



**Statement re:** Anti-competitive activities in the mega-brokerage insurance industry segment

**To:** New York Assembly Insurance Committee

**By:** Professional Insurance Agents of New York State, Inc.

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New York City

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The Professional Insurance Agents of New York State, Inc., representing approximately 18,000 insurance professionals throughout New York, offer the following comments in response to the notice of public hearing. We note, however, that the majority of questions on which testimony is invited appear to be directed toward witnesses other than Main Street insurance professionals. Accordingly, we will confine this statement to those selected points on which we have direct knowledge and a considered position to articulate.

**Illegal practices.** Like your Committee, PIANY and its members have been troubled by the allegations brought forward in the complaints by the Attorney General against certain insurance brokers. If the allegations made in these complaints are true, the actions of these brokers were in violation of the state's general business laws and antitrust provisions.

PIANY condemns such illegal activities. However, we maintain that the allegedly deliberate and systematic anti-competitive behaviors described in these complaints represent isolated and unusual cases, perpetrated by mega-brokers who are not representative of the local independent insurance professionals serving the majority of New Yorkers. Professional insurance agents and brokers do not engage in similar activities, and they should not be penalized because of the actions of a few. Moreover, such actions already were illegal, so we believe that enactment of additional laws could not be expected to prevent unlawful actions by those individuals who are intent on manipulating a market segment and frustrating market competition.

The complaints brought by the Attorney General characterize the brokers charged, as wielding outsized market clout and operating in a specialized realm of the insurance marketplace where illegal practices occurred. One, for example, is described as creating an exclusive "club" of individuals that would go along with its unusual and dishonest demands. Testifying before a U.S. Senate Subcommittee, New York Attorney General Eliot Spitzer said of this market segment: "We found that a small group of brokers and insurance companies essentially control the market."

It is the attempt to control the market by excluding legitimate competition that differentiates the agreements described in the Attorney General's complaints from the industry standards with which PIANY members are familiar. In fact, PIANY members operate in an extremely competitive environment in which customers are well aware of the many alternative sources of coverage available. Competitive forces ensure that clients consistently benefit from their agent's or broker's ongoing efforts to ensure that their business is not lost.

**Industry-standard contingency commission contracts.** Incentive or performance bonuses, commonly called contingency commissions, are paid by insurers to retail level insurance agents and brokers based on legal business contracts. These agreements are a standard feature of almost every contract that independent insurance professionals enter into with insurance companies. At this level of the market, PIANY members do not negotiate such agreements with just a few select insurers that aim to control their placements through outsized, "above-market" payments (as the October 14 complaint describes the operation of Placement Service Agreements).

PIANY would oppose any legislative or regulatory action that would interfere with these individual contractual agreements. We believe that contingency commission agreements encourage and perpetuate professionalism. They recognize and reward careful underwriting and the kind of consistent day-in, day-out service that supports business retention, industry reputation and, therefore, growth.

Moreover, since these agreements have been a feature of independent insurance professionals' business plans for decades, they provide crucial support for our members' ongoing operations. Over the past 20 years or so, insurers have systematically shifted many functions and their attendant costs from their own operations to those of their contracted agents. To cite just one important result of this process, local, independent professionals need to maintain the latest computer hardware, software, and online connectivity in order to provide essential services to both their clients and their insurers. Contingency commissions allow our members to make this type of ongoing investment in their business infrastructure, and to continue to serve their customers effectively as consumer expectations and company technology requirements evolve.

**Circular Letter 22.** In contrast to these industry-standard contingency commission contracts, which are standard features of virtually all our members' agreements with each company they do business with, the mega-broker's "Placement Service Agreements" are described as "undisclosed incentives to 'steer' business to certain insurance carriers in return for additional compensation" (Attorney General Spitzer's testimony to the U.S.

Senate's on Financial Management, the Budget, and International Security, Nov. 16, 2004).

New York addressed the possibility of “undisclosed receipt of additional compensation,” by providing guidance to insurance brokers on this point. Circular Letter 22 of 1998 says that insurance brokers should disclose all arrangements involving additional compensation (i.e., any compensation to be received in addition to commissions). We note that the complaints issued by the Attorney General specifically state that disclosure was absent, inadequate, or deliberately misleading in the cases where he brought action. So, we doubt that additional requirements would ensure any greater degree of compliance, when individual are intent on market manipulation.

Again, based on the public allegations, it appears that a small cadre of individuals, operating in a certain large-risk market segment, engaged in a systematic effort to manipulate that market and deliberately ignored both state law and regulatory guidance. It would be wrong to generalize the specifics of this discovery, to tar the vast majority of reputable, ethical insurance professionals serving their local communities, and bring them under a cloud of suspicion by less than careful reporting and a failure to make accurate distinctions. To be clear: No, New York should not adopt a prohibition against contingency payments from insurers to brokers, if that term is understood to mean the industry-standard contractual agreements we have described above.

**Faith in market integrity.** How can businesses have faith in the insurance market? They can initiate and maintain a frank and honest dialogue with their own insurance professionals. Responding to the issues raised by the Attorney General's complaint, PIANY prepared a Q&A information piece for our members' business customers. It included the question, “How can insurance buyers find out what insurers are paying their agents or brokers?” The answer: “Ask your agent or broker. It's that simple. Reputable insurance agents and brokers have nothing to hide. Moreover, they want their clients to be well-informed about normal practices involving compensation to professional agents and brokers.”

**State regulation.** We have noted that it was a joint state-level enforcement effort by the Attorney General and the Insurance Department that brought to light the alleged illegal activities by certain brokers and insurers. PIANY supports the efforts of the National Association of Insurance Commissioners to coordinate state-level investigations into similar practices, and to establish an on-line fraud reporting mechanism to receive “tips” from consumers and licensees for investigation by the states. (We note that the New York Insurance Department for some time has provided both toll-free and online mechanisms for reporting fraud.)

The rapid response by the NAIC and the National Coalition of Insurance Legislators to the unfolding situation demonstrates the effectiveness of state regulation. We urge New York lawmakers to await the outcome of the NAIC's investigations, and in turn we have asked the NAIC to tailor its ultimate recommendations to fit any additional illegal practices its members actually uncover. We are not prepared to agree that large numbers of individual firms have been engaging in such practices unless and until this is brought to light by the NAIC's efforts.

**Sophisticated purchasers.** One puzzling aspect mentioned by Superintendent Serio in his U.S. Senate testimony was the lack of complaints from insurance buyers affected by the alleged anti-competitive activities; the Superintendent said they may have been embarrassed. According to a summary published in *National Underwriter*, a recent anonymous survey of risk managers conducted by Advisen, a firm that regularly surveys these professionals, found:

“One thing buyers universally ‘hated’ was the global brokerage system, where the large accounts are placed centrally and out of touch for the risk manager. This system has kept buyers out of the loop and created a clubby atmosphere out of their sight that allowed this sort of thing to happen. Risk managers indicated they want system wide changes to prevent this type of abuse, including having their accounts handled by their local broker. They want to be more involved, have direct contact with the underwriters, be aware of the information being exchanged, and know exactly how the broker is being compensated in every step of the process.”

PIANY believes that both insurance buyers and potential competitors were harmed by the concerted effort to prevent normal competitive forces from operating. The business model of PIANY members is well equipped to provide what buyers desire—an open, collaborative process with their local insurance professionals that keeps insureds informed and promotes genuine competition for their business.

Ironically, even sophisticated buyers appear to have been taken in by the illusion that only a few insurance brokers could adequately handle their accounts. As the Chairman and this Committee know, PIANY has consistently maintained that most buyers can and do benefit from the existing protections afforded by New York law.