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

**Circular Letter No. 27 (1998)**
**October 8, 1998**

**TO:** **ALL INSURERS AUTHORIZED TO WRITE LIFE INSURANCE AND ANNUITIES**

**SUBJECT: SECTION 4228 -– CONDITIONS UNDER WHICH ADDITIONAL FIRST YEAR COMMISSIONS MAY BE PAID IN RENEWAL YEARS**

New Section 4228 of the New York Insurance Law (hereinafter referred to as Section 4228), which became effective January 1, 1998, resulted in significant changes in the regulation of agent compensation. It has come to the attention of the Department that some insurers have misinterpreted Section 4228 with respect to the payment of a first year commission on a portion of periodic premiums recorded in renewal policy years. Section 4228 (b)(21) is very explicit in defining qualifying first year premium and in setting forth the conditions under which a company may pay an additional first year commission in a renewal year. A company may pay an additional first year commission in a renewal year only when there has been an increase in the periodic premiums recorded in the renewal policy years and the qualifying first year premium in policy year one is less than the benchmark gross level premium.

Below are two examples to illustrate how a company may calculate qualifying first year commissions and how it may pay first year and renewal commissions. The examples assume that the maximum first year commission rate of 55% and renewal commission rates of 22%, 20% and 18% in policy years 2, 3 and 4, respectively, are being paid to the agent.

| | |
|---|---|
| Benchmark gross level premium | $1,000 |
| Periodic premiums recorded– Policy Year 1 | $ 800 |
| Qualifying first year premiums – Policy Year 1 | $ 800 |
| First year commissions – Policy Year 1 | $ 440 |

EXAMPLE 1: Assume level premiums recorded in policy years 2 through 4

| | Policy Year 2 | Policy Year 3 | Policy Year 4 |
|---|---|---|---|
| Periodic premiums recorded (PPR) | $ 800 | $ 800 | $ 800 |
| Qualifying first year premiums (QFYP) | $ 0* | $ 0* | $ 0* |

| | | | |
|---|---|---|---|
| First year commissions (55% x QFYP) | $ 0 | $ 0 | $ 0 |
| Renewal premiums (PPR – QFYP) | $ 800 | $ 800 | $ 800 |
| Renewal commissions<br>(Renewal commission rate x renewal premiums) | $ 176 | $ 160 | $ 144 |

* QFYP = PPR ($800) less total previous QFYP ($800) = 0

In Example 1, there are no additional first year commissions in any year after the first as there has been no increase in the periodic premiums recorded.

EXAMPLE 2: Assume non-level premium with recorded premiums increasing $100 each year in policy years 2 through 4

| | Policy Year 2 | Policy Year 3 | Policy Year 4 |
|---|---|---|---|
| Periodic premiums recorded (PPR) | $ 900 | $1,000 | $1,100 |
| Qualifying first year premiums (QFYP) | $ 100** | $ 100** | $ 0** |
| First year commissions (55% x QFYP) | $ 55 | $ 55 | $ 0 |
| Renewal premiums (PPR – QFYP) | $ 800 | $ 900 | $1,100 |
| Renewal commissions<br>(Renewal commission rate x renewal premiums) | $ 176 | $ 180 | $ 198 |

** QFYP = PPR up to the benchmark gross level premium less total previous QFYP

Policy Year 2  $900 - $800 = $100
Policy Year 3  $1000 - $900 = $100
Policy Year 4  $0 as PPR>benchmark gross level premium

In Example 2, there are additional first year commissions in policy years 2 and 3 since in each of those years there was an increase in periodic premiums recorded <u>and</u> the recorded premiums in those years (which are less than the benchmark gross level premium) less the total previous QFYP is greater than zero. However, there are no additional first year commissions in policy year 4 even though there was an increase in periodic premiums recorded because the recorded premiums in that year were greater than the benchmark gross level premium.

Please acknowledge receipt of this letter to Mr. Donald Pearsall at the State of New York Insurance Department, Agency Building 1, Empire State Plaza, Albany, NY 12257.

Very truly yours,

Martin F. Carus
Assistant Deputy Superintendent
and Chief, Life Bureau