SURPLUS LINES (E) TASK FORCE

Surplus Lines (C) Task Force Nov. 29, 2021, Minutes
   Surplus Lines (C) Working Group Sept. 22, 2021, Minutes (Attachment One)
      Trust Agreement for Alien Excess or Surplus Lines Insurers (Attachment One-A)
      Comment Letters (Attachment One-B)
      Andrea Best Comment Letter (Attachment One-C)
   Surplus Lines (C) Working Group E-Vote (Attachment Two)
   Proposed Friendly Amendment to 2.1 (Attachment Three)
Draft: 12/2/21

Surplus Lines (C) Task Force
Virtual Meeting (in lieu of meeting at the 2021 Fall National Meeting)
November 29, 2021

The Surplus Lines (C) Task Force met Nov. 29, 2021. The following Task Force members participated: James J. Donelon, Chair, Stewart Guerin and Tom Travis (LA); Larry D. Deiter, Vice Chair (SD); Lori K. Wing-Heier represented by Sian Ng-Ashcraft (AK); Jim L. Ridling represented by Jimmy Gunn (AL); Ricardo Lara represented by Libio Latimer (CA); Michael Conway represented by Rolf Kaumann (CO); Karima M. Woods represented by Angela King (DC); David Altmaier represented by Virginia Christy (FL); Dean L. Cameron represented by Randy Pipal (ID); Dana Popish Severinghaus represented by Kevin Fry (IL); Kathleen A. Birrane represented by Robert Baron (MD); Troy Downing (MT); Mike Causey represented by Shannen Logue (PA); Mike Kreidler represented by Jeff Baughman (WA); and Jeff Rude represented by Danie Capps (WY). Also participating was Robert Wake (ME).

1. Adopted its Summer National Meeting Minutes

Director Deiter made a motion, seconded by Mr. Baughman, to adopt the Task Force’s Aug. 5 minutes (see NAIC Proceedings – Fall 2021, Surplus Lines (C) Task Force). The motion passed unanimously.

2. Adopted the Report of the Surplus Lines (C) Working Group

Mr. Guerin reported that since the Summer National Meeting, the Surplus Lines (C) Working Group met Sept. 22 (Attachment One) to address two administrative tasks. He stated that the Working Group discussed amendments to the NAIC Standard Form Trust Agreement for Alien Excess or Surplus Lines Insurers. Mr. Guerin stated that after discussion of several amendments, the Working Group re-exposed the document for a 14-day public comment period ending Oct. 6. The Working Group conducted an e-vote that concluded Oct. 21 (Attachment Two) to adopt the amendments to the NAIC Standard Form Trust Agreement for Alien Excess or Surplus Lines Insurers.

Following the report, Robert Wake (ME) presented a few friendly amendments (Attachment Three) to the NAIC Standard Form Trust Agreement for Alien Excess or Surplus Lines Insurers.

Mr. Kaumann made a motion, seconded by Mr. Baughman, to adopt the amendments to the NAIC Standard Form Trust Agreement for Alien Excess or Surplus Lines Insurers. The motion passed unanimously.

Mr. Guerin concluded that the second administrative task covered during the Working Group’s Sept. 22 meeting covered the adoption of modifications to the NAIC Quarterly Listing of Alien Insurers.

Mr. Kaumann made a motion, seconded by Mr. Fuller, to adopt the report of the Surplus Lines (C) Working Group. The motion passed unanimously.

Commissioner Donelon addressed Mr. Guerin’s comments regarding Clark Fitz-Hugh (International Sureties Ltd.), who proposed the use of surety bonds as a means to fund collateral within the required trust funds that secure the solvency of insurers on the Quarterly Listing of Alien Insurers. Commissioner Donelon asked Mr. Fitz-Hugh to present his proposal. However, Mr. Fitz-Hugh was not in attendance. Commissioner Donelon asked for comments on the matter, and Director Deiter indicated that he has concerns with the use of surety bonds to fund the trusts as they are not admitted assets. Commissioner Donelon commented that his opinion aligns with Director Deiter. Mr. Latimer commented that California has a preference to maintain consistency between the surplus lines and reinsurance trust fund collateral requirements. Further, Mr. Latimer commented that there are concerns regarding the uncertainty regarding potential collectability. Mr. Wake commented that there are certain conditions that are necessary to fund a trust and a surety bond is not considered evergreen.

Director Deiter made a motion, seconded by Mr. Baughman, to table any further consideration regarding the use of surety bonds as a means to fund collateral within the required trust funds that secure the solvency of insurers on the Quarterly Listing of Alien Insurers. The motion passed unanimously.

3. Received an Update from the Model #870 Drafting Group

© 2021 National Association of Insurance Commissioners
Mr. Travis said that the drafting group for the *Nonadmitted Insurance Model Act (#870)* consisted of various participants from Colorado, Illinois, Louisiana, Texas, and Washington. He indicated that since the Summer National Meeting, the drafting group met three times: Nov. 4, Oct. 20, and Sept. 28. He stated that the drafting group discussed specific sections of the Model #870 while working through a revision-marked version. He said that once the drafting group has made it through its initial review of the model, it will integrate comments received and reconvene in open session to cover the revised draft. He concluded by indicating that the drafting group anticipates presenting a draft of the model to the Task Force during the first quarter of 2022.

4. **Heard an Update on Surplus Lines Industry Results**

Andy Daleo said that at year-end 2020, the *Quarterly Listing of Alien Insurers* consisted of 87 Lloyd’s syndicates and 75 non-U.S. companies for a total of 162 entities, an increase of four entities over the prior year. He stated that in comparison, U.S. domestic surplus lines insurers totaled 297. He indicated that during 2020, non-U.S. based entities (syndicates and companies) collectively wrote $18.6 billion in direct U.S. surplus lines premiums, a 10.3% increase over the prior year. In comparison, domestic insurers wrote $47.5 billion in surplus lines premiums in 2020, a 17.9% increase from the prior year. Mr. Daleo stated that in 2020, non-U.S. insurer surplus lines premiums accounted for 28.1% of total U.S. surplus lines exposure, slightly lower than 29.5% in 2019 and 30.6% in 2018. He summarized that as of Dec. 31, 2020, the non-U.S. entities recorded an aggregate $21.1 billion in gross loss, loss adjustment expenses (LAEs), and incurred but not recorded (IBBR) reserves. He stated that as of June 30, 2021, the gross reserves were partially secured by nearly $5.2 billion in individual U.S. trust fund assets.

Mr. Daleo indicated that the U.S. nonadmitted market wrote $731 million in cyber direct premiums. In comparison, non-U.S. surplus lines insurers wrote $1.3 billion in cyber direct premiums written; 86% was written within the Lloyd’s market, with the majority written as stand-alone coverage opposed to within a package policy. He stated that there were approximately 600,000 nonadmitted U.S. and non-U.S. cyber policies in force, and 24,697 nonadmitted U.S. and non-U.S. claims were reported during 2020 with total direct loss payments of approximately $804 million.

Mr. Daleo said that 2020 was the first full year of private flood data collected. He indicated that the U.S. nonadmitted market wrote roughly $247 million in private flood direct premiums written. In comparison, non-U.S. surplus lines insurers wrote $847 million in private flood direct premiums written; 73% was written within the Lloyd’s market. He concluded that there were approximately 346,000 nonadmitted U.S. and non-U.S. private flood policies in force, with 6,474 claims reported during 2020 with total direct loss payments of approximately $143 million.

Having no further business, the Surplus Lines (C) Task Force adjourned.
The Surplus Lines (C) Working Group of the Surplus Lines (C) Task Force met Sept. 22, 2021. The following Working Group members participated: Stewart Guerin, Chair (LA); Eli Snowbarger, Vice Chair (OK); David Phifer (AK); Michelle Lo (CA); Rolf Kaumann (CO); Robert Ballard (FL); Scott Sanders (GA); Marcy Savage (IL); James A. McCarthy (MA); Jose Joseph and Joana Lucashuk (NY); Amy Garcia (TX); and Steve Drutz (WA).

1. **Heard Comments on the Modifications to the Trust Agreement**

Mr. Guerin referenced call materials that included a re-draft of the NAIC Standard Form – Trust Agreement for Alien Excess or Surplus Lines Insurers (Trust Agreement) (Attachment One-A) and several comment letters (Attachment One-B). He introduced the comment letter contributors, who were asked to summarize their comments.

Ms. Lo indicated that she has no objections to removing the California provision in Section 2.7 of the Trust Agreement since the removal would not affect the department’s authority established in its statutes. Mr. Guerin commented that the re-draft of the Trust Agreement reflects that deletion.

Ms. Lucashuk summarized several minor technical edits to the Trust Agreement that clarify and improve the consistency throughout the document. Mr. Guerin agreed with the edits proposed by Ms. Lucashuk and indicated that these edits were not yet reflected in the re-drafted Trust Agreement. He indicated that these edits would be reflected in the Trust Agreement when re-exposed.

Andrea T. Best (McDermott Will & Emery LLP—MWE) indicated that MWE is generally in favor of the proposal to eliminate the current five-year notice period for termination of the trust. She summarized several recommendations for the new language proposed to Section 2.1 of the Trust Agreement. First, she suggested clarifying the role of the Domiciliary Commissioner by removing the language that indicates the Domiciliary Commissioner determines outstanding U.S. liabilities, as it conflicts with the requirement in Section 2.14 that requires a qualified actuary or accountant to prepare an independent audit of any outstanding liabilities. Second, regarding the termination of a trust by the transfer of liabilities, she proposed expanding the list of transferees to include accredited reinsurers and U.S. surplus lines insurers. Lastly, she suggested that the occurrence policy language be eliminated, given that an independent auditor is required to confirm that there are no U.S. liabilities before a trust is terminated. Mr. Guerin indicated that all of Ms. Best’s comments have been incorporated in the re-draft of the Trust Agreement.

Mr. Kaumann made a motion, seconded by Ms. Lo, to incorporate all the comments, including Ms. Lucashuk’s edits into the re-draft of the Trust Agreement, and solicit comments during an exposure period of 14 calendar days. The motion passed unanimously.

2. **Adopted Revisions to the Quarterly Listing of Alien Insurers**

Mr. Guerin summarized one comment received from Ms. Best regarding the Quarterly Listing of Alien Insurers (Attachment One-C) to maintain a listing of trust banks and contacts. He commented that NAIC staff already maintain this listing for reference. Following no additional discussion, the chair requested a motion to adopt the Quarterly Listing of Alien Insurers as presented. Mr. Phifer made a motion, seconded by Mr. Joseph, to adopt the revisions to the Quarterly Listing of Alien Insurers. The motion passed unanimously.

3. **Discussed Other Matters**

Clark Fitz-Hugh (International Sureties) requested that the Working Group consider the potential use of surety bonds to fund the trust securing the writings of alien insurers on the Quarterly Listing of Alien Insurers. He summarized various reasons to support the inclusion of surety bonds, such as being rated by the same rating companies as banks and regulated by state insurance departments. He also indicated that surety bonds are designed to serve the same purpose as a letter of credit, and the wording of surety bonds and letter of credits match exactly. He further indicated that surety bonds were created to be an alternative to banks, because they make the credit process easier and less onerous for applicants. He emphasized that surety

© 2021 National Association of Insurance Commissioners
bonds are used throughout the U.S. and guarantee various transactions from one party to another, such as payments of judgements, payment of construction loan defaults, and workers’ compensation claims. He suggested that the utilization of surety bonds as trust funding devices could be permitted on a limited use basis, perhaps to secure those insurers that require only a minimum trust fund balance.

Thomas M. Dawson (MWE) commented that he endorses the use of surety bonds on behalf of several of his clients. He also indicated that if the Working Group were to proceed with allowing surety bonds as a device to fund the trust, the Trust Agreement would need to be updated to accommodate the surety bond option.

Mr. Guerin suggested that the use of surety bonds as a trust funding device would be more appropriate for the Surplus Lines (C) Task Force, given it is a policy issue. Therefore, he proposed that he present this issue in his summary report to the Task Force during the next meeting.

Having no further business, the Surplus Lines (C) Working Group adjourned.
TRUST AGREEMENT FOR ALIEN EXCESS OR SURPLUS LINES INSURERS
(As Amended January 1, 2022)

This Agreement, dated ____________, effective as of ____________ between
__________________________, organized and existing under the ___________________, its country of
domicile and having its head office at ___________________________ (“Company”), and
__________________________, a (banking corporation/national banking association) organized and
existing under the laws of _______________________ (“Trustee”); having its principal offices at
___________________________________________________.

WITNESSETH:

WHEREAS the Company is engaged in the insurance business in its country of domicile and has
or will have Policyholders in the United StatesU.S. of America as a result of writing insurance on an
excess or surplus lines basis on risks therein; and

WHEREAS the Company desires to establish a trust fund in the United StatesU.S. as security for
said Policyholders and Third-Party Claimants and to qualify as an eligible or approved excess or surplus
lines insurer therein; and

WHEREAS, the Trustee is willing to act as Trustee of such trust fund; and

WHEREAS, the Trustee agrees to administer such trust fund principally from its office in the City
of _____________________________ and the State of ________________.

NOW, THEREFORE, the Company has transferred to the Trustee cash in U.S. currency, Letters
of Credit, Readily Marketable Securities, or any combination thereof, valued at a total of not less than the
Trust Fund Minimum Amount as defined in Paragraph 2.7 of this Agreement on the date hereof, receipt
of which the Trustee hereby acknowledges and agrees to hold in trust for the uses and on the conditions
hereinafter set forth:

ARTICLE 1
DEFINITIONS

The following terms used herein shall, unless the context otherwise requires, have the following meanings:

1.1 “AMERICAN United StatesUNITED STATES U.S. POLICY” means any contract or policy of
insurance issued or any agreement to insure made by the Company pursuant to the excess or surplus lines
laws of any state, district, territory, commonwealth or possession of the United StatesU.S. in which the
Company is not licensed to do an insurance business, provided that such Policies shall not include
reinsurance or life insurance.

1.2 “CLAIM” means either or both of the following:

(a) a claim against the Company by a Policyholder, as defined in paragraph 1.9, or Third-Party
Claimant for a loss under an American United StatesU.S. Policy excluding punitive or exemplary damages
awarded to or against a Policyholder and also excluding any extracontractual obligations not expressly covered by the American United StatesU.S. Policy (“Loss”) or;

(b) a claim against the Company by a Policyholder for the return of unearned premium (“Unearned Premium”) under an American United StatesU.S. Policy.

1.3 “DOMICILIARY COMMISSIONER” shall mean the Chief Regulatory Officer for Insurance in any state, territory, district, commonwealth or possession of the United StatesU.S., in which the Trust Fund is principally administered as identified on page one of this Agreement.

1.4 “EFFECTIVE DATE” shall mean the date as of which this Agreement is effective as specified on page one of this Agreement.

1.5 “IID” shall mean the International Insurers Department of the National Association of Insurance Commissioners (“NAIC”).

1.6 “LETTER OF CREDIT” means a clean, unconditional, irrevocable, evergreen Letter of Credit issued or confirmed by a Qualified United StatesU.S. Financial Institution.

1.7 “MATURED CLAIM” means a Claim which is enforceable against the Trust Fund as provided for in Paragraph 2.3 of this Agreement.

1.8 “NON-DOMICILIARY COMMISSIONER” shall mean the Chief Regulatory Officer for Insurance other than the Domiciliary Commissioner in any state, territory, district, commonwealth or possession of the United StatesU.S., in which the Company has Policyholders and who has provided the Trustee with written notice that he or she requires any notification required to be made to the Domiciliary Commissioner pursuant to this agreement.

1.9 “POLICYHOLDER” for the purposes of this Agreement, shall mean the holder of an American United StatesU.S. Policy that is a resident of or doing business in the United StatesU.S., and any other persons or associations who are assignees, pledgees, or mortgagees named therein.

1.10 “QUALIFIED UNITED STATESU.S. FINANCIAL INSTITUTION” means an institution that:

(a) Is organized and licensed or (or in the case of a U.S. branch office of a foreign banking organization, licensed) licensed under the laws of the United StatesU.S. or any state thereof; and,

(b) A national bank, state bank, or trust company which is adequately capitalized and qualified to accept securities as determined by the standards adopted by the U.S. banking regulators and regulated by state banking laws or a member of the Federal Reserve system; and

Is regulated, supervised and examined by U.S. federal or state authorities having regulatory authority over banks and trust companies; and

(c) Has been determined by the Securities Valuation Office of the NAIC as an acceptable financial institution; and

(d) Has been granted authority to operate with trust powers, if such qualified United StatesU.S. financial institution is to act as the fiduciary of the trust.
1.11 “READILY MARKETABLE SECURITIES” means debt or equity securities for which a public market exists and that is readily marketable on a regulated United States national security exchange, or principal regional security exchanges or those determined by the Securities Valuation Office of the NAIC to warrant an NAIC designation of 1 or 2.

1.12 “RECEIVER” shall mean for purposes of this Agreement, the Domiciliary Commissioner or such other person as may be appointed by a court of competent jurisdiction or designated by the statute of a state, territory, district, commonwealth or possession of the United States having jurisdiction over the conservation, rehabilitation or liquidation of the insurer.

1.13 “THIRD PARTY CLAIMANT” is one not a party to the insurance contract but having a final judgment against the Company for claims arising from an American United States Policy.

1.14 “TO TRANSMIT” or “TRANSMITTED” shall mean to send by telex, teletype, facsimile, modem or other similar means of electronic communication.

1.145 “TRUST FUND” or “TRUST” means the cash, readily marketable securities and letters of credit, or any combination thereof, in the actual and sole possession of the Trustee and held under the provisions of this Agreement.

1.156 “U.S. REPRESENTATIVE” shall mean the individual or firm designated by the Company or its successor in interest to act on behalf of the company.

ARTICLE 2
THE TRUST

2.1 Duration of Trust Fund. The Trust Fund shall be irrevocable and remain in full force and effect for a period of at least five years and may be terminated following notification of intent to terminate the trust by the Company to the Trustee, the passage of a 90-day period from the receipt of notification to the trustee, and only upon the occurrence of any of the following events:

(a) The passage of five (5) years from the date of written notice to the Trustee of the termination of the Trust Fund, the NAIC IID and all Non-Domiciliary Commissioners receive from the Domiciliary Commissioner or from the Company written confirmation that the Domiciliary Commissioner has determined that all claims attributable to the period while the Company was eligible and listed on the NAIC Quarterly Listing of Alien Insurers have been satisfied and that no outstanding liabilities remain with respect to United States insurance policies in accordance with 2.14(a) of this Agreement. Insurers with exposure to “occurrence” policies are not eligible for this option.

(b) The expiration of a sixty (60) days period after the Company has sent written notice to the Trustee and the NAIC IID by certified mail return receipt requested that it: (i) has become qualified and licensed insurer or eligible surplus lines insurer to conduct an insurance business in all States where it has direct insurance in force; or

(ii) has entered into an assumption and assignment agreement transferring all liability with respect to all risks covered by this Trust Fund to an insurer licensed to do an insurance business in such states or an insurer listed by the IID.
accredited, certified, or reciprocal reinsurer(s), or an assumption reinsurance or assignment agreement between the Company and a U.S. authorized insurer(s) or an accredited reinsurer, eligible surplus lines insurer(s), or an insurer(s) currently approved on the Quarterly Listing of Alien Insurers, pursuant to which the claimant has a direct claim against the authorized or eligible insurer(s) or accredited reinsurer(s), provided, however, that any such assuming insurer or reinsurer shall have capital and surplus in excess of the minimum capital and surplus required for inclusion on the Quarterly Listing of Alien Insurers, or (2) an insurer currently approved on the Quarterly Listing of Alien Insurers. Such written notice submitted to the Trustee by the Company shall include a list of all states in which the Company has American U.S. Policies in force as certified by the Company or U.S. representative.

The Trustee shall notify the IID and the Insurance Commissioners of said States in writing of its receipt of a notice as provided for in Subparagraphs (a), (b), or (c) of this paragraph within thirty (30) days of receipt of such notice from the Company.

2.2 Priority of Payments Out of Trust Fund. The Trust Fund shall be exclusively available first for the payment of all expenditures and fees under Paragraph 3.7 of this Agreement including legal fees and expenses actually incurred by or on behalf of the Trustee in connection with its administration, preservation or conservation of the Trust (“Trustee Priority Claims”); provided, however, that this amount shall not exceed $250,000 or 10% of the value of the Trust, whichever is less. Any amount in excess of the amount necessary to satisfy Trustee Priority Claims shall be available for the payment of Matured Claims, provided, however, that Losses shall always take priority over Unearned Premium in the payment of Claims so that the Trustee shall pay all Matured Claims for Losses in full prior to payment of any part of a Matured Claim for Unearned Premium. The Trustee shall pay a Matured Claim for Unearned Premium after receipt of a Claim for Losses which has not yet become a Matured Claim for any reason.

2.3 When Claims Become Enforceable Against the Trust. Subject to the payment of Trustee Priority Claims and to the priority of Losses over Unearned Premium, a Claim against the Company shall be enforceable against the Trust Fund when all of the following five conditions have been satisfied:

(a) The Policyholder or Third Party Claimant has obtained a judgment against the Company in any court of competent jurisdiction within the United States U.S. of America or has obtained a binding arbitration award in respect of the Company’s liability under an American U.S. Policy;

(b) Such judgment has become final in the sense that the particular litigation has been concluded, either through failure to appeal within the time permitted therefor or through final disposition of any appeal or appeals that may be taken, the word “appeal” being used herein to include any similar procedure for review permitted by applicable law;

(c) The service upon the Trustee of a certified copy of said judgment, together with such proof as to its finality as the Trustee may reasonably request;

(d) Certified written statements from the Policyholder, Third Party Claimant or their legal counsel stating, without qualification other than with respect to the passage of the time period described in Paragraph 2.3(e) hereof, that the Claim does not include exemplary or punitive damages, what part of the Claim, if any, is for Unearned Premium and that the Policyholder or Third Party Claimant has complied with all of the provisions set forth in Subparagraphs (a), (b), (c) and (d) of this paragraph; and
(e) The expiration of a period of thirty (30) days from the date of the service upon the Trustee of said certified copy of said judgment and all of said proofs without such judgment having been satisfied; provided, however, that in the event that the termination date of the Trust is less than thirty (30) days following such date of service, the expiration of the period of time equal to the amount of time left before the day before the termination date of the Trust.

A Claim which has satisfied each of the above five conditions shall be deemed to be a Matured Claim. The Trustee shall determine that the above conditions have been met on the basis of the evidence specified above and shall be held harmless in relying upon such evidence in its determination. Such determination shall be conclusive and binding upon all parties. Any Matured Claim shall, subject to Article 4, be paid by the Trustee by check mailed to the address of the Policyholder or Third Party Claimant solely out of the Trust Fund then in its actual and sole possession, without regard to the rights of any other Policyholder, unless the judgment shall be with respect to a Matured Claim for return of Unearned Premium in which case payment by the Trustee shall be made in accordance with the priorities stated above in Paragraph 2.2. The Trustee shall promptly notify the Company in writing of the receipt of a Claim which has been determined by the Trustee to meet conditions (a) through (d) of this paragraph and of the amount thereof. If a Matured Claim would, if paid, reduce the Trust Fund below the Trust Fund Minimum Amount as defined in Paragraph 2.7, or, if the Trustee has received notice that the Company is declared or deemed insolvent as set forth in Paragraph 4.1, then Article 4 shall govern the distribution of the Trust Fund. A Matured Claim which, if paid, would reduce the amount of the Trust Fund below the Trust Fund Minimum Amount shall only be paid in accordance with the provisions of Article 4 of this Agreement. The Trustee shall notify the IID, the Domiciliary Commissioner and the Non-Domiciliary Commissioner within ten (10) days of the Trustee’s receipt of any Matured Claim that would reduce the Trust Fund below the Trust Fund Minimum Amount as set forth in Paragraph 2.7. In determining whether payment of a Matured Claim would reduce the amount of the Trust Fund below the Trust Fund Minimum Amount, the Trustee shall rely upon the value of the Trust Fund as established at its most recent valuation as provided for in Paragraph 2.13 of this Agreement.

2.4 Limitations of Policyholder’s Source of Recovery. No Policyholder or Third Party Claimant shall have any right of any nature or description under this Agreement to seek to enforce a Claim or otherwise bring an action against the Trustee in respect of any assets of the Trustee or of any assets other than those in the Trust Fund. No Policyholder or Third Party Claimant, even after its Claim has become a Matured Claim, may require an accounting from the Trustee or inquire into the administration of the Trust, question any of the Trustee’s acts or omissions or otherwise enforce this Agreement, the sole right of such Policyholder or Third Party Claimant under this Agreement being to receive the amount of its Claim after it has become a Matured Claim from the assets then in the Trust Fund and available for such payment under this Agreement.

2.5 Sale of Trust Assets. Unless otherwise directed in writing by the Company, the Trustee shall retain the specific assets of the Trust Fund. Subject to the terms of this Agreement, at the time a Matured Claim becomes payable by the Trustee from the Trust Fund, payment shall be effected in accordance with the Company’s written instructions or, if no such instructions are received by the Trustee at least ten (10) days prior to the expiration of the time period set forth in Paragraph 2.3(e), then as follows: (i) first from any cash in the Trust Fund; (ii) then, from the proceeds of the sale by the Trustee of any or all of the Readily Marketable Securities or other investments (other than Letters of Credit) in the Trust Fund; (iii) then, any other assets or other property in the Trust Fund (other than the Letters of Credit); (iv) then, from drawings against any Letters of Credit. Subject only to the provisions set forth in the previous sentence, the Trustee in its sole discretion, may sell all or part of the Trust Fund, in any order it elects, needed to effect timely payment of any Matured Claims. The Trustee shall not be liable, except as provided by paragraph 3.11,
for any loss incurred in the sale of assets or for its selection of the assets to be sold, and shall only be
obligated to sell such assets at the market price then available to the Trustee.

2.6 Management of Trust Fund.

The responsibility for making investments of the Trust Fund shall, for the duration of the trust, repose
with the Company and unless and until otherwise directed by the Company in writing, the Trustee shall
not be required to take any action in regard to investments and property held in the Trust other than to
collect the interest and dividends or other sums payable thereon. Unless otherwise requested in writing by
the Company, and subject only to the provisions of Paragraph 2.5, the Trustee shall retain any and all
assets of the Trust held by it from time to time hereunder, notwithstanding that the same may not be
recognized as legal investments for trust funds under the laws of the state where the Trust Fund is
administered or other applicable law.

The Trustee shall deposit the assets of the Trust Fund, except to the extent the Trust Fund consists of
Letters of Credit, or any part thereof, in one or more such banks (which may include the Trustee) or trust
companies in the United States, or invest and reinvest the Trust Fund, except to the extent
the Trust Fund consists of Letters of Credit, or any part thereof, in any such stocks, bonds and securities
as the Company shall direct in writing, notwithstanding that such Investments may not be recognized by
the laws of the state where the Trust Fund is administered or other applicable law as legal investments for
trust funds.

The Domiciliary Commissioner and the Chief Regulatory Officer for Insurance in any other state,
territory, district, commonwealth or possession of the United States where the Company is eligible
for excess or surplus lines shall have the right to review the assets in the trust to determine whether such
assets are acceptable.

Nothing herein contained is intended to relieve the Company from furnishing investments in the Trust
Fund of the quality required by the Surplus Lines or Excess Lines Laws of all states where the Trust Fund
is required as a condition of the Company’s eligibility. Each investment instruction from the Company
shall be a representation by the Company that the investments specified therein meet such conditions and
the conditions imposed by the definitions set forth in this Agreement. The Trustee shall also make or
change any deposits and sell and dispose of any negotiable assets of the Trust, other than Letters of Credit,
by and with the direction in writing of the Company. The Trustee shall be under no duty to give any
investment advice to any person in connection with the Trust Fund but shall always, provided the Trustee
itself shall have received actual notice thereof, notify the Company as to any rights to conversion,
subscription, voting or other rights pertaining to any investments held in the Trust Fund and of any default
in the payment of principal or interest. The Company shall have the full, unqualified right to vote and
execute consents and to exercise any and all proprietary rights, not inconsistent with this Trust Agreement,
with respect to any of the property forming a part of the Trust Fund. All interest, dividends and other
income resulting from the investment of the property in the Trust Fund (subject to the Company’s
obligation to maintain the Trust Fund Minimum Amount and to the Trustee’s interests provided herein)
shall be the property of the Company. To the extent the Company shall be entitled to receive such income,
Trustee shall collect and pay it to the Company, upon the Company’s written instructions, not more
frequently than monthly, provided, however, that the Trustee shall have no obligation with respect to the
payment of income by the issuer of any security.

2.7 Trust Fund Minimum Amount and Quality. The Company, either directly or through its U.S.
representative, shall provide the Trustee with written notice of the minimum amount which the Company
is required by law to maintain in the Trust Fund (“Trust Fund Minimum Amount”). The Company may
amend the Trust Fund Minimum Amount from time to time by providing the Trustee with advance written notice thereof. In no event, however, may the Trust Fund Minimum Amount be less than the amount determined by the funding provisions contained within Section V. B(i) of the IID Plan of Operation or its successor provision. The maintenance of the trust fund minimum amount shall continue until it is terminated per the provisions of 2.1 (a), (b), or (c).

If the Company is transacting business in California, the Trust Fund Minimum Amount must consist of cash or readily marketable securities acceptable to the California Insurance Commissioner which are authorized pursuant to Sections 1170 to 1182, inclusive, of the California Insurance Code, and are listed on a regulated United States national or principal regional security exchange, or letters of credit acceptable to the California Insurance Commissioner and issued by a qualified United States financial institution.

If the Company is not transacting business in California, the Trust Fund Minimum Amount must consist of cash, readily marketable securities or letters of credit issued by a qualified United States financial institution.

Trust fund amounts in excess of the Trust Fund Minimum Amount shall consist of cash, securities, letters of credit or investments of substantially the same character and quality as those which are eligible investments for the capital and statutory reserves of admitted insurers to write like kinds of insurance in the state where the trust is principally administered.

2.8 Letters of Credit. In the event that the assets of the Trust Fund consist in whole or in part of a Letter of Credit (which Letter of Credit may be issued by the Trustee or an affiliate in its commercial and not its trust capacity) and said Letter of Credit shall bear a termination date prior to any stated or noticed termination date of the Trust, shall be evergreen until the termination of the Trustee shall, in the absence of notice at least thirty (30) days in advance of any termination of the Letter of Credit that the Letter of Credit will be renewed or extended, draw down and convert such Letter of Credit to cash and hold the same as assets of the Trust Fund pursuant to the terms hereof.

2.9 Contributions to the Trust Fund. The Company may make further contributions to the Trust Fund from time to time which further contributions shall be subject to the terms and conditions hereof.

2.10 Withdrawal of Excess Funds. From time to time the Company may direct the Trustee in writing to pay over to the Company any funds in excess of the Trust Fund Minimum Amount set forth in Paragraph 2.7.

2.11 Trustee’s Authority to Hold Investments. Legal title to the assets of the trust shall be vested in the Trustee for the benefit of the Company’s American United States Policyholders and Third Party Claimants in accordance with the provisions of this Trust. Trustee may hold any investments or other assets thereunder in the name of a nominee. The term “hold” shall include Trustee’s authority to deposit any part or all of the aforesaid property, which consists of securities in registered or unregistered form, at a Federal Reserve Bank under federal book entry procedure, a depository trust company or other centralized securities depository system, whether now or hereafter organized (one or all herein called “CSDS”). All securities in registered form are to be registered in the name of a nominee of Trustee or CSDS.

2.12 Assets of the Trust. Trustee shall be under no duty or obligation to require the Company to make any transfers or payments of additional assets to the Trust and it shall be conclusively presumed that any and all such transfers or payments to Trustee have been properly made.
2.13 Trustee to Certify Trust Assets.

(a) Whenever reasonably required by the Company, but not less often than annually and not more often than quarterly, Trustee shall prepare and submit to the Company a statement of the assets in the Trust and such other information as may be agreed upon between the Company and the Trustee.

(b) Trustee shall promptly certify the existence of the Trust Fund and the assets and their market valuation on the effective date of this instrument and quarterly thereafter, to the IID and the Domiciliary Commissioner. Such notification shall be made within thirty (30) days after the effective date of the end of each calendar quarter.

In addition, Trustee shall certify the existence and most recent value of the Trust Fund whenever so directed by IID, the Company, its U.S. representative, the Domiciliary Commissioner or any Non-Domiciliary Commissioner. Whenever the Trustee in the performance of its duties thereunder shall be required to value the assets of the Trust Fund, it may employ an agent for such valuation and the Company shall reimburse Trustee for any costs or expenses of valuations performed either by the Trustee or such agent. In the absence of the filing in writing with the Trustee by the Company of exceptions to any such statement within sixty (60) days, approval of such statement shall be deemed to have been given; and in such case or upon written approval, the Trustee shall be released, relieved and discharged with respect to all matters set forth in such statement as though such account had been settled in a court of competent jurisdiction in a proceeding where all parties having a beneficial or regulatory interest in the Trust were parties.

2.14 Trustee’s Duties Upon Termination of Trust Fund.

(a) In the event of termination in accordance with Paragraph 2.1 (a) through (c), the Company shall appoint either a qualified, certified public accountant or a qualified actuary with the consent of the Trustee, which consent shall not be unreasonably withheld, as auditor and an independent audit shall be made as of the date of such termination of the Trust Fund and the Company’s estimate of the outstanding liability, if any, of the Company for incurred and unpaid losses (both reported and unreported) and Unearned Premium on American United States Policies issued during the term of the Trust and up to and including the date of termination. The Company shall present to the Trustee such audit report together with a true and correct copy of the auditor’s practicing certificate or equivalent document issued by the authority governing the licensing or conduct of the auditor. If the auditor’s practicing certificate or equivalent document is unavailable, then the Trustee, upon the request of the Company, shall submit a request for the written approval of the auditor from the Domiciliary Commissioner. Approval of the auditor shall be deemed given if the Domiciliary Commissioner does not object to such auditor in writing to the Company and the Trustee within 90 days from the date of delivery of such request. The auditor shall upon the completion of such audit, and from time to time thereafter, at the request of the Trustee, issue a report to the Trustee expressing an opinion on the amount of any such outstanding liability at the date of such termination or at such later date specified in such report. The Trustee shall be protected in acting or relying upon any report of said auditor and shall have the right to retain such assets in the Trust Fund as may be necessary, in the Trustee’s sole discretion, and the Trustee shall pay or cause to be paid therefrom the amount of any such Losses in the manner provided in Paragraph 2.3. Upon the termination of the Trust and the payment of any fees and expenses of the Trustee provided for thereunder due and owing, the Trustee shall transfer, pay over and deliver to the Company the income and principal of the Trust’s assets then in its actual and sole possession, or the balance thereof then remaining if Losses are to be paid according to the report of the auditor, and such payment, transfer and delivery shall constitute a full, final and sufficient release, discharge and acquittance to the Trustee in respect thereof.
b) No officer of the Trustee shall recognize the audit report of either a certified public accountant or a qualified actuary, nor accept any annual audited financial report if such officer has actual knowledge that such audit report was prepared in whole or in part by any natural person who: (i) has been convicted of fraud, bribery, a violation of the Racketeering, Influenced and Corrupt Organizations Act, 18 U.S.C. Sections 1961-1968, or any dishonest conduct or practices under federal or state law; (ii) has been found to have violated the insurance laws of any state with respect to any previous reports submitted in connection with the aftermath of a trust established for excess or surplus lines eligibility purposes; or (iii) has demonstrated a pattern or practice of failing to detect or disclose material information in previous reports filed.

2.15 [Optional at the choice of the Company and Trustee] Company May Waive Conditions for Claims Payments. With respect to assets in excess of the Trust Fund Minimum Amount as defined in Paragraph 2.7, the Company may approve the Trustee’s payment of any Claim by waiving any or all of the conditions specified in Subparagraphs (a) through (e) of Paragraph 2.3 and directing the Trustee in writing to pay such approved Claim out of the Trust Fund whereupon the Trustee shall forthwith satisfy said Claim out of the Trust Fund without (i) regard to the rights of any other Policyholder and any obligations other than the observance of the priorities of Paragraph 2.2 and of the exceptions set forth in the last subparagraph of Paragraph 2.3; (ii) inquiring into or ascertaining the validity of such Claim or the propriety of such direction; or (iii) seeing to the application of such payment. Nothing herein, however, should be construed to permit the Company to order, or the Trustee to make, payment pursuant to this section if the Trustee is in receipt of a notice of insolvency as referenced in Paragraph 4.2 or if such payment would reduce the trust fund below the Trust Fund Minimum Amount set forth in paragraph 2.7.

ARTICLE 3
THE TRUSTEE

3.1 Trustee’s Qualification. Trustee shall always meet the requirements of Subparagraphs (a),(b), (c) and (d) of Paragraph 1.10.

3.2 Trustee’s Duties and Liability. Trustee’s duties and responsibilities shall be governed by applicable law and the terms of this Agreement.

The Trustee shall not be liable for any loss to the Trust Fund other than losses caused by its own negligence or willful misconduct. The Company agrees to indemnify and hold harmless the Trustee from and against any and all claims, damages, losses or other payments of any nature whatsoever arising out of the Trustee’s performance or nonperformance thereunder, unless such claims, losses, damages or other payments arise as a result of the Trustee’s own negligence or willful misconduct.

3.3 Trustee May Rely on Certain Writings. The Trustee shall be entitled to rely upon, be protected, held harmless and deemed to have exercised reasonable due care, if the Trustee relies upon any writing believed by it in good faith to be genuine and to have been signed (whether facsimile or otherwise) or coded or purported to be signed or coded and transmitted, sent or delivered by the proper parties.

3.4 What Constitutes Conclusive Proof for Trustee. If the Trustee deems it necessary or desirable that a matter be proven prior to taking or omitting any action thereunder, such matter, unless other evidence in respect thereof be herein specifically prescribed, may be deemed to be conclusively proven by a statement purported to be executed in the name of the Company or by any of its agents or U.S. representatives designated by it as such in writing to the Trustee and delivered to the Trustee for any such action or omission on its faith thereof; but the Trustee, in its discretion, may instead accept or require such other or
additional evidence on the matter as it may deem reasonable, provided that in the event the effect of the action would be to terminate the Trust, the Trustee may rely only on a statement or certification of officers or agents of the Company duly authorized for this purpose.

3.5 What Constitutes Proper Execution for Trustee. Except as otherwise expressly provided in this Agreement, any writing to be furnished by the Company shall be sufficiently executed if signed in the Company’s name by such of its officers or other agents or U.S. representative as it may designate in writing to the Trustee, which designation shall continue in effect until changed by subsequent written notice received by the Trustee. With respect to the authority conferred on it, the Trustee may rely on any writing of any such officers or agents.

3.6 Trustee’s Reliance on Opinions of its Counsel. The Trustee may consult with counsel selected by it and may rely on said counsel’s opinion as complete authority in respect of any action taken or omitted by the Trustee in good faith in accordance with said opinion and the Trustee shall be deemed to have exercised reasonable due care in reliance thereon.

3.7 Trustee’s Fees and Expenses. The fees of the Trustee for administering the Trust shall be mutually agreed upon from time to time between the Company and the Trustee.

The fees and all expenses of Trustee, including its counsel fees and expenses and other disbursements incurred in administering, preserving or conserving the Trust, shall be, and the Company hereby irrevocably grants to Trustee, a first priority security interest in and a lien no greater than the lesser of: (i) $250,000 of the Trust Fund Minimum Amount as defined in Paragraph 2.7 of this Agreement or, (ii) 10% of the value of the Trust if the value falls below the Trust Fund Minimum Amount specified in Paragraph 2.7. Nothing herein shall limit the right of the Trustee to assert a priority claim in any amount against amounts in excess of the Trust Fund Minimum Amount pursuant to Paragraph 4.5. All amounts to which the Trustee is entitled by reason of this paragraph shall be Trustee Priority Claims for purposes of Paragraph 2.2. Nothing in this Agreement shall be construed as requiring that the Trustee’s fees and expenses be satisfied solely from the corpus of the Trust Fund.

3.8 Maintenance and Inspection of Trustee’s Records. The Trustee shall keep complete records of the administration of the Trust which may be examined at any time, with reasonable advance notice, by the Domiciliary Commissioner or any Non-Domiciliary Commissioner. Any persons duly authorized by the Company in writing may examine during normal business hours upon ten (10) days written notice to the Trustee. The Company agrees to reimburse the Trustee for any reasonable expenses incurred by the Trustee as a result of any such examination.

3.9 Trustee’s Resignation or Removal; Appointment of Successor. Notwithstanding Paragraph 2.1 hereof, the Trustee may resign at any time by sending its notice of resignation by notifying certified mail return receipt requested, to the Company’s last known address and to the Domiciliary Commissioner, all Non-Domiciliary Commissioners, and the IID to take effect on the date specified in such notice, but not less than sixty (60) days after the date of such mailing or personal delivery thereof if not mailed, unless the Company shall accept shorter notice as adequate. Trustee or any Successor Trustee may be removed by the Company by sending written notice of such removal by certified mail return receipt requested, to such—the Trustee’s last known address and to—the domiciliary Commissioner, all non-domiciliary Commissioners, and the IID, to take effect on the date specified in such notice but not less than sixty (60) days after the date of such notification mailing or personal delivery thereof if not mailed, unless Trustee accepts shorter notice as adequate; provided that no such removal shall become effective without Trustee’s
consent until all sums due to it thereunder for its fees and expenses including legal fees and expenses have been paid to it.

The Trust Fund shall be retained by the Trustee who is resigning or who has been removed until payment of its fees and expenses as provided in Paragraph 3.7 and its Successor Trustee has accepted its appointment, at which time the Trustee shall transfer, pay and deliver to the Successor Trustee the assets comprising the Trust Fund as they may be then constituted. If a Successor Trustee has not accepted appointment and the Trustee wishes to be relieved of responsibility thereunder, the Trustee may tender the Trust Fund assets to the Domiciliary Commissioner and, if the Domiciliary Commissioner declines to accept responsibility for Trust Fund assets, the Trustee may deposit the Trust Fund with a court of proper jurisdiction and with regard to such action shall be responsible only for giving notice to the Domiciliary Commissioner, all Non-Domiciliary Commissioners, the IID, the Company and such Policyholders which have notified the Trustee in writing that they have an actual or potential claim against the assets of the Trust Fund. When Funds are accepted by the Domiciliary Commissioner or paid into court, the Trustee’s sole remaining responsibility shall be to render a final accounting of the Trust. Copies of the required notice or resignation or removal required by this Paragraph shall also be sent communicated by certified mail, return receipt requested, to the IID, the domiciliary Commissioner, and all Non-Domiciliary Commissioners.

3.10 Trustee’s Assets. No provision of this Agreement shall require the Trustee to expend or risk its own funds or to otherwise incur any financial liability in the performance of any of its duties thereunder or in the exercise of its rights including, but not limited to, prosecuting, defending or otherwise enforcing any claims by or against the Trust Fund unless and until it has been indemnified for any fees and expenses likely to be incurred thereby.

3.11 Trustee’s Liability. The Trustee shall not be liable for any of its actions or omissions thereunder (including any actions taken in accordance with Article 4), except for its own negligence or willful misconduct. If the Trust Fund is funded, in whole or in part, by a letter of credit issued by the Trustee or by an affiliate of the Trustee, the failure of the Trustee to draw against the letter of credit in circumstances where such draw would be required by this Agreement shall be deemed to be negligence and/or willful misconduct for purposes of this paragraph.

ARTICLE 4
INSOLVENCY

4.1 Insolvency of Trust Fund. The Trust Fund shall be deemed insolvent upon the happening of the earlier of the following events:

(a) The Trustee actually receives written notice from the Company, the Company’s U.S. representative, the insurance regulatory authority in the Company’s jurisdiction of domicile, the domiciliary Commissioner, any Non-Domiciliary Commissioner or the IID, that the Company has been declared insolvent in its country of domicile; or

(b) The expiration of sixty (60) days after the value of the Trust Fund as shown by the most recent valuation of the Trust Fund as provided for in Paragraph 2.13 of this Agreement (i) was reduced below the Trust Fund Minimum Amount as specified in accordance with Paragraph 2.7 or (ii) would be so reduced by the payment of a Matured Claim, whichever of the events described in (i) and (ii) occurs first. If said minimum has been replenished within said sixty (60) day period by or on behalf of the Company to offset any such reduction, notice thereof shall be given by the Trustee to the IID as provided.
below, and the insolvency shall be deemed cured. Promptly after such actual or anticipated reduction of
the value of the Trust Fund, the Trustee shall send notice to the Company of the actual or anticipated
reduction and a copy of such notice by certified mail return receipt requested, to the Domiciliary
Commissioner, all Non-Domiciliary Commissioners, and the IID.

4.2 Notice of Insolvency.
(a) If declared insolvent in its country of domicile, the Company shall promptly (i) transmit
send a written notice of this event and (ii) send a certified copy of such declaration by certified mail return
receipt requested to the Company’s U.S. representative, the trustee, the domiciliary commissioner, all
Non-Domiciliary Commissioners and the IID.

(b) If the Trust Fund is deemed insolvent as defined in Paragraph 4.1, the Trustee shall
promptly transmit send a written notice of this event by certified mail return receipt requested, to the
Company, its U.S. representative, the Domiciliary Commissioner, all Non-Domiciliary- Commissioners
and the IID.

4.3 Transfer of Trust Assets to Domiciliary Commissioner in Event of Insolvency. In the event that
the Trust becomes insolvent as specified in Paragraph 4.1 and notwithstanding the provisions of this
Article 4 or of any other provision in this Agreement, the Trustee shall comply with an order of the
Domiciliary Commissioner or a U.S. court of competent jurisdiction directing the Trustee to transfer to
the Domiciliary Commissioner or other designated Receiver all of the assets of the Trust Fund except
those assets which are necessary to satisfy the Trustee’s Priority Claims as determined in Articl

4.4 One Year Waiting Period After Insolvency. Except in cases where Trust assets have been
transferred to the Domiciliary Commissioner as provided for in paragraph 4.3 and unless otherwise
ordered by a court of competent jurisdiction, no Claims, other than the Trustee’s Priority Claims, shall be
paid out of the Trust Fund during the 12 month period (“Waiting Period”) commencing on the date the
Trustee receives written notice that the Company was declared insolvent in its country of domicile as set
forth in Paragraph 4.1(a) or the date the Trustee is required to transmit provide a notice to the Company
pursuant to Paragraph 4.1(b), unless the insolvency has been cured within the sixty (60) day period as
provided for in Paragraph 4. I(b), whichever occurs first.

Matured Claims, whether arising prior to or during the Waiting Period, may be filed throughout said period
by certified mail return receipt requested.

4.5 Final Distribution of Trust Fund Assets By Trustee. As soon as practicable after the end of the
Waiting Period specified in Paragraph 4.4, the Trustee shall distribute the balance of the Trust Fund in
accordance with state law.

Trustee Priority Claims shall first be paid out of any amount in the Trust Fund in excess of the Trust Fund
Minimum Amount. The Trust Fund Minimum Amount and any amount in excess of the Trust Fund
Minimum Amount not needed to satisfy Trustee Priority Claims shall then be distributed among the claimants with Matured Claims.

Such prorated distribution shall be in the ratio which the value of each such Matured Claim bears to such balance.

Any assets remaining in the Trust Fund after all matured claims have been paid in full shall be used to satisfy any outstanding and unpaid Trustee Priority Claims.

Any remaining assets shall be transferred by the Trustee to the Company or its successor in interest.

In performing its duties thereunder the Trustee may retain any person to act on its behalf or assist it as it deems necessary and shall pay the necessary and reasonable compensation and expense of such person thereunder out of the Trust Fund.

ARTICLE 5
MISCELLANEOUS

5.1 Governing Law. This agreement shall be governed by, and construed and enforced in accordance with, the laws of the United States jurisdiction in which the Trust Fund is principally administered as specified on page one of this Agreement.

5.2 Survival of Prior Obligations. Commencing on the Effective Date, this Agreement shall be binding upon the parties hereto and their successors and assigns and shall supersede such prior agreements, except for continuing obligations created by any prior agreements between the parties on the subject matter hereof as to matters arising prior to the Effective Date.

5.3 Procedure to Be Followed in Amending this Agreement.

(a) All amendments to this Agreement shall be in writing and signed by the Company and the Trustee. The Trustee shall have discretion either to give or withhold its consent thereunder and its decision to give or withhold its consent shall be binding and conclusive upon all persons and parties, and in no event shall it incur any liability for any decision made by it thereunder in good faith.

(b) Notwithstanding the provisions of Paragraph (a) of this section, no amendment shall become effective without the IID’s prior written consent.

(c) The company shall give written notice of any proposed amendment to all Domiciliary and Non-Domiciliary Commissioners together with a copy of the proposed amendment. If no Non-Domiciliary Commissioner disapproves the proposed amendment within thirty (30) days of receipt of the notice, the amendment shall be effective on the date specified by the Domiciliary Commissioner.

5.4 Notice. The Company shall provide the Trustee with the names and mailing addresses of the manager of the IID, the Domiciliary Commissioner, all Non-Domiciliary Commissioners and the Company’s U.S. representative, and shall update this list from time to time as may be necessary to keep the information in the list current. In providing the Notices required under any provision of this Agreement, Trustee may rely upon this list and in doing so shall be protected, held harmless and deemed to have exercised all reasonable due care.
5.5 **Partial Invalidity Does Not Invalidate Entire Agreement.** If any provision of this Agreement is held invalid or unenforceable, the balance of this Agreement shall be construed and enforced as if such provision had not been inserted herein.

5.6 **Interpretation.** The use herein of one gender shall be deemed to include the other and the singular the plural, as the context may require.

5.7 **Headings and References.** The headings herein are for reference only and not for defining any provisions hereof. Reference to this Agreement shall include its amendments, if any. All articles, paragraphs and subparagraphs as well as their subdivisions and abbreviations cited herein refer to this Agreement and its amendments, if any.

5.8 **Counterparts.** This Agreement may be executed in any number of counterparts, each of which when signed by the Company and the Trustee, shall be deemed to be an original.

IN WITNESS WHEREOF, the Company and the Trustee have caused this Agreement to be duly executed and their corporate seals affixed hereto.

Executed at ____________________________
[Seal] ____________________________ on ____________________________
Attest: ____________________________ By ____________________________
[Name and Title] [Name and Title]

Executed at ____________________________
[Seal] ____________________________ on ____________________________
Attest: ____________________________ By ____________________________
[Name and Title] [Name and Title]

[Notarizations]
Hi Bree,

At the Working Group’s July 7th conference call, Thomas Dawson from McDermott Will & Emery raised an issue over the California Requirement paragraph within Section 2.7 of the NAIC Trust Agreement Form. That paragraph mandates the trust fund’s composition for insurers transacting (nonadmitted) business in California. Thomas indicated that the NRRA preempts the California Requirement; and the mandated composition of the trust fund should only apply to insurers who wish to be on the California’s LASLI list.

While waiting to see how he could establish the NRRA preemption case, we want to inform you that we wouldn’t have any issue removing the California Requirement paragraph from the NAIC Trust Agreement Form since the removal wouldn’t affect the authority we have in our statues. California can continue to enforce the trust fund requirements at the initial LASLI application review stage and during the subsequent renewal periods.

Thank you for your consideration.

Regards,

Michelle

Michelle Lo, CPA, CFE
Division Chief
Financial Analysis Division
300 S. Spring Street, South Tower
Los Angeles, CA 90013
Tel: (213) 346-6334
Email: Michelle.Lo@insurance.ca.gov
Bree Wilson  
National Association of Insurance Commissioners  
International Insurers Department  
1100 Walnut Street, Suite 1500  
Kansas City, Missouri  64106-2197  

6 August 2021  

Dear Ms. Wilson,  

We are writing with respect to the NAIC International Insurers Department’s (“IID”) proposed draft changes to the Standard Form Trust Agreement for Alien Excess or Surplus Lines Insurers (“SFTA”), and the proposed changes to the Quarterly Listing of Alien Insurers. As you know, we are privileged to represent twenty-five (25) insurers that currently appear on the Quarterly Listing. We are not writing on behalf of any particular client, and the views expressed below are our own. Further to our comments on the Surplus Lines Working Group call on July 7th, we are pleased to provide the following written comments on the proposed drafts.

**Surplus Lines Trust Agreement**

1. **Trust termination**

We are in favour of the NAIC’s proposal to eliminate the current 5-year notice period for termination of the trust and the substitution of a 90-day notice period instead. Most of our comments on the SFTA concern the proposed new procedure for termination, specifically:

a. **Domiciliary regulator required to determine no outstanding U.S. liabilities**

Under Section 2.1 of the SFTA, it is proposed that the domiciliary regulator of the trust must determine that “all claims attributable to the period while the Company was eligible and listed on the NAIC Quarterly Listing of Alien Insurers have been satisfied and that no outstanding liabilities remain with respect to U.S. insurance policies.”

It is not clear how this determination by the domiciliary regulator is intended to work with the requirement that currently appears in Section 2.14 of the SFTA, which requires a qualified actuary or accountant (acceptable to the trustee bank) to prepare an independent audit of any outstanding liabilities. Such audit opinion is currently submitted only to the trustee bank; the domiciliary commissioner of the trust typically has no involvement in termination of the trust other than to receive notice of termination. The proposed change of requiring the domiciliary commissioner to determine that no U.S. liabilities remain would mark a significant deviation from longstanding practice that has the potential to introduce considerable uncertainty and potential delay to the trust termination process.
To the best of our knowledge, the current process of requiring the insurer to obtain an independent audit opinion confirming no remaining surplus lines liabilities and submit the opinion to the trustee bank has worked smoothly over many years, and we are not aware of any claimants that have been disadvantaged by this process. Therefore our preference would be to retain the status quo and not introduce a requirement for the domiciliary regulator of the trust to determine that no U.S. liabilities remain.

b. Transferring liabilities to another insurer

We welcome the NAIC’s proposal to allow insurers to terminate the trust on 90 days’ notice not just by transferring liabilities to U.S. admitted insurers or other insurers on the Quarterly Listing, but also by transferring liabilities to an accredited reinsurer. This change would give insurers a wider variety of options to transfer their liabilities to other re/insurers that are subject to regulatory oversight and have assets in the U.S. for the benefit of U.S. policyholders.

We would suggest that the Working Group may also wish to consider allowing insurers to terminate their SFTA by transferring liabilities to U.S. surplus lines insurers. Currently, the SFTA only permits transfers to other alien surplus lines insurers on the Quarterly Listing, or to U.S. insurers that are admitted in all states. As you well know, U.S. surplus lines insurers are subject to regulatory oversight by their domestic state regulator and must submit the same statutory financial statements and are subject to the same minimum capital and solvency requirements as admitted insurers in their domiciliary state. It would seem to us that U.S. policyholders would be equally well protected if an insurer on the Quarterly Listing were to transfer its surplus lines liabilities to a U.S. surplus lines insurer, perhaps limited to those insurers that would meet the IID’s minimum capital and surplus standards.

c. Occurrence policies

It is proposed that the 90 days’ termination option described above would not be available to insurers that have written occurrence policies. Therefore, an insurer that wrote a single occurrence policy many years ago would be barred from terminating the trust forever, no matter how old the occurrence policy or how confident the company or a qualified actuary or auditor is that no policy liabilities remained.

If, under Section 2.14 an independent auditor must confirm that no U.S. liabilities remain before the trustee bank would be able to terminate the trust, then it would not appear to be necessary to bar all insurers that wrote occurrence policies from terminating their trusts. Therefore, we would be in favour of eliminating this proposed exception prohibiting termination of the trust for insurers that wrote occurrence policies.
d. Assumption reinsurance

Currently, insurers are permitted to terminate the trust by transferring liabilities to another licensed or NAIC-listed carrier via an “assumption and assignment agreement.” The draft SFTA would instead allow insurers to transfer liabilities via an “assumption reinsurance agreement.” As we noted on the July 7th Surplus Lines Working Group call, while this was a positive addition for those companies who wish to transfer liabilities by way of reinsurance, it would seem to eliminate the well-trodden path of terminating a trust by transferring liabilities to another NAIC-listed carrier using a mechanism such as a Part VII transfer under English law, which of course is not a reinsurance arrangement. We appreciate the NAIC agreeing with our comment on the call and we understand that the previous language permitting transfer of liabilities by way of an assumption and assignment agreement will be re-inserted, in addition to the new option of using assumption reinsurance.

2. Investments

Section 2.7 of the SFTA requires listed insurers “doing business” in California to abide by California’s rules with respect to permitted investments. This is a provision that has been in the SFTA since the early 1990’s. In our view such a state-specific provision (like any similar provision that would obligate compliance with state-specific investment rules) is now subject to challenge based on the provisions of the federal Nonadmitted and Reinsurance Reform Act (“NRRA”). The NRRA’s command that no state can deny surplus lines eligibility to an IID-listed insurer is undercut at the very least to the extent that any state’s local eligibility requirements, investment-related or otherwise, could be imposed on IID-listed carriers. We would suggest that this provision should be removed from the SFTA as it pertains to IID-listed insurers.

Should California or any other state wish to impose such investment requirements, or other financial/solvency-related requirements, upon insurers that choose to maintain or obtain a place on the state’s voluntary listing of surplus lines insurers (the LASLI for California), then states are free to do so through their own statutes, regulations, or application requirements for their voluntary lists. Indeed, California and New York have done just that by enacting statutes imposing higher minimum capital and surplus standards for surplus lines insurers appearing on their state lists.

Quarterly Listing

Finally, the NAIC has proposed to eliminate all financial information from the Quarterly Listing of Alien Insurers. Specifically, the trust fund minimum amount and balance, identity of the trustee bank, and the company’s total assets and surplus, will be deleted and only the country of domicile and US representative contact information will remain. We understand this is due to concerns that brokers and insureds might be using the information on the Quarterly Listing to choose one insurer over another, which of course has never been the intent of the list.
We note that the list of trustee banks and contact information for the banks has always been useful for new applicants for the Quarterly Listing, as well as insurers who might be looking to change their trustee bank. Not all banks are familiar with the SFTA and therefore it is helpful to know which ones have experience acting as trustees for other insurers. To that end, while we understand that the NAIC no longer wishes to publish this information, we would appreciate if the NAIC could privately maintain a list of the trustee banks and make it available upon request to new applicants or companies already on the IID List.

***

We are grateful to the NAIC and the Working Group for the opportunity to provide these comments. We would be pleased to discuss any of our comments at your convenience, and we thank you in advance for your kind consideration.

Yours sincerely,

Andrea T. Best

cc: Andy Daleo, NAIC
Thomas M. Dawson, McDermott Will & Emery LLP
The Surplus Lines (C) Working Group of the Surplus Lines (C) Task Force conducted an e-vote that concluded Oct. 21, 2021. The following Working Group members participated: Eli Snowbarger, Vice Chair (OK); David Phifer (AK); Michelle Lo (CA); Rolf Kaumann (CO); James A. McCarthy (MA); William Leach (NJ); Amy Garcia (TX); and Steve Drutz (WA).

1. **Adopted the NAIC Standard Form – Trust Agreement for Alien Excess or Surplus Lines Insurers**

The Working Group conducted an e-vote to consider adoption of the modifications to the NAIC Standard Form – Trust Agreement for Alien Excess or Surplus Lines Insurers. The motion passed with a majority of the members in favor of adoption.

Having no further business, the Surplus Lines (C) Working Group adjourned.

SLWG Minutes Oct21 FINAL.docx
Proposed Friendly Amendment to 2.1, Updated November 3, 2021

2.1 Duration of Trust Fund. The Trust Fund shall be irrevocable and remain in full force and effect until terminated 90 days after notification by the Company to the Trustee and the IID of intent to terminate the trust, based upon any of the following grounds for termination:

(a) The Trustee and the NAIC IID have received written confirmation from the Company that all claims attributable to the period while the Company was eligible and listed on the NAIC Quarterly Listing of Alien Insurers have been satisfied and that no outstanding liabilities remain with respect to U.S. insurance policies, based on an independent audit conducted in the manner prescribed in 2.14(a) of this Agreement.

(b) The Company has become licensed to conduct insurance business in all States where it has direct insurance in force, or has redomesticated to a U.S. jurisdiction and is an eligible U.S. surplus lines insurer in all States where it has direct insurance in force and is not licensed; or

(c) An assumption reinsurance agreement has been executed by the Company and an accredited, certified, or reciprocal reinsurer(s), or an assumption reinsurance or assignment agreement has been executed by the Company and a U.S. authorized insurer(s) or eligible surplus lines insurer(s), or an insurer(s) currently approved on the Quarterly Listing of Alien Insurers, pursuant to which the claimant has a direct claim against the authorized or eligible insurer(s) or accredited reinsurer(s), provided, however, that any such assuming insurer or reinsurer shall have capital and surplus in excess of the minimum capital and surplus required for inclusion on the Quarterly Listing of Alien Insurers.