

Understanding surplus-lines policies in Connecticut

What is a surplus-lines policy?

It means a policy written by an insurance company that is not authorized (not licensed) in the state of Connecticut. While a policy from an unauthorized company may be written legally through a surplus-lines broker, this transaction places on the policyholder more responsibility for policy negotiation and protection against the insurance company's insolvency.

What is a surplus-lines broker?

A surplus-lines broker means a broker specifically licensed to place insurance with an unauthorized insurance company. Surplus-lines insurance purchased in Connecticut must include the name of the broker in the transaction. A retail broker must procure a policy through a wholesale broker (and as a surplus-lines broker) that provides the surplus-lines market.

Is a surplus-lines company more likely to be insolvent than an authorized company?

Not at all. A surplus-lines company is no more likely to be insolvent than an authorized company. The difference is that the Connecticut State Insurance Department is not monitoring in depth the company's financial records on an ongoing basis, although certain qualifying standards must be maintained to remain on the list

of unauthorized insurance companies that may transact surplus-lines insurance in Connecticut.

For your protection, significant protection is achieved through other means. This is in the jurisdiction where the company is domiciled examined by the state's financial records, as well as the supervision of agencies, such as A.M. Best. Surplus-lines brokers use due diligence in selecting an unauthorized insurance company to provide the desired coverage.

Are there standards to protect policyholders from insolvent agencies?

Yes. The Connecticut Insurance Department protects policyholders only for the insolvency of insurance companies that are authorized in Connecticut. This is a significant distinction. A policyholder insured by a surplus-lines company and the lack of insolvency protection must be considered when making the purchase decision. Nevertheless, placement with a financially sound surplus-lines insurance company may be more prudent than placement with an authorized insurance company that is financially impaired.

Why would my broker offer me a surplus-lines policy?

There are several reasons why it may be necessary to look for coverage in the surplus-lines market. First, the risk of loss may be too great for acceptance by regular markets. Second, the risk may be too little understood

by regular markets to accurately price the risk appropriately. Third, there may be no other way to acquire an exclusive program for a particular risk.

The placement of risks in the surplus-lines market is considered a last resort when authorized insurance companies have not been able to satisfy your insurance needs. Before placement can be made with a surplus-lines company, three declinations from authorized companies usually will be required, unless the type of risk is one that has been placed on the Insurance Department's "export list"—a list of risks assumed to be difficult to place with authorized companies. Note that a higher premium quoted by an authorized company is not considered a declination.

Also, an "exempt commercial purchaser" can request in writing that coverage be placed with a surplus-lines company. Among other requirements, an "exempt commercial purchaser" must employ or retain a qualified risk manager to negotiate insurance coverage.

What should I know about forms and rates used by a surplus-lines company?

A surplus-lines company is exempt from the laws requiring rates and forms to be filed with the Insurance Department. This means forms may vary significantly from standard forms used by authorized insurance companies. The flexibility offered by this freedom from filing can work to the benefit of the policyholder by permitting coverage

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to be tailored to individual needs. However, reductions in standard coverage may be necessary in order to turn an uninsurable risk into one that is insurable. The important thing to remember is that coverage analysis is essential in this market and insurance companies are more inclined to negotiate policy terms.

What about adherence to cancellation and nonrenewal laws?

Unlike many other states, surplus-lines companies in Connecticut must adhere to most of the policy termination rules applicable to authorized companies. These rules exist to protect policyholders from being disadvantaged by arbitrary nonrenewal and cancellation provisions in the policy.

Why am I being billed for a Connecticut state tax on my policy?

The 4 percent surplus-lines tax that you see on your bill is paid quarterly by the surplus-lines broker to Connecticut. It serves as a substitute for the franchise tax that would have been collected from the broker if it were authorized in Connecticut.

What other charges and fees might I be required to pay for a policy which is reinsured by a surplus-

Reimbursement: If a surplus-lines broker or broker to policyholder is required to pay an inspection or other expenses, those expenses will be passed on to the policyholder. Other expenses incurred by a retail broker or surplus-lines broker that are necessary for underwriting may be billed for reimbursement. These charges should be disclosed on the policy.

Sometimes, a retail broker may receive any fixed commission from a surplus-lines broker when writing a policy or the commission rate may be insufficient to cover all the services being provided the policyholder. In that case, it may be necessary to negotiate a service fee to adequately compensate the broker for services rendered. There also may be times the surplus-lines broker charges a fee for services rendered. Regulation places an aggregate cap on the combined service fee amount the retail broker and surplus-lines broker may charge.

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