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Circular Letter No. 18 (2010)  
November 5, 2010

**TO: All Licensed Insurance Producers and Authorized Insurers**

**RE: Implementation of and Compliance with 11 NYCRR 30 (Regulation 194)**

**STATUTORY REFERENCES: N.Y. Ins. Law §§ 201 and 301 and Article 21; 11 NYCRR § 30 (Regulation 194)**

The purpose of this Circular Letter is to set forth the Department's expectations regarding compliance by insurance producers and authorized insurers with 11 NYCRR 30 (Regulation 194 – *Producer Compensation Transparency*). Regulation 194 takes effect on January 1, 2011. In promulgating Regulation 194, the Department was committed to achieving the appropriate balance between informing purchasers as to the role and compensation of producers, while not unduly burdening producers, hindering the sales process, or imposing significant, additional costs on the sale and distribution of insurance<sup>1</sup> in New York. The Department is committed to providing appropriate and useful guidance to aid implementation of Regulation 194's requirements. Producers are encouraged to provide the Department information or evidence of any adverse effects of Regulation 194, and to submit any additional questions that they may have.

The Department expects licensees to comply fully with Regulation 194. In the first six months after the regulation's effective date, however, the Department's enforcement efforts will focus primarily on violations that are willful or egregious or demonstrate a pattern or practice of wrongdoing.

Identified below are certain methods of compliance that fulfill the requirements of Regulation 194. The list is not prescriptive or exhaustive. Other methods of compliance that producers choose to utilize may be equally reasonable and compliant with the Regulation. Though not

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<sup>1</sup> Throughout this circular letter, the terms "insurance", "insurance policy", and "insurance contract" also include bonds and annuity contracts.

required to do so, producers may wish to consult with the Department about any other method of compliance that they are considering.

### **General**

No particular format is required for the disclosures required under § 30.3(a), (b) and (d) of Regulation 194.

For annuity or other contracts also regulated by the Securities and Exchange Commission ("SEC"), any disclosure required under Regulation 194 may be incorporated into the federal prospectus disclosure required by the Securities Act of 1933 and SEC rules provided that the disclosure required under Regulation 194 is prominent. However, SEC disclosures may not be sufficient to comply with Regulation 194 and producers should be cognizant of any additional requirements imposed by the regulation.

A producer may incorporate any disclosure required by Regulation 194 into other written materials provided to the purchaser, as long as the disclosure is prominent.

Regulation 194 does not apply where an existing policy or contract is modified or otherwise amended. The regulation applies only upon the issuance of a new policy or contract.

A producer may combine all disclosures required by Regulation 194 into one document provided to the purchaser at or prior to the time of application for an insurance contract.

### **Section 30.2 – Definitions**

A producer is required under Regulation 194 to disclose compensation (as defined in the Regulation) only if the receipt of the compensation is based in whole or in part on the sale of an insurance contract or contracts.

### **Section 30.3(a) – Mandatory Initial Disclosure**

A producer that is a business entity, such as a corporation or partnership, and that sells insurance contracts through its employees or sublicensees, is the producer "selling an insurance contract" for purposes of § 30.3(a) of Regulation 194. Such a producer is therefore required to provide disclosure pursuant to Regulation 194. Such a producer need not disclose the compensation it pays to its individual employees (whether licensed or not) or sublicensees. Only one set of disclosures per transaction is required.

Initial disclosure required under this section may be made at or prior to the time of application for binding of an individual insurance contract. A producer's use of an application form to merely solicit multiple quotes does not trigger the disclosure requirements under Regulation 194.

No particular format is required for the disclosures mandated by § 30.3(a) of Regulation 194. A producer may satisfy the initial disclosure requirement with a "boilerplate" form to use for each written disclosure. An initial disclosure may be, but is not required to be, a statement a few sentences long.

In addition to the disclosures required by § 30.3(a), a producer may disclose other information such as: (1) if applicable, that the producer is prohibited by law from rebating commission or

other compensation to the insured or potential insured or otherwise providing an inducement to the insured or potential insured in order to make the sale; (2) if applicable, that compensation is limited by New York law and a general description of those limits; (3) additional information about the producer, the kind of insurance for which application is made, or the insurer; and (4) that compensation received for various sales may not be readily comparable due to differences in insurers' distribution systems and compensation structures.

The disclosures required by § 30.3(a) must be prominent.

### **Section 30.3(b) – Disclosure Upon Request**

In order to meet the requirement in § 30.3(b)(1) that the producer disclose the "amount" of compensation to be received, the producer may state the amount in a number of different ways. For example:

- A producer's known compensation may be described as the total dollar amount expected to be received based in whole or in part on the sale.
- A producer's known compensation may be described as the total amount expected to be received based in whole or in part on the sale stated as a percentage of one year of premium.
- Unlike other kinds of insurance, life insurance policies, annuity contracts, long-term care insurance policies and disability income insurance policies last for a number of years, but compensation is typically greater in the early years that the policy is in effect. Accordingly, a producer may disclose the known compensation as a percentage of the total premium paid over the expected duration of the policy or contract. For such a disclosure to be acceptable, it must state (1) the expected duration used (which must take account of appropriate mortality and termination rates for the kind of policy being sold), and (2) that most compensation is paid in the first year if such is the case, or that most of the compensation is paid in the first 5 years if such is the case. Example: "I expect to receive from the insurer 8% of the total premium you pay on this policy if you keep the policy in place for 13 years which is the expected average duration of this type of policy. Most of that compensation will be paid in the first year."

A producer may explain the § 30.3(b) compensation information orally and in an abbreviated form when a request is made so long as the information required to be disclosed is subsequently provided in a prominent writing at or prior to the issuance of the insurance contract.

A producer is not required to provide separate disclosures for multiple lines of coverage provided at the same time so long as the disclosure contains total compensation for each of the multiple lines.

Material ownership interest under § 30.3(b)(3) does not include shares of mutual funds or other substantially similar indirect ownership vehicles.

### **Section 30.3(d) – Disclosure of Reasonable Estimate of Compensation**

Compensation is "not known at the time of disclosure" when it is contingent upon some future occurrence such as meeting sales volume, profitability or retention targets.

Compensation that may not be paid, or that the producer may be required to return to the insurer, merely because the policyholder cancels or ceases paying premiums on the policy (e.g., commissions subject to chargeback) does not constitute compensation "not known at the time of disclosure."

A producer is not required to disclose detailed compensation structures but must provide a description of the circumstances that may determine the receipt and amount or value of any compensation not known at the time of disclosure. For example: "I may also be eligible for additional compensation depending upon a number of factors including premium and policy volume, losses and profitability."

In order to meet the requirement in § 30.3(d)(2) that the producer disclose "a reasonable estimate" of the amount or value of unknown compensation to be received, the producer may estimate the amount in a number of different ways. For example:

- A producer may estimate the unknown compensation as a reasonable range of percentages of premium based on the amount of such compensation the producer has received on the sale of similar policies in prior years.
- A producer may estimate the unknown compensation as a reasonable range of dollar amounts based on the amount of such compensation the producer has received on the sale of similar policies in prior years.
- When a producer's unknown compensation received based on the sale of similar policies in prior years is not readily available or calculable, the producer may use an estimate provided by the insurer and based on the average amount of such compensation paid to producers per dollar of premium for similar policies in prior years.
- For life insurance policies, annuity contracts, long-term care insurance policies and disability income insurance policies, a producer may estimate the unknown compensation as an additional range of percentages of the total premium paid over the average duration of the policy or contract in accordance with the paragraph discussing life insurance policies and annuity contracts under Section 30.3(b) above.
- A producer who works exclusively for one insurer may estimate unknown compensation by stating all such compensation the producer receives in a given year as a percentage or range of percentages of the producer's total yearly compensation.

### **Section 30.5 – Exceptions**

For purposes of the disclosure requirement in § 30.5(e), the payment of premium installments does not constitute a renewal. However, as a practical matter, the producer should be prepared to provide additional information about compensation if the purchaser requests it.

Subject to the exceptions set forth in § 30.5, any producer that is acting as a producer (i.e., requires a producer license for the activity at issue) must comply with Regulation 194.

Section 30.3 provides that the insurance producer selling an insurance contract has the disclosure obligations required by the regulation. The disclosure requirements of the regulation do not apply to:

- a salaried, licensed employee representative whose activities do not require a producer's license and who does not receive compensation based in whole or in part on the sale of insurance. Such a salaried employee may receive compensation for meeting criteria that are not based in whole or in part on insurance sales, such as number of applications taken by phone, payments made by phone and obtaining customer feedback surveys; or
- a producer, such as a wholesaler or managing general agent, whose primary contact is with the selling agent or broker, and who has no contact with the purchaser that involves sales or solicitation. A producer, such as a wholesaler or managing general agent, does not have "direct sales or solicitation contact" with the purchaser under § 30.5(c) solely because the selling producer provides the name and contact information of the wholesaler, managing general agent or other producer to the purchaser.

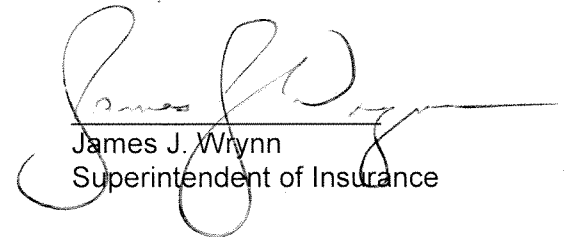
**Section 30.6 – Obligations of an Authorized Insurer**

An insurer may delegate to a licensed insurance agent its obligation under § 30.6 to maintain records regarding the amount of compensation paid to the agent, provided that the agent maintains the records in accordance with 11 NYCRR 243 (Regulation 152).

Please direct any questions or comments regarding the contents of this Circular Letter to:

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Very truly yours,



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