The Regulation of Insurance Producers

Insurance Career Training, Inc.
www.insurancecareertraining.com

You may access this class presentation after class at
www.insurancecareertraining.com/classhandouts
The file password is quayle25852

The Regulation of Insurance Producers

Courts have long held that insurance is an industry vested in the public interest, thus creating a need for regulation.
The Regulation of Insurance Producers

State vs. Federal Regulation

- Paul vs. Virginia (1869)
  - Reinforced states rights to regulate insurance activity
- Southeastern Underwriters (1944)
  - Enacts federal regulation for the insurance industry

Current Regulation by the State

- **Legislative**
  - Maintaining solvency of the insurance industry, insurance rating, sales/claims practices, taxation of insurance companies
- **Judicial**
  - Interpretation of policy clauses and provisions, legality of administrative actions by state departments, constitutionality of state insurance laws

State vs. Federal regulation

- McCarran-Ferguson Act (1945)
  - Congress declared that the continued regulation and taxation by the several states of the business of insurance is in the public interest, and that silence on the part of the Congress shall not be construed to impose any barrier to the regulation or taxation of such business by the several States

Current Regulation by the State

- **Executive/State Departments of Insurance**
  - Regulates companies and agents, frequently making rulings that have the binding force of law while exercising judicial power in interpreting and enforcing the insurance code of the state.
The Regulation of Insurance Producers

National Association of Insurance Commissioners

- (NAIC)
  - Encourage uniformity in state insurance laws, assist officials in administering laws, protect interest of policy owners, preserve state regulation of insurance business

NAIC

- Model Legislation
  - Includes representative bills or statutes presented to the individual state legislatures for consideration and passage
  - Examples include:
    - "Unfair Trade Practices Act"
    - "Life Insurance Solicitation Regulation"
    - "Life Insurance Replacement Regulation"
    - "Life Insurance Policy Illustration Model Regulation"
    - "Unfair Claims Settlement Practices Act"
    - "Medicare Supplement Insurance Minimum Standards Model Act"

Some current and emerging insurance issues in discussion:
- Use of artificial intelligence in insurance
- Air ambulances billing practices
- Health care cost drivers
- Challenge of urban flooding
- Data protection and privacy
- Cyber insurance
- Annuity suitability and best interest standards
- Climate/natural catastrophe risks
- Long-term care insurance
- Autonomous vehicles
- Cannabis and insurance

Federal Regulations
The Regulation of Insurance Producers

The Securities and Exchange Commission (SEC)
- Supreme Court – has held that variable annuities are securities, and subject to federal regulation
- Investment Advisers Act (Release 1-A 1092)
  - Defines who is an investment adviser as any person who provides investment advise, is in the business of providing investment advise, and is compensated for providing investment advise
  - (exceptions include banks, news publishers, brokers or dealers, persons advising on US government securities, and those whose advise is incidental to their profession – lawyers, accountants, engineer, and teachers)
- FINRA – agents who sell variable insurance products must be registered with the Financial Industry Regulatory Authority (FINRA)

Federal Insurance Administration
- Administers the National Flood Insurance Program that makes flood insurance available nationwide
- Write Your Own Program – allows participating insurance companies and insurance agents to write and service federal flood insurance

The Federal Fair Credit Reporting Act
- Requirements of the Act
  - An applicant for insurance must be informed in advance that an inspection or consumer report may be ordered
  - Consumer reporting agencies must disclose to the consumer all information in the consumer's file when requested
  - If the insurer makes an adverse underwriting decision based on the information, they must advise the consumer of decision and the report(s) used
- The NAIC Information and Privacy Protection Model Act
  - Prohibits pretext interviews except in certain claims situations
    - Pretext Interview
    - When an investigator pretends to be someone other than who he or she is in or to secure information

State Regulations
Licensing Laws

- All states require that agents and brokers be licensed, usually requiring a written exam or a completion of a course.

Unfair Trade Practices

- Unfair Trade Practices Act
  - Seeks to regulate insurance practices by defining and prohibiting unfair trade and business practices such as defamation, unfair discrimination, unfair claims settlements, and false advertising.

- Misrepresentations and false advertising of insurance policies – prohibits making, issuing, or circulating material which misrepresents the features of the policy or condition of the company.
- False information and advertising generally – prohibits creating or publicizing statements in any form that misrepresent any aspect of insurance business.
- Defamation – prohibits creating or publicizing any oral or written statement that is false, maliciously critical of, or derogatory about the financial condition of any person or insurance company.
- Boycott, coercion, and intimidation – prohibits entering into any agreement to commit, or by concerted action committing any act of boycott, coercion, or intimidation resulting in restraint of or monopoly in the insurance business.

- False statements and entries – prohibits knowingly filing or publicizing any false material regarding the financial condition of a person or business.
- Stock operations and advisory board contracts – prohibits issuing agency company stock or special advisory contracts promising returns or profits as an inducement to buy insurance.
- Unfair discrimination – prohibits discrimination between individuals of the same class and of essentially the same hazards in rates charged, benefits paid, or policy issued.
  - NAIC Model Regulation to Eliminate Unfair Sex Discrimination does not prohibit the use of sex-based pricing, but rather prohibits the denial of insurance on the basis of sex or marital status.
Unfair Trade Practices
- rebating – prohibits giving a premium reduction or other financial advantage to an individual as an inducement to purchase a policy
- unfair claim settlement practices – prohibits committing with such frequency as to indicate a general business practice a list of activities designed to settle a claim for less than the amount a reasonable person would believe they are entitled to

Other Unethical Practices
- Twisting – convincing a life policyholder to drop one policy for the purpose of selling another policy to the detriment of the policyholder by misrepresenting the either policy
- Churning – convincing a policyholder to use the values of an existing contract of insurance to purchase another contract for the purpose of generating additional commissions
- replacement means convincing a policyholder to lapse or replace an existing contract with the purchase of another from the agent (regulations are in effect to guard against unethical activities advocating such activity)

Unfair Trade Practices
- failure to maintain complaint handling procedures – requires maintaining a complete record of all complaints received since the date of last examination
- a complaint is any written communication that primarily expresses a grievance
- misrepresentations in insurance applications – prohibits making false or fraudulent statements regarding an insurance policy application for the purpose of obtaining a fee, commission, money, or other benefit from any insurer, agent, broker, or individual

Other Unethical Practices
- solicitation and disclosure requirements
  - illustrations – requires a signed illustration for life insurance polices with non-guaranteed components such as interest rates, dividends, and risk charges
  - buyer’s guides – a general statement of benefits and provisions of life insurance written in a way the average consumer may understand
  - policy summaries – a specific statement showing the benefits and values of a particular policy (often included in the illustration)
**Evolution in CE Requirements**

- Ethics – many states require licensees complete ethics training during each renewal cycle
- LTC – many states require producers complete LTC certification courses before selling the product and to take refresher LTC courses to maintain certification
- Annuities – most states require producers to complete an annuity suitability course before selling annuity contracts
  - this has further been refined by states (like New York Regulation 187 "Suitability and Best Interests in Life Insurance and Annuity Transactions")

**Handling of Premiums**

- Most agents are authorized to collect initial premiums from applicants; most are also allowed to collect renewal premiums
- Agents have fiduciary duty to account for all funds they receive in connection with the insurer’s business

**Dealing with Suitable Insurers**

- Unless agents are specifically licensed to, they are prohibited from writing insurance with an insurance company that is not licensed to do business in the state
- Producers are held responsible for written contracts
Debate Concerning Regulation

- State or federal regulation?
  - Federal advocates believe this creates better uniformity in law
  - State advocates believe individual states have the experience and expertise necessary to solve issues

Overview of the Agency Relationship

- Termination
  - Concluding a principal/agent relationship
  - Agency relationship cannot be terminated without legal rights lying against the party ending the agency in the following situations:
    - where either the principal or agent terminates the agency relationship in violation of a contractual right, and
    - where an agency coupled with an interest is involved

Authority of Insurance Agents

- Authority (the legal power of the agent arising from the agency relationship)
  - Actual or Expressed
  - Implied
    - can't be present without expressed authority
  - Perceived or Apparent
  - Limitations

- Fiduciary (must exercise a high degree of fairness and good faith and act in the best interest of the insurance company)
The Regulation of Insurance Producers

Major Sections of the Agency Contract

- Authority
- Ownership of Expirations (next several slides)
- Billing Procedures
- Commissions
- Expenses
- Termination

“Ownership of Expirations”

- Agency ownership of its expirations is core to agency culture, core to the agency’s value, and core to the owners’ livelihoods. Yet today, the ownership and even more important, the value of the expirations, is being threatened, and most agency owners do not see it happening. The analogy to the old story of the frog enjoying the warm water until the instance before death is possibly apropos.

Consider the following examples.

- The first example is the most obvious. Producers – and often far more important, CSRs – taking clients. Most agency owners recognize this threat, but their producer contracts are entirely inadequate and their contracts with CSRs are even worse. What is possibly even more damaging is how many agency owners underestimate the control some CSRs have over clients. Their client relationships are often far stronger than the relationships producers have.

- The second example is also mostly obvious, and that is an agency’s carrier taking the expiration list. I am not too terribly concerned about a company brazenly taking ownership of expirations. Usually when this happens, it happens because the agency has failed to pay its premiums on time or has lost its license.

- Always read your contracts, not only for what they say, but what they do not say, too.

- The third example involves companies, and is bold, but not as obvious. Owning an expiration list in the old days was good protection, but in today’s information age, owning data is far more important. The agency may own the list but does the agency own all the pertinent data? I have seen companies effectively cause agencies to lose material business by using client information, in my opinion, nefariously but permissible per the contract. Check your contracts.

- The fourth example involves companies who simply give client information to agents and brokers they like better than you, once you move a policy to a competitor. I do not understand some insurance companies’ fixation that clients only move because agents facilitate their moving. This is why companies give policy information to other agents. It is why companies secretly buy agencies and then prevent the staff from moving accounts. It is why companies like service centers. Some companies seriously believe customers will not shop if an agency does not remind them to shop.

- Protect yourself in these situations, including the use of service centers. Always read your contracts, not only for what they say, but what they do not say, too.

“Ownership of Expirations” cont.

- The fifth example is relatively new. Now that many companies are writing directly, what happens to the data they have regarding your clients? Just asking.

- The sixth example is actually old, and that involves programs. A famous case involving a program for softball leagues where a company stole the program from the agency was resolved in favor of the agency. If you have a program or even the thought of a program, make sure your company, or companies, sign non-disclosure agreements and even non-compete agreements before you share the details. I know your companies are special and they are your friends, and they would never take a program from you, so it should be no problem for them to sign these reasonable agreements.

- The seventh example is maybe the scariest, as I look from the outside in. In the past five years, the largest brokers have purchased many wholesale brokerages. These brokers’ wholesale businesses now contribute as percent to 30 percent of the brokers’ commission revenues. These are large sums.

- I continually find most agencies have not adjusted to this new reality. Their broker relationships are lax. Sometimes they do not even have a contract with their brokers. If you do not have a contract, what is to prevent a broker from sharing your expirations, your data, with their retail branch? Maybe I have become too jaded over time or maybe I have just seen too many instances of Chinese walls that were imaginary at most, but I would err on the presumption that data gets shared.

- A related issue is how I have seen many programs develop on a handshake basis, and these programs have run well for years, sometimes decades. All parties have complete confidence in each other and maybe rightly so.

- However, all agencies and brokers are eventually sold. The appetite for purchasing wholesalers and certain program business does not seem to be slowing. Given the inevitable sale and the potential purchasers, doesn’t it make sense to build protection while you still have a friendly face on the other side of the deal?
The Regulation of Insurance Producers

“Ownership of Expirations” cont.

Aggregators

- The eighth example involves clusters and aggregators. The question here varies considerably depending on how the cluster contract is written. In general, when an agency joins a cluster, it may not retain 100 percent ownership.
- I recently saw a situation in which a company claimed ownership of a cluster member’s expirations – and it was correct!
- I have seen other situations where an aggressive cluster operator took advantage of more trusting “partners” and took control of the expirations.
- An interesting example is some agency owners join a cluster designed as a service center. The cluster services the business alleviating much woe for small agency owners. This is fine on paper and fine if the agency owner stays in touch with clients. Some agency owners are lazy though, and they quit selling much and they let the cluster’s service center build relationships. Then, if the cluster contract is not designed well, the owner can be kicked out. Sure the owner can claim ownership, but exactly where are they going to go?

“Ownership of Expirations” cont.

- Ownership of expirations has been so inculcated into agency culture that many agency owners take it for granted. They have not stayed in-tune with the times. They do not understand that other entities controlling data and relationships can severely damage the value, possibly eliminate the value, traditionally associated with owning the expirations.
- The solutions are fairly simple, but work is involved. Is protecting your agency’s value, your wealth, worth the work and investment?

Responsibilities of Insurance Agents

- Loyalty
- Skill and Performance
- Full Disclosure
- Prompt Action and Follow-up
- Handling of Premiums
- Conflicts of Interest
- Careful Solicitation
- Competitive Integrity

Responsibilities of Insurance Agents

- Selling to Needs
- Commitment to Knowledge and Skills
- Commitment to Educating the Client
- Service the Sale
- The Application
- Confidentiality
- Full Disclosure to the Applicant
- Policy Delivery
You may access this class presentation after class at
www.insurancecareertraining.com/classhandouts
The file password is quayle25852