

**FORC QUARTERLY JOURNAL
OF
INSURANCE LAW AND REGULATION**

Summer 1997 June 6, 1997 Vol. IX, Edition II

NEW YORK INSURANCE DEPARTMENT VOIDS COMMITMENT AGREEMENTS

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Until recently, New York domestic life insurance companies had been required by the New York Insurance Department ("Insurance Department"), as a condition of initial licensure, to execute a document entitled, "Commitment Agreement to the New York Insurance Department" ("Commitment Agreement"). Those acquiring control of such insurers were also required, prior to the approval of any such acquisition of control, to enter into such agreements. Where the immediate parent of the insurer was not the ultimate controlling party, both the immediate and the ultimate parent were required to sign the agreement.

On January 5, 1995, New York Governor George Pataki, issued Executive Order No. 2, directing all Executive Department agencies, including the Insurance Department, to identify for modification, rescission, or withdrawal those regulations which had unduly burdened the economy of New York and caused job losses or were more demanding than required to meet legislative goals. On January 31, 1995, the Superintendent of Insurance ("Superintendent") issued a memo inviting insurers and other interested parties to furnish an analysis of burdens imposed by particular regulations, and to make recommendations for the elimination, modifications or retention of insurance regulations.

The Commitment Agreement, some seven pages long and containing sixteen sections, had been perceived by many New York domestic insurers as imposing an unfair burden on life company operations. They believed (and some in fact so asserted in their responses to the Superintendent's request under Executive Order No. 2) that although many of the provisions of the Commitment Agreement substantially reiterated the requirements of New York statutes and regulations, a significant number went beyond statutory or regulatory requirements. In fact, although it may well be asserted that the provisions of the Commitment Agreement were all designed to facilitate more effective regulation of life insurers, not all of the provisions are based on provisions of the Insurance Law or the regulations of the Superintendent.

Accordingly, in an announcement warmly received by many New York domestic life insurers, the Superintendent released those domestic insurers who had entered into Commitment Agreements with the Insurance Department from the terms of those agreements. In a Circular Letter dated December 20, 1996, the Superintendent wrote:

The Insurance Department has determined that these Commitment Agreements do not meaningfully enhance regulation of subject companies, have given an unfair competitive advantage to companies not subject to a Commitment Agreement, and have likely impeded the development of the life insurance industry in New York. Effective immediately, therefore, all companies subject to a Commitment Agreement are forever released from its terms.⁽¹⁾

With the repeal of the Commitment Agreement, insurers and their parent companies who had entered into such agreements have been carefully scrutinizing the terms of the agreement to determine what their continuing obligations are.⁽²⁾ Although space limitations will not permit a discussion of all of the Commitment Agreement provisions, some of the provisions of the Commitment Agreement that have been of particular concern to life insurers are discussed below.

Stock Options

Stock Options

Paragraph 1 of the Commitment Agreement provided that neither the parent company nor any affiliate could sponsor any form of stock option plan for the officers, directors, agents, or employees of a Subsidiary except in connection with services provided to the parent or affiliate and without the prior approval of the Superintendent of Insurance, pursuant to Regulation 54.⁽³⁾

This provision had become largely irrelevant in light of amendments to Insurance Law Section 1207⁽⁴⁾ and the repeal of Regulation 54, effective December 1, 1996. In 1993, with the amendment of Insurance Law Section 1207, domestic stock life insurance companies that were not directly or indirectly subsidiaries of domestic mutual life insurance companies were relieved from the requirement that stock option plans be approved by the Superintendent. Nevertheless, Regulation 54 continued to impose prior approval requirements on all parent company plans, including those covering officers and employees of New York domestic life insurance companies that were not direct or indirect subsidiaries of domestic life insurance companies. Accordingly, until Regulation 54 was repealed, an inconsistency existed between the statute and the regulation.

While the repeal of Regulation 54 eliminated this inconsistency, the repeal also eliminated the Regulation's implicit sanction for certain plans of parent corporations that compensated the subsidiary company's officers and employees. Accordingly, companies wishing to extend parent company stock option plans to a New York domestic insurer's officers and employees must still consider the requirements of Section 1505⁽⁵⁾ (Transactions within a holding company system affecting controlled insurers), 1507⁽⁶⁾ (Management of controlled insurers) and Regulating 33⁽⁷⁾ (Allocation of Income (Receipts) and Expenses).⁽⁸⁾

Management

The Commitment Agreement also required that the Subsidiary maintain, at its home office in New York, at least one full-time administrative officer who was unaffiliated with any other company in the holding company system and who had full responsibility and authority for making management and administrative decisions and carrying out established policy.⁽⁸⁾

It seems clear that no section of the Insurance Law or regulation promulgated thereunder now requires that a company maintain on its staff a full-time officer who is unaffiliated with any other company in the holding company system. Nevertheless, insurers will continue to be subject to the requirements of Insurance Law Section 1507, which requires that even though an insurer may be a controlled insurer under New York's holding company law, the insurer be managed "so as to assure its separate operating identity consistent with this chapter [the Insurance Law]." Indeed, the Commitment Agreement provision seems likely to have been designed to help ensure compliance with Section 1507.

Presence Requirements

Probably the least popular (among life insurers) of the Commitment Agreement provisions were the requirements that New York domestic life insurers maintain, at their home offices in New York State, qualified personnel who performed certain insurance company functions. Paragraph 4 of the Commitment Agreement provided that the

Subsidiary will maintain at its home office, in the State of New York, officers and qualified personnel knowledgeable of and responsible for directing and performing the daily operations of the Subsidiary, including but not limited to the following primary insurance company functions:⁽⁹⁾

These included policyholder services, record keeping, accounting, underwriting, claims, and marketing. For a newly formed company, the underwriting, claims, and marketing functions, for the first five years of the company's operations, could be performed outside of New York. At the end of that five-year period, however, substantially all underwriting, claims, and marketing, as defined in the Commitment Agreement, was required to be performed in New York State. For example, with respect to policyholder services, the Commitment Agreement provided:

Policyholder services - such services shall comprise any and all activities involving personal contact or communication with a policyholder or beneficiary, including but not limited to policy loan applications and payments, surrender requests including computation and payment of benefits, determination and payment of policy benefits, policy conversions, beneficiary changes, policy changes, request for general information, dividend computations, premium payments policy

beneficiary changes, policy changes, request for general information, dividend computations, premium payments policy lapses and reinstatements, and consumer.⁽¹⁰⁾

Regarding the maintenance of records, the Commitment Agreement provided:

Record keeping - The Subsidiary will maintain at its home office in New York, all records, files and other sources of information relating to the operations of the company. Such record keeping shall include but not be limited to ledgers, journals, trial balances and adjusting journal entries, vouchers annual statement workpapers, and all related back-up records including EDP printouts. If it is necessary to transfer records in connection with the performance of specific services, copies of such records shall be transferred and the originals maintained at the home office of the Subsidiary. Persons providing services shall forward to the home office of the Subsidiary the originals or copies of all work papers, related records and documents prepared and utilized in connection with such services. While records which are maintained solely on EDP tapes, disks, etc., need not be forwarded to the Subsidiary, the servicer, when requested, shall provide printouts of such tapes, disks, etc. which shall be available for inspection by the Superintendent at the home office in New York.⁽¹¹⁾

In fact, it is with respect only to record keeping that some support may be found in the New York Insurance Law for the New York-presence requirements formerly imposed upon insurers by the Commitment Agreement. Insurance Law Section 325 provides:

Every domestic insurer . . . shall, except as hereinafter provided, keep and maintain at its principal office in this state its charter and by-laws . . . and its books of account, and if a domestic stock corporation a record containing the names and addresses of its shareholders, the number and class of shares held by each and the dates when they respectively became the owners of record thereof, and if a domestic corporation the minutes of any meetings of its shareholders, policyholders, board of directors and committees thereof.⁽¹²⁾

The phrase, "books of account," as used in this statute, has never, it appears, been interpreted by a court. Accordingly, because the scope of the requirement is unclear, the record keeping requirements of the statute are at the moment somewhat ambiguous. Some insurers have sought the prior advice of the Insurance Department on this issue before undertaking substantial changes in their record keeping procedures.

Company Names

As noted above, many sections of the Commitment reflect (although often with some embellishment) the requirements of provisions of the Insurance Law that remain in effect today. Section 15 of the Commitment Agreement describes a policy of the Insurance Department that clearly is based in authority granted to the Superintendent under the Insurance Law and Regulations. That Section of the Commitment Agreement provided:

In keeping with the Department's requirement that the name of the Parent or any of its affiliates or subsidiaries not be used in the Subsidiary's name unless a modifier is placed in front of the Parent or its affiliate or subsidiary's name, the Parent will not change its name nor will it permit any of its affiliates or subsidiaries to change their names in such a way as to circumvent the intention of this requirement. The Parent and the Subsidiary further agree that they will not use any advertising or printed material which circumvents the intention of this requirement by stressing or emphasizing the name of the Parent or its affiliates or subsidiaries.⁽¹³⁾

Thus, under the Insurance Department's "modifier rule," a parent or affiliate's name could not be used in the Subsidiary's name unless a modifying word was placed in front of the parent or affiliate's name. Broad authority for approving the name of any insurance corporation is, however, contained in Insurance Law Section 1201⁽¹⁴⁾, with respect to newly formed companies, and in Insurance Law Section 1206⁽¹⁵⁾, with respect to amendments of charters.

It should also be noted, however, that the approach of the Insurance Department with respect to certain kinds of names has evolved recently. Accordingly, counsel, in advising clients who are considering the formation of a New York domestic life insurer or the amendment of a charter to change an existing company's name, should not rely heavily on what have until recently been considered established policies of the Insurance Department regarding permissible names.

Counsel for companies that were affected by the terms of the Commitment Agreement should stay alert for possible regulatory activity at the New York Insurance Department in this area. Earlier this year, Insurance Department personnel took preliminary steps toward developing a regulation that would partially replace the Commitment Agreement.

1. N.Y. Ins. Dep't, Cir. Letter No. 19 (1996).

2. The initial paragraph of the Commitment Agreement provided:

Pursuant to your [the Superintendent's] request, the undersigned, [ultimate parent], [immediate parent], (hereafter collectively referred to as the "Parent") and [New York subsidiary] (the "Subsidiary") represent and commit they will not on behalf of the Subsidiary do, indirectly or through the medium of another entity, that which is prohibited to the Subsidiary by statute, or regulation or administrative ruling of the New York Insurance Department (the "Department"), including but not limited to the following:

Thus, the scope of the Commitment Agreement expressly included any "statute, regulation or administrative ruling" that was applicable to the subsidiary, not only those set forth in the Commitment Agreement, and in effect extended the operation of those provisions to the ultimate and immediate parents. Nevertheless, the author is not aware that regulatory action stemming from the terms of the Commitment Agreement was often undertaken with respect to requirements not expressly and specifically set forth in the Commitment Agreement. It should be noted, however that New York's holding company act itself imposes certain requirements on holding companies that would otherwise apply only to controlled insurers. Insurance Law Section 1509 provides:

No holding company or controlled person shall directly or indirectly or through another person do or cause to be done for or in behalf of the controlled insurer any act intended to affect the insurance operations of the insurer which, if done by the insurer, would violate section [4228, 4229, 4230] or any sections specified in section [2402] of this chapter.

N.Y. Ins. Law 1509 (McKinney 1985).

3. 11 N.Y.C.R.R. Pt. 82.

4. N.Y. Ins. Law 1207 (McKinney Supp. 1997).

5. N.Y. Ins. Law 1505 (McKinney 1985).

6. N.Y. Ins. Law 1507 (McKinney 1985).

7. 11 N.Y.C.R.R. Pt. 91.

8. Commitment Agreement 3.

9. Commitment Agreement 4. Despite the all-inclusive wording of the Commitment Agreement, the Insurance Department generally required that only those functions specified in the Commitment Agreement be performed in New York.

10. Commitment Agreement 4(a).

11. Id. 4(b).

12. N.Y. Ins. Law 325(a)(McKinney Supp. 1997)(emphasis added).

13. Commitment Agreement 15.

14. N.Y. Ins. Law 1201 (McKinney 1985).

15. N.Y. Ins. Law 1206 (McKinney 1985).