STATE OF NEW YORK
INSURANCE DEPARTMENT
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Circular Letter No. 8 (2008)

April 14, 2008

TO: All Authorized life insurers

RE: Interpretation of "retirement" in Insurance Law § 4228(b)(24) with respect to non-qualifying employee benefit plans

STATUTORY REFERENCE: Insurance Law § 4228 and Internal Revenue Code § 409A

N.Y. Insurance Law § 4228 (McKinney 2007) governs compensation to insurance agents and brokers with respect to individual life insurance policies and annuity contracts, and imposes limitations on the amount that agents and brokers may receive. Certain "security benefits," as defined by Insurance Law § 4228(b)(24)(B), are excluded in the computation of those limits by reason of Insurance Law § 4228(e)(5). An excluded "security benefit" is:

> [A]ny benefit provided to an agent that is both (A) provided under an employee benefit plan, as defined in the Employee Retirement Income Security Act of 1974, 29 U.S.C. §§ 1001, et seq. and (B) either (i) a benefit under an employee benefit plan that qualifies as such under the relevant sections of the Internal Revenue Code and regulations thereunder that require compliance with standards of non-discrimination in benefit coverage and eligibility, or (ii) a benefit that does not permit an agent to obtain a cash payment other than at the time of death, permanent and total disability, or retirement.

Subparagraph (ii) refers to what are generally referred to as "nonqualified plans" or "nonqualified deferred compensation." For those plans, absent the death or permanent and total disability of the participant, payments of benefits under the employee benefit plan depend upon "retirement" – a term that is nowhere defined in the statute.

The termination of employment or retirement date for a life insurance agent is not always easily ascertained because of the manner and timing of agent compensation. Life insurance agents are not compensated solely for time or items completed. An agent is paid compensation when he or she originates an insurance contract, but also if the contracts remain in force. An agent who has had a successful career may well continue to receive substantial compensation, even though no longer performing origination services. Further, because of the personal relationships established between agents and customers, an agent may be asked to originate a new contract (and thus earn new compensation) for a past customer, even though the agent is not actively pursuing new business.

Because life insurance agent compensation and services generally decrease gradually rather than stop abruptly, it is very difficult to identify a specific date upon which retirement or separation from service has occurred. That difficulty has been highlighted by recent changes made to the federal tax law applicable to such plans by the American Jobs Creation Act of 2004, P.L. 108-357 effective, generally, for amounts deferred after December 31, 2004.

Specifically, § 409A(a)(2)(A) of the Internal Revenue Code of 1986 (IRC), as amended, as implemented in Treas. Reg. § 1.409A-3 (effective generally on January 1, 2009), now require that nonqualified plans pay distributions of previously deferred compensation only upon the occurrence of one of six events:

- Separation from service;
- The date the participant becomes disabled;
- Death;
- An objectively determinable specified time (or pursuant to a fixed schedule specified in the plan) after which the compensation can no longer be deferred;
- A change in the ownership or effective control of the corporation or assets of the corporation, to the extent provided in regulations; or
- The occurrence of an unforeseeable emergency.

In addition, under IRC § 409A(a)(2)(B), key employees (as defined in IRC § 416(i)) of publicly traded corporations may not take distributions until six months after separation from service or, if earlier, the date of death of the employee.

Life insurance companies must modify their present benefit plans to conform to the requirements of IRC § 409A no later than December 31, 2008. However, the federal tax provisions do not correspond to the historical employment practices for life insurance agents who often decrease services and compensation gradually and unevenly. Specifically, a “separation from service” under Treas. Reg. § 1.409A-1(h)(1), applicable to employees, requires that bona fide services continue at a level less than 20 percent of the average level of services performed during the preceding 36-month period. For independent contractors, a “separation from service” under Treas. Reg.§ 1.409A-1(h)(2) requires a complete termination of the contractual relationship.

In order to reconcile federal and state requirements, life insurers have requested that this Department interpret the term “retirement” under Insurance Law § 4228(b)(24)(B)(ii) to include certain combinations of age and years of service that could be ordinarily viewed as appropriate for retirement without regard to whether the agent in fact continues to perform services or receive compensation for past services. These combinations of age and service are intended satisfy the “objectively determinable” standard for the commencement of benefits at a specified time as required by the Department of Treasury’s regulations [Treas. Reg. § 1.409A-3(i)(1)].

Taking into account the above facts, and giving meaning to the term “retirement” in Insurance Law § 4228(b)(24)(B), to produce both a practical and reasoned interpretation, the Department will consider certain age and service requirements, which are representative of the age and service requirements for receiving immediate payments under existing security benefit plans, as satisfying the retirement criteria. In particular, an insurer may consider payments made after the following specified times as being made after retirement for purposes of Insurance Law § 4228:

(1) The earliest date on which the agent’s age is at least 55 and the sum of the agent’s age and years of service with the insurer is at least 70; or

(2) The earliest date on which the agent’s age is at least 60 and the sum of the agent’s age and years of service with the insurer is at least 65.

Other specified times that are later than those listed above, so that both the attained age and the age plus service thresholds are higher than either of those in the examples above, should equally satisfy the retirement criteria. However, an insurer that wishes to use a specified time for purposes of IRC § 409A(a)(2)(A)(iv) that differs from the standards in both (1) and (2) above and from the standards of the preceding sentence must demonstrate to the Department that the proposed standard satisfies the retirement criteria based on expected agent experience.

All questions and comments regarding this circular letter should be directed to:

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Very truly yours,

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