STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
NEW YORK STATE INSURANCE FUND - WORKERS' COMPENSATION FUND	:	DETERMINATION DTA NO. 820589
for Redetermination of a Deficiency or for Refund of Franchise Tax on Insurance Corporations under Article 33 of the Tax Law for the Years 1999 and 2000.	:	

Petitioner, New York State Insurance Fund - Workers' Compensation Fund, 199 Church Street, New York, New York 10007-1102, filed a petition for redetermination of a deficiency or for refund of franchise tax on insurance corporations under Article 33 of the Tax Law for the years 1999 and 2000.

A hearing was held before Brian L. Friedman, Administrative Law Judge, at the offices of the Division of Tax Appeals, 500 Federal Street, Troy, New York, on January 25, 2006 at 10:30 A.M., with all briefs to be submitted by September 18, 2006, which date began the six-month period for the issuance of this determination. Petitioner appeared by Crane, Parente, Cherubin & Murray, Esqs. (Gregory A. Mountain, Esq., of counsel). The Division of Taxation appeared by Mark F. Volk, Esq. (Clifford M. Peterson, Esq., of counsel).

ISSUE

Whether the Division of Taxation properly determined that certain New York State Insurance Fund extended payment plan service and finance charges are "premiums" for the purpose of computing the franchise tax imposed on its total gross direct premiums.

Along with its brief, the Division of Taxation ("Division") submitted 74 proposed findings of fact, each of which has been substantially incorporated into the following Findings of Fact except for: (a) the last sentence of proposed finding of fact "14" which is not supported by the record; (b) proposed findings of fact "28" and "29" which are conclusory in nature; and (c) the last sentence of proposed finding of fact "64" which is conclusory and is not supported by the record.

In its reply brief, petitioner incorporated its Statement of Facts, consisting of six pages, from its initial brief and further submitted the same as its proposed findings of fact. Even though State Administrative Procedure Act § 307(1) requires a ruling "upon each proposed finding of fact," because petitioner did not separately number each of its proposed findings of fact, they have not been ruled upon. Nevertheless, a substantial portion of petitioner's Statement of Facts has been incorporated into the following Findings of Fact.

FINDINGS OF FACT

1. New York was the first state to create a system for workers' compensation by enacting its Workers' Compensation Law in 1914. As a result of this law, three state agencies were created, the Workers' Compensation Board ("WCB"), the State Insurance Fund ("SIF") and the New York Compensation Insurance Rating Board ("NYCIRB").

2. The WCB was created to administer the Workers' Compensation Law. It also oversees the adjudication of claims under the law and ensures that proper coverage is provided by employers.

3. Since employers are required to provide workers' compensation insurance, the SIF was created to provide insurance to employers. It issues workers' compensation insurance that

protects employers from liability associated with on-the-job injuries resulting in employee disability or death and provides monetary relief and medical benefits to injured employees.

4. The SIF, a nonprofit agency, is required to provide insurance to employers who cannot find coverage elsewhere. In addition, it provides insurance to employers who determine SIF's rates to be more competitive than private insurers who are authorized to provide workers' compensation insurance. By law, the SIF provides workers' compensation insurance at the lowest possible cost to employers within the State.

5. For its workers' compensation insurance, the SIF charges two different types of premiums: an estimated premium and, in some instances, an audited premium. An estimated premium is assessed at the commencement of the insurance contract and is calculated based on the amount of remuneration (or payroll) the insured estimates it will pay out over the policy term. An audited premium is assessed after the expiration of the insurance contract and is based on the audited amount of remuneration the insured actually paid out during the policy term, but only to the extent the audited amount is in excess of the estimated amount of remuneration that was the basis of the estimated premium.

The estimated premium is a deposit made for future insurance coverage and must be refunded to the extent the estimated premium is not thereafter earned by the SIF for providing insurance coverage on a day-to-day basis. If the insurance contract is canceled before its expiration or if the audited amount of remuneration indicates that the insured actually paid out less than the estimated amount of remuneration during the policy term, the SIF must refund to the insured any unearned portion of the estimated premium.

6. By statute, the Superintendent of Insurance is authorized to designate an organization to collect pertinent data from each insurance carrier and to develop a rate structure for workers'

compensation insurance premiums. Since the enactment of the Workers' Compensation Law in 1914, the NYCIRB has been designated as the official organization for the collection of data regarding the development of workers' compensation rates. The NYCIRB is a nonprofit, unincorporated association of insurance carriers which includes the SIF. After analyzing data, the NYCIRB makes recommendations to the State Insurance Department concerning reductions or increases in workers' compensation insurance premium rates. The NYCIRB develops and publishes the New York Workers' Compensation and Employers' Liability Manual ("the Manual"). The Manual, which is also approved by the State Insurance Department, contains rules, procedures, classifications and rates that govern the underwriting of workers' compensation and employers' liability insurance in New York.

7. The SIF administers two funds, the Workers' Compensation Fund and the Disability Benefits Fund. It files separate tax returns for each of the funds. The SIF is the largest provider of workers' compensation insurance in the State, representing approximately 35% to 40% of the market. The only product other than workers' compensation insurance which SIF sells is disability benefits insurance.

8. The SIF's premiums for a workers' compensation insurance policy are established by its underwriting department. The first part of the premium is the manual rate. Manual rates are recommended by the NYCIRB and established by the State Insurance Department. Manual rates account for a certain portion of total administrative expenses.

Independent carriers may deviate from a manual rate with the approval of the State Insurance Department. These deviations are identified as differentials by the SIF. Unlike private carriers, the SIF does not need the approval of the State Insurance Department to adjust

individual rates by the use of a differential. However, a differential must be based on certain risk factors such as a policyholder's payment history, i.e., the potential for a nonpayment default.

The rates established by the NYCIRB are intended to fund the projected benefits which are required to be paid to injured workers and to cover the expenses of the insurance company and provide the company with a reasonable profit.

9. Another component of a premium is the employer's own loss experience or its individual risk if the insurance is over $5,000.00. The experience modification factor or rate compares a company with others in its classification and is a means of allocating premiums among employers within a classification according to their relative contribution to a class cost. This experience rating is applied to all policies with an annual premium of at least $5,000.00.

10. An additional factor in the computation of a premium is the expense constant which is a statutory amount ($200.00) established by the NYCIRB that is added to every workers' compensation insurance policy premium regardless of the amount of the policy premium. The Manual requires that every workers' compensation insurance policy, including those issued by the SIF, include an expense constant. The expense constant is intended to account for the costs of expenses associated with the issuance, recording and auditing functions that are common to an insurance company's processing of workers' compensation insurance policies. Unlike the SIF's extended payment plan service charges which are at issue in this proceeding, the expense constant is assessed prior to and is required for the issuance of every workers' compensation insurance contract. The expense constant does not cover the additional expenses that might be incurred by a carrier in the course of providing optional installment payments.

11. Another component of premiums is assessments. The assessment is based on a set percentage of premium for every employer and the percentage changes every year. The WCB

does not receive any funding through general tax revenue; therefore, it must fully recover all the costs it incurs in the delivery of its services through its own revenue sources.

The recovery of the Board's administrative costs which include the cost of personnel, plant, supplies, travel, etc., is done through a series of general administrative assessments levied against insurance carriers and self-insured employers. Assessments also fund several ancillary programs that reimburse carriers or claimants under special circumstances, including the Second Injury Fund, Special Disability Fund, Fund for Reopened Cases, Uninsured Employers Fund and Special Fund for Disability Benefits.

The assessments against carriers are passed on to employers through the annual premiums. As the losses and liabilities for these programs rise and fall, so does the assessment charged to carriers.

In 1993, the Legislature amended the Workers' Compensation Law (chapter 729 of the Laws of 1993) to require assessments to be treated as separate costs by insurance carriers rather than elements of loss for insurance ratemaking purposes. This change was intended to generate savings in premiums and other costs for employers. Carriers thereafter assessed such costs on their policyholders in accordance with rules set forth by the NYCIRB, as approved by the Superintendent of Insurance.

Chapter 729 of the Laws of 1993 also amended Tax Law § 1510(c)(1) by adding to the definition of "premium" the phrase "any separate costs by carriers assessed upon their policyholders."

For 1999, for purposes of the Workers' Compensation Fund, the SIF reported that assessments for the administration of the WCB and the NYCIRB represented 22% of the Workers' Compensation Fund's budget or approximately $60 million. For 2000, SIF reported

that assessments for the same agencies represented 21% of the Workers' Compensation Fund's budget or somewhat in excess of $61 million.

12. As an alternative to workers' compensation insurance, the SIF coordinates Safety Groups for certain industries. Safety Groups are plans designed for employers in the same trade or industry who can and will work together to curtail occupational diseases or accidental injuries. The goal of the Safety Groups is to reduce the insurance costs of all participants in the Groups. Participants in the Groups receive an advance discount and then may receive a dividend based on the safety performance of a group.

The dividends that the SIF calculates and pays to the participants in its approximately 100 Safety Groups are the only dividends that the SIF pays while managing the Workers' Compensation Fund. For the year ended December 31, 1999, dividends to participants of Safety Groups averaged about 32.5%. In 1999, dividends paid and incurred to insureds totaled $136.7 million. In 2000, dividends paid and incurred to insureds averaged about 30% and payments totaled $111.1 million.

For both 1999 and 2000, on the balance sheets for the Workers' Compensation Fund, the SIF provided for contingency accounts for future dividends to be paid to policyholders. The contingency for dividends was calculated by deducting losses, expenses and previous dividends from premiums billed and included applicable investment income. On its annual statements, the SIF reported dividends paid to stockholders not as a reduction in premiums earned but as a separate line item under "Other Income."

13. As early as November 16, 1998, the SIF allowed "qualified safety group" policyholders to pay their premiums in 12 equal monthly payments.

14. The type of investments in which the SIF may invest is provided for by statute, Workers' Compensation Law § 87. The investment income which the SIF reported on the financial statements for the Workers' Compensation Fund and the Disability Benefits Fund is income from the statutorily prescribed investments.

15. The SIF's only tax liability is for New York State franchise tax and the MTA surcharge. It is exempt from Federal taxation. The SIF's tax liability was provided for under the limitation of tax section and was calculated, pursuant to Tax Law former § 1502-a, at the rate of 2.6% of its total gross direct premiums. The SIF did not pay any taxes on its income from its statutorily authorized investments.

16. In 1999, the SIF reported that it paid New York State franchise and MTA taxes in the amount of $19 million which constituted 7% of the Workers' Compensation Fund's fiscal costs. In 2000, the SIF reported that it paid New York State franchise and MTA taxes in the amount of $29 million which represented 10% of the Workers' Compensation Fund's fiscal costs.

17. Chapter 28 of the Laws of 1993 amended Workers' Compensation Law § 92 to permit the SIF to offer policyholders with estimated premiums of at least $1,000.00 the option of paying the premium in three installments. The first payment was required to be 50% of the estimated premium followed by two equal payments at three-month intervals.

Chapter 149 of the Laws of 2000 further amended Workers' Compensation Law § 92 by removing the aforementioned three-payment installment option and permitting the commissioners of the SIF to make rules regarding installment options. This amendment took effect on July 18, 2000.

It must be noted that the SIF implemented its current ten-payment extended payment plan prior to the 2000 amendment to Workers' Compensation Law § 92. On November 13, 1998,

Memorandum U-19 was issued by the Director of the SIF Underwriting to all underwriters which advised as follows:

> On new and renewal policies effective January 1, 1999 and thereafter a new endorsement will appear. The effect of this new endorsement is to allow the application of interest and service charges on premium billing.
>
> As part of the Phase II billing initiative, policyholders with annual premium of $1,000 or more can elect to pay their deposit premium via our new extended payment plan. After the initial deposit has been paid the remaining balance can be paid in installments through the tenth month of the policy period. In addition, all policyholders can elect to pay earned premium billed within the first nine months of the policy period in installments through the tenth month of the current policy period.
>
> Interest will apply on outstanding earned premium bills over 30 days old. A service charge will apply to any installment bill issued subsequent to the initial deposit or earned premium bill. However, only one service charge will apply per installment.
>
> Attached is a copy of the text of the new endorsement.

An Interest & Service Charge Endorsement (referred to in Memorandum U-19) amended section E of Part Four[1] of the SIF's workers' compensation policies by providing, in pertinent part, as follows:

> Policyholders with annual deposit premium of $1,000 or more can elect to pay the deposit premium via our extended payment plan. Once the initial deposit on your premium has been paid the remaining balance can be paid in installments through the tenth month of your policy year. There will be a service charge of $10 per installment for those who opt for an extended payment plan.
>
> You also can elect to pay audit premium in installments. Audit premium billed within the first nine months of the policy period can be paid in installments through the tenth month of your policy period. Interest will be charged at a rate of 1% per month (12% APR) on the outstanding audit balance in addition to the $10 per month service charge.

[1] Section E of Part Four - Premium states: "You will pay all premium when due. You will pay the premium even if part or all of the Workers' Compensation Law is not valid."

> Payment of any amount less than the full bill will be deemed a request for an extension of time to pay that would result in interest and/or service charges as set forth in the billing statement.

18. Pursuant to Memorandum U-20, issued by the SIF on November 16, 1998, the new 10-payment plan required policyholders with an annual premium of $0 to $999.00 to pay the premium in full at the beginning of the policy period. For policyholders with an annual premium of $1,000.00 to $9,999.00, a 50% down payment was required, with the balance to be paid in 9 installments. For policyholders with an annual premium of $10,000.00 and over, a 25% down payment was required, with the balance to be paid in 9 installments.

19. According to Allan Simpson, Controller of the SIF, the $10.00 service charge is intended to cover the cost of issuing the bill and all related expenses associated with reissuing bills month after month on policies where there has been an election to pay under the SIF's extended payment plan. Mr. Simpson did not know how the $10.00 fee was arrived at by the SIF.

Mr. Simpson indicated that the finance charge (1% per month), which is assessed only upon audited (or earned) premiums, is an interest charge intended to cover the insured's use of SIF money, or otherwise act as a partial replacement for investment income which the SIF would have earned if the premium had been paid up front. Mr. Simpson did not know how the 1% finance charge was established by the SIF.

20. The income earned by the SIF from the 1% finance charge was not included in the income that it earned from its investments. Instead, the income from the 1% finance charge was reported as "Other Income" on its Annual Statements.

21. The SIF's monthly service charge and the finance charge are set forth on the invoice to the insured separate from the SIF's premium charges under the heading "New Charges" and

are not assessed on the first invoice, but only upon the occurrence of each additional installment transaction. In the case where the full premium is not paid upon the initial invoice, the $10.00 service charge and the 1% finance charge (if applicable) become part of the "Minimum Amount Due Calculation" on invoices sent to policyholders.

An insured who is eligible for the SIF's extended payment plan may pay its premium in full at the commencement of the insurance contract to avoid the imposition of a service or finance charge or, in the alternative, may pay the balance of the premium due at any time thereafter to avoid the future assessment of service or finance charges. Nonpayment of any payment by a policyholder, including the charges for the extended payment plan, could result in cancellation of the policy.

It is less expensive for an insured to pay the SIF's extended payment plan fees than it would be for the insured to finance the premium through a premium finance company. A premium finance company provides financing to an insured to permit the insured to pay the entire premium up front. The insured would then pay a monthly payment to the premium finance company to repay the premium.

22. The SIF's premium charges are established by its underwriting department while the SIF's extended payment plan charges are established by the management of the SIF. The extended payment plan does not impact in any way the underwriting department's calculation of a premium. The premium must be calculated before the SIF can determine if an insured is eligible for the extended payment plan.

23. In 1980, the Division issued a Technical Services Bureau Memorandum, TSB-M-80(8)C, which instructed taxpayers that a flat fee service charge for installment payments

charged by an insurance company is includable as a taxable premium for the purpose of the premium tax imposed by section 1510(a) of Article 33 of the Tax Law.

TSB-M-80(8)C was based on a February 13, 1980 letter from Ralph J. Vecchio, former Deputy Commissioner and Counsel for the Division, to Morton Greenspan, former Deputy Superintendent and General Counsel for the State Insurance Department. Mr. Vecchio's letter indicated that the Division's interpretation of the definition of premiums for purposes of Tax Law § 1510(c)(1) was in accord with a prior Division interpretation of premiums for purposes of Insurance Law former § 550(1) and Tax Law former § 187(9)(E) which was the predecessor to Tax Law § 1510(c)(1). The prior interpretation by the Division was set forth in a letter dated July 5, 1962 from the Division's former Counsel, Edward H. Best, to Theodore R. Ayervais, former Assistant General Counsel of the State Insurance Department. The Best letter stated, in relevant part, as follows:

> Our analysis of the question raised in your letter leads us to agree with your conclusion that additional amounts charged by insurers for the privilege of paying premiums in installments come within the *definition* of "premium" in section 550 of the Insurance Law, and therefore could be made subject to tax under Article XVII of that law and section 187 of the Tax Law. However, as the additional revenue involved does not appear to be too substantial I believe a top level policy determination should be made before holding this item taxable at this time.
>
> In any event, if a ruling to this effect is to be made I believe it should be issued jointly or simultaneously by your Department and by this Department in view of the previous contrary ruling by your Department. (Emphasis in original.)

24. On August 15, 1967, the State Insurance Department issued Circular Letter No. 6, addressed to all fire and casualty insurance companies, wherein former Superintendent of Insurance Richard E. Stewart addressed the issue of whether premium payment service charges attributable to New York risks were properly includable in taxable premiums pursuant to Tax

Law former § 187 and Article XVII of the Insurance Law. It was the opinion of the Superintendent of Insurance that:

> all additional charges for service, except such as are derived from direct financing of premiums by the company upon a premium finance agreement as defined in Section 554 of the Banking Law, made by an insurer to an insured in connection with the voluntary extension of credit to the latter in payment of any insurance premium, is deemed part of the premium collected and, therefore, taxable under Article XVII of the Insurance Law pursuant to the provisions of Section 187 of the Tax Law.

The basis for Circular Letter No. 6 was an opinion, dated May 8, 1967, written by former Deputy Superintendent and General Counsel, Theodore R. Ayervais.[2] Circular Letter No. 6 was made effective no later than April 1, 1968 and, as of December 31, 2001, was still in effect.

25. In its training manual for auditors involved with audits of franchise tax on insurance corporations, the Division directs its auditors to include finance and service charges in the computation of total gross direct premiums. The auditor who performed the desk audit of the SIF stated that he had performed desk audits for the Division for about nine years, that he conducted approximately 100 audits of insurance companies per year and that in all of his audits, he had to make an adjustment to a taxpayer's tax liability to include the effect of finance and service charges only once or twice in his career.

26. The staffs of the Division (Income/Franchise Desk Audit Bureau) and the State Insurance Department (Taxes and Accounts Section) are often in contact with each other when auditing the tax returns of insurance companies.

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[2] It must be noted that this four-page letter is, for the most part, illegible and the contents thereof will not, therefore, be considered for purposes of this proceeding.

The supervising auditor who approved the audit which is the subject of this proceeding indicated that TSB-M-80(8)(C) was the basis for the Division's policy of including a taxpayer's finance and service charges in the computation of the tax on total gross direct premiums.

27. During a desk audit of the SIF's tax returns for the Workers' Compensation Fund, the Division determined that the SIF's computation of its total gross direct premiums was understated because it had failed to include finance and service charges in its computation.

On its Insurance Corporation Franchise Tax Return (form CT-33) filed for 1999 for the Workers' Compensation Fund, the SIF reported an amount of $755,253,477.00 as its total gross direct premiums subject to tax. On its return for 2000, the SIF reported an amount of $986,055,666.00 as its total gross direct premiums subject to tax. Neither return included an explanation as to how these amounts of total gross direct premiums were calculated.

28. For 1999 and 2000, the SIF filed annual statements with the State Insurance Department each of which included a Schedule T, Exhibit of Premiums Written. On the schedules T, there is a column 2 entitled "Direct Premiums Written" whereon the SIF entered the amount of $900,125,934 on the 1999 annual statement and $1,104,627,262 on the 2000 annual statement.

On the schedules T, there is a column 8 entitled "Finance and Service Charges Not Included in Premiums." For 1999, the SIF entered the amount of $3,809,817 and for 2000, it entered the amount of $6,399,587 in column 8.

Column 4 of the schedules T is entitled "Dividends Paid or Credited to Policyholders on Direct Business." For 1999, the SIF entered $136,390,281 in this column; for 2000, it entered $111,103,067 in column 4.

29. To calculate the SIF's tax liabilities for the years at issue, the Division deducted dividends from written premiums and added back finance and service charges to arrive at the SIF's total gross direct premiums. The auditor indicated that in making these computations, he relied on the Division's audit guidelines and its insurance franchise tax manual.

The Division's auditor shared his calculations with Mr. Martin Fobare, a senior auditor in the State Insurance Department's Taxes and Accounts Section. When asked by the Division to research the basis of the State Insurance Department's policy of including finance and service charges in taxable premiums, Mr. Fobare shared the Insurance Department's Circular Letter No. 6 (1967) with the Division's audit staff.

30. Insurance companies doing business in New York State must also file a Report of Premiums along with their Annual Statement. The Report of Premiums must be filed with the State Insurance Department and with the Division. Column 3 of the Report of Premiums is entitled "Finance & Service Charges." In order to compute "Gross Taxable Premiums" in column 7 of the Report of Premiums, a taxpayer is directed to add the amounts set forth in columns 1, 2, 3 and 4. To compute "Net Taxable Premiums" (column 9), the taxpayer is instructed to subtract dividends paid or credited from gross taxable premiums.

31. On July 27, 2000, the office of General Counsel of the State Insurance Department issued an informal opinion on the issue of whether an insurer may allow an insured to make premium payments in installments. The opinion stated in part as follows:

> Installment fees are not considered a part of the insurer's base premium and need not be included in the insurer's rate filing to the Department. Installment fees are separate and distinct from the premium and should be displayed on the billing notice and/or cancellation notice. Any filing of an "installment fee schedule" with the Department would be accepted for informational purposes only.

> An installment fee is an "obligation in connection with the payment of premiums on a policy of insurance or any installment of such premium," N.Y. Ins. Law § 3425(a)(10) (McKinney Supp. 2000) and N.Y. Ins. Law § 3426(a)(3) (McKinney Supp. 2000), that the insured may be required to pay and failure to pay such amounts would be nonpayment of premium. Therefore, an insurance company may cancel a policy, pursuant to the above cited sections of law, if the insured fails to pay installment fees.

32. The Division's audit file for the SIF for 1999 and 2000 did not include a copy of a Report of Premiums. The SIF's controller and the person responsible for its tax returns, Allan Simpson, stated that he saw the Report of Premiums form for the first time in the weeks preceding the hearing held in this matter.

33. As a result of the adjustments made by the Division (***see***, Finding of Fact "29"), it issued a Notice and Demand for Payment of Tax Due dated February 28, 2003 which asserted for the year 1999 additional franchise tax on insurance corporations in the amount of $319,592.22 and additional MTA surcharge in the amount of $3,489.08, plus interest imposed on each. For 2000, the Notice and Demand asserted additional franchise tax of $360,571.33 and additional MTA surcharge of $4,150.10, plus interest imposed on each. The total amount due, including interest, as set forth in the Notice and Demand was $816,830.62.

34. In April 2003, based on additional information provided by the SIF, the Division reduced the liabilities previously asserted in the Notice and Demand. The total franchise tax and MTA surcharge for both years at issue was reduced to $299,904.00, plus interest.

35. At the hearing held in this matter, the SIF provided the Division with additional information which indicated that the Division had erroneously determined that the total amount of extended payment plan finance and service charges for the years at issue is defined as the total amount set forth in the Annual Statements on Schedules T in Line 33, Column 8 entitled "Finance and Service Charges Not Included in Premiums" (***see***, Finding of Fact "28"). An

affidavit of the SIF's Controller, Allan Simpson, stated that other income is included in that line item which should not have been included. This other income included, among other things: return check fees; safety group transfer fees; third-party administrator fees; and third-party administrator interest. As a result, the Division further revised SIF's tax liabilities as follows:

Period Ended	Tax Type	Amount Due
12-31-99	Franchise Tax	$98,179.00
12-31-99	MTA Surcharge	$12,644.00
12-31-00	Franchise Tax	$164,770.00
12-31-00	MTA Surcharge	$21,272.00
TOTAL		$296,865.00

Accordingly, the total amount asserted to be due from the SIF for the years at issue is $296,865.00, plus interest.

SUMMARY OF THE PARTIES' POSITIONS

36. The position of the SIF may be summarized as follows:

a. The SIF's extended payment plan charges are not paid in consideration for an insurance contract. These charges are not, therefore, taxable premiums. The extended payment plan charges are optional and are assessed only at the request of and for the benefit of the insured and are not assessed in the first instance (on the first invoice);

b. The SIF's extended payment plan service and finance charges are not taxable because they do not meet the Tax Law definition of a "premium" as interpreted by binding New York case law;

c. The SIF's finance charges are not taxable because they are nothing more than an interest charge and are no different from nontaxable investment income;

d. The SIF's extended payment plan charges do not impact the underlying insurance coverage. A fee paid in consideration for an insurance contract is, by its nature, paid in advance, as a deposit for insurance coverage while the extended payment plan charges are assessed and collected upon the completion of the service associated with the underlying installment transaction;

e. The fact that the SIF may cancel any policy for nonpayment of the extended payment plan charges is of no consequence since the SIF can cancel a policy for the nonpayment of *any* fee owed to it, including charges which the Division has determined are not taxable premiums, such as the SIF's returned check fee, safety group transfer fee, third-party administrator fee and third-party administrator interest charges;

f. The Division's interpretation of the Tax Law's definition of a taxable premium should not be afforded any deference as it is unreasonable, irrational, lacks supporting authority and is inconsistent with State case law; and

g. If the SIF is forced to pay a franchise tax on the extended payment plan charges, the statutory mission of the SIF, i.e., ensuring that every New York business can afford workers' compensation insurance, will be greatly impacted due to the additional cost resulting from an increased franchise tax liability;

37. The Division, in opposition, asserts the following:

a. The SIF's extended payment plan finance charges and fees qualify as "separate costs by carriers assessed upon their policyholders" or "every other compensation" for an insurance contract and, therefore, are consideration given for an insurance contract pursuant to Tax Law § 1510(c)(1). If the Legislature had wanted to limit "premiums" to only expenses or fees associated with the risks against which a taxpayer was issuing

insurance coverage, it could have easily done so. Instead, by using "every other compensation for such contract," the Legislature has indicated that its focus was on all compensation paid under the terms of the legal agreement, not just on fees paid for the underlying insurance coverage;

b. Including the installment fees in SIF's gross direct premiums is reasonable and rational since the Tax Law definition of premiums is not limited to the risks associated with the insurance contract. The expense constant, a flat amount intended to cover some of the costs of the insurer, has no direct relation to any of the risks covered by a workers' compensation policy yet is still part of the taxable gross direct premium;

c. The interpretations of the State Insurance Department and the Division should be given great deference. Other states' case law supports the State Insurance Department's and the Division's interpretations; and

d. The SIF's installment fees are not paid in consideration for premium financing agreements as proscribed by the Banking Law. The SIF's endorsement to its insurance contract is not a premium financing agreement and neither the Workers' Compensation Law nor the Banking Law sanctions the SIF to be a premium financing provider.

CONCLUSIONS OF LAW

A. For purposes of this proceeding, the SIF is assessed a franchise tax on "all gross direct premiums, less return premiums thereon, written on risks located or resident in this state." (Tax Law § 1510[a].)

"Premium" is defined in Tax Law § 1510(c)(1) as follows:

> The term "premium" includes all amounts received as consideration for insurance contracts or reinsurance contracts, other than for annuity contracts, and shall include premium deposits, assessments, policy fees,

> membership fees, any separate costs by carriers assessed upon their policyholders and every other compensation for such contract.

B. The SIF cites to two cases which it contends are precedential and are, therefore, controlling as to the issue in this matter.

In ***Matter of American Credit Indemnity Co. v. State Tax Commn.*** (31 AD2d 27, 31, 294 NYS2d 818, ***affd*** 25 NY2d 707, 307 NYS2d 216), the Appellate Division, in 1968, held that fees charged an insured by its credit insurer (one who indemnifies merchants or other persons extending credit against loss or damage resulting from the nonpayment of debts owed to them) for collection of accounts which are delinquent, but which are not of a nature for which insurance claims may be lodged, are not premiums and are not, therefore, subject to the franchise tax on premiums. The Court stated that those fees, while embodied in a credit insurance policy, are independent of the insuring provisions and are, therefore, not part of the contract of insurance for which premiums are paid. While this case involved an interpretation of the predecessor statute (Tax Law former § 187), the Court based its decision on the fact that the fees charged by the credit insurer are "independent of the insuring provisions for which consideration is paid in the form of a premium calculated according to the risk. The payment of a fee, additional to the basic premium, for collateral benefits extend[ed] under a policy does not necessarily constitute the payment of a premium or additional premium."

Subsequently, in 1970, in ***Matter of Inter-County Title Guaranty & Mortgage Co. v. State Tax Commn.*** (33 AD2d 251, 307 NYS2d 156, ***affd*** 28 NY2d 179, 320 NYS2d 924), a case involving service charges imposed by a title insurance company for title examination, the Appellate Division, in holding that title examination fees were taxable because they were a

necessary incident of the insuring of the risk, distinguished the ***American Credit Indemnity Co.*** case by stating:

> Therefore, the fees subjected to tax in the American Credit Indemnity Company case did not fall within the definition of premium which "may be defined as the agreed price for assuming and carrying the risk–that is, the consideration paid an insurer for undertaking to indemnify the insured against a specified peril." (29 Am Jur, Insurance, § 501.)

Based on these court decisions, the SIF asserts that the extended payment plan service and finance charges are not taxable premiums because they are not paid in consideration for an insurance contract. This is true, the SIF states, because these charges are not required to be paid as a condition precedent to the issuance of the insurance contract and are independent from the insurance contract. The SIF contends that the service and finance charges are purely optional, i.e., they are assessed only at the request and for the benefit of the insured and are not assessed in the first instance on the first invoice to the insured. In support of that contention, the SIF points out that the insured which does elect to pay on the extended payment plan may, at any time, prepay or pay the balance of its premium, which then eliminates the need for subsequent services by the SIF and the future assessment of these charges. Moreover, the extended payment plan charges were established by the management of the SIF, not by its underwriting department which establishes both the eligibility of the insured and the amount of the premium. Therefore, the charges in no way impact the coverage to the insured.

The SIF also asserts that the extended payment plan charges are also distinguishable from a fee paid in consideration for an insurance contract because they are earned, assessed and immediately collected upon the completion of the service associated with the underlying installment transaction while, in contrast, a fee paid in consideration for an insurance contract is paid in advance, as a deposit for insurance coverage and is, therefore, earned on a daily basis for

each day the insurance remains in effect. If the insurance contract is canceled, the premium must be refunded to the extent any portion thereof remains unearned as of the date of the cancellation while the charges for the extended payment plan are not affected.

C. The Division points out that the terms of the SIF's extended payment plan are detailed in an endorsement to the insurance contract which amends Section E of Part Four of the contract (***see***, Finding of Fact "17") and that endorsements are generally recognized as amendments to a contract. Therefore, since the SIF's installment fees were authorized and controlled by the terms of an insurance contract, they qualify as "separate costs by carriers assessed upon their policyholders" or "every other compensation" for an insurance contract and are "consideration" given for an insurance contract pursuant to Tax Law § 1510(c)(1).

The Division further asserts that the extended payment plan charges and fees qualify as consideration for an insurance contract because a policyholder's nonpayment of these charges and fees could result in cancellation of the insurance contract. The Division points out that the SIF considered the fees to be consideration or compensation for the contract because the fees are incorporated into a policyholder's minimum amount due, and bills to the policyholders include language informing policyholders that the failure to make payments will result in cancellation of the policy. The bills do not distinguish nonpayment of premium from nonpayment of the installment fees.

The Division maintains that including extended payment plan charges and fees in the SIF's gross direct premiums is reasonable and rational since the Tax Law definition of premiums is not limited to the risk associated with an insurance contract. As an example, the Division points to the expense constant, a set amount which is intended to cover those expenses normally associated with the issuance, recording and auditing functions common to the processing of

workers' compensation insurance policies. The Division asserts that this expense constant bears no direct relation to any of the risks being covered by the insurance policy. Another example cited by the Division is the assessments, another component of premiums, which are levied against insurance carriers to fund the WCB and several ancillary programs. As noted by the Division, in 1993, the Workers' Compensation Law was amended (chapter 729 of the Laws of 1993) to require assessments to be treated as separate costs by insurance carriers rather than elements of loss for insurance ratemaking purposes, and the definition of premiums in Tax Law § 1510(c)(1) was changed at that time to include the phrase "separate costs by carriers assessed upon their policyholders."

The Division contends that its interpretations and those of the State Insurance Department should be given great deference. Since the issuance of Circular Letter No. 6 in 1967, the State Insurance Department's position has been that except for fees associated with premium finance agreements, all fees made by an insurer in connection with the voluntary extension of credit to an insured are properly includable in the computation of an insurance company's total gross direct premiums.

As to the Division's own interpretations, it points to the 1962 letter from its former Counsel, Edward H. Best, to Theodore R. Ayervais, former Assistant General Counsel of the State Insurance Department, and its subsequent issuance of a Technical Services Bureau Memorandum (TSB-M-80[8]C). The Division maintains that its interpretations are reasonable and rational because: (1) It is generally accepted that premiums are intended to account for all of the expenses of an insurance contract, including interest; (2) Inasmuch as dividends are deducted when computing total gross premiums, it follows that finance and service charges imposed upon policyholders for paying premiums in installments must be included in such computation;

(3) The definition of "premiums" for purposes of Article 33 of the Tax Law including the phrase "every other compensation for such contract" is evidence that the Legislature did not want to limit "premiums" to only expenses or fees associated with the risks against which a taxpayer was issuing insurance coverage; and (4) Other states' cases have found that flat fee charges and interest charges should be included in a carrier's computation of total taxable premiums.

The Division also states that because the SIF should be held to the form of the contract which it selected, contrary to the SIF's assertions, its installment fees are not paid in consideration for premium financing agreements as proscribed by the Banking Law.

Finally, the Division asserts that despite the SIF's contention that having to pay a tax on its installment fees would impair its ability to provide low cost insurance as mandated, the SIF should be treated no differently from other taxpayers, i.e., private insurance carriers. If it does not want to have to pay taxes on these fees, it should seek such preferential treatment from the Legislature, not from the Executive or Judicial branches of New York State government.

D. The Division, in its brief, notes, "[w]hile not quite an issue of first impression, there is no extant precedential case law directly addressing whether an insurance company's fees charged to policyholders for paying their premiums in installments are 'premiums' for the purposes of computing its tax on total gross direct premiums."

This assertion by the Division conveniently ignores the cases of ***American Credit Indemnity Co.*** (***supra***) and ***Inter-County Title Guaranty & Mortgage Co.*** (***supra***). While it is true that these cases did not interpret the statute at issue in this matter, Tax Law § 1510(c)(1), that is because both of these cases were decided prior to the enactment of Article 33 of the Tax Law in 1974. Moreover, as the SIF correctly asserts, while these cases do not directly address the issue of whether extended payment plan charges are taxable premiums, they do provide

significant guidance as to what fees qualify in New York as premiums for purposes of a taxpayer's computation of its total gross direct premiums. In addition, these cases, which were affirmed by the New York State Court of Appeals, have never been reversed and are, therefore, binding authority. Both cases stand for the general principle that certain fees paid for collateral benefits, not of a nature for which claims may be lodged and which are independent of the insuring provisions, are not part of the contract for insurance for which premiums (the agreed price for assuming and carrying the risk) are paid.

The SIF's position, as articulated in its reply brief, is that in order to be a premium, a charge must be paid as "consideration for insurance contracts" (Tax Law § 1510[c][1]) and, therefore, must be more than just related to the contract. It correctly states that if an insured is able to obtain an insurance contract without being assessed the charge, then the charge is not paid as compensation or consideration for an insurance contract and is not, therefore, a taxable premium. An insured who is eligible for the SIF's extended payment plan may pay its premium in full at the commencement of the insurance contract and thereby avoid the imposition of a service or finance charge, or may pay the entire balance of the premium due at any time thereafter and avoid any future service or finance charges. Therefore, it seems logical that if an insured can obtain an insurance contract without being assessed the service or finance charges, then the charges are not paid "in consideration for an insurance contract" and are not taxable premiums.

Citing expense constants and assessments, the Division contends that the definition of premiums is not limited to the risk associated with an insurance contract. The expense constant, which is a set amount intended to cover those expenses normally associated with the issuance, recording and auditing functions common to the processing of workers' compensation insurance

policies, and the assessments, a component of premiums levied against insurance carriers to fund the WCB and certain ancillary programs, bear no direct relation to any of the risks being covered by the insurance policy. However, as correctly noted by the SIF, the Manual makes the expense constants and assessments applicable to every policy and, unlike the service and finance charges, an insured cannot obtain a workers' compensation insurance policy without first being required to pay expense constants and assessments.

E. The Division asserts that its interpretations and those of the State Insurance Department should be given great deference. The Division cites to McKinney's Consolidated Laws of NY, Book 1, Statutes § 129, for the principle that a continuous course of action over a long time by State or local administrative officers should be accorded great weight. However, it must be noted that the same statutory section states, in part, as follows:

> Generally, a court should not hide behind the ruling of an administrative officer or agency and thus escape the duty to interpret the statute, since the court is the final arbiter as to the proper construction. In other words, a court should not blindly follow the rulings of administrative officers in construing statutes. Even though practical construction by an officer or agency charged with administration of a statute, especially when followed by a long period of time, is entitled to great weight and may not be ignored, such an interpretation is not necessarily binding on court.

At this juncture, the bases for the Division's and the State Insurance Department's interpretations must be examined.

F. In 1980, the Division issued a Technical Services Bureau Memorandum, TSB-M-80(8)C, which instructed taxpayers that a flat fee service charge for installment payments charged by an insurance company is includable as a taxable premium for the purpose of the premium tax imposed by section 1510(a) of the Tax Law. The memorandum cited to section 1510(c)(1) of the Tax Law, most notably to the phrase "and every other compensation for such

contract" as justification for its position. However, as noted by the Tax Appeals Tribunal in ***Matter of AIL Systems, Inc.*** (Tax Appeals Tribunal, May 4, 2006):

> Technical Service Bureau Memoranda are merely informational statements issued by the Division to disseminate current policies and guidelines and are advisory in nature, have no legal force or effect, are not binding and do not rise to the level of a promulgated rule or regulation.

As previously noted, TSB-M-80(8)C was based upon a February 13, 1980 letter from former Deputy Commissioner and Counsel for the Division, Ralph J. Vecchio, to Morton Greenspan, former Deputy Superintendent and General Counsel of the State Insurance Department, who sought the Division's opinion as to the taxability of certain premium payment service charges. At the time of the letter, the insurer referred to in the letter offered its customers a "two-payment option" which permitted an insured to pay its premium for the entire six months or divide the premium into two three-month portions, each due prior to the period of coverage for which it represented payment. The charge for the two-payment option was a fixed fee of two dollars.

Mr. Vecchio's letter indicated that the Division had previously responded to a State Insurance Department request as to the taxability of installment charges, referring to a letter of former Counsel Edward H. Best dated July 5, 1962. That letter stated, in part, as follows:

> Our analysis of the question raised in your letter leads us to agree with your conclusion that additional amounts charged by insurers for the privilege of paying premiums in installments come within the *definition* of 'premium' in section 550 of the Insurance Law, and therefore *could* be made subject to tax under Article XVII of that law and section 187 of the Tax Law. (Emphasis added.)

However, as noted in Finding of Fact "23", the Best letter cited no legal authority for his position, stated that the amounts charged by insurers for the privilege of paying premiums in

installments "could be made subject to tax" and also took note of "the previous contrary ruling by your Department."

If the Division's position was, as stated in the Vecchio letter, meant to be consistent with a previous Division interpretation (the Best letter of July 5, 1962), a close examination of these letters reveals little or no reason to rely on either.

Mr. Vecchio noted that the taxes on premiums imposed by section 1510 of the Tax Law are the successors to section 187 of the Tax Law, and the definition of "premium" in section 1510(c)(1) is identical to the definition of "premium" in section 550(1) of the Insurance Law and section 187(9)(E) of the Tax Law. Mr. Vecchio indicated that it was his opinion that the service fees for the two-payment option were includable as taxable premiums for purposes of the tax imposed by section 1510(a) of the Tax Law. The Vecchio letter referred to ***Matter of Inter-County Title Guaranty and Mortgage Co. v. State Tax Commn.*** (***supra***) and also to ***Matter of Stuyvesant Insurance Co. v. State Tax Commn.*** (39 AD2d 804, 332 NYS2d 314), the latter case which held that the portion of premium paid by an applicant for a bail bond and retained by the subagent as his compensation for services performed by him was an integral part of the charge for the bail bond and, as such, was a "premium" and includable in the franchise tax on premiums imposed by Tax Law former § 187. The letter also cited to other states' cases (which shall not be addressed herein) which were cited by former Deputy Superintendent and General Counsel of the State Insurance Department Theodore Ayervais in his May 8, 1967 opinion which became official policy of the State Insurance Department in Circular Letter No. 6 (***see*** , Finding of Fact "24"). Mr. Vecchio further stated that there was no decision by the New York courts on the taxability of installment charges.

Of great relevance to the present matter is Mr. Vecchio's statement, in his letter, that the ***Inter-County Title Guaranty and Mortgage Co.*** case "held that fees charged by a title insurance company for title examinations were part of taxable 'gross direct premiums'." What the letter failed to include was the Court's reasoning in that case which, as previously noted (***see***, Conclusion of Law "B"), was that title examination fees were taxable because they were a necessary incident of the insuring of the risk. Also, for whatever reason, the letter failed to mention ***Matter of American Credit Indemnity Co. v. State Tax Commission*** (***supra***) which is specifically mentioned in the ***Inter-County Title Guaranty*** case and which held that the payment of a fee, additional to the basic premium, for collateral benefits extended under a policy does not necessarily constitute the payment of a premium. For these reasons, it appears that the Vecchio letter which conveyed the Division's opinion was seriously flawed and should, therefore, be entitled to little, if any, deference. Accordingly, the Technical Services Bureau Memorandum, TSB-M-80(8)C, which the Division concedes was based upon the Vecchio letter of February 13, 1980, is likewise entitled to little, if any, deference.

G. As to the State Insurance Department's position as set forth in Circular Letter No. 6 issued on August 15, 1967, it must be noted that the letter was addressed not to insurers who issued workers' compensation insurance contracts, but to fire and casualty insurance companies. Moreover, this position letter predated ***Matter of American Credit Indemnity Co. v. State Tax Commn.*** (***supra***) and ***Matter of Inter-County Title Guaranty & Mortgage Co. v. State Tax Commn.*** (***supra***) which were issued in 1968 and 1970, respectively. Of greater relevance is a more recent opinion of the office of the General Counsel of the State Insurance Department, issued July 27, 2000 (***see***, Finding of Fact "31") wherein the State Insurance Department stated that: "[i]nstallment fees are not considered a part of the insurer's base premium and need not be

included in the insurer's rate filing to the Department. Installment fees are separate and distinct from the premium and should be displayed on the billing notice and/or cancellation notice." This opinion issued during the second of the years at issue in this matter is, therefore, entitled to much greater consideration and weight than the 1967 Circular Letter No. 6.

While, as asserted by the Division, as a general matter courts should defer to the interpretation given a statute by the agency (or agencies) charged with its enforcement, that proposition is true only if the interpretation is neither irrational, unreasonable nor inconsistent with the governing statute (***see***, ***Matter of Trump-Equitable Fifth Ave. Co. v. Gliedman***, 57 NY2d 588, 457 NYS2d 466). For the reasons set forth herein, it has been shown that the interpretation of Tax Law § 1510(c)(1) by the Division is not rational, reasonable or consistent with the statute, in light of existing case law, and no deference to the Division's interpretation is, therefore warranted. As to the interpretations of the State Insurance Department, for the reason set forth above, only the opinion of the office of the General Counsel issued July 27, 2000 is entitled to deference in this matter.

H. Much is made by the Division that the SIF's installment charges and fees qualify as "consideration for an insurance contract" because a policyholder's nonpayment of these charges or fees could result in cancellation of the insurance contract. In support of its position, the Division points to Workers' Compensation Law § 93(a) which states that "[i]f a policyholder shall default in any payment required to be made by him to the state insurance fund after due notice, his insurance in the state fund may be cancelled and the amount due from him shall be collected by civil action . . . ."

The SIF correctly notes, however, that Workers' Compensation Law § 93(a) provides for the cancellation of an insurance policy for the default (or nonpayment) of *any* fee required by the

policyholder to be made. As noted in Finding of Fact "35", the Division conceded that certain nontaxable fees such as return check fees, safety group transfer fees and third-party administrator fees and interest are nontaxable yet nonpayment of these fees by a policyholder could, pursuant to the provisions of Workers' Compensation Law § 93(a), lead to cancellation of the policy.

Moreover, as the SIF points out in its reply brief, the finance charges (1% per month) are charged only on the audited premium, i.e., the finance charges are assessed only after the completion and audit of the insurance contract. Therefore, if an insured defaults on the payment of the finance charges and no longer has an insurance contract with the SIF because either the insured is out of business or has elected to obtain insurance from another provider, the SIF could not cancel the contract because there is no insurance contract in existence. Therefore, it is hereby found that the fact that nonpayment of the installment charges and fees could lead to cancellation of the insurance contract does not logically lead to the conclusion that these fees qualify as "consideration for an insurance contract."

In further support of this finding is a reference in the July 27, 2000 informal opinion of the office of General Counsel of the State Insurance Department (***see***, Finding of Fact "31") to Insurance Law §§ 3425(a)(10) and 3426(a)(3) which define "nonpayment of premium." In both statutes, the term includes premiums directly payable to the insurer *and* indirectly under any premium finance plan or extension of credit. Even in the State Insurance Department's Circular Letter No. 6, dated August 15, 1967, which the Division contends is entitled to great weight and deference, charges for services derived from direct financing of premiums upon a premium finance agreement are excepted from "all additional charges for service," which the letter states are deemed part of the premium and, therefore, taxable under Tax Law former § 187. If nonpayment of charges pursuant to a premium finance agreement, which the State Insurance

Department concedes are not part of the premium, can properly result in cancellation of the insurance contract, the fact that an insurance contract can be cancelled for nonpayment of sums arising from extension of credit from the insurer (the SIF) does not logically lead to a conclusion that the SIF's installment charges and fees qualify as "consideration for an insurance contract."

I. The Division asserts that because dividends are deducted when computing a taxpayer's gross direct premiums, it is, therefore, logical to include in the computation of gross direct premiums its finance and service charges to policyholders for paying premiums in installments. Attached to its brief are select pages from Green, Glossary of Insurance Terms, and Davids, Dictionary of Insurance, wherein the term "dividend" is defined. In general, both define "dividend" as the return of part of the premium paid for a policy or a portion of the surplus paid to the stockholders of the corporation. The Division then points to the SIF's annual reports for 1999 and 2000 where it is reported that the Workers' Compensation Law provides that dividends (referred to in the annual statements as "Contingent Policyholder Dividends") may be paid to safety groups that seek to curtail accidental injuries and occupational diseases. The annual reports indicate that the estimated dividend liability recorded by the Workers' Compensation Fund is based on the available contingent balance, which is calculated by adding premiums billed and applicable interest income less reported losses, expenses and previous dividends.

The Division states that, in effect, the SIF's tax liability has been reduced by the amount of interest that it paid to those of its policyholders, which the SIF voluntarily determined earned dividends and which interest was intended to reimburse the policyholders for the SIF's use of their money. Therefore, the Division contends, it is logical that the SIF's tax liability be increased by its charges to those of its policyholders who accepted the SIF's voluntary offer of an extension of credit.

Clearly, the $10.00 service charge was not intended to reimburse the SIF for use of money; the service charge was instituted to cover the SIF's costs of issuing the bill and other expenses associated with reissuing bills month after month where the insured has elected to pay under the extended payment plan. Therefore, the deduction of dividends by the SIF is of no relevance to the service charges collected by the SIF.

With respect to the finance charges, while there may, in fact, be some correlation between the finance charges (intended to act as a partial replacement for investment income which the SIF would have earned if the premium had been paid up front) and deductible dividends, the annual reports indicated that the estimated dividend liability recorded by the Workers' Compensation Fund is based on the available contingent balance as of the most recent group accounting date and an estimate of the contingent balance for the period since the last group accounting. The contingent balance is calculated by adding premiums billed and applicable investment income less reported losses, expenses and previous dividends. Simply because the finance charges are an attempt by the SIF to partially recoup some of its investment income which was lost due to its inability to have access to the entire premium proceeds, it cannot be inferred that these charges are properly includible in the computation of premiums for purposes of the New York State franchise tax on "all gross direct premiums." This is true because there is no evidence that the SIF included the finance charges as part of its investment income which went into its calculation of dividends.

In its brief, the Division asserts that "[t]he petitioner's service charge of 1% does not qualify as income from its investments." In support of that position, the Division states that Workers' Compensation Law § 87 sets forth the investments in which the SIF may invest and that its extended payment plan is not one of those investments. Moreover, the Division concedes

that the investment income reported by the SIF on its annual reports to the State Insurance Department is income only from its investments permitted by statute and its income from the 1% finance charge is included within "Other Income" on its annual reports.

Accordingly, since there is no evidence that the SIF included the amounts of the finance charges in its calculation of investment income and the Division concedes that it did not include these charges in investment income, the fact that it was entitled to deduct the amount of its dividends is of no consequence or relevance in this matter.

H. Pursuant to Article 12-B of the Banking Law and Article 6 of the Workers' Compensation Law, the SIF, unlike private insurance carriers, cannot be a premium finance agency or issue premium finance agreements which would, pursuant to the provisions of State Insurance Department Circular Letter No. 6 (***see***, Finding of Fact "24"), exempt service and finance charges from being deemed part of the premium collected.

The SIF points out that it cannot utilize this device to avoid the Division's imposition of tax liabilities and therefore asserts that if the Division is successful in its attempt to include the finance and service charges in the computation of gross premiums for the purposes of the franchise tax imposed pursuant to Article 33 of the Tax Law, the effect would be to hinder the SIF from accomplishing its statutory mission to provide low cost workers' compensation insurance.

While it is true, as pointed out by the SIF, that the reason why the Division's auditor testified that he did not encounter similar issues with other taxpayers is because other insurers have the advantage of issuing premium finance agreements, that factor can be of no relevance to this proceeding. The issue of whether the service and finance charges were properly includible

in premiums for purposes of computing the tax imposed on insurance companies' total gross direct premiums must be resolved based upon an interpretation of the relevant statute, Tax Law § 1510(c)(1), and not because a determination could have an adverse effect on the statutory mission of the SIF.

I. In summary, it is hereby determined that the SIF's extended payment plan charges are not paid in consideration for an insurance contract and are not, therefore, taxable premiums. The charges do not meet the definition of "premium" as interpreted by binding New York case law. The relevant cases state that payment of fees additional to the basic premium for collateral benefits (in this case, the right to pay premiums over an extended period) do not constitute the payment of a premium and a review of the record presented in this matter reveals that the SIF's extended payment plan fees and charges are "collateral benefits" which are optional to policyholders and which do not, in any way, impact the insurance coverage contracted for between the SIF and the employers who obtain workers' compensation insurance. The fact that nonpayment of the extended payment plan charges may result in cancellation of the insurance contract is of little import in this matter since nonpayment of charges which are clearly not part of the premiums subject to tax may also result in cancellation of the insurance contract.

The Division's and, other than the most recent relevant opinion of the office of the General Counsel issued during the audit period, the State Insurance Department's interpretations of what these agencies perceive to be included in the definition of a taxable premium should be afforded no deference since such interpretations are unreasonable, irrational, lack supporting authority and are inconsistent with State case law. While the Division, in its extensive brief, sets forth numerous factors which it deems relevant to the adjudication of this matter, most are collateral factors which do not alter the conclusion reached herein.

J. The petition of the New York State Insurance Fund - Workers' Compensation Fund is granted and the Notice and Demand issued February 28, 2003 is hereby cancelled.

DATED: Troy, New York
March 15, 2007

/s/ Brian L. Friedman
ADMINISTRATIVE LAW JUDGE