Update on the Surplus Lines Market in Louisiana

This month I'd like to focus on one of the bright spots in insurance right now - the surplus lines market. In addition to being in a sound financial position, the market is keeping pace with the latest technologies and innovations. As regulators, it is our responsibility to also adapt to emerging trends and foster the continued growth of this market.

Surplus lines reported profitable results in 2014, including favorable reserve development, and it marked the second consecutive year of underwriting profits following three years of underwriting losses. 2014 surplus lines direct premiums were reported at just over $40 billion - approximately seven percent of total P&C direct premiums written – the highest direct premium in its history. With $1.44 billion in surplus lines premium, Louisiana ranked sixth nationally in writings in 2014. A special report issued last month by A.M Best – "Surplus Lines Profit from Underwriting Discipline and Core Competencies" - illustrates how surplus lines insurers have continued the momentum of the previous two years. According to the report, results have been driven by a combination of product diversification, underwriting discipline, and advantageous market conditions.

One factor touched on in the A.M. Best Report is the impact of the National Association of Registered Agents and Brokers Act of 2015 (NARAB II) which was signed into law in January 2015. The Act establishes a national clearinghouse that aims to streamline market access for nonresident insurance producers – and reduce the cost of compliance. The market view is that NARAB II will improve productivity, making it more efficient for agents and brokers to conduct business.

An attribute of the surplus lines market is innovation and the creation of solutions to address emerging risks. Cyber liability coverage is an example of this and is filling the need for an up-and-coming growth product. It's not that cyber liability is a new threat but with high profile attacks such as those on Target and Anthem more and more businesses are now realizing that if they were victims of such an attack, it could be quite costly. As Excess and Surplus carriers see some of their first sizable claims – they are getting a better understanding of cyber risk and what their appetite is for such risk.

Another new and developing area addressed by Surplus Lines is the growth of Transportation Network Companies such as Uber. For example, California has been at the forefront of the Transportation Network Company (or TNC) trend. The director of the California Surplus Lines Association has said that commercial auto liability coverage was up more than 112 percent in 2014, due in large part to companies like Uber and Lyft taking out state-mandated commercial policies to cover their drivers.

Here in Louisiana, the Legislature passed Act 266, called the Transportation Network Company Motor Vehicle Responsibility Law. It was based on a compromise model bill that was supported by the American Insurance Association (AIA), the Property and Casualty Insurers Association of

America (PCIAA), several major insurers as well as the transportation network companies. It establishes insurance guidelines for ridesharing companies and their drivers. The law also states that insurers writing auto insurance in Louisiana may exclude any or all coverage under a policy issued to a driver who is logged onto a TNC network.

Legislatively, we have also made some changes that impact the surplus lines market. Act 386 authorized Louisiana's withdrawal from participation in the Non-Admitted Insurance Multi-State Agreement (NIMA) effective October 1. We issued Bulletin 2015-06 this summer which provides guidance for calculating, reporting and paying surplus lines taxes as a consequence of Louisiana's withdrawal from NIMA and the reduction of the surplus lines tax rate from 5 percent to 4.85 percent.

Act 386 also exempts universities managed by a system board of supervisors (i.e. LSU, Southern, University of Louisiana and the Louisiana Community and Technical College) from the tax on surplus lines insurance. It also exempts political subdivisions with a population of more than 350,000 from this tax. According to the U.S. Census, only East Baton Rouge and Jefferson Parish meet the population requirement.

As of October 1 there are also several changes to surplus line reporting. In the past, surplus lines brokers have been required to submit quarterly surplus lines tax reports even when there is nothing to report. For many non-Louisiana and some Louisiana brokers, there is no Louisiana home state surplus lines premium to report for an entire calendar year. Act 386 eases the reporting burden on brokers, no longer requiring a quarterly reports, or "zero reports," for any quarter in which a broker does no Louisiana business. A surplus lines broker is required to file at least an annual report by March 1st certifying the reporting of all business done - or the absence of any business during the preceding calendar year.

And lastly, Act 193 created the new category of *domestic surplus lines insurer* who is authorized to write any type of insurance in Louisiana that may be placed with a surplus line carrier. The idea was pioneered in Illinois in the 1990s. It has also been adopted in Oklahoma, Arkansas, Montana, North Dakota, New Hampshire, New Jersey and Delaware.

As the surplus lines market adapts to developing issues, regulators will keep responding in ways that encourage innovation and growth. Particularly in hard markets, the surplus lines market clearly is a prosperous area in the insurance industry. And as emerging risks and exposures drive up the need for innovative solutions, the surplus lines market will continue to grow in importance.