Producer Responsibilities - Other Related Concepts

A. Policy Delivery

The underwriting process for an insurance application can be time consuming. Most insurance companies strive to complete the process within a 21-day period if there are no delays. Delays can occur whenever an underwriter needs additional information from the applicant and relays that request through the agent, or when a counteroffer, different policy, or different rate is made to the applicant (again through the agent).

An agent's ethical responsibilities to his or her client during the underwriting process pertain to promptness and policy delivery.

An insurance agent needs to ensure that there are no unnecessary delays in the underwriting process. This does not mean that the agent has to rush from an applicant's home to the nearest post office to mail an application. However, it does mean the agent should check the application for accuracy and give careful thought to it before the application is actually submitted. Many underwriting delays occur simply because the application is not complete or is not clear.

Applications should be submitted as quickly as possible. The time frame will vary, of course, depending on the plan of insurance and the complexity of the case. An agent must take these factors into account to act in an efficient manner. If it appears that the underwriting process may take longer than anticipated, the agent should notify the applicant of the delay.

Most policies are issued as applied for. In such cases, the agent owes his or her new policyowner prompt delivery of the policy and a review of its features and benefits. Not only does this help solidify the sale, it also represents a step toward making the policyowner a lasting client.

On occasion, a policy will be rated or rejected. When this happens, the agent has 2 responsibilities:

1. Personally review the rating or rejection. Was it for medical reasons? Was there an unfavorable medical report? Was something overlooked or not made known to the underwriter? Should additional information be submitted? Is the rating or rejection proper? Should the application be reconsidered? In any event, the agent should have as much information as possible and be able to explain the rating or rejection to the applicant.
2. Assuming that the rating or rejection was valid, notify the applicant promptly. To withhold this information is a breach of ethics that could actually harm the applicant and his or her family.

B. At Claims Time

The agent is often the first person contacted when a loss has occurred under an insurance policy. The agent must be familiar with all of the insurer's claims procedures and be prepared to guide the client through the process. (Remember: Notice to the agent is considered the same as notice to the insurer.)

The agent must be careful about advising the policyholder about whether a particular loss will be covered or not. An agent should not provide legal advice or make decisions on behalf of the insurance company.

1. Fraudulent and/or Exaggerated Claims

Studies have shown that even individuals who consider themselves "honest" think there is nothing wrong with inflating insurance claims in order to collect after a loss. The following are some examples of fraudulent claims.

- "Malingering," or resisting a return to work after a disability by falsely claiming that a medical condition still exists
- Claiming a non-work-related injury as a work-related injury in order to qualify for workers compensation benefits
- Inflating the value of stolen property or including items that were not stolen as part of a list of stolen property on a claim form
- Including pre-existing damage as part of an auto claim (e.g., a previously a dented bumper)

What should an agent do when a fraudulent or exaggerated claim is suspected?

The agent must be careful not to accuse someone of fraud when there is no specific evidence. It is best to contact the insurer's Special Investigative Unit (SIU).

C. Providing Continued Service

Selling to needs is only part of what an agent must do to meet the ethical responsibilities that he or she owes to a policyholder. Providing service during and after the sale is just as important. Quality and productivity experts see service as a process in which the customer's wants and needs are anticipated and then satisfied. Most companies today are committed to giving their customers quality service.

In insurance, producers should be providing an annual policy review that takes into account family changes, such as marriage, divorce, birth of a child, acquisition of new property (and new automobiles), and death. The producer acts as the representative of the company in changing beneficiaries, adding amounts of insurance, and providing advice and support during the claims process.

1. Ethics & Service

Perhaps one of the most important aspects of business ethics is that the characteristics one associates with an ethical person – fairness, honesty, and personal responsiveness – affect the level of service that a company provides. For example, an insurance agent who doesn't promptly return a client's telephone calls or procrastinates in giving a client important information about a policy will only hurt his or her reputation as a responsible professional. Therefore, treating clients with ethical principles will result in a higher level of quality service.

Keep in mind that the term "service" means many things, and no two people would define all that it entails in precisely the same manner. However, for the purpose of this discussion, we will cover the elements of service in the context of ethical selling and professional responsibility. Thus, we will define "service" to mean

- Educating the client before, during, and after the sale

- Ensuring that the client fully understands the application and underwriting processes, the policy purchased, and any attached riders
- Treating the client's financial and personal affairs with confidentiality
- Disclosing all information needed by the policyholder or applicant so that he or she can make an informed decision
- Showing loyalty to the client, which includes providing the full range of services offered by the insurer

D. Producer Responsibilities to the Public

Our society depends on insurance as a means of protection from financial disaster. Property insurance coverage forms part of every mortgage contract and lease agreement, and it is often found in construction, service, and maintenance agreements. In some cases, casualty coverages, such as auto liability and workers compensation, are required by law. Medical insurance provides a cushion against economic disaster. Life insurance benefits and cash values may represent a substantial part of the financial holding and retirement planning for many individuals and families.

HOW INSURANCE CAN IMPACT THE PUBLIC

- *A policyholder dies; his or her survivors are able to remain financially comfortable in their own home because the policyholder's life insurance provided the funds that were needed for both mortgage liquidation and living expenses.*
- *A couple is able to enjoy a worry-free retirement because a life insurance or an annuity fund was started years prior, and has made the money the couple needs available to them at the right time.*
- *A young person is able to attend college or vocational school because someone made the timely purchase of a policy designed to provide the necessary funding in the event of the premature death of the family provider.*
- *The physical assets of a business are destroyed by fire or other peril but are quickly replaced, and people are soon put back to work earning their incomes because insurance against the occurrence of such an event was secured.*
- *The financial ruin of a policyowner is averted because he or she had adequate insurance to cover an automobile accident for which he or she was legally responsible.*

Considering how important insurance is and how it benefits our lives, it's surprising how many people do not understand even the fundamentals of insurance. Given that some consumers remain ignorant about insurance, it's possible for unscrupulous agents to take advantage of these people by inducing them to buy policies that are unnecessary or do not live up to the promised benefits.

Many consumers feel that insurance is one area in which a wrong purchase is easy to make. The terminology is confusing, and the conditions and exclusions seem complicated. Furthermore, it may not always appear that the agent is working in the consumer's best interest.

To combat this perception, the professional insurance agent must offer the public an honest and fair explanation of the policies and services that he or she represents. In addition, the insurance agent has to be dedicated to the principle of needs selling.

This means that the agent must clearly explain policy features and benefits without misleading the consumer or misrepresenting the policy and its benefits. And the professional insurance agent must be ready to back up his or her promises with solid performance and encourage other agents to do the same.

The insurance agent has more influence over the public's attitude toward insurance than sales representatives for most other consumer products. This is because the insurance agent initiates contact with a prospect, determines a prospect's need for insurance, recommends a certain product or solution, makes the sales presentation, and eventually develops a long-term relationship with the client by providing annual coverage reviews and ongoing service. In many cases, the prospect has little or no direct contact with the insurance company.

Because this special relationship involves a great deal of contact between the consumer and agent, the public's perception of the insurance industry are based on how well, or how poorly, an agent does his or her job. Thus, the professional insurance agent has two main ethical responsibilities to the public.

- To inform the public about insurance with the highest level of professional integrity
- To strive for an equally high level of professionalism in all public contacts, in order to maintain a strong, positive image of the industry

E. Producer Responsibilities to Regulators

The responsibility to regulate the insurance industry is shared by the federal and state governments. However, the states carry the burden of regulating insurance affairs, including the ethical conduct of licensed insurance agents. In some states, the regulation of ethical conduct falls under the category of "marketing practices," while other states refer to it in the context of "unfair trade practices."

Whatever it is called, all states have established a code of ethical standards for insurance agents by defining, through laws and regulations, what an agent can and cannot do. Although these laws differ from state to state, there are enough similarities to discuss them in general terms.

The state Insurance Code articulates, in many different ways, the legal and ethical aspects of the client-agent relationship. Fiduciary responsibilities are very high on the list. These responsibilities include the contact an agent has with the money or premiums of insureds, or the advice and recommendations given to others which have implications for their money or financial security.

An insurance agent must practice and demonstrate the highest level of ethics, integrity, and morals. Failures or lapses in any of these areas can result in great financial harm to others. Misrepresentation, twisting, concealment, diverting client money to personal use, commingling client money with general business funds (even if there was no bad intent), and other practices are ethical, integrity, and moral issues that are prohibited in various ways by the Code. Failing to answer, or giving an intentional wrong answer to questions that insureds or prospects ask is also an ethical problem, because it can lead a client to make a choice that might not be in their best interest. Unethical conduct can lead to suspension or loss of license, monetary penalties, and even time in jail or prison.

Agents must make recommendations to clients based on the clients' best interests. An agent should not recommend products or services to a person that he or she would not recommend for himself or herself in the same circumstances. To do so would constitute an ethical dilemma. This is often described as "conflict of interest." The normal conduct of business can present agents with many opportunities for conflicts of interest, especially in the insurance industry.

Agents are typically paid on a commission basis. Commissions are usually calculated on the basis of an "annual" premium submitted, even though the client may have paid just the first monthly installment with their application. For an agent, then, the higher the premium he or she collects, the higher his or her commission check is. If the higher premium and the higher commission are the result of an inappropriate recommendation for the client, that is a conflict of interest and an unethical act.

Ethics demands that others and their families are of primary importance. An agent who demonstrates the highest respect for others will have the most successful career. Agents who neglect this respect for others often have success initially, but they rarely have long-term success. The responsibility for ethical behavior is squarely on the agent.

1. Controlled Business

States limit the amount of “controlled business” that a producer can write. Controlled business is insurance on the agent’s own property or interests, or that of the agent’s family, employer, or any partnership, association, or corporation in which the producer has an interest as an officer, director, stockholder, partner, or employee.

The amount of controlled business that is permitted varies from state-to-state, but a producer cannot earn commission on controlled business in excess of a stated amount (10% to 50% of total compensation) during a calendar year. For example, in the state of Texas, at least 25% of a licensee's total volume of premiums in a calendar year must be from business other than controlled business. Violations may result in license revocation or suspension.

F. Special Ethics Concerns Regarding Senior Citizens

Seniors are among the least likely to report financial crimes or abuses against them because they might be embarrassed at having “been taken,” or because they do not wish to appear to be losing the ability to manage their lives or personal finances. Medicare supplement and long-term care insurance regulations address unethical practices such as inaccurate or misleading comparisons of existing and proposed replacement contracts, selling multiple and unnecessary policies. Annuity suitability regulations address inappropriate sales of annuity contracts to senior consumers. Some states have enacted Financial Elder Abuse statutes, which, in part, specifically address insurance agent abuses of persons age 65 or older. California, Florida, Illinois, Louisiana, North Carolina, Texas, and Washington are some of the states where the financial exploitation of an older person is a criminal offense.

Under most circumstances, insurance institutions, agents, and insurance-support organizations are not allowed to use **pretext interviews** to obtain information that relates to an insurance transaction. However, a pretext interview is acceptable when the purpose is to obtain information from a person or institution that does not have a generally or statutorily-recognized privileged relationship with the person to whom the information relates. Also, it is further required that the reason for the interview must be to investigate a claim where there is a reasonable basis for suspecting criminal activity, fraud, material misrepresentation, or material nondisclosure in connection with a claim.

Specifically **prohibited** are high-pressure tactics and cold lead advertising. High-pressure tactics include any sales presentation that induces a person to purchase insurance through undue pressure, such as fright, threat, or force. Cold lead advertising is a marketing method that fails to disclose that solicitation of an insurance product is occurring and additional contact will be made by an insurance producer or company representative.

NOT A SMALL PROBLEM

From the Wisconsin Department of Insurance (OCI)

- *One insurer that claims to specialize in the sale of annuities holds annual sales contests to increase agent sales but has no written procedures or standards for determining suitability, relying instead on managing general agents and broker-dealers to provide such supervision.*
- *The insurer reported that 61% of its in-force and 74% of annuities issued were to seniors age 65 and above, and 35% of the annuities issued to seniors age 65 and above involved replacement.*
- *Another insurer reported that 76% of new annuities issued were to seniors age 65 and above, and 37% were issued to seniors age 76 and above.*
- *Eight of the insurer's top 10 agents writing annuities sold more than 50% of annuities to seniors age 65 and above, and two agents sold more than 90% to seniors, yet seven of the 10 agents were relatively new agents with less than 3 years of insurance experience.*
- *A review of a sample of 10 of the agent investigations conducted by the office in the last 2 years shows those investigations and enforcement actions resulted in forfeitures totaling $422,550.00, and the revocation of the insurance licenses of eight agents for alleged violations of Wisconsin insurance regulations relating in part to the agent's failure to consider suitability when selling annuities to seniors.*

ENFORCEMENT ACTIONS

An agent repeatedly violated the law by making unsuitable sales of annuities to elderly consumers.

The OCI alleged that the agent:

- *Made false and misleading communications in the marketing of annuities.*
- *Failed to obtain sufficient information from consumers to establish the suitability of the annuities he recommended.*
- *Used methods that endangered the legitimate interests of his customers and the public.*

The agent was ordered to pay restitution to 7 elderly consumers and a $40,000 forfeiture. His license to sell insurance was also revoked.

An agent repeatedly violated the law by making unsuitable sales of annuities to elderly consumers. The agent was also alleged to have

- *Made multiple misrepresentations to consumers, insurers, and the Office of the Commissioner of Insurance (OCI).*
- *Forged signatures.*
- *Used false and misleading advertisements and representations in the sales of annuities.*

The OCI ordered the agent to pay restitution to 40 elderly consumers and pay a $281,000 forfeiture. The OCI also revoked the agent's license to sell insurance.

An agent made an inappropriate sale of an immediate annuity to a 92-year-old woman, causing her to incur surrender penalties when existing products were replaced. The $500,000 annuity provided for a death benefit *of 25% of the initial premium if death occurred within 10 years after purchasing the policy, which would have required the woman to live to be 102 to avoid her beneficiary losing 75% of the funds in the annuity. She died 6 months after purchase, and her estate suffered more than a $300,000* *loss. The agent disputed the allegations, including with respect to suitability, but agreed to a stipulation imposing a forfeiture.*

G. Penalties

1. Interstate Commerce

It is considered **unlawful insurance** fraud for any person engaged in the business of insurance to willfully, and with the intent to deceive, make any oral or written statements that are either false or omit material facts. This includes information and statements made on an application for insurance, renewal of a policy, claims for payment or benefits, premiums paid, or financial condition of an insurer.

If a person transacts insurance in a way that affects interstate commerce and knowingly makes a false material statement/report, alters records with an intention to deceive, or intentionally overvalues any land, property, or security in an attempt to deceive an insurance regulatory official or agency, the person could be fined and/or imprisoned for a period of up to 10 years (or 15 years if the safety or soundness of the insurer was jeopardized).

It is also illegal for those who transact insurance in a way that affects interstate commerce to willfully embezzle, abstract, purloin, or misappropriate any of the moneys, funds, premiums, credits, or other property. The punishment for this offense is a fine or imprisonment for up to 10 years (or 15 years if the safety or soundness of the insurer was jeopardized). If the amount of misappropriated money does not exceed $5,000, the term of imprisonment could be reduced to a 1-year sentence.

2. Prohibited Persons in the Insurance Industry (18 USC 1033)

Federal law makes it illegal for any individual convicted of a crime involving dishonesty, breach of trust or a violation of the Violent Crime Control and Law Enforcement Act of 1994 to work in the business of insurance affecting interstate commerce without receiving written consent from an insurance regulatory official (Director of Insurance, or Commissioner of Insurance) - a **1033 waiver**.

The consent of the official must specify that it is granted for the purpose of 18 U.S.C. 1033. Anyone convicted of a felony involving dishonesty or breach of trust, who also engages in the business of insurance, will be fined, imprisoned for up to 5 years, or both.

Any person who engages in conduct that is in violation of Section 1033 may be subject to civil penalty of not more than **$50,000** for each violation or the amount of compensation the person received as a result of the prohibited conduct — whichever is greater.

H. Agent Errors and Omissions

An insurance agent or broker may wish to obtain professional liability insurance to protect against financial losses that could occur due to his or her negligent acts or actions. This is known as **errors and omissions (E&O)** liability insurance.

Errors and Omissions insurance is written for professionals (such as insurance producers) to provide protection from actions resulting in charges that the professional failed to render reasonable duties or services. While some professional liability insurance coverage is written with a limit of liability on an occurrence basis and the insurance company is required to obtain the insured's consent for any out-of-court settlement, the modern trend is to provide coverage on a claims-made basis and to delete previous requirements for consent of the insured for out-of-court settlements.

Errors and omissions liability contracts are renewable annually and usually written with "per claim" deductibles of at least $500 or $1,000. Such contracts will also usually have either a "limit per claim" or "limit for all claims during the policy period" provision that describes the contract's maximum benefit.

The following are *examples* of acts or omissions that could lead to professional liability claims:

- An agent unintentionally records an answer incorrectly on an application for insurance, concealing the client's actual response to a question regarding qualifying information. Upon investigation of the claim, the insurer discovers the correct information and lawfully rejects the claim and voids the contract on the basis of the incorrect answers in the application, then refunds premiums paid. The E&O policy would pay for the actual claim losses of the agent's client.
- The agent fails to disclose material information about a contract of insurance, such as deductibles, coinsurance, copayments, surrender charges, premium increases, or principal exclusions. Actual demonstrated damages incurred by the agent's client could be covered by the E&O policy.
- The agent tells a client, "I guess I made a mistake," in calculating the original premium quotation when, in fact, the increased premium was due to the client's substandard rating. If an insured later discovers the misrepresentation and decides to cancel the contract, an E&O policy could pay the difference between the actual premiums paid and what the client was originally quoted by the agent as the periodic premium, from the date of the client's discovery of the error.
- The agent leads a client to believe that projected investment results in a variable contract, or that the sales illustration for a contract with nonguaranteed interest, are guaranteed elements of the contract. Actual client losses could be paid for by an E&O policy.
- The agent accepts a check from a client that represents an unscheduled deposit to the cash account in a variable or flexible premium policy, but then fails to send it to the insurer on a timely basis. Actual investment or interest losses could be restored by an E&O policy.

Errors and Omissions insurance does not offer any protection for liabilities that result from a person's criminal acts, such as fiduciary crimes, unfair business or trade practices, or material misrepresentations which result in financial loss or damages to a client.

It must be understood that if any of the previously named liability claims arise out of a criminal conviction, or result in a criminal conviction, the E&O policy will not pay the claim, and the agent or broker will remain personally liable for the client's damages.

Because of the risk of injuring a person as a result of the advice or services rendered (an error) or not rendered (an omission) to that person, E&O insurance is a necessity.

At any time during the sales process, there can be a misunderstanding or misrepresentation that could lead to legal action being taken by the insured. Agents should "**document, document, document**" everything from interviews to phone conversations, or requests for information. The sales interview and the policy delivery are the most common time for E&O situations to occur.

According to Insurance Journal's 2014 Agency E&O Survey, while half of all agencies (50%) indicated they had never had an E&O claim, 31% reported having an E&O claim within the past 5 years. Insurance Journal's Agency E&O Survey for 2014 drew 569 respondents.

Chapter Complete