



25 Chamberlain St. • P.O. Box 997 • Glenmont, NY 12077-0997 • (518) 434-3111 • Fax (518) 434-2342

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Testimony re—Producer Compensation 7-25-08

Thank you for the opportunity to provide this written testimony. My name is Gary Ricker Jr. I am president of the Professional Insurance Wholesalers Association of New York Inc. (PIWA). PIWA is the only group representing independent insurance wholesalers in New York. PIWA members are primarily small businesses located throughout New York State. They provide specialty property/casualty insurance markets for retail producers. These markets are through admitted and nonadmitted insurance companies.

As wholesalers, we do not deal directly with the public. Rather, we deal with retail producers who do not have the market for the kinds of risks they are trying to place. Many of these risks are special, unique or hard-to-place, and don't lend themselves to the standard markets.

Wholesalers hold excess line brokers licenses. As excess line brokers, we have to comply with the complicated provisions of the Insurance Law and Regulation 41. Also, since an excess line broker is a broker, we are also subject to Section 2119 of the Insurance Law. This provision states:

“No insurance broker may receive any compensation, other than commissions deductible from premiums on insurance policies or contracts, from any insured or prospective insured for or on account of the sale, solicitation or negotiation of, or other services in connection with, any contract of insurance made or negotiated in this state ... unless such compensation is based upon a written memorandum, signed by the party to be charged, and specifying or clearly defining the amount or extent of such compensation.”

PIWA members, when placing excess line risks, use the “TOTAL COST FORM”. The Total Cost Form is provided by the retail producer to the insured for signature. It is combined with the Notice of Excess Line Placement, which provides the requisite disclosure requirements when placing coverage in the nonadmitted market. The Total Cost Form discloses the policy premium, insurer imposed charges (policy fees and inspection fees) and service fee charges (the excess line tax, the stamping fee, the broker fee, the inspection fee and other specified expenses).

The Total Cost Form is signed by the insured, returned to the retailer. The retailer, in turn, returns it to the wholesaler.

Regarding disclosure, PIWA believes that this disclosure, which satisfies the law, is sufficient.

The expectation of retailers in using wholesalers is to obtain coverage for the hard-to-place risks, and to minimize problems if a claim occurs sometime in the future. Intrinsic in this is that a commission will be paid to the wholesaler. Also intrinsic is the payment of commission to the retail producer from the customer's point of view. In the various states which have adopted producer disclosure regulations, the independent wholesaler has been exempted from these regulations, since the wholesaler does not deal directly with the public.

As you know, contingent commissions are permitted under New York law. They are implicitly recognized by the Court of Appeals in *Amusement Business Underwriters v A.I.G.*, 498 NYS 2d 760 (1985), and explicitly by the First Department Appellate Division in *People v. Liberty*, 2008 NY Slip Op 05570, (June 19, 2008) and in *Hersch v DeWitt Stern Group, Inc.*, 43 AD 3d 644, (2007): "Contingent commission agreements between brokers and insurers are not illegal (*see Amusement Bus. Underwriters v A.I.G.*, 66 NY 2d 878 (1985), and, in the absence of a special relationship between the parties, defendant had no duty to disclose the existence of the contingent commission agreement...".

With this as a background, let me address the questions:

Q. Whether contingent commissions or other forms of producer compensation create irreconcilable conflicts of interests for producers.

A. We would answer this in the negative. The problem was that large brokers used their economic leverage to obtain the best deal for themselves, not necessarily their clients. Contingent commissions provide opportunities for brokers to share in the success of the placements and should not be discouraged.

Questions have been raised by the department that the producer will not advocate on the customer's behalf if the producer's contingent commission is based on the profitability of the business. In other words, the perception is that this is an inherent conflict of interest, the producer won't fight to have the claim paid. The reality is anything but this. The producer, whether he or she is a retailer, wholesaler, agent or broker who would engage in this would find themselves quickly without any clients.

Q. Whether contingent commissions or other forms of producer compensation lead producers to "steer" clients to less favorable insurers or insurance products.

A. We don't really see that. Even in the cases against the four brokerage companies, there was never an issue regarding the quality of the insurers or the insurance products.

Q. Whether such steering should be considered an unfair act or practice within the meaning of Article 24 of the Insurance Law.

A. No.

Q. Whether contingent commissions, supplemental commissions or other incentive-based producer compensation should be permissible.

A. Yes, they are legal. Often producers have to work harder when placing coverage with a company that does not have a “brand” name, which is, is not familiar to the customer.

Q. Whether insurance producers in this state should be required to disclose fully to the insured any compensation from the insurer or other entity relating to the issuance, renewal of the insured’s insurance policy or annuity contract.

A. While we do not think this is necessary, when a person goes to a store or automobile dealership, is there a requirement for disclosure of the sales commission? We think the independent wholesaler should be exempted from any such requirement, beyond that currently required.

Q. Whether insurance producers in this state should be required to obtain the insured’s written consent before receiving any compensation.

A. Again, we think the current practice is fine.

Q. Whether disclosure and/or written consent requirements should apply to all agents and brokers and all insurance products.

A. No.

Attachment: SAMPLE TOTAL COST FORM

NOTICE OF EXCESS LINE PLACEMENT

Date:

Consistent with the requirements of New York Insurance Law and Regulation 41 _____ is hereby advised that after a diligent effort to place the required insurance with companies authorized in New York to write coverages of the kind requested, all or a portion of the required coverages have been placed by _____ with insurers not authorized to do an insurance business in New York and which are not subject to supervision by this State. Policies issued by such unauthorized insurers may not be subject to all of the regulations of the Superintendent of Insurance pertaining to policy forms. In the event of insolvency of the unauthorized insurers, losses will not be covered by any New York State Insolvency Fund.

TOTAL COST FORM (NON TAX ALLOCATED PREMIUM TRANSACTION)

In consideration of your placing my insurance as described in the policy referenced below, I agree to pay the total cost below which includes all premiums, inspection charges⁽¹⁾ and a service fee that includes taxes, stamping fees, and (if indicated) a fee⁽¹⁾ for compensation in addition to commissions received, and other expenses⁽¹⁾.

I further understand and agree that all fees, inspection charges and other expenses denoted by⁽¹⁾ are fully earned from the inception date of the policy and are non-refundable regardless of whether said policy is cancelled. Any policy changes which generate additional premium are subject to additional tax and stamping fee charges.

Re: Policy No.

Insurer

Policy Premium	\$
<u>Insurer Imposed Charges:</u>	
Policy Fees ⁽¹⁾	\$
Inspection Fees ⁽¹⁾	\$ _____
Total Taxable Charges	\$
<u>Service Fee Charges:</u>	
Excess Line Tax (3.60%)	\$
Stamping Fee	\$
Broker Fee ⁽¹⁾	\$
Inspection Fee ⁽¹⁾	\$
Other Expenses (specify) ⁽¹⁾ _____	\$ _____
Total Policy Cost	\$ _____

(Signature of Insured)

⁽¹⁾ = Fully earned