



National Association of Professional Surplus Lines Offices, Ltd.

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Richard M. Bouhan
Executive Director

September 16, 2010

The Honorable James J. Donelon
Louisiana Department of Insurance
P.O. Box 94214
Baton Rouge, LA 70804-9214

Dear Commissioner Donelon:

In response to the request for comments made on the September 13, 2010 conference call of the Surplus Lines Implementation Task Force, the National Association of Professional Surplus Lines Offices (NAPSLO) and the American Association of Managing General Agents (AAMGA) would like to comment on the process of compact creation and the SLIMPACT proposal. This response also addresses the request for the delineation between the International Fuel Tax Agreement (IFTA) and SLIMPACT.

Proper Adoption of the Compact

In response to the legislative reforms requested and provided, we believe it is essential that the tax allocation mechanism to be implemented under the Non Admitted and Reinsurance reform Act (NRRA) be properly adopted so that it can both facilitate the mandate of modernization and survive legal challenges that inevitably arise in the process of tax collection. It is well established that there needs to be a specific offer and acceptance between the state legislatures of the agreement to allocate taxes. The "Law and Use of Interstate Compacts" by Frederick L. Zimmerman and Mitchell Wendell discusses this issue at length. The offer and acceptance requirement has almost universally meant adopting a specific compact in the statutes of a state. The "Law and Use of Interstate Compacts" does acknowledge that a statute could empower a state agency to enter into a contract if the statute is so specific in terms of an agreement that it evidences an offer and acceptance.

In the case of a surplus lines tax, the enabling statute would not only have to define the specifics of an agreement but would also have to contain the tax allocation formula. Tax policy-level decisions generally must be made by the legislature. We believe it would be more difficult to construct detailed enabling legislation that includes a tax allocation formula, than it would be to adopt a straight-forward tax compact. We do not believe that the necessary offer and acceptance would exist if the state simply adopted broad enabling legislation granting state agencies the option of executing a contract for the allocation of taxes. If the agreement does not yet exist there could be no offer and acceptance. There could be no requisite meeting of the minds because there was nothing sufficiently specific to form an agreement on the part of the legislature.

IFTA Adoption Model—Not a Good Approach

During the recent conference call, a request was made for regulators and interested parties to provide additional comments on delineating the variances between the IFTA and the prospective solution SLIMPACT could provide. As noted, we do not believe the adoption of IFTA is a good model to follow for establishing a surplus lines tax compact. The needs of the marketplace in regard to surplus lines taxes is more specific and requires more than a

generalized recitation of IFTA protocols. Further, Congress compelled the states to use the exact IFTA contract. IFTA was already in existence between some states when Congress prohibited states from collecting any fuel tax from truckers unless it was pursuant to IFTA. The states were not consistent in passing the IFTA enabling legislation, but there is little doubt that they intended to enter into the IFTA. The IFTA contract was already in existence when the enabling legislation was adopted by the compacting states.

In the case of surplus lines tax we do not have the luxury of Congressional compulsion or an existing detailed clearinghouse contract between the states. To try to build a consensus on the details of a tax allocation system without knowing which states will participate, actually make it more difficult to reach an agreement. There are no bylaws, no voting process and no structure for reaching an agreement. In addition, it would mean negotiating contract specifics with a number of parties that are not members of the compact and may never become members of the compact.

In our view, the Congressional deadline of July 21, 2011 is more likely to be met by the "normal" process of compact creation which includes first identifying the states willing to join a compact. This "normal" compact procedure has a greater possibility of reaching a timely result than a process in which the states first try to agree upon all of the details of the allocation formulae and distribution process without knowing which states are actually going to participate in the compact and without the benefit of the organizational structure created by the compact bylaws.

SLIMPACT

We would also like to comment specifically about SLIMPACT. We believe that SLIMPACT is a fairly straight forward tax allocation compact, with the exception of some of the non-tax provisions contained in Article V Uniform Standards Authority. Note that the Uniform Standards Authority allows for uniformity of certain specified surplus lines regulations with a 2/3 vote. States could still opt out of a Uniform Standard adopted by the compact. These provisions would provide a forum to discuss uniformity, but because it is difficult to get a 2/3 vote and states retain the ability to opt out, the impact of provision is speculative. These provisions were included because most state surplus lines laws are similar, but minor nuances from state to state make compliance more onerous than it needs to be. The surplus lines notice is a good example of something that could be uniform. For a variety of reasons the states have minor language differences in the surplus lines notices notwithstanding the fact surplus lines notices are similar in substance.

Insurer eligibility is an issue that was partially regulated by the NRRA, but some discretion was left to the states. The NRRA permits non-domiciliary states to impose only two eligibility requirements on domestic surplus lines insurers unless the state adoptees alternative uniform standards through a compact or other procedure. It would be difficult to establish nationwide uniform standards for company eligibility unless there is a mechanism, such as a compact, to facilitate the adoption of the standards. The SLIMPACT draft included the subject of insurer eligibility as an issue that could benefit from the Uniform Standards provisions. It would appear to be in the interest of the states to have a mechanism, such as a compact, to facilitate the adoption of alternate uniform insurer eligibility requirements to augment those contained in the NRRA.

Although SLIMPACT focuses on surplus lines tax and the Interstate Insurance Product Regulation Commission (IIPRC) compact deals with the approval of policy forms, the standard

“boilerplate” language of the compacts is very similar. Many of the definitions and the following articles in SLIMPACT are all based upon the language in the IIPRC compact:

Article III	Establishment of the Commission and Venue;
Article IV	Authority to Establish Mandatory Rules;
Article V	Uniform Standards Authority;
Article VI	Powers of the Commission;
Article VII	Organization of the Commission,
Article VIII	Meetings and Acts of the Commission;
Article IX	Rules, Operating Procedures, Uniform Standards;
Article X	Commission Records and Enforcement;
Article XI	Dispute Resolution;
Article XII	Review of Commission Decisions;
Article XIII	Finance;
Article XIV	Compacting States, Effective Date and Amendment;
Article XV	Withdrawal, Default and Termination;
Article XVI	Severability and Construction;
Article XVII	Binding Effect of Compact and Other laws.

The vast majority of these provisions were considered essential for the efficient administration of a tax allocation compact, just as they were considered critical for the operation of the IIPRC. The vast majority of them are standard boilerplate provisions regarding the administration of a compact.

To achieve the uniformity necessary to divide tax money, the states must use the same allocation formulae as well as the same rules, data elements, forms and payment dates. It is simply not possible to achieve uniformity unless the compact Commission is given sufficient authority to implement a uniform allocation formula as well as uniform rules, forms, definitions and payment dates. The SLIMPACT draft contains the provisions required to achieve the uniformity necessary to allocate and distribute surplus lines taxes. Unless the Commission is given the authority to create uniformity among the states participating in the tax allocation mechanism, it will not be able to function properly.

Although it is essential that the commission have sufficient authority to create a uniform tax allocation system, please note that the scope of SLIMPACT is very limited. The main thrust of SLIMPACT is the efficient allocation of surplus lines taxes. The allocation of Surplus Lines Tax is not a core function of an insurance department today. The operation of SLIMPACT would mean no change at all for most insurance departments. In contrast to SLIMPACT, the IIPRC deals with functions that are broader in scope and a core function of the insurance department—product approval. SLIMPACT may have borrowed some language from the IIPRC, but SLIMPACT’s impact on the insurance departments would be barely noticeable.

We believe the quickest way to comply with the Congressional deadline of July 21, 2011 is for the states that are able to adopt SLIMPACT or some version of it, to do so as promptly as possible. The states that simply wish to contract with SLIMPACT for clearinghouse services could do so. There is likely not enough time to start from scratch to develop a detailed agreement like IFTA prior to drafting detailed enabling legislation. The compact bylaws and meeting rules would allow compacting states to quickly adopt uniform allocation formulae,

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reporting data elements, reporting dates and forms. Without the structure of compact and compact by-laws, it will be difficult to reach decisions quickly.

In terms of speed, SLIMPACT has a decided advantage over any other proposal. SLIMPACT has already been endorsed by NCOIL. SLIMPACT has also been vetted by compact legal experts. A resolution was passed in at least one legislature in support of SLIMPACT. All insurance commissioners have been provided copies of SLIMPACT. Stamping offices and producer trade associations are also familiar with SLIMPACT. The fact that SLIMPACT was drafted by industry and regulators working together and the fact that it has been vetted over the last three years should not be overlooked. The other alternative is to start from scratch on a new proposal and it is not clear if there is enough time to create a new legislative proposal and have it vetted, approved and implemented before July 21, 2011. We would urge you to quickly begin adopting SLIMPACT so the Congressional deadline can be met.

Sincerely yours,



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