2. (2.25 points)

   a. (0.25 point)

      Briefly describe one advantage for an insurer of being a surplus lines carrier rather than an admitted carrier.

   b. (2 points)

      A start-up company has proposed entering a state as a surplus lines carrier to compete with admitted carriers by offering similar rates on a direct-to-consumer basis. Identify four surplus lines regulatory requirements and briefly describe why this start-up may or may not meet those requirements.

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SAMPLE ANSWERS AND EXAMINER'S REPORT

FALL 2019 EXAM 6U, QUESTION 2	
TOTAL POINT VALUE: 2.25	**LEARNING OBJECTIVE: A1**
SAMPLE ANSWERS	
Part a: 0.25 point	

Sample Responses:

- Free from state imposed rate and form requirements
- Surplus carriers do not participate in guaranty funds, so the carrier won't be assessed if a different insurer can't meet claim obligations.
- Only has to be licensed in domiciliary state
- Less competition since there are much more admitted carriers than surplus lines.
- The surplus carrier only pays the state premium tax to the state of domicile
- Surplus carriers have the ability to be more flexible with their policies so they can provide the exact coverage the policyholder needs more easily.
- The coverage would be more tailored to the customer's need.

Part b: 2 points

Bolded sample answers indicate unique subject responses, any four of which were required. Italicized sample answers are common variations on the unique response.

Surplus/Capital Requirements

- *Must meet capital requirements – may not meet requirement because start-up may not have access to capital.*
- *Required to have sufficient capital/surplus - start-up company could have sufficient capital and surplus.*

Coverage for the Risk Must be Declined by the Admitted Market

- *Diligent search requirement: Insureds have to prove they could not get coverage in voluntary market. They would then go through a surplus lines broker. A direct-to-consumer basis would then not be effective.*
- *There has to be a "diligent search" by the broker before being able to use surplus lines insurance. This won't apply as there are admitted insurers in the state.*

Surplus Lines Do Not Compete with Admitted Market

- *Product must not be available in private market for insured – if competing with admitted carrier, product is likely available*

Surplus Lines Insurer Must be Admitted in Domicile State

- *To be eligible to write surplus lines, needs to be authorized/licensed in state of domicile to write the same business. It it's start up, it may not meet requirement.*
- *Needs to be admitted in its domiciliary state. Since this is already a start-up company, it is assumed it meets this requirement.*

No Guaranty Fund

- *No guaranty fund support, so insured may willing to get business from admitted carrier covered by fund -> peace of mind*

SAMPLE ANSWERS AND EXAMINER'S REPORT

Only Specialty Licensed Producers are Permitted to Sell Surplus Lines Insurance

- *Surplus lines carrier must export business through a surplus lines broker, thus the "direct-to-consumer" is not allowed.*
- *Permit only specially licensed agent or producer to place surplus line business. The start-up may meet their requirement if their agents are licensed.*

Must Meet Specified Managerial Requirement (Seasoned)

- *The startup is required to be experience in writing that line first through the admitted market. If they are a startup, will not have experience to meet this requirement.*
- *Seasoning – start-up may not have been in business long enough in its own state to be recognized by this state.*
- *Meets managerial requirements: it's possible it meets this.*

State May Require in-state office or producer residence

- *Location – company may not have an office in state/US which may be required.*

Direct to Consumer

- *As surplus lines are not regulated, DOI may not allow direct selling to consumers unless consumer is a sophisticated business of sufficient size with risk manager negotiated purchases.*
- *Direct to consumer only applies to specialized consumer purchasers or consumers unable to find coverage in admitted market so they will not be able to compete with admitted carriers.*

Premium Taxes paid only imposed by home state of the insured

- *Only home state of insured impose premium tax on surplus line business. The start-up meets the requirement.*

EXAMINER'S REPORT

Candidates were expected to understand the advantages of being a surplus lines carrier and the regulatory requirements for surplus lines carriers.

Part a

Candidates were expected to briefly describe one advantage for an insurer of being a surplus lines carrier rather than an admitted carrier.

Common errors include:

- Stating that regulations were different without being clear why different regulations were an advantage.
  For example: "An insurer who is a surplus lines carrier is not subject to the same rate regulation as an admitted carrier"
- Listing items that were not true for surplus lines carriers.
  For example: "Faster and easier to enter the market" or "The insurer can directly offer insurance without admitted by regulators"

- Listing items that were incomplete and needed further discussion to determine if it was an advantage or applied to surplus lines regulations.
  For example: "Do not have to participate in state guaranty funds" or *"Offer cheaper insurance because of lower cost"*

- Listing items that are also true for the admitted market.
  For example: "*By offering on a direct to consumer basis, a surplus lines carrier can cut costs*" or "*They are able to service a different market that may be in lines with their business goals"*

- Listing items that were advantages to consumers rather than the surplus lines insurer.
  For example: "*Can make unique coverages available and affordable*" or "*Surplus lines carrier benefit from writing to insureds that need insurance not found in the admitted market therefore the insurance is highly specialized*"

Part b

Candidates were expected to list four surplus lines regulatory requirements and explain whether or not the start-up insurer, described in the question, could meet the four requirements.

Common errors include:

- Describing surplus lines insurers in general rather than the specific example provided in the question. For example stating that insurer could appoint specialty licensed producers when the example company intended to use direct writers.
- Discussing items common to admitted and surplus lines insurance such as financial reporting and financial examination.
- Discussing regulatory requirements for surplus lines brokers rather than the surplus lines insurer.
- Discussing items that would be beneficial to a start-up insurer but not a surplus lines regulatory requirement (e.g. discussing lack of actuarial and underwriting expertise).

FALL 2019 EXAM 6U, QUESTION 3	
TOTAL POINT VALUE: 3.25	**LEARNING OBJECTIVE: A2**
SAMPLE ANSWERS	
Part a: 1 point	

<u>*Sample Responses - Any four of the following*</u>:

- Frequency and extent the regulator was able to identify and rectify potential issues before they could cause harm to policyholders (i.e. Taking actions to prevent insolvencies)
- Rate of insolvencies and payments to policyholders in those insolvencies (i.e. Effectiveness of guaranty funds)
- Effectiveness and efficiency of rehabilitation actions
- Healthy, competitive insurance market
  Sample responses – Any one of the following: