



NEW YORK STATE
DEPARTMENT *of*
FINANCIAL SERVICES

Andrew M. Cuomo
Governor

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Superintendent

Insurance Circular Letter No. 5 (2016)
September 22, 2016

TO: All Domestic Stock Life Insurers

RE: Distribution of Dividends

**STATUTORY REFERENCES: Insurance Law § 4207(a); 11 NYCRR 83
(Insurance Regulation 172)**

I. Introduction

The purpose of this Circular Letter is to provide guidance to all domestic stock life insurers with respect to distributing and reporting ordinary dividends and providing notice of proposed extraordinary dividends for approval in light of recent changes to Insurance Law § 4207(a).

II. Background

Prior to amendment by Chapter 586 of the Laws of 2015 and Chapter 1 of the Laws of 2016, Insurance Law § 4207(a) provided that a domestic stock life insurer could issue ordinary dividends only in an amount that did not exceed the lesser of ten percent of its surplus or its net gain from operations, exclusive of realized capital gains. As amended, Insurance Law § 4207(a) now provides a domestic stock life insurer with two alternative methods for distributing ordinary dividends: a “greater of” method set forth in § 4207(a)(2), or a “lesser of” method, set forth in § 4207(a)(3). These amendments, described more fully below, took effect as of December 28, 2015.

III. Summary of the Law, as Amended

Insurance Law § 4207(a)(2) allows a domestic stock life insurer to distribute an ordinary dividend out of earned surplus where the aggregate amount of the dividends in any calendar year does not exceed the greater of: (1) 10% of the insurer’s surplus to policyholders as of the immediately preceding calendar year; or (2) the insurer’s net gain from operations for the immediately preceding calendar year, not including realized capital gains, provided that the dividends do not exceed 30% of the insurer’s surplus to policyholders as of the immediately preceding calendar year. Section 4207(a)(2) further states that an insurer may not distribute an ordinary dividend in the calendar year immediately following a calendar year in which the insurer’s net gain from operations, not including realized capital gains, was negative, without the approval of the Superintendent of Financial Services (“Superintendent”) in accordance with Insurance Law § 4207(a)(5).

Insurance Law § 4207(a)(1) defines earned surplus as an amount equal to an insurer's positive unassigned funds (page 3, line 35, of the annual statement, or the corresponding annual statement line in future years), excluding 85% of the change in net unrealized capital gains or losses less capital gains tax, for the immediately preceding calendar year (page 4, line 38, of the annual statement, or the corresponding annual statement line in future years). An insurer must pay ordinary dividends distributed under Insurance Law § 4207(a)(2) from earned surplus.

Insurance Law § 4207(a)(3) permits a domestic stock life insurer to distribute an ordinary dividend to its shareholders where the aggregate amount of the dividends in any calendar year does not exceed the lesser of: (1) 10% of the insurer's surplus to policyholders as of the immediately preceding calendar year; or (2) the insurer's net gain from operations for the immediately preceding calendar year, not including realized capital gains.

Insurance Law § 4207(a)(4) provides that an insurer may not distribute an ordinary dividend pursuant to both Insurance Law § 4207(a)(2) and (3) in any calendar year.

Insurance Law § 4207(a)(6) requires an insurer to report to the Superintendent all dividends distributed pursuant to § 4207(a)(2) within five business days following the declaration thereof and at least ten days prior to the payment thereof.

Insurance Law § 4207(a)(7) requires that an insurer's surplus to policyholders remain reasonable in relation to the insurer's outstanding liabilities and adequate to meet its financial needs after distributing an ordinary dividend under § 4207(a)(2).

Insurance Law § 4207(a)(8) permits the Superintendent to limit or disallow any ordinary dividend distributed under § 4207(a)(2) if the Superintendent determines that an insurer's surplus to policyholders is not reasonable in relation to the insurer's outstanding liabilities and not adequate to meet its financial needs, or the insurer is financially distressed or troubled.

If an insurer wants to distribute a dividend in excess of the amounts permitted under either Insurance Law § 4207(a)(2) or (3) (an "extraordinary dividend"), then Insurance Law § 4207(a)(5) requires the insurer to file notice of the proposed distribution and the amount thereof with the Superintendent not less than 30 days in advance, and permits the Superintendent to disapprove the distribution if the Superintendent finds that the financial condition of the insurer does not warrant the distribution.

IV. Discussion

A. Dividends Under the "Greater of" Standard (§ 4207(a)(2))

Insurance Law § 4207(a)(2) allows a domestic stock life insurer to distribute an ordinary dividend only out of earned surplus. A payment of an ordinary dividend under Insurance Law § 4207(a)(2) that exceeds the amount of positive unassigned funds could leave the insurer with a level of surplus to policyholders that is not reasonable in relation to the insurer's outstanding liabilities and thus may not be adequate to meet its financial needs under Insurance Law § 4207(a)(8).

For purposes of determining whether an insurer's surplus to policyholders is not reasonable in relation to the insurer's outstanding liabilities and not adequate to meet its financial needs, the Superintendent will consider all relevant factors, including: (1) the size of the insurer as measured by its assets, capital and surplus, reserves, premium writings, insurance in force, and other appropriate criteria; (2) the extent to which the insurer's business is diversified among life insurance, annuity contracts, accident and health insurance, legal services and salary protection insurance; (3) the number and size of risks insured; (4) the extent of the geographical dispersion of the insurer's insured risks; (5) the nature and extent of the insurer's reinsurance program; (6) the quality, diversification, and liquidity of the insurer's investment portfolio; (7) the recent past and projected future trend in the size of the insurer's surplus to policyholders; (8) the surplus to policyholders maintained by comparable insurers with respect to the foregoing factors; (9) the adequacy of the insurer's reserves; (10) the quality and liquidity of investments in subsidiaries; (11) the quality of the insurer's earnings and the extent to which the reported earnings include extraordinary items; and (12) the extent to which any proposed dividends pursuant to § 4207(a)(2) are the result of unrealized capital losses.

B. Dividends Under the "Lesser of" Standard (§4207(a)(3))

If an insurer does not have sufficient positive earned surplus to pay an ordinary dividend under § 4207(a)(2), then the insurer only may distribute an ordinary dividend under Insurance law § 4207(a)(3). An insurer may not distribute an ordinary dividend under § 4207(a)(3) in the calendar year immediately following a calendar year in which the insurer's net gain from operations, not including realized capital gains, was negative.

An insurer may distribute ordinary dividends pursuant to § 4207(a)(3) from surplus only (page 3, line 37 of the annual statement, or the corresponding annual statement line in future years). In accordance with National Association of Insurance Commissioners Accounting Practices and Procedures (IP No. 84; SSAP No. 72), which the Department of Financial Services ("Department") has adopted pursuant to § 83.2(c) of 11 NYCRR 83 (Insurance Regulation 172), dividends from, or restatement of, gross paid-in and contributed surplus may occur in accordance with a quasi-reorganization approved by the Superintendent only.

C. Dividend Reporting; Requests for Extraordinary Dividends

An insurer's report to the Superintendent required under Insurance Law § 4207(a)(6) for dividends distributed pursuant to Insurance Law § 4207(a)(2) should cite to the applicable section of law and provide the calculations made to arrive at the amount of the dividend distribution (including references to the prior year's annual statement). The report should include a detailed list of any securities or assets other than cash that the insurer intends to distribute. If there are any material changes to the list of assets or securities that occur between the time the insurer declares and distributes the dividend, then the insurer should provide an updated report to the Superintendent before the insurer distributes the dividend.

The report also should include the insurer's: (1) most recent quarterly balance sheet and income statement on file with the Department, both actual and as adjusted to reflect the dividend as if it had been paid during that prior quarter; and (2) risk-based capital ("RBC") ratio for the immediately preceding calendar year end, both actual and as adjusted to reflect the dividend as if it had been paid during that prior calendar year. In addition to reporting the amount of the ordinary

dividend payable, the report should include the cumulative amount of ordinary dividends that the insurer has paid in the current calendar year. The Superintendent will acknowledge receipt of the insurer's report and payment date, but generally will not issue a subsequent letter of non-disapproval because it is not required by law.

An insurer is not required under the law to make a report to the Superintendent for dividends distributed under Insurance Law § 4207(a)(3). However, the Department strongly encourages insurers to report such dividends in a manner substantially similar to Insurance Law § 4207(a)(6).

If an insurer wants to distribute a dividend in excess of amounts permitted under §§ 4207(a)(2) or (3) (i.e., an extraordinary dividend distribution), then the insurer must file notice of the proposed distribution with the Superintendent pursuant to § 4207(a)(5). In addition to reporting the amount of the proposed extraordinary dividend, the notice should include the: (1) insurer's most recent quarterly balance sheet and income statement on file with the Department, both actual and as adjusted to reflect the dividend as if it had been paid during that prior quarter; (2) insurer's RBC ratio for the immediately preceding calendar year end, both actual and as adjusted to reflect the dividend as if it had been paid during that prior calendar year; and (3) cumulative amount of ordinary dividends that the insurer has paid in the current calendar year. If the superintendent does not disapprove the proposed extraordinary dividend within the time prescribed pursuant to paragraph § 4207(a)(5), then the insurer may distribute the extraordinary dividend.

V. Conclusion

Please direct any questions regarding this circular letter to Mark McLeod, Deputy Chief, at (212) 480-4937 or Mark.McLeod@dfs.ny.gov, or James Matheson, Assistant Chief, at (212) 480-5040 or James.Matheson@dfs.ny.gov.

Very truly yours,

James V. Regalbuto
Deputy Superintendent for Life Insurance