

## FEDERATION OF REGULATORY COUNSEL, INC.

# REORGANIZATION OF MULTIPLE INSURANCE AGENCIES

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Since its adoption by the National Association of Insurance Commissioners, the Producer Licensing Model Act (PLMA) has been enacted in approximately three-quarters of the states. Although it has been adopted in various forms, it has influenced the way that insurance agents and agencies navigate the regulatory minefield. In addition, it has opened the way for many multiple agency organizations to reorganize their licensing in order to simplify their overall structure. The following article includes a general description of the background of the PLMA and offers a few suggested considerations for insurance agencies and holding companies that may be thinking about reorganizing their corporate structures and insurance licensing in a manner consistent with the PLMA.

### I. The Producer Licensing Model Act - Background

Over the past half-century, state insurance departments have regulated insurance agency licensees in various ways. Early during this period, each state developed its own laws, regulations, and "desk drawer rules" that made each state's licensing unique. For insurance agencies carrying a book of business that stretched across the country, the rules were difficult to follow with any accuracy. In response, many holding companies and owners of insurance agencies formed or acquired a separate corporate agency within each desired jurisdiction in order to conduct business. Over time, these variances in state insurance laws underscored the fact that one of the only consistent characteristics of nationwide insurance agency licensing was that it was inconsistent. Adhering to these variances and many others created a regulatory maze that was unworkable.

In response, the NAIC sought to reduce the number of disparities among state insurance licensing laws by focusing its attention on the development of model legislation that would encourage greater uniformity among the states. The result was the PLMA, which the NAIC adopted in 2000. Aside from the development of uniform applications for insurance licensing, one of the principle innovations of the PLMA was the establishment of a system whereby an insurance producer (i.e., an individual agent or an agency) <sup>1</sup> could obtain a resident license in his/her/its home state <sup>2</sup> and a nonresident license in all other states in which he/she/it will first and foremost transact insurance business. This innovation had the effect of requiring an entity to conform only to the state licensing requirements of the state constituting its principal place of business rather than the full array of licensing requirements of all states in which it planned to conduct business. Accordingly, pursuant to the PLMA, an insurance agency could adopt a more typical corporate structure while still permitting it to do business on a nationwide basis.

Today, many licensed agency groups remain organized as if the PLMA had never been adopted. Oftentimes, a parent corporation (sometimes it may be an insurance company) serves as owner of several subsidiary corporate agencies that are legally incorporated in different states and with each corporate subsidiary agency holding a separate resident insurance license. This organization includes many different entities operating

## FEDERATION OF REGULATORY COUNSEL, INC.

under various federal employer tax identification numbers (FEIN). As such, one can see the organizational complexities that come into play. The corporate annual filings are difficult to track and manage due to the wide array of FEIN numbers, and one can only imagine the undesired internal accounting issues presented by multiple subsidiary corporate agencies. Moreover, the insurance licensing is needlessly complicated by the fact that each FEIN must be matched to each agency license in order to perform license renewals and other record maintenance. In view of these complexities and the recent changes provided by the PLMA, corporate agencies increasingly are reorganizing their current corporate structure into a simpler and more workable organization.

Perhaps the biggest disincentive to undertaking such a reorganization is the specter of converting all company appointments and agent affiliations to a new FEIN and insurance license. However, there are ways to simplify this process. The following section offers a detailed analysis and description of a method for effecting a reorganization of a corporate structure involving wholly-owned corporate insurance agencies.

### II. A Suggested Plan for Reorganizing an Insurance Agency's Corporate Structure - A Hypothetical Scenario

As noted above, given the multi-jurisdictional nature of insurance regulation, a number of businesses have established myriad corporate agencies under varying FEIN's and legal domiciles over time. Pursuant to the new PLMA, however, these businesses now have the opportunity to consolidate their corporate agency structure in order to achieve greater corporate efficiency. While such reorganization is not required by the PLMA, it is a characteristic that most nationwide existing agencies should find worthy of welcome.

As one might suspect, agency licensing is multifaceted and an explanation of it can quickly spin out of control. Therefore, for the sake of this discussion, we will employ the use of a hypothetical scenario that explains the intricacies, lesser-known details, and observations pertaining to the world of producer licensing. Due to formatting limitations, we are unable to produce diagrams for the reader's use; however, we would entreat you to diagram the corporate structure involved in order for the discussion to remain cogent.

Let us assume that ABC Insurance Agency, Inc. was incorporated in 1962 under the laws of the State of X where its offices and principal place of business are also located. Its immediate parent and sole owner is Holding Company, Inc., and Holding Company, Inc. is wholly owned by Ultimate Parent, Inc. As its business developed and the value of ABC Insurance Agency, Inc.'s business activity grew in State X, Holding Company, Inc. determined that it should broaden the agency's focus and develop a regional marketing program encompassing seven additional states (State A, State B, State C, State D, State E, State F, and State G). Accordingly, Holding Company, Inc. began establishing and acquiring new corporations in the expanded region. In States A, B, C, and D, Holding Company, Inc. acquired Agency 1, Agency 2, Agency 3, and Agency 4, all of which were separate corporate entities. In States E, F, and G, Holding Company, Inc. utilized the existing FEIN for ABC Insurance Agency, Inc. and obtained a nonresident license in those states. By 1985, the goal of licensure in all eight states (including its home state of State X) was fully realized, and Holding Company, Inc. was then operating in its desired eight-state region (i.e., State X and States A, B, C, D, E, F, and G). However, the corporate structure was such that Holding Company, Inc. owned five corporate entities: ABC Insurance Agency, Inc., Agency 1, Agency 2, Agency 3, and Agency 4, which hold the eight insurance licenses among them as to each of the eight states.

In 2008, and in the wake of the adoption of the PLMA, Ultimate Parent, Inc. is now committed to

## FEDERATION OF REGULATORY COUNSEL, INC.

streamlining its organizational structure. In so doing, it is committed to consolidating ABC Insurance Agency, Inc., Agency 1, Agency 2, Agency 3, and Agency 4, with the resulting entity being ABC Insurance Agency, Inc. In addition, it desires to place the resulting agency (ABC Insurance Agency, Inc.) under its immediate control, which will require the removal of Holding Company, Inc. from the organizational structure. In essence, Ultimate Parent, Inc.'s insurance operations will go from a complex, three-tiered structure to a simple two-tiered structure whereby the surviving agency (ABC Insurance Agency, Inc.) exists as a resident insurance licensee in State X (the home state) and with nonresident insurance licenses in States A, B, C, D, E, F, and G. Naturally, Ultimate Parent, Inc. intends to achieve this reorganization in a manner that allows all insurance operations to continue without interruption.

Step 1: Obtain Nonresident Licenses for ABC Insurance Agency, Inc. in All Desired Jurisdictions While Leaving All Other Licensing in Place. Assuming that Agency 1, Agency 2, Agency 3 and Agency 4 have adopted the DBA name of "ABC Insurance Agency, Inc." in order that they may do business collectively under that name, the first goal is to obtain nonresident licenses for ABC Insurance Agency, Inc. in States A, B, C, and D (Note: as noted above, ABC Insurance Agency, Inc. already holds licenses under its FEIN in States X, E, F, and G). Generally speaking, all states now accept the NAIC's "Uniform Application for Business Entity Insurance License/Registration" (available online at [http://www.naic.org/documents/committees\\_d\\_plwg\\_busapp.doc](http://www.naic.org/documents/committees_d_plwg_busapp.doc)). Each state will require ABC Insurance Agency, Inc. to submit the NAIC uniform agency application, a fee, proof that the entity is registered in its home state, and possibly supporting documentation reflecting that the name has been registered with that state's secretary of state. <sup>3</sup>In so doing, ABC Insurance Agency, Inc. must list on each application the name and social security number of a designated insurance producer who is licensed in that state on an individual basis and in the same lines of authority for which the agency is applying.

Step 2: Advise the Appointing Carriers of the Consolidation Plan. Because commission flow is a significant factor in any sophisticated insurance agency operation, Holding Company, Inc. should give notice to the appointing carriers for ABC Insurance Agency, Inc., Agency 1, Agency 2, Agency 3 and Agency 4 that its subsidiary insurance agencies are being consolidated into one agency (ABC Insurance Agency, Inc.). If ABC Insurance Agency, Inc. does not already hold appointments that are identical to those held by Agency 1, Agency 2, Agency 3, and Agency 4, then ABC Insurance Agency, Inc. will first need to obtain those appointments in order to ensure proper and uninterrupted commission flow through the corporate reorganization process.

Insurance companies generally organize their commission payment systems by FEIN's and subproducer codes. Each agency is identified by its FEIN, and within each agency, each location might be assigned a subproducer code that facilitates commission flow directly to an agency's alternate locations. This system of compensation is particularly well-suited for agencies that operate multiple locations and desire a more targeted system of compensation that directly compensates each responsible producer's business location rather than requiring processing through a central agency clearinghouse. In view of these considerations, Holding Company, Inc. should include in its letters to the appointing carriers that the FEIN should be changed to that of ABC Insurance Agency, Inc. but that all subproducer codes previously on file for Agency 1, Agency 2, Agency 3, and Agency 4 should be maintained intact. <sup>4</sup>As long as ABC Insurance Agency, Inc. ends up collectively holding all necessary appointments for the entire agency operation, then the above notice to the appointing carriers, if properly followed, will ensure that payments continue uninterrupted to Agency 1, Agency 2, Agency 3, and Agency 4. <sup>5</sup>

Step 3: Affiliate Agents to ABC Insurance Agency, Inc. Affiliations are tracked by insurance departments in

## FEDERATION OF REGULATORY COUNSEL, INC.

approximately half of the states. 6 An "affiliation" refers to the record kept by an insurance department of the fact that an individual agent represents, or works on behalf of, a particular insurance agency. The states have various procedures for affiliating such individuals, but generally this process requires the agency to submit a form signed by an officer requesting the affiliation of individuals and the payment of a fee.

In our hypothetical scenario, the agents affiliated to Agency 1, Agency 2, Agency 3, and Agency 4 need to be affiliated to ABC Insurance Agency, Inc.'s new nonresident licenses in those states in which he or she will transact business on behalf of the agency (i.e., States A, B, C, or D). Once complete, all of the agents formerly affiliated exclusively to Agency 1, Agency 2, Agency 3, and Agency 4 will be dually affiliated to ABC Insurance Agency, Inc. Accordingly, assuming these individuals are individually appointed where required by state law, they may continue transacting insurance business under either license without interruption.

Step 4: Merge Agency 1, Agency 2, Agency 3 and Agency 4 with and into ABC Insurance Agency, Inc. Generally speaking, as compared with dissolution, merger of an insurance agency is a simpler method of eliminating undesired insurance agencies. Merger allows an entity to take advantage of tax free reorganization provisions, which may avoid undesired tax obligations. In some states, it also avoids franchise tax and certain income tax requirements and the additional filings that accompany them. Finally, merger avoids the possibility that certain income distributions would need to be paid as a result of dissolution.

In our hypothetical case, Agency 1, Agency 2, Agency 3, and Agency 4 should now be merged with and into ABC Insurance Agency, Inc. The merger will affect only the corporate identity of the agencies and will not unilaterally affect the licensing aspect. In those states whose secretaries of state require notice of a merger or dissolution involving a foreign business entity that is registered to do business in that state, such notice must be given subsequent to each merger if required by law by both the surviving and nonsurviving entities to the relevant secretaries of state.

Step 5: Surrender Previous Licenses for Agency 1, Agency 2, Agency 3 and Agency 4. In view of the fact that ABC Insurance Agency, Inc. is now licensed in State X (the home state) on a resident basis and States A, B, C, D, E, F, and G on a nonresident basis, the prior resident licenses of Agency 1, Agency 2, Agency 3 and Agency 4, which reflect four separate FEIN's, should be surrendered to the relevant insurance departments in States A, B, C, and D.

Step 6: Merge Holding Company, Inc. with and into ABC Insurance Agency, Inc. As noted above, Ultimate Parent, Inc. desired the elimination of Holding Company, Inc. an intermediate holding company pursuant to the overall corporate reorganization; therefore, Holding Company, Inc. should subsequently be merged downstream with and into its subsidiary, ABC Insurance Agency, Inc. In those states requiring notice of a merger involving a foreign business entity that is registered to do business in that state, such notice must be given to such states' secretary of state or corresponding entity subsequent to the merger if required by law. Upon completion of this final step, ABC Insurance Agency, Inc. will be the sole insurance agency with Ultimate Parent, Inc. as its immediate parent and sole owner. Accordingly, ABC Insurance Agency, Inc. will be licensed and appointed in all desired jurisdictions.

In sum, the legal work involved in successfully accomplishing such a reorganization, without any interruption of business, is far more detailed and complex than one might imagine. Accordingly, such a project, depending on the number of agencies and states involved, could likely take anywhere from four to twelve months to achieve completion.

## FEDERATION OF REGULATORY COUNSEL, INC.

### III. Conclusion

In conclusion, enactment of the PLMA has enabled insurance agencies that have been historically "cobbled together" for various reasons to streamline their corporate organizations in order to achieve greater efficiency. As more and more insurance agencies transacting insurance business nationwide realize the potential and value of such change, it is likely that they will choose to institute such reorganizations. The structure outlined in this article is a suggested reorganization model that achieves the desired change over a period of time without any interruption of business.

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### **Endnotes**

1. "Producer" is the collective term under the PLMA to include agents and agencies. "Insurance producer" is defined as any "person required to be licensed under the laws of this state to sell, solicit or negotiate insurance." See PLMA § 2(D) (2007).
2. "Home state" is defined by the PLMA as "the District of Columbia and any state or territory of the United States in which an insurance producer maintains his or her principal place of residence or principal place of business and is licensed to act as an insurance producer." See PLMA § 2(B) (2007).
3. ABC Insurance Agency, Inc. should confirm that it is registered to conduct business on a foreign basis with the secretary of state of each state in which it plans to obtain a nonresident insurance agency license.
4. We have found that many carriers will require proof that the FEIN has changed. Generally speaking, they require the submission of an IRS W-9 and possibly a carrier-specific form signed by an officer of the agency.
5. It has been our experience that the agency must remain vigilant about maintaining contact with each appointing carrier during this process in order to confirm that each carrier properly effects the requested changes. Many carriers will require answers to follow-up questions. Therefore, in order to avoid confusion amidst these changes, it is imperative that the notice to the carriers be carefully and clearly expressed. We would suggest that such a notice be sent in the form of a letter on agency letterhead so that the recipient is not confused by the sender's request.
6. Some states have alternate terminology for affiliations such as "designations," "members," "associations," or "subagents."