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Opinion No. 10-115

Compensation Expense Ratio under Tenn. Code Ann. § 56-22-120

QUESTION

Under Tenn. Code Ann. § 56-22-120, the Department of Commerce and Insurance is authorized to promulgate rules to set appropriate expense ratios for a county mutual insurance company. Under Department rules, "compensation expense ratio" means the ratio of the total compensation paid to officers and employees "who exercise authority over the underwriting decisions" of such a company to its gross premium. In calculating this figure, may the Commissioner of Commerce and Insurance include the compensation of an employee who does not have underwriting authority for the company?

OPINION

Under the Commissioner's rules, the compensation expense ratio may include the compensation of an employee who does not have direct or final underwriting authority for the company, so long as he or she plays a role in evaluating a risk or recommending that the company underwrite it.

ANALYSIS

This opinion concerns the determination of a "compensation expense ratio" for county mutual insurance companies. These companies are governed by Tenn. Code Ann. §§ 56-22-101, *et seq.* Under Tenn. Code Ann. § 56-22-104, a county mutual insurance company must obtain a certificate of authority from the Commissioner of Commerce and Insurance (the "Commissioner"). Tenn. Code Ann. § 56-22-107(b) provides:

> (1) No officer, director or other person whose duty it is to determine the character of risk and upon whose decision the application for insurance shall be accepted or rejected shall receive as any part of the person's compensation a commission upon the premium, but the compensation shall be a fixed salary, and/or a share of the net profits of the county mutual insurance company that the board of directors may determine appropriate.

> (2) Nothing under subdivision (b)(1) shall be construed to prohibit a county mutual insurance company from providing for its directors, officers and other employees reasonable benefits, including, but not limited to, directors' compensation, health insurance benefits and retirement benefits. Such benefits may be offered by a county mutual insurance company.
>
> (3) The commissioner may promulgate rules to set appropriate expense ratios to address those expenses incurred in subdivisions (b)(1) and (2).

The Commissioner has adopted rules governing county mutual insurance companies at Tenn. Comp. R. & Regs. ch. 0780-1-78. These rules define the term "compensation expense ratio" as follows:

> "Compensation expense ratio" means the ratio of the total compensation (including, but not limited to, salaries, commissions, insurance benefits and retirement account contributions, as well as all local, state and federal taxes associated with such compensation) paid to all officers, directors, employees and other individuals *who exercise authority over the underwriting decisions of a county mutual insurance company* to the gross premium of the county mutual insurance company[.]

Tenn. Comp. R. & Regs. ch. 0780-1-78-.02(2) (emphasis added). Section -.03 of the rules provides:

> (1) No county mutual insurance company's compensation expense ratio may exceed thirty percent (30%) for any given year.
>
> (2) Any county mutual insurance company whose compensation expense ratio exceeds thirty percent (30%) for any given year shall be considered to be operating in a hazardous financial condition.

The request asks whether the Commissioner, in calculating a compensation expense ratio, may include the compensation of an employee who does not have underwriting authority for the company. Under the rule, the ratio is to include the compensation of "all officers, directors, employees and other individuals *who exercise authority over the underwriting decisions* of a county mutual insurance company." This language is not limited to individuals with final underwriting authority. It may include other individuals who are involved in evaluating a risk or recommending that the company underwrite it. For this reason, the compensation expense ratio may include the compensation of an employee who does not have direct or final underwriting authority for the company, so long as he or she plays a role in evaluating a risk or recommending that the company underwrite it.

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