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Bulletin 457

Surplus Lines Eligibility for Property Insurance

Placement of Insurance in Surplus Lines Market
(Supersedes Bulletins 328, 414, and 439)

This Bulletin replaces Bulletins 328, 414, and 439. It explains the conditions under which a risk may be placed in the surplus lines market, addresses a 2019 change to the Maine Insurance Code which allows disability insurance to be placed in surplus lines subject to the statutory requirements outlined in this Bulletin, and clarifies when surplus lines coverage is appropriate for property insurance.[1]

Producers should keep in mind, as a matter of professional competence,[2] that placing coverage in surplus lines should always be the exception, not the rule. The Bureau of Insurance does not license surplus lines carriers. These carriers are exempt from most of the Insurance Code's consumer protections, and do not participate in the guaranty associations that protect policyholders if an insurer becomes insolvent. The Insurance Code provides clear rules for producers to follow in determining whether to place coverage in surplus lines:

- Life insurance, health insurance (except disability insurance), and employee benefit excess ("stop-loss") insurance;[3] reinsurance;[4] and workers' compensation[5] insurance may not go into surplus lines.

- Motor vehicle insurance should not generally go into surplus lines because an assigned risk market is available.[6]

[1] P.L. 2019, Ch. 20 (L.D. 260), effective April 5, 2019, *amending* 24-A M.R.S. § 2002-A(1)(B).
[2] 24-A M.R.S. § 1420-K(1)(H).
[3] 24-A M.R.S. § 2002-A(1).
[4] 24-A M.R.S. § 2002-A(2).
[5] 39-A M.R.S. § 102(14).
[6] 24-A M.R.S. § 2325.

For other risks, the following conditions apply:

- The insurance must be procured through a licensed producer with surplus lines authority.

- The coverage must be necessary for the adequate protection of a risk in this state. This requires the producer to review the needs of the particular risk. If adequate protection is available in the admitted market, then the producer may not place the risk in the surplus lines market.

- The coverage must be one that an authorized insurer may write.

- The producer must have made a diligent effort to place the coverage with authorized insurers.[7] This is not a mechanical exercise. Therefore, doing a specific number of inquiries does not mean that the producer has fulfilled this requirement. Rather, this is a function of many variables, including for example the type of insurance sought and the coverage limits needed. The diligent effort requirement does not end when coverage is placed in surplus lines. At renewal, the producer should investigate whether circumstances exist, such as improved loss history or improved market conditions, which favor returning the risk to the admitted market.

These conditions are cumulative; therefore, all of them must be met before the risk may be placed outside of the admitted market.

Other considerations apply to the decision to place coverage in surplus lines:

- Surplus lines coverage is often more expensive than comparable coverage in the admitted market. However, sometimes a surplus lines insurer might offer similar coverage terms at a lower premium than an authorized insurer would. This is not a reason to place the risk in the surplus lines market.

- A producer may not place a risk in the surplus market if the desired coverage exists in the admitted market. The test under Section 2004 is whether admitted coverage is available to the insured, not whether it is available to a particular producer. An admitted carrier's decision not to deal with a producer does not give that producer preferential access to the surplus lines market.

- For property risks, the use of surplus lines might be appropriate when a certain level of coverage is available in the admitted market but more extensive coverage is needed to protect the financial interests of the property owner. For example, if the admitted market offers only actual cash value coverage for valuable equipment and the prospective insured needs more extensive protection—such as replacement cost or enhanced

[7] 24-A M.R.S. § 2004. Producers may place some coverages in surplus lines without adhering to the diligent effort requirement. These coverages are wet marine and transportation insurance, insurance on out-of-state risks, and insurance on interstate railroad and aircraft operations. *See* 24-A M.R.S. § 2002-A(3) for more details. Liability insurance purchased through a risk purchasing group is also exempt from this requirement. See the Maine Liability Risk Retention Act, 24-A M.R.S. §§ 6091–6104. Last, the Nonadmitted and Reinsurance Reform Act of 2010 ("NRRA") exempts placement of coverage for exempt commercial purchasers under some circumstances. *See* Bulletin 378, Changes to the Nonadmitted Insurance Laws, for more information.

replacement cost coverage—and a diligent effort to find that coverage on the admitted market has been unsuccessful, then Section 2004(2) would permit export to surplus lines. In this case, Section 2004 would allow a surplus lines insurer to provide the entire coverage, not just the coverage enhancements.

- The desired coverage must be in a line of business that an authorized insurer may lawfully write. The producer must make a diligent effort to place the coverage in that market. If the producer does not have appointments with any insurers that offer the desired coverage, and wishes to compete for the account, the first step to fulfill the diligent effort requirement must be to seek the necessary appointment or to place the coverage through an appointed producer.

- The admitted market is available even if a producer is blocked from placing an account with an authorized insurer because the account has a relationship with that insurer. In such cases, unless the requirements of Section 2004 are otherwise met, the coverage must remain in the admitted market, and the producer must obtain a broker of record letter in order to represent that account. A potential client's reluctance to sign a broker of record letter does not make admitted market coverage unavailable.

- The admitted market is available even if a producer loses its appointment with the authorized insurer, and the insurer is willing or, as in the case of personal property and casualty coverage, required to retain the insured. Bulletin 391, Personal Lines Agency Terminations and Book Rollovers, explains how producers and insurers should handle these terminations.

- Producers may place disability insurance coverage in surplus lines, subject to the same restrictions that apply to all other surplus lines placements. Producers should seek admitted market coverage and, if necessary, may look to surplus lines carriers for coverage in excess of that provided by the admitted market. Only in the case of a risk that will not be written by admitted market carriers (*e.g.*, due to the insured's profession) may a producer place the entire risk into surplus lines.

Last, the Superintendent reminds producers of other matters relevant to the surplus lines market:

- If the Superintendent determines, after a hearing, that a line does not have a reasonable or adequate market, the Superintendent may issue an order exempting that line from the diligent search requirement.[8] As of the date of this Bulletin, no lines are declared eligible for surplus lines placement ("eligible for export") by order of the Superintendent.

- Although surplus lines insurers are, by definition, not licensed in Maine, they do need to be eligible under the surplus lines law.[9] The status of eligibility is not a license to transact insurance in Maine. Eligibility indicates that the insurer appears to be sound financially and to have satisfactory claims practices, and that the Superintendent has no credible evidence to the contrary. A producer may not knowingly place surplus lines insurance with a financially unsound or ineligible insurer. A current list of eligible surplus lines insurers is available through the Bureau's license portal at https://www.maine.gov/pfr/insurance/licensee_search.html.

[8] 24-A M.R.S. § 2006.
[9] 24-A M.R.S. § 2007.

- Upon placing surplus lines coverage through a producer with surplus lines authority, a producer must promptly issue and deliver evidence of the insurance to the insured: either the policy issued by the insurer or, if the policy is not available, the surplus lines producer's certificate.[10]

- Each surplus lines policy must display the name of the surplus lines producer who procured the policy and the following notice:

  > This insurance contract is issued pursuant to the Maine Insurance Laws by an insurer neither licensed by nor under the jurisdiction of the Maine Bureau of Insurance.[11]

  The Superintendent interprets this in part to be a warning to the policyholder that the insurer does not participate in MIGA and that, should the surplus lines insurer become insolvent, MIGA will not pay the insurer's losses.

- Producers must keep "a full and true record" of each of their surplus lines placements.[12] [12]Paragraphs 2015(1)(A) through (H) list specific items that the record must include. Paragraph 2015(1)(I) allows the Superintendent to require other information. As of the date of this Bulletin, the Superintendent expects producers also to document thoroughly the basis for each surplus lines placement, including renewals of existing policies. The record should explain how the placement qualifies for export under Section 2004.

- Surplus lines producers must keep monthly reports of their surplus lines transactions. Producers must keep these reports in their offices and provide them upon the Superintendent's request.[13]

- Surplus lines premiums are subject to a 3% premium tax. The surplus lines producer is responsible for remitting this tax to Maine Revenue Services.[14] More information regarding this tax and the applicable procedures and forms is available directly from Maine Revenue Services at this link: http://www.state.me.us/revenue/.

The Superintendent expects that producers will comply with the Surplus Lines Law and the standards announced in this Bulletin. Any producer who has moved coverage from the admitted market to surplus lines should review carefully – and thoroughly document its review – whether the coverage should return to the admitted market at the policy's next renewal. Producers who fail to do so may be subject to disciplinary action.

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NOTE: This Bulletin is intended solely for informational purposes. It is not intended to set forth legal rights, duties, or privileges, nor is it intended to provide legal advice. Readers should consult applicable statutes and rules and contact the Bureau of Insurance if additional information is needed.

[10] 24-A M.R.S. § 2008.
[11] 24-A M.R.S. § 2009.
[12] 24-A M.R.S. § 2015.
[13] 24-A M.R.S. § 2016.
[14] 36 M.R.S. § 2531(2).