

Arkansas Insurance Department

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Allen Kerr
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BULLETIN # 14-2015

TO: ALL LICENSED PROPERTY & CASUALTY INSURERS, PRODUCERS, BROKERS, SURPLUS LINES INSURERS, PRODUCER AND TRADE ASSOCIATIONS AND OTHER INTERESTED PARTIES.

FROM: ARKANSAS INSURANCE DEPARTMENT

SUBJECT: ARK. CODE ANN. § 23-66-310(c)(2) APPLICATION TO UNDERWRITING EXPENSES FOR SURPLUS LINES BROKERS & OTHERS

DATE: OCTOBER 2, 2015

The Arkansas Insurance Department (“AID”) has received inquiries by surplus lines insurers and brokers over expenses permitted to be charged to insureds by surplus lines brokers for “underwriting expenses,” and, relatedly, whether such expenses are subject to the fees restriction in Ark. Code Ann. § 23-66-310(c)(2). Ark. Code Ann. § 23-66-310(c)(2) prohibits additional fees to be charged to an insured by a broker or producer if the sum of all fees and commissions or compensation exceed 20% of the total gross premium (hereafter, “the 20% aggregate limit”).

This Bulletin is specifically intended to clarify: (1) AID’s statutory interpretation of whether “underwriting expenses” permitted to be charged by surplus lines brokers under Ark. Code Ann. § 23-66-310(b)(2)(A) include “inspection expenses”; (2) whether such expenses are “fees” subject to the 20% aggregate limit; and (3) AID’s position on whether the surplus lines market is subject to the 20% aggregate limit in Ark. Code Ann. § 23-66-310(c)(2). This Bulletin supplements AID’s website publication, “Producer Frequently Asked Questions,” located at http://www.insurance.arkansas.gov/License/F_A_Q.htm.

I. Inspection Fees

The first inquiry is whether a surplus lines broker may collect an “inspection fee” as an “expense of underwriting” from an insured under Ark. Code Ann. § 23-66-310(b)(2)(A). Ark. Code Ann. § 23-66-310(b)(2)(A) states:

(b) (1) No person shall willfully collect as a premium or charge for insurance any sum in excess of the premium or charge applicable to the insurance in accordance with the applicable classifications and rates as filed and approved if necessary by the Insurance Commissioner, or in cases in which classifications, premiums, or rates are not required by the Arkansas Insurance Code to be so filed and approved, the premiums and charges shall not be in excess of those specified in the policy and as fixed by the insurer.

(2) *However, the provision in subdivision (b)(1) of this section shall not be deemed to prohibit:*

(A) *The charging and collection by surplus lines brokers licensed under § 23-65-101 et seq. of the amount of applicable state and federal taxes in addition to the premium and expense of underwriting as required by the insurer on risks written pursuant to the surplus lines law; (Emphasis Added)*

The phrase or term, “expense of underwriting,” is not defined in the insurance code or rules of AID. It is referenced but not defined in Arkansas Insurance Department Rule 24, “Surplus Lines Insurance.” For purposes of the statutory subdivision referenced above and this Bulletin, AID interprets an “expense of underwriting” to mean a cost associated with a review or inspection of a risk to be insured, including a physical inspection, or a review of loss history, that facilitates an insurer’s decision to accept or decline a risk, or to rate or classify a risk, at policy inception or renewal. AID interprets “inspection fees” charged to the insured or proposed insured by a surplus lines broker to meet this definition if the inspection is routinely required by the surplus lines insurer at policy inception or at renewal for purposes of underwriting classification of the risk by the surplus lines insurer. Inspection fees might also include expenses for review or inspections of the risk during the course of coverage of the policy if required or permitted by the insurer in the policy.

II. Underwriting Expenses & The 20% Aggregate Limit

The next issue is whether an “expense of underwriting” constitutes a “fee” subject to the 20% aggregate limit in Ark. Code Ann. § 23-66-310(c)(2). Ark. Code Ann. § 23-66-310(c)(2) states:

(c) Nothing shall prohibit a duly licensed property or casualty agent or broker from charging a fee to the insured in addition to the premium properly charged for a policy or contract according to the insurer's rate and rule filings with the State Insurance Department, provided that:

- (1) Each such fee is separately disclosed on the invoice or billing statement mailed or delivered to the insured; and
- (2) *The aggregate sum of the fees and all producers' commissions or other compensation due and owing for that policy or contract does not exceed twenty percent (20%) of the total gross premium charged the insured by the insurer for that policy or contract. (Emphasis Added)*

The term “fees” is not defined in Ark. Code Ann. § 23-66-310(c)(2). However, for purposes of that statutory section as well as subdivision and this Bulletin, AID interprets the term “fees” to mean fees customarily associated with the solicitation, negotiation, or servicing of an insurance policy or contract. The Department infers it is the intent of Ark. Code Ann. § 23-66-310(c)(2) to mean fees for solicitation, negotiation, or servicing of an insurance policy because of the next subsection’s exclusion of that restriction, which permits additional fees or charges which are not customarily associated with the solicitation, negotiation and servicing of an insurance policy, assuming the written agreement and disclosure requirements are followed. (Emphasis Added)

In both the non-admitted and admitted markets, AID does not interpret routinely required underwriting risk evaluation requirements of an insurer to be an activity of solicitation, negotiation, or servicing of an insurance policy; therefore, it is the Department’s position that for surplus lines brokers, as well as for producers in the admitted market, these persons or firms may charge an expense or cost to the insured for underwriting expenses, if the underwriting evaluation is required by the insurer. These expenses are however not included in “fees” in the 20% aggregate limit.

III. Applicability of Ark. Code Ann. § 23-66-310(c)(2) to the Surplus Lines Market

During AID’s inquiry of whether inspection fees and underwriting expenses are considered additional “fees” for purposes of the 20% aggregate limit, it was separately raised whether the surplus lines market is subject to Ark. Code Ann. § 23-66-310(c)(2) in general, and therefore to any 20%

aggregate limit for “fees” customarily associated with the solicitation, negotiation, or servicing of an insurance policy or contract. This is raised due to a clause in Ark. Code Ann. § 23-66-310(c) referencing insurance policies or contracts subject to rate filings with AID, and that it is noted surplus lines do not file for rate approvals with AID. The Department’s position however is that the provisions and restrictions in Ark. Code Ann. § 23-66-310(c)(2) applying to additional fees are also intended to apply to surplus lines brokers. Ark. Code Ann. § 23-66-310(b)(2) states:

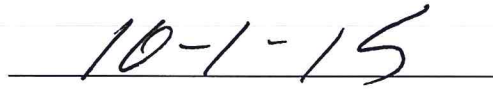
(b) (1) No person shall willfully collect as a premium or charge for insurance any sum in excess of the premium or charge applicable to the insurance in accordance with the applicable classifications and rates as filed and approved if necessary by the Insurance Commissioner, or *in cases in which classifications, premiums, or rates are not required by the Arkansas Insurance Code to be so filed and approved, the premiums and charges shall not be in excess of those specified in the policy and as fixed by the insurer.* (Emphasis Added)

The Department interprets the above subsection to mean that the additional fee restrictions in this insurance code section are intended to apply to both the admitted market as well as to the non-admitted or surplus lines market due to the expressed reference “to cases in which premiums or rates not required to be filed and approved by AID.” (Emphasis Added) Therefore, surplus lines brokers should be aware that the 20% aggregate limit in Ark. Code Ann. § 23-66-310(c)(2) applies if they are considering charging for an additional fee customarily associated with the solicitation, negotiation, or servicing of surplus line insurance policy.

For any questions regarding this Bulletin, please contact Booth Rand in the Legal Division of the Arkansas Insurance Department at 501-371-2820.



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