[INSIGHT] By Peter H. Bickford

The Sausage Factory

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There are a number of variations to an old saw comparing the messy legislative process with sausage making. A common current iteration observes that: "*If you love the law or sausages you should never see either one made.*" Given the vagaries of law-making mills, imagine the possibilities when relying on legislation to solve a simple regulatory issue that has evaded resolution for two decades!

Case in point: the 20-year and counting attempt by New York's insurance regulators to address a seemingly simple regulatory problem – preventing the issuance of insurance certificates that improperly expand or provide coverages not included in the policy itself. As described in my column last June ("*Certificates of Reliability*," ***IA*** June 23, 2014), the problem seems to have developed from a growing insistence by a number of city, state and municipal agencies and other public authorities and corporations that brokers issue forms of certificates expanding coverages of, or are inconsistent with, the actual policy.

For more than 15 years the regulators have been unable to stop the practice or to protect its licensees, the brokers caught between the regulators and the pressure from their customers. From 1995 through 2011 NY regulators issued at least two circular letters and seven opinion letters on the topic. At first these efforts were focused solely on the brokers, who were the pawns in the middle. When that limited effort did not work, the rulings were expanded to include the public agencies and authorities, which largely ignored the directives. After all, the Insurance Department (and now the Department of Financial Services) had no regulatory authority over them, and the brokers were no match for the insistence of the agencies. So it is understandable that a legislative cure was deemed necessary.

For three years running, legislation was introduced designed to target the end-user of certificates and not just the broker by making it a violation to "prepare, issue, request, or require the issuance of a certificate" that expands, adds or alters terms of coverage, or to knowingly request the issuance of a certificate of insurance that contains false or misleading information. The legislation also provided regulators with enforcement teeth beyond just being against the hapless brokers. Although the Governor vetoed the first two attempts without formal comment, there was some optimism that the 2014 attempt would be successful. Passed by both houses of the Legislature in June, the bill was submitted to the Governor at the last possible moment – December 30th – and the Governor took almost the entire 30 days he had to act on the bill. This time he approved the bill so that it is now law effective at the end of March. The cure is now law. Problem solved! Not so fast!

Governor Cuomo's approval memo reads in its entirety as follows:

> "This bill would regulate the form and content of certificates of insurance to ensure that such certificates are not misused or abused. As drafted, however, it contains a number of technical flaws and would not provide sufficient oversight authority to the Department of Financial Services. The Legislature has agreed to amend this bill and enact a chapter amendment to correct these deficiencies and on that basis, I am signing this bill."

Technical flaws? Insufficient oversight authority to the DFS? The expanded authority granted DFS over end-users of insurance certificates in the bill did not go far enough to control the abusive use of insurance certificates? Throw a couple more sausages on the grill and let's take a look at what the Legislature has proposed as "technical" changes!

In early February the technical adjustment legislation was introduced in both houses of the NY Legislature. Remarkably little of the bill signed into law in January remains intact in this legislative fix. It is, in essence, a complete rewrite of the bill leaving little of its original wording intact. While in some respects the revised bill may be a better drafted, clearer presentation of the issue, in two significant ways the proposal is a giant step backwards. First, the revised bill adds the element of willfulness for there to be any enforcement. For instance, an agency requiring that a broker use an unapproved certificate is only subject to the enforcement provisions of the bill if it acted "willfully." Conversely, one may assume, if the act was not "willful" the use of an improper certificate would be acceptable and not subject to penalty. I am not sure how insisting on the use of a non-approved certificate could be anything other than willful, but if the law is revised as proposed, any enforcement action by the DFS will most assuredly be met with the defense that the action was not willful. Adding such a requirement to a seemingly cut and dried, black and white rule is effectively de-fanging the law.

The second major setback is the proposed bill's exclusion of governmental

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agencies from the enforcement provisions of the law. Given that governmental agencies are among the principal beneficiaries of improper certificates, this would seem to be yet a further dilution of the law's effectiveness. Rather than increasing the enforcement capabilities of the DFS as called for by the Governor's approval memo, the proposed technical corrections to the law would appear to do the contrary.

The certificate issue is not an issue affecting a large segment of the insurance industry. It is an annoying issue for those affected, and particularly for brokers attempting to service their public, municipal or civic agency customers without incurring the wrath of insurers or regulators. The story here, however, is the inability of regulators and legislators to find a meaningful solution to a seemingly simple issue.

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One can imagine the political considerations that have been brought to bear on this simple issue – pitting public authorities against insurers and regulators. But those political realities only make the concerns more real. Two decades of failed regulatory and legislative efforts to control an identified abuse of a bright light rule does not bode well for solving other more significant, broad-based issues.[IA]

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