

September 8, 1960

SUBJECT: INSURANCE

TO ALL AUTHORIZED INSURERS WRITING GROUP LIFE, ANNUITIES AND ACCIDENT AND HEALTH BUSINESS:

Gentlemen:

The purpose of this circular letter is to acquaint all authorized insurers, writing group life, annuities and accident and health business, with the Department's position regarding a proposed rider form whereunder the amount required to be paid as the insurance premiums, for group life and group accident and health insurance, by the policyholder after the first policy year shall be limited to the amount actually paid for claims only (subject to a specified maximum) plus an administrative and contingency charge. Under this rider the policyholder agrees, in the event the group contract is terminated, to pay to the insurance company the amount of all claims (due and unpaid, in course of settlement, and incurred but unreported) as they emerge after termination of the group contract.

This proposal and analagous "cost plus-no claim reserve-stop loss" types of group contract depart from the traditional form of insurance contract whereby the insurance company's obligation to pay an insurance benefit is conditioned upon the payment of a stipulated consideration or insurance premium, payable during the contract year in an amount sufficient to pay all claims incurred in such year. Instead, under this new type of agreement, the insurer relies on a promise of the group policyholder to pay to the insurer in the future and after the claims are incurred, such as the benefits upon the death or continued disability of the persons insured, a sum of money which is not in fact an insurance premium but an amount equal to the incurred claims plus an administrative and contingency charge. This type of agreement, in effect, transfers the reserves for outstanding claims (due and unpaid, in the course of settlement, and incurred but unreported) from the insurance company to the policyholder. There is a serious question whether the agreement is, in fact, one of insurance.

The making of such an agreement would be inconsistent with the obligation of the insurance company to report the full reserve liability for outstanding claims (due and unpaid, in course of settlement, and incurred but unreported) in its annual statement, notwithstanding that, at the same time, the company may not take credit as an admitted asset under the Insurance Law for the obligation of the policyholder to pay to the company the amount of incurred claims plus an administrative and contingency charge, so that, in effect, the claim reserves must be advanced from the company's surplus.

The rider form referred to in the first paragraph, by incorporating therein the concept whereby the insurance premiums are determined and are collectible after the losses have occurred, rather than in advance of the occurrence of the losses, with its resulting adverse effect upon the surplus of the insurance company, is no[ILLIGIBLE WORDS] approvable by this Department because:

- (1) the issuance of the life insurance benefit thereunder, in the judgment of the Superintendent of Insurance, would encourage misrepresentation and be prejudicial to the interests of policyholders generally and the form contains provisions which are unjust, unfair and inequitable; and
- (2) to the extent that accident and health insurance benefits are involved, the form contains provisions which encourage misrepresentation and are unjust, unfair, inequitable, and contrary to the public policy

of this State.

In addition, the Department has concluded that the terms for making these so-called premium payments which would be granted to particular group policyholders under the proposed policy provision or endorsement, in the absence of any justifiable basis for the differential in charges to such policyholders, would constitute an unfair discrimination.

Very truly yours,

(Signed)THOMAS THACHER

Superintendent of Insurance