



The Surplus Line
Association of California

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**RE: California Surplus Lines Stamping Fee Changes to 0.25% on
January 1, 2020**

The Board of Directors of the Surplus Line Association (SLA) of California has voted to adjust the stamping fee to 0.25%, effective January 1, 2020. Starting December 1, 2012, the stamping fee has been set at 0.2% for seven years and one month, the longest recorded period of time that the SLA has gone without changing the stamping fee.

Aside from modest returns on conservative investments, the stamping fee is the sole source of revenue for the SLA, a 501(c)6 non-profit association. These revenues fund all SLA operations, including a Data Analysis Department that reviews approximately 800,000 surplus lines filings annually on behalf of the California Department of Insurance (CDI). As the appointed surplus lines advisory organization for the CDI, the SLA is responsible for thoroughly reviewing **every** surplus lines policy filed in the State of California to ensure compliance with all applicable laws and regulations. It also reviews out-of-state insurers for solvency to ensure policies are placed with companies that can pay claims, helps brokers comply with all applicable laws and regulations, provides free continuing education courses, and advocates for a healthy, fair and competitive surplus lines marketplace.

“We did not take this action lightly,” said Robert Gilbert, chair of the SLA Board of Directors. “We know that a change in the stamping fee is a cost and an inconvenience for policyholders, as well as our members and their employees who file surplus lines policies with the SLA. In fact, our members have told us that they prefer no change at all, whether it is an increase or a decrease, because the clerical adjustments create extra work and system changes can be confusing. That is why we kept the stamping fee constant for seven years. We did this by focusing on expenses, including moving our offices, which saved over \$800,000 a year. However, the increasing costs associated with a rapidly growing marketplace, as well as the need to address a large pension liability, made it necessary to raise the stamping fee at this time. We set the effective

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date for January 1, 2020, to give our members plenty of time to make the necessary adjustments.”

The speedy and massive growth of the surplus lines industry in recent years has meant significantly more work, and therefore more monetary costs, for the SLA. In 2012, the last year the SLA changed the stamping fee, the association reviewed and processed 471,319 policies the entire year. By 2018, that number had increased to 687,194. In 2019, the SLA has processed 325,952 policies in just the first four months of the year. The overwhelming majority of these policies (94.3%) cost more to process than the SLA receives in stamping fees from those policies.

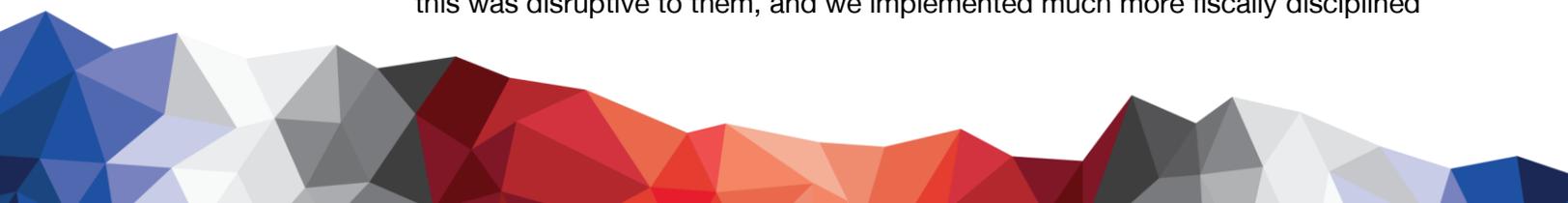
“The share of commercial insurance premiums going into surplus lines in California has risen from about 7 percent a decade ago to approximately 18 percent today, and this has fueled a dramatic growth in policies for us to analyze,” said Benjamin J. McKay, the SLA’s CEO and executive director. “To keep up with the marketplace growth, we have had to significantly increase hiring in our department that reviews these policies and ensures they are in compliance with all the pertinent laws and regulations governing surplus lines in California.”

Also looming large in the board’s decision is the need to retire the SLA’s pension liability. The SLA phased out its pension in 2011 in favor of a 401(k) program, but employees covered under the pension plan prior to then are eligible for lifelong benefits upon retirement. The SLA has received numerous estimates indicating that annuitizing the pension—thereby taking it off the SLA’s books—will cost approximately \$15 million. With the carrying costs of the pension quadrupling from about \$140,000 to \$560,000 a year, maintaining the pension has become a significant annual material cost to the SLA.

“Fiscal responsibility dictates that eliminating this liability is the smart thing to do,” McKay said. “In addition to our retirees, we have a number of current employees who are eligible to draw pension funds when they retire, which is still decades down the road for some of them. By earmarking a portion of the added stamping fee revenues for retiring this liability, we are putting our fiscal house in order.”

McKay notes that the SLA promised its members it would keep the stamping fee unchanged for at least five years. It has more than fulfilled that promise by going seven years without a change.

“We used to raise the stamping fee whenever it was necessary to meet a budget shortfall, and then lower it when we had raised the revenue we needed,” said McKay, who has led the SLA since 2012. “This happened almost every year or two, and sometimes even twice a year. In listening to our members, we realized this was disruptive to them, and we implemented much more fiscally disciplined



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budgeting to keep the stamping fee steady. When we have raised more revenues than needed, we have put the balance aside and used it to smooth our budget when we faced shortfalls or higher-than-expected expenses. While we will continue this practice, we know that we cannot not keep the stamping fee at 0.2% and also pay off the pension or accommodate our continued growth. The modest increase to 0.25% will enable us to do both of these things.”

The 0.25% stamping fee—which amounts to \$1 in revenue for the SLA for every \$400 it processes in premiums—is below the midpoint (0.3%) of the SLA’s stamping fee variance since 1977, and very close to the mean (0.24%) during that time. The lowest stamping fee for the SLA over the last 42 years was 0.1% over a four-year period from January 1, 1987 to December 31, 1990, while the highest was 0.5% over a two-year period from January 1, 1994 to December 31, 1995.

After several months of discussions, and a careful review of pro forma budgets and market forecasts, Gilbert said the board and SLA management agreed that the time was right to make this change.

“We wanted to do this while the economy and the surplus lines marketplace were booming,” Gilbert said. “The worst time to raise the stamping fee is when the economy is stagnant or in a recession, or when business is in a down cycle. By raising it now, when times are good, we avoid exacerbating the pain by raising it when times are not as good. If and when a downturn comes, this action will have placed the SLA on a sound fiscal footing, so that it can continue to do its part in promoting a healthy, fair and competitive surplus lines marketplace in California.”

