

NEW YORK INSURANCE DEPARTMENT ISSUES DRAFT REGULATION REQUIRING DISCLOSURE OF PRODUCER COMPENSATION

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With the release of a proposed regulation entitled “Producer Compensation Transparency”, the New York Insurance Department (the “Department”) has taken a step toward requiring insurers to notify their insureds of the compensation paid to brokers and agents (“producers”). Among the purposes of the proposed New York Insurance Regulation (the “Regulation”), issued as a discussion draft, is “to protect the interests of the public by establishing minimum disclosure requirements relating to the role of insurance producers and the actual or potential conflicts of interest created by compensation paid to insurance producers.”

The Regulation defines compensation as follows:

Compensation means anything of value, including money, credits, loans, interest on premium, forgiveness of principal or interest, vacations, prizes, gifts or the payment of employee salaries, benefits or expenses, whether paid as commission or otherwise.

The heart of the Regulation provides for a prior written notice to an insured and imposes obligations on producers to supply insureds with compensation information. Section 30.3 of the Regulation provides, with emphasis added, that:

...*prior* to the issuance or renewal of any insurance contract, an insurance producer selling the insurance contract shall give the purchaser a *prominent written disclosure* that includes:

- (1) a description of the nature and amount of compensation to be received by the producer in connection with the sale;
- (2) a description of any material ownership interest the insurance producer has in the insurer issuing the insurance contract;

(3) a description of any material ownership interest the insurer issuing the insurance contract has in the insurance producer; and

(4) the following notice:

“You are purchasing a(n) [insurance policy, annuity contract, guarantee contract, surety bond] from an insurance producer.

An insurance producer is often paid by the insurance company based on the [insurance policies, annuity contracts, guarantee contracts, surety bonds] the producer sells.

The compensation that insurance companies pay to insurance producers varies from company to company and from [insurance policy to insurance policy, annuity contract to annuity contract, guarantee contract to guarantee contract, surety bond to surety bond]. Therefore, an insurance producer may have incentives to recommend a particular [insurance policy, annuity contract, guarantee contract, surety bond] to you based on the amount of compensation paid in connection with that [policy, contract, bond].

The insurance producer is required to provide you with information about his or her compensation in connection with the [insurance policy, annuity contract, guarantee contract, surety bond] you are purchasing. You also have a right to receive information from the insurance producer about any quotes or alternative [policies, contracts, bonds] the insurance producer considered and the relative amounts of compensation the insurance producer would have received in connection with those quotes or alternatives.

If you would like such information about quotes and alternatives, just ask the insurance producer. If you are not satisfied with the information you receive, you may contact the New York State Insurance Department.

Section 30.3 of the proposed Regulation also addresses a variety of situations:

(b) If the amount or value of any compensation to be received by the insurance producer is not known at the time of the sale, then the insurance producer shall describe to the purchaser in writing the method of calculating the compensation, including the factors on which compensation is based such as volume, profitability and retention, and a reasonable estimate of the amount or value. The insurance producer may state the amount as a percentage of premium.

(c) An insurance producer shall not make statements to a purchaser contradicting the disclosures required by this section or any other misleading or inaccurate statements about the role of the insurance producer in the sale.

(d) Upon a purchaser's request, an insurance producer shall provide comprehensive information about quotes solicited and received and alternative insurance contracts considered, including but not limited to a description of coverage, the premium and the compensation the insurance producer would have received in connection with those quotes or alternatives.

(e) If at the initial issuance of an insurance contract, the disclosure provided pursuant to subdivision (a) of this section expressly applies to future renewals of the insurance contract, then no additional disclosure shall be required upon renewal except if there has been a material change in the information required to be disclosed pursuant to subdivision (a) at the time of renewal.

By its terms the Regulation does not apply to:

- a) the placement of reinsurance;
- b) the placement of insurance with a captive insurance company;

- c) an insurance producer that has no contact with the purchaser, which may include wholesale brokers or managing general agents.

The Regulation requires that copies of disclosure documents be maintained by producers for three years. Insurers are required to maintain records showing the amount of any compensation an authorized insurer pays to a producer and the reasons for the compensation.¹

Contravention of the Regulation shall be deemed to be an unfair method of competition or an unfair or deceptive act and practice under the New York Insurance Law.

The Regulation is available on the home page of the Department, www.ins.state.ny.us under "New! Producer Compensation Transparency." Comments can be submitted to the Department. No deadline for comments has been set.

Clearly the Regulation represents a major expansion of regulatory oversight of producer compensation in New York. The existing standard in New York, set forth in New York Insurance Law Section 2119 requires a writing setting forth any charges to be paid to the producer by the insured. By calling for total disclosure of producer compensation, the Regulation, generated in the aftermath of the contingent commission investigations of 2006, pulls aside the curtains that have heretofore obscured producer compensation practices. Insurers and producers alike can be expected to offer resistance, out of concern that the information required to be disclosed to insureds will raise questions concerning where loyalties lie in the relationships among insureds, insurers and producers. Some will urge the Department to let well enough alone and not to arm consumers with information that could cause them to question the integrity of the process, particularly the portion of the required notice stating that "an insurance producer may have incentives to recommend a particular (insurance product) to you based on the amount of compensation paid in connection with that [policy, contract, bond]."

1. Part 243.2)(b) (1) of Regulation 1542 (11 NYCRR 243.2) requires that "...an insurer shall maintain: (1) A policy record for each insurance contract or policy for six calendar years after the date the policy is no longer in force or until after the filing of the report on examination in which the record was subject to review, whichever is longer."