

OPINION NO. 82-091**Syllabus:**

1. 3 Ohio Admin. Code 3901-1-15 limits the ability of a non-admitted or unauthorized reinsurer, which is controlled by an admitted credit insurer that intends to issue credit coverage to certificate holders of a vendor and cede the business to the reinsurer, to pay dividends to the vendor stockholders based upon the profit from the vendor. The Rule is not applicable, however, if the reinsurer is not controlled by the credit insurer.
2. The Department of Insurance may refuse to accept a security registration filing pursuant to R.C. 1707.09, or may revoke such registration, if the issuer's intended method of operation violates Rule 3901-1-15.

To: Robert H. Katz, Director, Department of Insurance, Columbus, Ohio
By: William J. Brown, Attorney General, November 4, 1982

I have before me your request for my opinion regarding certain reinsurance transactions involving credit insurance for life or disability coverage. Your specific questions are:

- 1) Does the Department's "Credit Life and Credit Accident and Health Insurance" Rule, 3901-1-15 of the Ohio Administrative Code (the Rule) prohibit a non admitted or unauthorized reinsurer, which is controlled by an admitted credit insurer that will issue credit coverage to certificate holders of a vendor and cede the business to the reinsurer, from paying dividends to the vendor stockholders, based upon the profit from the vendor.
- 2) Does the Rule prohibit a reinsurer from paying dividends to vendor-stockholders if the non admitted or unauthorized reinsurer is not controlled by the admitted credit insurer but the insurer agrees to cede all business submitted by vendor stockholders to the reinsurer.
- 3) If the Rule prohibits dividend payments in either the circumstances described in paragraphs 1 or 2 above, can the Department refuse to accept a security registration filing pursuant to Section 1707.09 O.R.C., if it offers such dividends to vendor stockholders that invest in the non-admitted or unauthorized reinsurer.
- 4) Can the Department revoke a prior registration by qualification, if the offering is as outlined in the facts presented.
- 5) If you conclude that the conduct outlined in requests 1-4 above, [is] violative of the Department's Rule, is the Department estopped from enforcing said Rule since it had aborted a Rule promulgation attempt to restrict reinsurance mechanisms in 1974?

3 Ohio Admin. Code 3901-1-15 provides, in pertinent part:

(A) **Applicability and Intention**

This rule is promulgated pursuant to Chapter 3918 of the Ohio Revised Code regulating credit life insurance and credit accident and health insurance. The intention of the Superintendent of Insurance in promulgating this rule is to guard the solvency of insurance companies writing credit insurance by limiting remunerations, dividends, service charges, rate credits, commissions, expenses or

service fees, or anything of value, etc., paid to agents, policyholders or any other person(s), so that credit insurers may maintain funds sufficient to pay claims and costs of administration. Any combination of pay-outs that exceeds forty per cent (40%) of net premiums will be considered as prima facie intent to violate the 50% presumptive loss ratio adopted as the "Richmond Resolution" by the National Association of Insurance Commissioners.

(B) Limitation on Total Remuneration Payable

(1) No insurance company offering credit insurance coverages in the State of Ohio shall pay directly or indirectly, or allow to be paid or credited through agents or otherwise, as total remuneration to any creditor policyholder or his affiliated agency, more than 32 1/2% in value of the net premiums paid on any class of credit insurance written in Ohio.

(2) As used in this rule, "total remuneration" comprises, by way of illustration and not by way of limitation, service or other administrative charges, retrospective or refund rate credits, dividends, bonuses, finder's fees, allowances or subsidies for rent, payroll, or advertising, and commissions, electronic data process equipment, profit sharing plans, expense allowances and any other form of credit, including monies, commissions for reinsurance ceded or assumed, or expenditures in any form whatsoever, direct or indirect, paid by or on behalf of the insurer or by any subsidiary or parent or subsidiary of the parent of the insurer or by any other person to or on behalf of any policyholder, agent or general agent or withheld by any policyholder, agent or general agent.

. . . .

(4) No more than ten per cent (10%) of net premium on a case basis may be paid to or withheld by the creditor policyholder as service or administrative charges at the time certificates of insurance are issued, and such service or administrative charges shall be included within the 32 1/2% total remuneration limitation specified in subsection (1) above. No dividend or rate credit with respect to premiums payable during a calendar or policy year shall be granted by an insurer prior to the end of such calendar or policy year and then only retrospectively based upon experience.

(5) The total acquisition and subsequent costs paid for credit insurance written in Ohio shall not exceed forty per cent (40%) of net premiums. Accordingly, whereas subsection (1) above establishes a limitation of 32 1/2% payable to any policyholder or his affiliated agency, no insurance company offering credit insurance coverages in the State of Ohio shall pay more than five per cent (5%) of net premiums to any other agents, except with prior approval of the Superintendent of Insurance, the insurance company may pay an additional 2 1/2% to a recognized servicing agent. . . .

(E) Suspension or Revocation

The Superintendent of Insurance may suspend, revoke, or refuse to renew the license of any agent, or the Certificate of Authority of any company, found to be in violation of this rule. Such suspension, revocation, or refusal to renew shall be in addition to, not a substitution for, the penalties provided in Section 3918.99 of the Revised Code.

Rule 3901-1-15 quite clearly prohibits the payment by an insurance company, directly or indirectly, of total remuneration in excess of 32 1/2% of the net premiums to a credit policyholder or its affiliated insurance agency. As used in the rule "total remuneration" includes "dividends. . . paid by or on behalf of the insurer or by any subsidiary or parent or subsidiary of the parent of the insurer or by any other person to or on behalf of any policyholder, agent or general agent or withheld by any policyholder, agent or general agent." It is clear that the rule is intended to prohibit all methods by which an insurer might attempt to pay indirectly that which cannot be paid directly. The issue to be addressed is, therefore, whether the character of remuneration is materially changed in a reinsurance transaction.

It is my understanding that in the "controlled" reinsurance transaction, the ceding company owns or controls the voting stock of the non-admitted reinsurer. This voting control enables the ceding company to control the board of directors of the reinsurer, and, consequently, the decision to pay or not to pay dividends to shareholders is controlled indirectly by the ceding company. Since the admitted ceding company controls the timing and amount of dividends to vendor shareholders, these dividends are "remuneration" under the Rule both for the purpose of determining commission payments in excess of 32 1/2% and for the purpose of determining if a total of more than 40% of net premiums have been paid out for the 50% presumptive loss ratio test.

In the second circumstance, the facts are identical except there is no "control" or ownership relationship between the admitted and non-admitted companies. Whether or not to declare dividends are decisions resting within the discretion of a board of directors elected independently of any control by the admitted company. Payment of dividends to vendor shareholders in such circumstances does not violate the Rule.

Accordingly, it is my opinion that the nature of the controlled relationship determines the nature of the remuneration received. In the first circumstance, it is apparent that the dividends received by vendor shareholders from the non-admitted reinsurer, should be added to other remuneration to determine if the Rule has been violated. Since the dividends received by shareholders under the second circumstance are presumed to have been received as a result of a bona-fide non-controlled and arms-length relationship, such dividends are not remuneration under the Rule.

Since I have concluded that the Rule applies in "controlled" reinsurance circumstances, it is necessary for me to address your remaining questions. You have also asked my opinion as to whether the Department may refuse to accept a securities registration filing pursuant to R.C. 1707.09 under the first "controlled" circumstance if unlawful remuneration is offered to prospective vendor shareholders. A related question is whether a prior registration by qualification may be revoked where the registrant's proposed method of operation is subsequently determined to be in violation of the Rule.

R.C. 1707.32 provides, in pertinent part: "If an issuer of securities is incorporated or organized to make any insurance named in Title XXXIX [39] of the Revised Code, the superintendent of insurance shall, for all the purposes of section 1707.01 to 1707.45, inclusive, of the Revised Code, be substituted for the division of securities. . . ." R.C. 1707.09, which prescribes the procedures for registration by qualification, provides, in pertinent part:

All securities, except those enumerated in section 1707.02 or 1707.05 of the Revised Code and those which are the subject matter of a transaction permitted by section 1707.03, 1707.04, or 1707.06 of the Revised Code, shall, before being sold in this state, be qualified in the manner provided by this section.

R.C. 1707.13 prescribes the procedures for the suspension and revocation of registration and states, in part:

The division of securities may suspend the registration by description or by qualification of any securities, . . . if the division finds that the issuer has violated sections 1707.01 to 1707.45, inclusive, of the Revised Code, or any lawful order or requirement of the division, has fraudulently conducted its business, or has been engaged in or is engaged or about to engage in deceptive or fraudulent acts, practices, or transactions; that such security is being disposed of or purchased on grossly unfair terms, in such manner as to deceive or defraud or as to tend to deceive or defraud purchasers or sellers, or in disregard of the lawful rules and regulations of the division applicable to such security or to transactions therein; or, in the case of securities being sold under a registration or qualification, that the issuer is insolvent. (Emphasis added.)

Since it is my opinion that dividends constitute "remuneration" when paid by a non-admitted company controlled by an Ohio admitted insurer, and since the Department has the authority to suspend, and ultimately revoke, a registration by qualification if it finds the issuer has violated any requirement of the Department, the Department may consider the revocation of registration if the registrant's intended method of operation violates Rule 3901-1-15. For the same reason, the Department may refuse to accept a securities registration which, on its face, intends to violate the Rule.

Finally, you have asked if the Department could be estopped from enforcing the Rule based on a decision in 1974 not to promulgate a specific rule placing restrictions on the use of reinsurance. It is my opinion that the Rule speaks for itself and that the lack of a Rule specifically relating to reinsurance, for whatever reason, is irrelevant to the interpretation or enforcement of Rule 3901-1-15.

It is, therefore, my opinion, and you are advised, that:

1. 3 Ohio Admin. Code 3901-1-15 limits the ability of a non-admitted or unauthorized reinsurer, which is controlled by an admitted credit insurer that intends to issue credit coverage to certificate holders of a vendor and cede the business to the reinsurer, to pay dividends to the vendor stockholders based upon the profit from the vendor. The Rule is not applicable, however, if the reinsurer is not controlled by the credit insurer.
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