the Department of Insurance. Until further notice, the telephone number to be inserted into the required disclosure statement is 1-800-927-4357.

Second, the mandatory disclosure statement must be printed in 16-point type in both English and in the language principally used by the surplus line broker and the nonadmitted insurer to advertise, solicit or negotiate the sale and purchase of surplus line insurance. If both language versions of the disclosure statement cannot be printed on a single page, then use 2 disclosure statements; one printed with the full text in English and one with the full text in the other language. In such instances, both versions must be affixed to the front of the policy and each version must be presented to, and signed by, the applicant.

Finally, §1764.1 has been amended to require that each surplus line broker maintain a copy of the signed disclosure statements in his or her records for a period of at least five (5)

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years. These records must be made available to the Commissioner and the insured upon request. Prior Approval of Surplus Line Insurers

For the first time in the history of surplus line regulation in California, the Insurance Commissioner has been given statutory authority to approve the eligibility of surplus line insurers before those insurers conduct surplus line business in California. This authority to restrict entry into the surplus line marketplace is considered to be essential to the protection of consumers from financially unstable or fraudulent nonadmitted insurers.

### **Creation of a List of Eligible Surplus Line Insurers**

SB 959 requires the Commissioner to establish a list of all surplus line insurers that have met the eligibility requirements set forth in the new §1765.1 (a) through (e). Surplus line brokers are prohibited...from making placements with any nonadmitted insurer that has not been placed on the list of eligible surplus line insurers.

The Commissioner must publish the master list of eligible surplus line insurers at least twice a year. Until further notice, the Department intends to publish the master list on June 30th and December 31st of each year. Insurers that receive eligibility approval in the interim will be added by addendum to the list at the time of approval. Addenda to the list will be provided to, and available from, The Surplus Line Association of California.

### **Eligibility Requirements**

The eligibility requirements for surplus line insurers are substantially the same as the requirements set forth in existing California Code of Regulations section 2174. 1. One significant difference is that, unlike Regulation 2174. 1, SB 959 does not provide specific exemptions from the \$15 million minimum capital and surplus requirement for insurers that are serving unique or specialized markets or which are providing unique or specialized coverages. SB 959 permits, but does not require, the Commissioner to consider the eligibility of any surplus line insurer that does not have the requisite minimum capital and surplus of \$15 million. In order for the Commissioner to affirmatively find that an insurer with less than \$15 million in capital and surplus is adequate to protect California policyholders, the Commissioner will consider factors such as quality and integrity of the company and its management, the capital and surplus of any parent company, the underwriting profit and investment income trends, and the record of claims payment and claims handling practices of the nonadmitted insurer.

To be considered for placement on the initial list of eligible surplus line insurers, the nonadmitted insurer must submit, through a surplus line broker, the documents specified in §1765.1 (c). The documents to be provided to the Commissioner are the same documents

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that are currently required for an initial submission under Regulation 2174. 1. These include: 1. a copy of an annual statement not more than 12 months old 2. a copy of an audited financial report showing the insurer's condition as of a date not more than 12 months prior to submission 3. a certified copy of the trust agreement for alien insurers including a verified copy of the most recent quarterly statement or list of assets in the trust 4. a certified copy of the insurer's license including a certificate of good standing, certificate of compliance or other equivalent certificate 5. identification of the insurer's agent in California for service of process 6. the complete street address, mailing address, and telephone number of the insurer's principal place of business 7. a certified or verified explanation, report or other statement from the insurance regulatory office of the insurer's domiciliary jurisdiction concerning the insurer's record regarding market conduct and consumer complaints 8. a verified statement from the insurer or surplus line broker regarding any currently known regulatory actions pending against the insurer.

For an alien insurer, in lieu of an annual statement, the surplus line broker may submit Department Form B and Department Form C which are identified as Appendix B and Appendix C to existing Regulation 2174. 1. Letters of credit used to fund the U.S. trust account for alien insurers should continue to conform to the format set forth in Appendix D to existing Regulation 2174. 1.

### **Filing Fees and Updates**

The documents required by §1765.1 (c) must be submitted to the Commissioner in the manner set forth in Regulation 2174.4 (d). A filing fee of \$1,500.00 must accompany the documents. Once the insurer is placed on the list of eligible surplus line insurers, the insurer must submit to the Commissioner, through a surplus line broker, updated information as set forth in the existing Regulation 2174.4 (b). The filing fees for updated documents are the same as set forth in the existing Regulation 2174.4 (b) (3).

The new §1765.1 (i) requires at least annually, the submission of records and statements as are reasonably necessary to ensure that the requirements of §1765.1 are maintained. Pending further notice, the Department will continue to require an annual submission of updates of the documents set forth in §1765.1 (c) as listed and described in items 1 through 8 above.

The annual submission of these required documents must be accompanied by a filing fee in the amount of \$1500.00.

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### **Form A Filing Requirement**

Surplus line brokers are permitted to make placements with any insurer appearing on the list of eligible surplus line insurers. The Form A filing required under Regulation 2174.1 will not be required when making a placement with an insurer appearing on the list of eligible surplus line insurers established pursuant to SB 959.

### **GAP Exemption**

Section 1765.1 (k) permits insurance to be placed, on a limited basis, with insurers not appearing on the list of eligible surplus line insurers if certain conditions are met as follows:

#### **Placement Conditions:**

1. Multiple insurers are needed to obtain coverage for 100% of the risk. 2. Eighty per cent (80%) of the risk is placed with listed or admitted insurers. 3. Unlisted insurers do not represent a disproportionate portion of the lower layers of coverage. 4. Within thirty (30) days of placement and annually thereafter, the placing broker must submit to the Commissioner copies of all documentation that the broker relied upon to determine that the financial stability, reputation and integrity of the company was adequate to safeguard the interest of the insured. The documentation should be sent to the California Department of Insurance at the following address:

45 Fremont Street, 24th Floor  
San Francisco, Cal. 94105  
Attention: Surplus Line Enforcement Unit Gap Exemption

#### **Requirements For The Insured:**

1. The insured must be a sophisticated insurance purchaser. 2. The insured must have annual aggregate insurance premiums, excluding workers compensation and health insurance, totalling at least \$100,000. 3. The insured cannot be a multiple employer welfare arrangement as defined in §1002 (40) (A) of Title 29 of the United States Code, or any other arrangement among two or more employers that are not under common ownership or control, which is established or maintained for the primary purpose of providing insurance benefits to the employees or two or more employers.

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**Security Requirements:**

1. The nonadmitted insurer must demonstrate financial stability, reputation, and integrity. 2. The nonadmitted insurer must not have been previously objected to, removed from the eligibility list or denied placement on the list.

**Coverage Limitation:**

1. Unlisted insurers cannot be used if the coverage includes employer-sponsored health insurance or insurance mandated by government.

**Revised Report of Surplus Line Placement- [Form SL-1(REV.11/94)]**

The SL-1 form has been revised to capture information regarding placements made with Gap Exemption insurers. A copy of the revised SL-1 is attached to this bulletin.

The revised SL-1 must be used to report any placements made on or after January 1, 1995. Transition for Insurers Presently Listed under Regulation 2174.1 Insurers listed under Regulation 2174.1 must file for approval to be placed on the eligibility list established pursuant to SB 959. 2174.1 listed insurers are not grandfathered, nor otherwise guaranteed approval, under SB 959.

However, to facilitate the transition from the file and use system under Regulation 2174.1 to a prior approval system, SB 959 provides that any insurer authorized under Regulation 2174.1 as of December 31, 1994 need not file for approval under SB 959 until the first annual expiration of their listing after January 1, 1995. For example, if an insurer is placed on the listing of filings under Regulation 2174.1 on December 31, 1994, then that insurer's filing will expire on December 31, 1995. That insurer would not be required to be approved as an eligible surplus line insurer under SB 959 until December 31, 1995.

Thus, during 1995, two(2) lists of authorized surplus line insurers will exist: 1) insurers appearing on the 2174.1 Listing of Filings and; 2) those insurers approved under SB 959 and placed on the eligible list of surplus line insurers. Any surplus line broker proposing to place business with an insurer which is listed under Regulation 2174.1 must continue to comply with the Form A filing requirement as set forth in Regulation 2174.4 (c) (2).

The Department encourages 2174.1 listed insurers to file for approval under SB 959 as soon as possible to give the Department adequate time to evaluate, and act upon, the SB 959 filing before the insurer's 2174.1 listing expires. The Department suggests that 2174.1

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insurers consider renewing their 2174.1 filing in December, 1994 and thereby extend their surplus line authority thru December, 1995.

Additionally, if so requested by the submitting surplus line broker, the Department will accept the 2174.1 renewal submission as a filing for approval under SB 959. Thus, with one submission and one \$1,500 filing fee, an insurer can renew its 2174.1 listing thru December, 1995 and also file for approval under SB 959. All 2174.1 renewals received in December, 1994, that are in substantial compliance with Regulation 2174. 1, will be placed on the 2174.1 listing of filings with an expiration date of December 31, 1995. Submissions that also request approval under SB 959 will be handled on a first come, first serve basis.

Please note, however, that the above offer DOES NOT apply to any insurer that is listed under 2174.1 with an exemption approval. Those insurers may continue to accept appropriate surplus line placements until the expiration of their 2174.1 listing as shown on the Listing of Filings as of December 31, 1994. To extend their surplus line authority beyond the 2174.1 expiration date, the insurer must qualify as an eligible surplus line insurer under SB 959. Mexican

## Insurance

Insurance issued by a nonadmitted Mexican insurer affording coverage exclusively in the Republic of Mexico on property located in, or operations conducted within the Republic of Mexico, are exempt from the diligent search and disclosure statement requirements set forth in §§1763 and 1764.1, respectively. Additionally, placements made with an insurer domiciled in Republic of Mexico providing coverage for liability arising out of the ownership, maintenance, or use of a motor vehicle, aircraft or boat in the Republic of Mexico are exempt from the surplus line insurer eligibility requirements set forth in §1765.1.

Insurer Responsibility For Premiums Collected Section 1766 has been added to the Insurance Code. This section provides that payment of premium to the surplus line broker shall be deemed to be payment to the insurer.

### **Service of Suit**

Section 1772 has also been added to the Insurance Code. This section provides that surplus line insurers may be sued in California courts for any cause of action arising in this state under an insurance policy issued by it, or upon any evidence of insurance issued or delivered by the surplus line broker.

The substance of Section 1772 must be included in any policy or evidence of insurance issued by the insurer or the surplus line broker. The policy and evidence of insurance must designate the person to whom the Commissioner shall mail service of process.

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### **Civil and Criminal Penalties**

SB 959 expands the list of Insurance Code sections for which criminal penalties may be imposed. Nearly all provisions of the surplus line law are now punishable by imprisonment in state prison for one year and/or a fine not exceeding \$10,000.

### **Conclusion**

Thousands of insurance consumers in this state have been victimized by con artists who exploited a weak regulatory environment and a marketplace in which certain types of insurance were either unavailable or unaffordable. The Department of Insurance, the State Legislature, and reputable members of the surplus line industry have worked diligently during the past four years to root out the fraud element and to strengthen surplus line laws and enforcement. The results of that effort have been extremely successful.

SB 959 offers an opportunity to build on that success by establishing a fair and stable surplus line marketplace. Industry cooperation and compliance is essential.

Questions regarding this bulletin should be addressed to the following:

State of California  
Department of Insurance  
45 Fremont Street  
San Francisco, CA 94105  
Attn: Surplus Line Enforcement Unit

JOHN GARAMENDI  
Insurance Commissioner

CONFIDENTIAL  
REPORT OF SURPLUS LINE PLACEMENT

Please refer to the instructions on Page 3. This form must be accompanied by a diligent search report and a copy of the declarations page or certificate or binder. (California Insurance Code Section 1763(a))

1. \_\_\_\_\_ hereby submits that he/she is:  
(A) A duly licensed surplus line broker, license number \_\_\_\_\_  
or (B) A transactor on the surplus line license of \_\_\_\_\_  
(Name of Organization)  
\_\_\_\_\_, license number \_\_\_\_\_

and (C) that he/she or said organizational licensee was engaged by the insured, or the insured's broker, named herein, to obtain insurance against certain risk as described in this report.

## 2. RISK DESCRIPTION

(A) Name of Insured \_\_\_\_\_  
(B) Address of Insured \_\_\_\_\_  
(Street and Number)  
\_\_\_\_\_  
(City) (State) (Zip Code)  
(C) Description of the Risk \_\_\_\_\_  
(e.g. Laundromat, Liquor store, NOT TYPE OF COVERAGE)  
(D) Location of the Risk \_\_\_\_\_  
(Street and Number)

\_\_\_\_\_  
(City) (State) (Zip Code)  
(E) Type of Insurance coverage \_\_\_\_\_  
(Enter Appropriate Code Number - See Codes on Page 3)

## 3. PLACEMENT DESCRIPTION

(A) Policy Number \_\_\_\_\_  
(B) Policy Premium \$ \_\_\_\_\_

(C) List Nonadmitted Insurer(s) Underwriting This Policy.  
NAME OF NONADMITTED INSURER(S) PERCENTAGE OF PREMIUM

\_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_

(Include an attachment if additional space is needed or  
attach a lines lineslip  
SL-1 (REV.11/94)

Unconfidential Report

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## 4. GAP EXEMPTION

Complete this section only if one or more of the nonadmitted insurer(s) listed in 3(C) is not currently approved in California. (See-page 4 for the Gap Exemption placement conditions and requirements)

(A) Total limits of Coverage Placed for  
This Risk as Described in Item 2 \$ \_\_\_\_\_  
(B) List Gap Insurer(s) Underwriting This Policy.

GAP INSURER(S) PERCENTAGE OF  
TOTAL COVERAGE

_____	_____
_____	_____
_____	_____
_____	_____
_____	_____

(Include an attachment if additional space is needed)

(C) Is this a layered risk? Yes \_\_\_\_\_ No \_\_\_\_\_

(D) How many layers make up this risk? \_\_\_\_\_

(E) Which layer of the risk is this policy?  
(i.e. 1st layer, 2nd layer..)

\_\_\_\_\_  
SIGNATURE OF PERSON NAMED ON LINE 1 DATE

SL-1 ~(REV.11/94)

**Confidential Report**

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**INSTRUCTIONS**

**WHAT MUST ACCOMPANY THE REPORT:** This report must be accompanied by a copy of the declarations page or certificate or binder, and a diligent search report Form SL-2. Note: The surplus line broker submitting this form is responsible to ensure that a diligent search is made among admitted insurers and that the risk meets the conditions for surplus line exportation. (California Insurance Code 1763 (a).)

**WHEN TO FILE:** This report must be filed by the surplus line broker withip 60 days of placing the insurance with a nonadmitted insurer. (California Insurance Code (1763(a).)

**WHERE TO FILE:** This report must be submitted to The Surplus Line Association of California as designee for the California Insurance Commissioner.

**LOWER RATE FILINGS:** This report may not be used to file a risk placed with a nonadmitted insurer when such insurance is procured at a lower rate of premium or lower premium than the lowest rate or premium available from an admitted insurer. Please contact the Department of Insurance or The Surplus Line Association of California for information regarding the procedures applicable to such "lower rate" filings.

CODE TYPE OF INSURANCE CODE TYPE OF INSURANCE

- 050 Auto Liability-Private 510 Aviation
- 051 Auto Liability-Commercial 550 Errors & Omissions - All others
- 100 Auto Physical Damage
- Private 551 Errors & Omissions - Dir. & off.
- 101 Auto Physical Damage
- Commercial. 600 Malpractice - All Other

150 Crime 606 Malpractice - Hospitals  
151 Crime-Kidnap & Ransom 650 Miscellaneous  
200 Combined Auto  
-Liability & P.D  
-Private 651 Miscellaneous - Glass  
201 Combined Auto  
-Liab & P.D.-Comm 652 Miscellaneous - Boiler & Machinery  
300 Excess Liability  
(Incl. Umb.) 653 Miscellaneous - Nuclear Risks  
350 Fidelity, Surety & Bonds  
- Bonds 655 Miscellaneous - Political Risks  
351 Fidelity, Surety Bonds  
- Fidelity 700 Accident  
400 Fire-Sgl Fam. Dwelling,  
Duplex 701 Accident - Disability Income  
401 Fire - Commercial 702 Accident - Group Health Insurance  
402 Fire - Homeowners 703 Accident - Individual Health Ins.  
403 Fire - Homeowners  
- Multiple Peril 800 Garage Liability  
404 Fire - Farm owners  
- Multiple Peril 980 Excess Workers Compensation  
450 Inland Marine 990 Commercial Property - All Risk  
500 General Liability 994 Commercial Property - Sp. M. Peril  
501 Gen. Liability  
- Pollution  
Legal Liability 996 Commercial Property - DIC  
502 General Liability  
- Product Tampering 997 Commercial Property - Earthquake

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**GAP EXEMPTION PLACEMENT CONDITIONS/REQUIREMENTS (California Insurance Code Section 1765.1(k))**

**Placement Conditions:**

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2. Eighty percent (80%) of the risk is placed with listed or admitted insurers.
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4. Within thirty (30) OF placement, and annually thereafter, the placing broker must submit to the Commissioner copies of all documentation that the broker relied upon to determine that the financial stability, reputation and integrity of the company was adequate to safeguard the interest of the insured. The documentation should be sent to the California Department of Insurance at the following address:

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Attention: Surplus Line Enforcement Unit

**GAP EXEMPTION**



**Requirements For The Insured:**

1. The insured must be a sophisticated insurance purchaser.
2. The insured must have annual premiums, excluding workers compensation and health ~insurance, totalling at least \$100,000.
3. The insured cannot be a multiple employee welfare arrangement as defined in 1002 (40) (A) of Title 29 of the United States Code, or any other arrangement among two or more employers that are not under common ownership or control, which is established or maintained for the primary purpose of providing insurance benefits to the employees or two or more employers.

**Security Requirements:**

The nonadmitted insurer must demonstrate financial stability, reputation, and integrity. The nonadmitted insurer must not have been previously objected to, removed from the eligibility list or denied placement on the list. Coverage Limitation: Unlisted insurers cannot be used if the coverage includes employer-sponsored health insurance or insurance mandated by government. SLA (REV. 11/94)