STATE OF NEW YORK
INSURANCE DEPARTMENT
25 BEAVER STREET
NEW YORK, NEW YORK 10004

David A. Paterson
Governor

James J. Wrynn
Superintendent

OGC Op. No. 10-03-02

The Office of General Counsel issued the following opinion on March 5, 2010, representing the position of the New York State Insurance Department.

Re: Prior Approval of Reinsurance Agreement

Questions:

1) N.Y. Ins. Law § 1308(e)(1)(A) (McKinney 2006 & Supp. 2009) requires, during any period of twelve consecutive months, a domestic insurer (other than a life insurer) to submit its reinsurance agreements that cede an amount of insurance "on which the total gross reinsurance premiums are more than fifty percent of the unearned premiums on the net amount of its insurance in force at the beginning of such period" to the Superintendent of Insurance for prior approval. Does "insurance in force," as those words are used in Insurance Law § 1308(e)(1)(A), mean all of the in-force policies issued by an insurer, or a sub-class thereof, such as in-force policies that are reinsured and cover risks located in New York?

2) Should XYZ, a property/casualty insurer, submit to the Superintendent of Insurance its proposed reinsurance agreement to reinsure all, or almost all, of its motor vehicle lessor/creditor gap insurance policies through an insurer that is not authorized to do an insurance business in New York?

Conclusions:

1) "Insurance in force," as used in Insurance Law § 1308(e)(1)(A), means all of the in-force policies issued by an insurer, regardless of whether the policies are reinsured or cover risks located in New York.

2) Yes. XYZ should submit to the Superintendent of Insurance its proposed reinsurance agreement to reinsure all, or almost all, of its motor vehicle lessor/creditor gap insurance policies through an insurer that is not authorized to do an insurance business in New York

Facts:

XYZ, a domestic property/casualty insurer, reported that it is considering writing a new line of business, which it identified as "Other Liability insurance or Creditor GAP insurance" and described as "a policy [issued] to a lender (could be licensed auto dealer) to insure their contractual obligations under Debt Waiver addenda they sell in conjunction with loans they initiate." In fact, XYZ had described "motor vehicle lessor/creditor gap insurance," which is a sub-kind of insurance that is authorized by Insurance Law § 1113(a)(26)(A).

XYZ made reference to an opinion that was issued by the Insurance Department's ("Department") Office of General Counsel ("OGC"), dated January 4, 2006 ("OGC Op. 1/4/06"). XYZ contends that OGC Op. 1/4/06 "defines which reinsurance agreements require the superintendents' [sic] prior approval." Referring to that opinion, XYZ wrote:

> It says ***no domestic insurer, except life, shall by any reinsurance agreement or agreements cede an amount of its insurance on which the total gross reinsurance premiums are more than fifty percent of the unearned premiums on the net amount of its insurance in force at the beginning of such period*** without the superintendent's prior approval. Does the fifty percent

> of the unearned premium mean the unearned premium in force for our entire company, not just this particular business in New York? (Emphasis added.)

The emphasized portion of the statement, above, is a reiteration of Insurance Law § 1308(e)(1)(A). By asking whether "fifty percent of the unearned premium mean[s] the unearned premium in force for our entire company, not just this particular business in New York" XYZ essentially asks whether "insurance in force," as those words are used in Insurance Law § 1308(e)(1)(A), means all of the in-force policies issued by an insurer, or a sub-class thereof, such as in-force policies that are reinsured and cover risks located in New York.

XYZ also noted that OGC Op. 1/4/06 expresses the Department's concern with authorized insurers ceding risk for the purpose of assisting unauthorized insurers do an insurance business in New York, a practice commonly known as "fronting." XYZ then reported that it plans to enter into a reinsurance agreement with an insurer that is not authorized to do an insurance business in New York to cede all or almost all of the risk associated with the new line of motor vehicle lessor/creditor gap insurance business. With respect to the reinsuring company, XYZ wrote: "This other company is licensed in many states but not currently in New York. They are in the process of obtaining their certificate of authority but as you know that process can take years. They have immediate business they would like to participate in the state of New York but would require our assistance."

Although XYZ did not specifically ask whether it should submit its proposed reinsurance agreement to the Department for prior approval, it is apparent that it provided information about the transaction for the purpose of obtaining some guidance in this regard.

Analysis:

I. Insurance Law § 1308(e)(1)(A)

Insurance Law § 1308(e)(1)(A) reads as follows:

> (e)(1) During any period of twelve consecutive months, without the superintendent's permission:
>
> (A) no domestic insurer, except life, shall by any reinsurance agreement or agreements cede an amount of its insurance on which the total gross reinsurance premiums are more than fifty percent of the unearned premiums on the net amount of its insurance in force at the beginning of such period;

XYZ asked whether "insurance in force," as those words are used in Insurance Law § 1308(e)(1)(A), means all of the in-force policies issued by the insurer. In fact, that is the interpretation historically accorded by the Department, as indicated in OGC Opinion dated September 12, 1947, and the Seventy-First Annual Report of the Superintendent of Insurance for the Year Ended December 31, 1929. The Department's interpretation of Insurance Law § 1308(e)(1)(A) is the one most consistent with the plain language of the statute.

Thus, Insurance Law § 1308(e)(1)(A) requires a domestic (non-life) insurer to submit its proposed reinsurance agreement to the Superintendent for prior approval, when such insurer seeks to cede, during any period of twelve consecutive months, an amount of its insurance on which the total gross reinsurance premiums exceed half of the unearned premiums on the net amount of its "insurance in force" (meaning, all of the in-force policies issued by the insurer) at the beginning of such period.

II. Submission of Reinsurance Agreement

XYZ provided little information about its proposed transactions, other than noting that XYZ is considering writing motor vehicle lessor/creditor gap insurance business, and anticipates ceding all, or almost all, of the risk arising from that new business with an insurer that is not authorized to do an insurance business in New York. Although XYZ did not specifically ask whether the proposed reinsurance transaction is permissible under the Insurance Law, it is apparent that it provided such information for the purpose of seeking guidance.

The Department cannot opine as to whether the reinsurance transaction XYZ proposes is permissible under the Insurance Law without full disclosure of all the facts. As noted in XYZ's inquiry, the Department, in OGC Op. 1/4/06, expressed its concerns about an insurer ceding all, or substantially all, of its risk to an unauthorized insurer, because such extensive reinsurance may indicate "fronting" in violation of Insurance Law §§ 1102 and 2117. OGC Op. 1/4/06 describes fronting in relevant part as follows:

> This situation occurs when unauthorized insurers, in order to avoid New York's statutory requirements, enter into reinsurance agreements with domestic companies who, in essence, act as fronting companies for the unauthorized insurers. Any arrangement or activity that would constitute the aiding of an unauthorized insurer would violate Section 2117 of the Insurance Law, and any authorized insurer that did any business that is equivalent to one of the specified types of insurance contained in N.Y. Ins. Law § 1101(b)(1) (McKinney Supp. 2005) in a manner designed to evade the provisions of the Insurance Law would be in violation of N.Y. Ins. Law § 1102 (McKinney Supp. 2005).

The reinsurance transaction that XYZ described seems to suggest that the reason it wishes to write motor vehicle lessor/creditor gap insurance business, and reinsure it with an unauthorized insurer, is to allow the reinsurer to engage in the motor vehicle lessor/creditor gap insurance business in New York while it awaits licensure in New York – an act that constitutes fronting. Therefore, XYZ should submit its proposed reinsurance agreement to the Department's Property Bureau for review and analysis.

For further information you may contact Associate Attorney Sally Geisel at the New York City Office.