

August 16, 1989

SUBJECT: INSURANCE

Circular Letter No. 11 (1989)

August 16, 1989

TO: ALL LICENSED PROPERTY/CASUALTY INSURERS & PRODUCER ORGANIZATIONS

RE: STATUTORY REVISIONS AFFECTING CANCELLATION, CONDITIONAL RENEWAL AND NONRENEWAL OF COMMERCIAL RISK, PROFESSIONAL LIABILITY AND PUBLIC ENTITY INSURANCE POLICIES IN NEW YORK STATE

Chapter 235 of the Laws of 1989, which became effective July 1, 1989, contains a number of significant amendments to Section 3426 of the Insurance Law. Originally enacted in 1986 as part of Omnibus Insurance Legislation (Chapter 220 of the Laws of 1986), Section 3426 sets forth provisions governing the cancellation, conditional renewal and nonrenewal of commercial lines insurance policies. The changes are generally designed to simplify complicated provisions that, even after these changes, remain relatively complex. The purpose of this Circular Letter is to outline the major changes that have been enacted.

EXCESS LIABILITY POLICIES, HYPER LIMITS EXCESS POLICIES AND JUMBO RISKS

Section 3426 now provides certain special rules or exceptions for excess liability policies, hyper limits excess liability policies and policies insuring jumbo risks, from otherwise applicable rules regarding cancellation, conditional renewal and nonrenewal.

Section 3426(a)(6) defines an excess liability policy as a policy written over one or more underlying policies providing, in the aggregate, at least \$ 500,000 in liability coverage.

Section 3426(a)(7) defines a hyper limits excess liability policy as an excess or umbrella policy which is written over an underlying policy or policies providing, in the aggregate, at least \$ 10 million in coverage.

Section 3426(a)(8) defines a jumbo risk as a business entity that generates gross revenues in excess of \$ 100 million annually, and develops an annual liability premium of at least \$ 500,000. However, this definition does not include any public entities or not-for-profit corporations.

Cancellation of Excess Policies

In addition to the grounds for cancellation specified in § 3426(c)(1), (2) and (3), another ground for cancellation has been added for excess policies only. Section 3426(c)(4) now permits an insurer to cancel an excess policy if one or more of the underlying policies is cancelled for one of the reasons specified in § 3426(c)(1), (2) or (3), and such underlying policy is not replaced without a lapse in coverage.

Example 1. Company A has in effect a \$ 1,000,000 excess of \$ 500,000 umbrella policy on Insured X. Company B, providing the primary coverage of \$ 500,000 cancels its policy due to non-payment of premium, effective October 15, 1989. Company A would have the right to cancel its umbrella policy

unless Insured X replaced the primary policy with another policy having an effective date not later than October 15, 1989. Even a single day lapse in coverage would be adequate grounds for cancellation of the excess policy.

Renewal of Excess Policies and Jumbo Risk Policies

There are two exceptions to the provisions of § 3426(e) regarding renewal:

1. The provisions of § 3426(e), regarding conditional renewal or alternative renewal only, no longer apply to hyper limits excess liability policies [§ 3426(e)(9)]. However, its provisions regarding nonrenewal continue to apply to such policies; and

2. In the case of excess policies and jumbo risk policies, notices are required to be given at least 30, but not more than 120, days prior to policy expiration. For non-excess policies, the required time frame remains at least 60, but not more than 120, days prior to policy expiration, pursuant to § 3426(e)(3).

Required Policy Period for Excess Policies

Section 3426(d)(2) now permits an excess policy to be written for a term of less than one year, where the specific term is made to coincide with the term of an existing underlying policy written by any insurer.

RENEWAL PROVISIONS

In addition to the foregoing changes relative to excess policies, the following provisions apply to all covered policies:

Late Notice of Nonrenewal

A notice of nonrenewal is considered late if it is mailed less than 60 days prior to the policy's expiration date. The provisions regarding a late nonrenewal notice remain essentially unchanged.

If a late nonrenewal notice is mailed prior to policy expiration, coverage shall remain in effect at the same terms and conditions, and at the lower of the current rates or the prior period's rates, for a period of 60 days from the date such late notice is mailed.

In the event that a late notice of nonrenewal is mailed on or after the expiration date, or not mailed at all, coverage shall continue for another required policy period at the same terms and conditions of the expiring policy, and at the lower of the current rates or those of the expiring policy. If the insured elects to replace the policy or cancels during this additional required policy period, such policy shall be cancelled on a pro-rata basis.

Late Notice Conditional Renewal

A notice of conditional renewal is considered late if it is mailed less than 60 days prior to the policy's expiration date. The effect that a late notice of conditional renewal will have on an insured will vary, based upon whether or not the notice was mailed prior to policy expiration and, if mailed prior to expiration, whether it was more or less than 30 days prior to such expiration.

Notice Mailed Between 59 and 30 Days Prior to Expiration. In the event that an insurer mails a late notice of conditional renewal at least 30 days prior to expiration of the policy, coverage shall remain in effect at the same terms and conditions, and at the lower of the current rates or the prior period's rates, for a period of 60 days from the date such late notice is mailed. However, if the insured elects to renew the policy, the terms, conditions and rates of the renewal policy shall apply at the renewal date. If the insured elects to replace the coverage or cancel the policy prior to the

expiration of the additional required coverage period, such policy shall be cancelled on a pro-rata basis.

Example 2. Insured Y has a \$ 300,000 CGL policy with Company C, scheduled to expire on September 30, 1989. On August 25, 1989, Company C mails Insured Y a conditional renewal notice, advising that the renewal policy will contain an aggregate limit and that the rate will be increased by 15%. Insured Y is entitled to coverage under the terms, conditions and rates (since they are lower) of the expiring policy, until October 24, 1989. Insured Y attempts to find alternative coverage with another insurer; however, it finds that better terms, conditions and rates are not available. On October 15, 1989, Insured Y advises Insurer C that it wishes to remain with the company and will accept the renewal policy. The terms, conditions and rates of the renewal policy take effect retroactive to October 1, 1989, the renewal date of the policy.

Example 3. Assuming the same facts as set forth in Example 2 above, if Insured Y elected to replace the coverage with another carrier effective October 15, 1989, Company C would be entitled to pro rata premium for the period September 30, 1989 to October 15, 1989, based upon the rates of the expiring policy (since they are lower than the current rates).

Notice Mailed Less than 30 Days Prior to Expiration. In the event that a late notice of conditional renewal is mailed prior to policy expiration, but less than 30 days before expiry, coverage shall remain in effect at the same terms and conditions, and at the lower of the current rates or the prior period's rates, for a period of 60 days from the date such late notice is mailed. However, if the insured elects to renew the policy, the terms and conditions of the expiring policy, and the lower of the current rates or those of the expiring policy, shall continue to apply until the expiration of the required 60 day period. At that time, the terms, conditions and rates of the renewal policy will take effect. The same rule regarding pro rata premium computation applies with respect to any termination of coverage during the additional coverage period.

Example 4. Assuming the same facts as Example 2, if the required notice of conditional renewal were not mailed until September 15, 1989, coverage would remain in effect until November 14, 1989, at the terms, conditions and rates (since they are lower) of the expiring policy. If Insured Y elects to accept the terms of the renewal, the terms, conditions and rates of the renewal policy would take effect November 14, 1989.

Notice Mailed On or After Expiration Date. In the event that a late notice of conditional renewal is mailed on or after the expiration date, or not mailed at all, coverage shall continue for another required policy period at the same terms and conditions of the expiring policy, and the lower of the current rates or those of the expiring policy. If the insured elects to replace the policy or cancels during this additional required policy period, such policy shall be cancelled on a pro-rata basis.

It should be apparent that it is in the insurer's best interests to mail its nonrenewal and conditional renewal notices within the appropriate time frames established by § 3426. Thus, in addition to any penalties which this Department may impose as a result of a company's failure to comply, the Insurance Law itself imposes on insurers additional burdens that increase in proportion to the lateness of the notice.

GROUP POLICIES. MASS MERCHANDISING AND SAFETY GROUPS

Section 3426 now contains provisions that specifically deal with the unique situations involving group policies and policies issued under mass merchandising and safety group programs. These include:

Section 3426(a)(1) clarifies that any contract, certificate or other evidence of insurance is considered a "covered policy";

Section 3426(d)(2)(D) permits the first policy or certificate issued to a new participant in a group policy, mass merchandising program or safety group, to be issued for a term of less than one year, if done in order to bring such policy or certificate into coincidence with the group's common expiration date;

Section 3426(g)(4) specifies that each certificate holder is entitled to their own loss information; and

Section 3426(j) specifies that, with respect to group property/casualty policies only, the provisions regarding nonrenewal and conditional renewal of the policy only apply to the master contract, and do not apply individually to each certificate holder.

BLANKET OR MASS NONRENEWALS

Section 3426(a)(10) defines a blanket or mass nonrenewal as a situation in which an insurer, within a six-month period, is nonrenewing policies representing more than 1% of a market. It is believed that such situations would only come about if an insurer decided to totally withdraw from an insurance market.

Section 3426(e)(8) specifies that an insurer may not issue blanket or mass cancellation notices unless, at least 45 days prior to the mailing of such notices, a plan of orderly withdrawal is filed with the Superintendent, describing the proposed nonrenewals, indicating the underlying basis, and indentifying any measures the insurer intends to take to minimize market disruption.

TERMINATED AGENTS AND BROKERS

Section 3426(k) specifies that, in the event an insurer terminates its contract or account with a licensed agent or broker, such insurer must offer each affected insured the opportunity to continue policy coverage with the terminated agent or broker for the remaining portion of the required policy period. The terminated agent or broker is entitled to receive commission on all business so continued. However, the foregoing provisions do not apply to agents or brokers: (1) who exclusively represent one company or group of companies under common management; (2) who have had their license revoked by the Superintendent; or (3) whose account has been terminated, due to the agent or broker's insolvency or gross misconduct.

OTHER PROVISIONS

Among other changes enacted, here are some of the more significant:

1. Notices of cancellation must now be mailed to both the first named insured and the insured's agent or broker;
2. In lieu of cancellation pursuant to § 3426(c)(1)(D) or (E), an insurer may impose a mid-term premium increase, pursuant to § 3426(d)(1).

Example 5. Although policy conditions require maintaining an automatic fire extinguishing system in the restaurant's kitchen, Insurer D discovers that the system became inoperative 3 months into the policy period and will remain inoperative for several months. In lieu of cancelling the policy on Insured Z's restaurant, Insurer D elects to continue coverage upon the payment of an additional premium to cover the increased hazard.

3. Surety policies are now exempt, pursuant to the provisions of § 3426(1)(2); and
4. A suspension of coverage shall not be considered a cancellation of such coverage, pursuant to § 3426(m).

Any questions regarding this Circular Letter should be addressed to:

Mark Presser (212-602-0386)
Supervising Insurance Examiner
Property & Casualty Insurance Bureau
New York State Insurance Department
160 West Broadway -- 13th Floor
New York, New York 10013

A § 3426 conditional renewal "Decision Tree", devised by Mr. Presser, is annexed as an aide. This chart as well as the points discussed here are illustrations to assist insurers and insurance professionals in understanding Section 3426, as amended. The statutory revisions require close review.

Very truly yours,

[SIGNATURE]

JAMES P. CORCORAN

SUPERINTENDENT OF INSURANCE

[ATTACHMENT]

Section 3426

Conditional Renewal Notice

Decision Tree

[See illustration in printed version.]