

Powered by
ExamFX - Online
Training &
Assessment

Select Chapter ▾



Study Chapter Practice Question

Quiz

Ethics Define

Ethics is derived from the Greek words *ethikos*, meaning “moral,” and *ethos*, meaning “character.” By textbook definition, ethics is “a branch of philosophy that deals with the values of human life in a coherent, systematic, and scientific manner.” The Oxford English Dictionary defines ethics as “the department of study concerned with the principles of human duty” and the “rules of conduct recognized in certain associations or departments of human life.”

Ethics is more simply defined as principles of moral conduct. In the insurance industry, the basis of a business relationship is the ethical execution of the terms of the [contract](#). In view of the special agent-client relationship, ethical behavior must encompass the following qualities:

- Honesty
- Integrity
- Fairness
- Fidelity and loyalty
- Compassion
- Personal responsibility and accountability

Though there are moral considerations for employing the highest ethical standards in business dealings, there are also other considerations that reflect on the well-being and reputation of the agent. The most important of these are:

- Social responsibility towards the community at large, including insurers;
- Avoidance of public criticism (this has a direct bearing upon the volume and type of business that can be generated);
- Adherence to government regulations (and [avoidance](#) of government penalties); and
- Minimization of errors and omissions exposures.

The purpose of this course is to provide a foundation of the knowledge and understanding that a producer must possess in order to function ethically in his or her role as an insurance professional.

At times, insurance companies and insurance agents receive negative publicity due to bad professional judgment or poor ethical conduct. News about unethical actions usually attracts far more attention than news about the actions of the legions of insurance producers who perform their daily sales and service tasks in a thoughtful, honest, fair, and ethical manner.

A. Ethical Behavior - The Golden Rule

To a certain extent, ethics is a set of instructions on how to deal with a group and a community on a daily basis. These instructions revolve around a single theme – social behavior that favors the group over the individual. Antisocial behavior usually stems from individual selfishness and greed – characteristics that are against the common good and disrupt overall balance and harmony. Because ethical behavior on the part of the individual historically result in group harmony, communities turned to such ethics as the basis for common law, which in turn became the basis for modern civil and criminal codes of conduct.

You won't find universal agreement among philosophers as to what is ethically right. Immanuel Kant, a German philosopher, believed that what is right is based on pure reason. On the other hand, Jeremy Bentham, an early 19th-century British philosopher, believed *right* to be that which will produce the greatest good.

Ethics is the name we give to our concern for good behavior. We feel an obligation to consider not only our own personal well-being but also that of others and of human society as a whole.

Dr. Albert Schweitzer

Dr. Albert Schweitzer, a French medical missionary and philosopher, applied this idea of “duty beyond the group” to all humanity. He believed that the ultimate goal of ethics is the fullest measure of justice for all. If we were to condense the philosophy of Dr. Schweitzer into three words, those words would be “regard for others.”

The Chinese philosopher Confucius said that ethics is the foundation of peace in a society. He believed that a body politic of “good brothers” living in moral harmony would result in an orderly and peaceful nation. In fact, The Golden Rule originates from Confucius, who said, “What you do not want others to do to you, do not do to others.”

When we discuss ethics, we are not dealing with a set of hard-and-fast rules, but rather with attitudes, ideas, and beliefs. Ethics is really the foundation for a way of life. Ethics presents an individual with a way to live harmoniously with others.

Ethics, like religion, favors the group over the individual. If the individual is completely self-seeking, then the group will most likely suffer. The phrase “Love thy neighbor as thyself” is based in pure ethics because it serves to curtail problematic behavior and foster empathy.

B. The Ethical Balance Sheet

Unfortunately, our society isn't always critical of wrongdoing. For example, many people are impressed with the wealth accumulated by some individuals. Those people may therefore ignore the means by which the individual obtained that wealth.

This tendency to emphasize personal financial gain is a common way that many businesses motivate their employees. Financial gain is often regarded as the primary measure of success. This is not to say that pursuit of financial gain is wrong. However, consider how competitions and incentives to achieve “Top Producer of the Month” have the tendency to spotlight financial achievements while ignoring the winners' professionalism and public service.

When confronted with an agency atmosphere that stresses results by any means, it is important to remember that the ends do not justify the means where ethics is concerned. Shouldn't those who achieved ethical success by serving the needs of their insurers and the public also be honored? An overemphasis on financial rewards

can lead to looking at prospects and clients on the basis of “What can I get from them?” as opposed to “What I can do for them?”

Insurance agents certainly should expect to be adequately rewarded for success, and production figures are vital to the well-being of any agency or insurance company. However, meeting the needs of clients and the public in a proper and ethical manner is no less important.

Ethics does not have to be incompatible with capitalism. “Profit” is not a dirty word. In the long run, good ethics is indeed good business. Hard but fair competition cannot help but benefit the public.

Selling insurance is an aggressive profession with vigorous competition. This competition can be healthy because it encourages insurers to provide better service to the public.

Applying the The Golden Rule to your work does not mean that you should trust others implicitly. You shouldn't let someone else make a sale in the hope that he or she will let you make the next one. If someone asks you to sign a written agreement after telling you what the document contains, ethics would not demand that you blindly sign the document without reading it. Ethics is personal in nature. You have no control over the conduct of others, only over your own.

1. A Word on Rationalizations

There are a variety of reasons why we do not take the actions necessary to maintain the high ethical standards that we would like to have. To make ourselves more comfortable with our actions, we often revert to **rationalizations**, such as

- "I'm just fighting fire with fire."
- "If it is legal, it must be okay."
- "I was just doing it for someone else."
- "We all do it; it's just how you play the game."
- "If it doesn't hurt anyone, it's okay."
- "It's necessary to get the order."
- "Business is business. I'll be as ethical as the competition allows."
- "I deserve this: I have it coming."

Rationalizations make it easier to live with ourselves when we do the things that we want to do, rather than the things that we know we should be doing.

C. Ethics as a Legal Force

Ethics deals with the way things ought to be, which is not necessarily practical in our society. Some people get wrapped up in the differences between what is ethical and what is legal, which are two completely different concepts. Ethics is doing the right thing, while the law represents a set of minimum standards that society demands.

Ethics usually precedes the law. While many ethical standards of conduct have been codified, many have not. As a result, something can be legal while not being ethical. For example, it is legal to sell a prospect more life insurance than he or she can afford, but this is not ethical. Ethics goes beyond the letter of the law and entails not only what a person must do, but also what a person should do.

However, it should be noted that the law does not provide a very specific ethical direction for everyone through civil and criminal statutes. The law sometimes just defines illegal and improper conduct and the penalties for such conduct.

In spite of any crossover between legal and ethical concerns, there is still a distinction between the two. Often, when someone is told that his or her actions are perfectly legal, that person will also assume that those actions were ethically acceptable.

The integrity and honesty of a company's policies are subject to scrutiny by the general public. Public pressure may force a business to revise its practices. All of this means that what is legal but unethical today could become illegal tomorrow, depending on the demand by the community to bring reform.

However, relying on legalities alone can become the easy way out. Paying attention to "have to" rules and regulations at the expense of "choose to" ethical standards can keep the individual out of legal trouble but may eventually taint the person's success. Ethics has more to do with approval from the man or woman in the mirror than it does with approval from one's manager or the insurance company that one represents.

D. Insurance and Industry Ethics

1. Industry Codes of Ethics

The following tenets are derived from the ethical codes of major organizations within the insurance industry:

- Place the customer's interest first
- Know your job and continue to increase your level of competence
- Identify the customer's needs, then recommend products and services that meet those needs
- Accurately and truthfully represent products and services
- Use simple language. Speak the layman's language when possible
- Stay in touch with customers and conduct periodic coverage reviews
- Protect your confidential relationship with your client
- Keep informed of and obey all insurance laws and regulations
- Provide exemplary service to your clients
- Avoid unfair or inaccurate remarks about the competition

THE AMERICAN COLLEGE'S CODE OF ETHICS AND PROCEDURES, INCLUDING THE PROFESSIONAL PLEDGE AND THE 8 CANONS

Professional Pledge

"In all my professional relationships, I pledge myself to the following rule of ethical conduct: I shall, in light of all [conditions](#) surrounding those I serve, which I shall make every conscientious effort to ascertain and understand, render that service which, in the same circumstances, I would apply to myself."

The Canons

- I. Conduct yourself at all times with honor and dignity.*
- II. Avoid practices that would bring dishonor upon your profession or The American College.*
- III. Publicize your achievements in ways that enhance the integrity of your profession.*
- IV. Continue your studies throughout your working life so as to maintain a high level of professional competence.*
- V. Do your utmost to attain a distinguished record of professional service.*

VI. Support the established institutions and organizations concerned with the integrity of your profession.

VII. Participate in building your profession by encouraging and providing appropriate assistance to qualified persons pursuing professional studies.

VIII. Comply with all laws and regulations, particularly as they relate to professional and business activities.

E. The Ethical Bottom Line

History is made and lives are changed not by those who follow the crowd, but by those who are prepared to take the ultimate risk and stand up for what is right. It is always a challenge to do the right thing regardless of any potential costs.

We reinforce our own moral character and influence others. We do not develop that ability overnight. It is developed in small steps as we do the right thing each day.

F. When Unethical Behavior by Insurance Professionals Turns into Fraud

Unethical insurance professionals sometimes commit full-on **fraud**, and that includes insurance producers, underwriters, adjusters, and sometimes even insurance company personnel. These types of frauds include premium theft, false applications, fraudulent placement, and "sliding." Fraud is a crime that is punishable by law.

Public Adjuster Arrested for Felony Embezzlement, Grand Theft, Forgery

LOS ANGELES, Calif. - A 60-year-old San Clemente resident, a former licensed public adjuster, was arrested at his home in San Clemente on multiple felony counts of embezzlement, grand theft, and forgery after allegedly cashing **claim** checks with counterfeit **endorsement** seals and stealing a total of \$400,000 from fire victims in the Los Angeles area.

After receiving multiple complaints from consumers, the California Department of Insurance Investigation Division launched an investigation. Evidence revealed that the licensed public adjuster, doing business as Statewide Claims Advisors, allegedly cashed and deposited multiple claims checks with counterfeit endorsement seals that were issued by insurance companies to fire victims to repair and rebuild their damaged properties.

"These consumers were victimized twice," said California Insurance Commissioner Dave Jones. "Once when their home was damaged by fire and then again when (the adjuster) allegedly forged endorsements on their insurance payments and stole the money intended to rebuild their homes."

The public adjuster solicited fire victims to sign public adjuster contracts allowing him to handle their claims, but instead of forwarding these checks to lenders for endorsements and proper handling, he deposited the checks into his business accounts and diverted the funds for his personal use.

The man refused to release claim funds to many victims who desperately needed to rebuild their homes. He released some funds to contractors, using forged endorsements, and in one case, hired an unlicensed contractor whose work was substandard, which led to a second fire in the home which further victimized the homeowners.

CASE UPDATE: The former licensed public adjuster was convicted of two felony counts of embezzlement, PC 504, grand theft, PC 487 (a), with enhancements of PC186.11(a)(3) and PC 12022.6 (a)(2), and two felony counts of forgery counterfeit seal, PC 472. He was sentenced to seven years in prison. This case was prosecuted by the Los Angeles County District Attorney's office.

Florida: False Applications: License Revoked

In 2016, a Clearwater agent was found to have submitted seven false and fraudulent life insurance applications for the sole purpose of receiving commissions.

An audit undertaken by the issuing insurer determined that the applications were false and that none of the applicants actually existed or desired to purchase the insurance, and premiums were never received. Because the applications were false and material misstatements of fact, the agent was charged with violating Florida Insurance Code prohibiting fraudulent or dishonest practices in the conduct of business under the license. The agent's license was revoked and she is ineligible to reapply for 2 years.

Florida: Fraudulent Placement: License Revoked

In May 2016, a Melbourne agent licensed for life, health and variable insurance as well as a customer service representative was found to have fraudulently represented himself as a general lines agent for the purpose of fraudulently transacting homeowners insurance.

The investigation found that he collected premiums without completing applications, provided false evidence of coverage, and never placed the coverage with an insurer and allowed existing coverage to [lapse](#). These activities are considered unfair or deceptive acts/practices under Florida law, engaging in fraudulent or dishonest practices in the conduct of business under the license or appointment, and misappropriating, converting, or unlawfully withholding moneys belonging to insurers or insureds received in conduct of business under the license. The agent's license was revoked and other disciplinary penalties are under way.

Illinois: Agency Fraudulently Bills Customers

An indictment handed down by an Illinois grand jury charged an Illinois insurance agency with 19 counts of wire [fraud](#) and one count of mail fraud in connection with the principal's alleged fraudulent activity.

The owner obtained bank account information from applicants and used that information to create fictitious checks purportedly issued by the applicants, according to the U.S. Attorney's Office for the Northern District of Illinois. The fake checks were then deposited into bank accounts connected with the agency.

Complaints were filed by former clients with both the Illinois Department of Insurance and the Missouri Department of Insurance. Both regulators have revoked or nonrenewed the agency license based on a pattern of wrongly debiting funds from client accounts. Accounts were allegedly debited even when premiums had already been paid or the policy had been cancelled.

Prosecutors believe the agency defrauded more than 100 former insurance clients out of over \$800,000.

If convicted, the defendant faces a maximum of 20 years in prison and a maximum fine of \$250,000 for each of the 20 counts against him, along with restitution.

Premium Theft – With the Producer’s Help

An investigation led by the Florida Department of Financial Services (DFS) Bureau of Insurance Fraud has led to the arrest of a Miami insurance agent for attempting to evade a higher insurance premium for a client who was operating an assisted living facility (ALF). (Assisted living facilities are long-term care residences that offer various services such as health and medicine management, transportation and meal services in an effort to support seniors and developmentally or physically disabled individuals.)

The insurance agent helped the client submit a fictitious insurance [application](#) in order to fraudulently obtain a less expensive [insurance policy](#).

The two colluded to submit a residential homeowners insurance application for a building that was being used as an assisted living facility. Florida law requires ALFs be covered by a commercial, not residential, policy.

The investigation found the agent knew the property was being used as an ALF and was attempting to help her client obtain a lower premium. As a result, the insurance company lost \$1,536 in underpaid premiums. Worse, any claims submitted on the issued policy would have been denied.

The agent was arrested and charged with insurance fraud, grand theft and organized scheme to defraud. If convicted, she could face up to 15 years in prison. The customer was also arrested and charged with insurance fraud and grand theft. If convicted, he could face up to 10 years in prison.

Source: Florida Department of Financial Services

New York Fraud Bureau

An investigation revealed that for more than three years, a licensed wholesale insurance [broker](#) who had secured a policy for a client had created invoices reflecting inflated premiums and had pocketed \$58,000 in illegal profits. The broker also failed to forward more than \$200,000 in premium payments to the insurer.

An individual who had lost his license in 2002 to transact business with the New York Automobile Insurance Plan (NYAIP) was arrested for submitting more than 2,500 insurance applications to the NYAIP. He placed the new business among 27 insurance companies using the license of a former co-worker (who was unaware of the scheme). The insurers issued 485 checks totaling more than \$1.3 million in commissions and fees in the former co-worker's name; the suspect forged the former co-worker's signature and deposited them in his own account.

Georgia Insurance Agent Charged with 6 Counts of Comp Fraud

The Georgia Department of Insurance has arrested a Floyd County insurance agent on [fraud](#) charges related to the misappropriation of workers compensation insurance premiums.

Department investigators discovered that between 2015 and 2017, the owner of an agency accepted \$20,000 from clients to pay premiums for workers comp

insurance, which he then used for personal transactions instead of forwarding to the insurance company to place coverage.

The agency owner was charged with three counts of insurance fraud for the misappropriation of premiums and three counts of insurance fraud for issuing fraudulent certificates of insurance.

In Georgia, insurance fraud is a felony with a penalty of between 2 to 10 years in prison and/or a fine of up to \$10,000.

“The actions of (this agency owner) have put consumers and business at significant financial risk. We will not tolerate any insurance agent stealing from policyholders,” the Georgia Deputy Insurance Commissioner said in a statement. (*August 2017*)

Sliding

Sliding is when an insurance producer "slips" additional coverages into an [insurance policy](#) without the insured's knowledge. The extra charges are hidden in the total premium. Since the insured is unaware of the coverage, this crime is rarely ever detected.

Celebrity Rip Off

A Southern California insurance agent agreed to plead guilty to three felony mail [fraud](#) charges for bilking high-profile celebrity clients including Tom Hanks and Rita Wilson, as well as Andy Summers of The Police, overcharging and double charging them for property coverage.

The producer created false invoices on agency letterhead for premium payments, inflating them by as much as 600%. The fraud was discovered when Hanks and Wilson asked another insurance [broker](#) to review the policies and the new broker reported that the premiums were extraordinarily high for the coverage provided, and some coverages were duplicated.

Hanks and Wilson filed a civil lawsuit against the agent, who had written business and personal coverage for them for more than 20 years, accusing him of professional [negligence](#), breach of [fiduciary](#) duty, fraudulent [misrepresentation](#) and unjust enrichment.

The producer was sentenced to 27 months in prison and ordered to pay over \$800,000 in restitution. He is also prohibited from working in any job requiring professional licensing or certification without the approval of his probation officer.

Source: U.S. District Court for the Central District of California, 2013

Chapter Complete

© 2020 ExamFX All rights reserved.

[Contact Us](#) | [Privacy Statement](#) | [Terms Of Use](#) | [Terms and Conditions](#)

Study Chapter

Producer's Ethical Responsibilities

A. The Role of Agents/Producers

A **producer** is a legal entity, either human or corporate, that acts on behalf of, or in the place of, its **principal**. In insurance, the producer is the agent, and the principal is the insurer.

In applying the law of agency, as long as any agent/producer is acting within the scope of his/her authority, the acts of that agent/producer are seen as the acts of the insurer.

An agent (or producer) will always be deemed to represent the insurer, not the insured. With regards to an insurance **contract**, any knowledge of the agent is presumed to be knowledge of the insurer. **If the agent is working within the conditions of his/her contract, the company is fully responsible for the agent's actions.**

The agent is responsible to the insurer when completing applications for insurance, submitting the application to the insurer for underwriting, and, a policy is issued, delivering the policy to the **policyowner** and explaining the contract. Also, if the insured submits payment to the agent, it is the same as submitting a payment to the insurer.

Agents legally represent the insurer, not their clients. In other words, all of an agent's actions are considered to be made on behalf of the insurer, not the insured. In the case of brokers, however, this is reversed. **Brokers legally represent their clients**, not insurance companies. They negotiate contracts of insurance on their clients' behalf.

The broker represents, and is expected to act in the best interests of the client, not those of the insurance company. Although a broker could receive compensation from an insurance company for a transaction, typically the broker receives a fee for his or her services directly from the client. It could be unethical for a broker to accept both a fee from the client and a commission from the insurer.

1. Brokers vs. Agents

An insurance **broker** is a person who places business with more than one company and has no exclusive **contract** requiring that his or her business first be offered to a single company. Legally, a broker obtains insurance for anyone who requests him or her to do so. The insurance broker is an agent of the **applicant** and represents that applicant. "Broker" and "brokerage" are not interchangeable terms. In insurance, **brokerage** is often used to describe business placed by persons who are not regular members of the insurers agency force.

A full-time career agent of one insurer may also have a broker's license and submit occasional applications to a second insurer. This can happen when coverage is available through the second insurer that is not offered by the first.

Any life insurance agent may represent the insurer for some purposes and the applicant for others. This occurs frequently in the brokerage business.

There is an exception to the general rule that an insurance broker represents the client. This occurs when an insurer gives a policy to a broker for delivery to an insured. During the delivery process, the broker becomes the agent of the insurer. Should collection of premium be involved, payment to the broker would be considered as payment to the insurance company.

The insurance broker represents the buyer of insurance in most parts of the insurance transaction and, therefore, owes all of the duties of an agency relationship to the client. However, even though a broker technically represents the clients, the ethical and **fiduciary** standards that apply to an agent also apply to a broker.

For example, a broker has the duty to fully disclose all information that he or she has regarding an application for insurance. A broker is expected to carry out his or her actions with utmost skill and care. A broker should seek quality business and provide prompt, exacting service. A broker must compete fairly and ethically, relying on his or her abilities, and must not operate at the expense of other agents.

Actually, it makes little difference whether an individual represents one insurer or works with a number of insurers. The ethics and fiduciary standards are virtually identical.

2. Agent's Licensing Relationships

An insurance agent must first establish a licensing relationship with the state or states within which the agent wishes to conduct business. This requires meeting educational standards and passing required tests for the type of insurance which will be sold. This licensing relationship is separate from, and can exist without, any agent/insurer relationship being established.

The **independent agent** has contracts with more than one insurer. Ideally, this places the agent in an enhanced position to offer clients a wide range of product options.

When the time to renew a policy comes, the independent agent is said to **own the renewal or own the expiration**. This means that the independent agent can move the client to a different insurer for the renewal. This would best be done only if it is to the client's advantage. An ethical challenge facing the independent agent is to avoid moving clients simply to generate new or higher commissions.

The **exclusive or captive or career agent** chooses to have a contract with one company. An agent may choose to do this when he or she finds the insurer's products to be of extraordinary quality and applicability and feels no need to have other insurer relationships. An agent might also make this choice because the insurer only allows its products to be sold through its exclusive agents.

The opportunity an agent may have to represent multiple insurers can be in the best interest of the client. But it can also lead to conflicts of interest, especially if a decision to place business with a particular company is made on the basis of which company is offering the best "perks" to its agents. Incentives such as commission bonuses, trips, computers, or other sales-based contests all present opportunities to do what's right for the agent instead of what's right for the client.

Consider this question in different scenarios: *Is it ethical for an insurance agent to do any of the following?*

- Obtain a list of prospects from individuals who registered for a new home in a supermarket drawing?
- Call himself or herself a financial planner or an estate planning specialist without the proper training, experience, or qualifications?
- Show a prospect a policy illustration without explaining the difference between guaranteed and nonguaranteed benefits?

The answer to all of these questions is, of course, "NO." None of these situations shows acceptable ethical behavior by an insurance agent. No matter how extreme these examples might seem, they represent ethical responsibilities that an insurance agent is expected to fulfill. An agent has ethical responsibilities to 4 parties:

1. Insurer
2. Insured
3. Public
4. Regulators

Likewise, the insurer has ethical responsibilities to 4 parties: the agent, the insured, the public, and the regulators.

3. The Role of an Agent – Inside Perspective

The Role of an Agent

Someone asked me recently: "What is the role of an agent?" Although I have been doing what I do for a living for 31 years, it is not easy describing what it is that I do. So for starters, I will select certain words and then come up with a brief description of those words. Hopefully, this will help define what I do.

The One Who Asks Questions
I need to be willing, able and committed to ask my prospects and clients several times the tough questions that no one else is asking them. Through "kid glove" questioning, I learn about their plans, hopes, dreams, goals, relationships, finances, health, fears, hates, loves and their lives yesterday, today and tomorrow.

Thinker
I think a lot about my clients and how I might make their lives better. I need to think on my feet and to think all the time about how to help them do the right thing before the wrong time.

Planner
I am responsible for how I spend every minute of my day, working with clients and taking care of their needs. When I do this correctly and

ethically, they will take care of my needs (I will get a check someday). From this check, I can first pay the people who work with me to help my clients, the government (taxes) and finally the home front. I plan my clients' future by helping them save money and cover their financial risks. I plan my staff's future by going to work yet another day and keeping them employed, and I plan my future and that of my family by the amount of investment I put in my work.

Solution finder
I examine my clients' needs against available options, plans, costs and benefits to help make sure their money lasts longer than they do.

Negotiator
I discuss and negotiate the different opinions of spouses, underwriters and company personnel. I also negotiate with my clients when I know that one financial strategy might work better than another (e.g., investing for the long term even in a challenging market) and help them think logically instead of emotionally.

Deliverer
I deliver information, education and written plans that address the goals and dreams of my clients.

Minister
I am there to console and answer my client's one tough question: "Will I be OK?" I am there with the families and am sometimes considered part of them. I am called to the hospital before the real minister is called, and I show up weeks and months later to help wipe away yet more tears for those still grieving the loss of a loved one. I get to deliver hope, which is founded on faith.

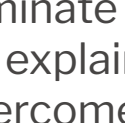
Business owner
I am a human resource director, architect, general contractor, accountant, market analyzer, compliance officer and purchasing agent.

Upstanding citizen
I am a social director, committee member, fund-raiser, coach, president, volunteer, donor, hard worker and someone who is giving, friendly, truthful, ethical and honest.

The next time someone asks you what you do, mention the numerous tasks I have described in this article—they will help demonstrate our multifaceted role and the valuable services we provide to our clients. □

—Elsie J. Fleming, CLU

Reprinted with permission from The National Association of Insurance and Financial Advisors.



B. Producer's Responsibilities to the Insurer

The duties of an insurance agent to his or her insurer are established by the concept of **agency**. This concept is tangibly represented by the agency **contract**, which both parties agree to and sign. Within the scope of that contract, the insurance agent owes it to his or her insurer to behave according to the principles of honesty, good faith, fair dealing, and loyalty. To that end, the agent is obligated to reveal to the insurer all material facts concerning the applicants and the agency.

In carrying out his or her duties, the insurance agent **represents the insurer**. The agent's day-to-day activities reflect on the insurer. If the agent behaves unethically, it is natural for the community to believe that the insurer is also unethical.

1. Fiduciary Duty

A **fiduciary** is someone in a position of trust. The term fiduciary describes both the responsibility inherent in handling another person's financial affairs, and the individual holding such responsibility. Insurance licensees commonly act as a "conduit," receiving and transferring funds from client to insurer, and, eventually, from insurer to client.

An agent's **fiduciary** responsibilities extend not just to the insured but also to the insurance company. An insurer places a great deal of trust and confidence in its agents. Consequently, an agent must exercise a corresponding high degree of fairness and good faith by acting in the best interests of the insurer.

Through his or her appointment, an insurance agent is generally given the power and express authority to act for the insurer by

1. Soliciting applications for coverage
2. Describing coverage and policies to prospects and applicants and explaining how the policies can be purchased
3. Collecting premiums (or in some cases, only initial premiums)
4. Providing service to prospects and the insurer's policyholders

The primary ethical responsibility that an agent owes to the insurer is loyalty. This means that he or she must act in the insurer's best interest in every matter involving the insurer's business. By extension, an agent cannot act for himself or herself if his/her personal objectives run counter to the insurer's interest.

For instance, although it is common for independent insurance agents and brokers to represent several insurers with the full knowledge and consent of the other insurers, in many agency relationships, the agent cannot represent competing principals unless he/she is specifically authorized to do so.

An agent is also charged with conforming to the limits of his or her authority and staying within the guidelines of the agency **contract**.

2. Handling of Premiums

Most agents are authorized to collect initial premiums from applicants. Some are also allowed to collect renewal premiums. By law, payment to an agent is considered to be payment to the insurer. The agent has the **fiduciary** duty to account for all funds that he or she receives in connection with the insurer's business and to turn over these funds promptly. Even if there is no legal intent, it is unethical to delay or withhold premium payments. In many states, it is illegal to combine premium monies with personal funds. It is rarely ethical to do so anyway, regardless of whether a specific law exists.

3. Care and Skill

An agent has a duty to carry out his or her actions with utmost care and skill. As the insurer's authorized agent, the agent represents the company to the public and must act accordingly. In some cases, this means that the agent must refer the business to others who are more qualified if the agent is not qualified to handle the situation.

4. Full Disclosure

An agent is obligated to fully disclose all information that may affect the insurer and its ability to conduct business. Practically speaking, **full disclosure** is most important during the **application** and claims-handling processes. An agent must complete all application and claim forms as accurately as possible. Failure to do so could lead the insurer to follow a course of action that it would not otherwise take, such as issuing a policy to an applicant whose bad health was concealed.

Therefore, it is the agent's or broker's responsibility to see that the answers to questions on the application are recorded fully and accurately. Anything less than full disclosure may prompt the insurer to act in a way that is contrary to its own interest.

5. Prompt Action and Follow-Up

An agent has the obligation to act promptly in all matters regarding the insurer's business, but most significant is the responsibility to transmit completed applications and notice of premium receipts as quickly as possible. The insurer cannot begin the process of issuing insurance until it receives an application. Unless the **applicant** has been given a binding receipt, he or she remains at risk until the policy is issued. On the other hand, if an applicant is given a binding receipt at the time of application, the insurer is obligated to provide coverage, until and unless the applicant is formally rejected. In either event, if an agent fails to turn over an application or notice of premium receipt promptly, the applicant or the insurer may be in jeopardy.

6. Avoiding Conflicts of Interest

Ethically, an insurance agent who has signed an exclusive **contract** with his or her insurer cannot serve two principals at the same time. As a "captive" agent, he or she owes a singular loyalty to that insurer. It would be unethical for that agent to represent two insurance companies selling the same policies. In addition, an agent has the ethical obligation to inform his or her company about any other related services that he or she provides and receives payment for. For example, an agent who does part-time preparation and filing or who serves as a **consultant** to a local business, should inform his or her company of this activity. The insurer can then determine if there is a conflict of interest.

Independent agents also face this issue when they attempt to serve their clients while being contracted to an insurer. Conflicts can be avoided if **independent agents** follow these guidelines for dual-agency:

- The agent represents the insurance company when insurance is being applied for and when it is in the process of being underwritten, in recordkeeping and in **claim** settlement or other insurer-related activities.
- The agent "represents" his or her client through the process of helping the client select the insurance plan best suited to the client's needs.

7. Careful Solicitation

An agent has the ethical duty to protect the insurer's interest by soliciting business that appears to be good and profitable for the insurer. At some point, every agent will submit an **application** that is rejected or will write business that quickly lapses, but the obligation to exercise reasonable care in soliciting quality business is constant.

At the same time, once an agent has taken an application, he or she has the duty to submit it, even if it appears that the **applicant** may be a poor or uninsurable risk. Whether or not an individual is issued coverage is a decision for the insurer's underwriters.

8. Competitive Integrity

The insurance industry is highly competitive. For an agent, there exists ample opportunity to conduct business inappropriately at the expense of a competitor. Misrepresentation or **defamation** of a competitor casts a dark reflection on the entire industry. As a duty to his or her insurer and to the industry itself, an agent must resist this temptation. Ethics requires that an agent acknowledge the worth of other agents and their policies and compete only on the basis of the value of the products and service that he or she can provide.

9. Field Underwriting

Underwriting is the risk selection and classification process. It involves the careful analysis of many different factors to determine the acceptability of applicants for insurance. In other words, underwriting is the process in which an insurance company determines whether or not a particular applicant is insurable, and if so, what premium to charge.

The agent is the company's front-line. He or she is often referred to as a **field underwriter** because the agent is usually the one that has solicited the potential insured. As a field underwriter, the agent has many important responsibilities, including the following:

- Helping prevent adverse selection
- Properly soliciting applicants
- Completing the **application**
- Obtaining the required signatures
- Collecting the initial premium and issuing the receipt, if applicable
- Delivering the policy

Pre-Selection: The agent or **broker** accomplishes good pre-selection through a complete, accurate and thorough completion of the insurance application. The application will ask for all of the legally allowed information which an insurer may gather in order to do effective **post-selection** underwriting.

During the application process, the agent is in a position to terminate the process at any time if he/she finds that the client poses an untenable risk to the insurance company or if he/she wishes to explain to the clients why their risk may be higher than normal. Warning clients of a possible premium rating can help them overcome "sticker shock" later.

For example, if an applicant for life insurance is morbidly obese, the application could still be submitted, but the agent could warn the applicant that because of the applicant's condition, the insurer may charge a higher premium. The same applies to smokers, extreme sports enthusiasts, pilots, skin divers, and other applicants who may present a similar type of risk.

The producer is not allowed to collect information which is not asked for on the application, but may seek details for the questions that do appear. These details can include extent of involvement in hazardous activities, specifics regarding employment duties, etc. It is also necessary to emphasize the responsibility of the producer to not withhold any information which may be negative in regard to the client's risk.

Chapter Complete

Need Help

Powered by
ExamFX - Online
Training &
Assessment

Select Chapter ▼



Study Chapter Practice Question

Quiz

Producer's Responsibilities to the Insured

Some people believe that an insurance agent's greatest single obligation is to his or her policyowners. But if you're an agent of the insurer, how can this be? How can an insurance sales representative serve the best interests of both the insurer and policyowner? The answer lies in knowing that these interests are not really in conflict. By promoting the concepts that insurers stand for and selling the appropriate products in a competent, professional manner, the agent meets the needs of both the insurer and the insured. In this section, we discuss how agents can fulfill their ethical responsibilities to policyowners through needs selling and quality service.

The following are the duties of an agent to his or her client:

- Provide adequate coverage
- Provide proper legal notification
- Place business on the best possible terms for the client
- Investigate carrier stability
- Give correct coverage options related to the insurance
- Other duties as determined by the courts

The agent is legally obligated to perform his or her duties in an ethical manner. An insurance agent who agrees to obtain coverage for a client is obligated to exercise the same degree of care as would be expected from a reasonable, prudent, and competent professional in the field. This responsibility is referred to as the agent's **fiduciary responsibility**.

A. Fiduciary Duty

If **fiduciary** funds are received by a licensed producer, he or she must

- Remit and return premiums received to the insurer (minus commissions due)
- Maintain fiduciary funds at all times in a trustee bank account separate from any other accounts, in an amount at least equal to the premium
- Return premiums that are received by the producer and/or unpaid to the person entitled to those funds

The responsibility of the licensee is to **transfer** the funds to the appropriate party as soon as practicable. If authorized through the written agreement of all involved parties, the licensee may place the funds in U.S. government instruments, certificates of deposit, or government bonds which meet specified guidelines until such time as they are to be transferred. Any losses resulting from such investments are the responsibility of the licensee. Such losses in no way reduce the amount of funds they must transfer.

PENALTY BOX

Commingling is something agents get in trouble for all the time. Here is a recent listing of actions for which producers may be penalized.

- *Misappropriating or converting money belonging to an insurer or insured*
- *Failing to deposit premiums in a designated premium account*
- *Failing to promptly forward refunds to applicants*
- *Failing to submit applications and premiums promptly to the insurer*
- *Agent license was revoked and ordered to pay \$5,000 fine plus \$10,000 restitution for failing to submit applications to the insurer and converting premiums to his own use*
- *Taking an application, failing to submit it to the insurer, and failing to inform the insured that no coverage was in effect.*

A licensee with the authority to **transfer** the funds to the appropriate party is usually a **managing general agent** whose **fiduciary** capacity includes

- Having a written management **contract** and an appointment with one or more admitted insurers that cover a substantial portion of the insurance business in the state
- Managing transactions of either all or some classes of insurance for those insurers
- Appointing, supervising, and terminating the appointments of local agents
- Accepting and declining risks
- Collecting premium funds from producing broker-agents and remitting the funds to the insurers

PENALTY BOX

Insurance Commissioner Announces Sentencing of Insurance Agent for Fraud

Agent misappropriated \$400,000 in premiums for personal use

*Licensed agent X, 54, of Bakersfield was sentenced to one year in jail for each of three felony counts of **fraud** he was charged with in Kern County Superior Court. X was immediately remanded to the Kern County Sheriff where his sentence has begun, and where his remaining time will be served concurrently in the Kern County Jail. X was also sentenced to three years felony probation and ordered to make restitution to 21 of his victims in an amount to be determined by the probation department.*

"This agent's egregious behavior put his clients at great financial risk," said Commissioner Jones. "His deceit and disregard for his policyholders could have led to tragic results."

X's conviction and sentencing resulted from an investigation conducted by the California Department of Insurance (CDI), Investigation Division, Valencia Regional Office. According to investigators, as the owner of X Insurance Agency, X accepted over \$400,000 from his clients to pay premiums for homeowners insurance, commercial liability insurance and performance (construction) bonds. Instead of paying the premiums on behalf of his clients, he misappropriated the premiums for his own personal use.

X failed to place coverage with insurers and knowingly prepared fraudulent Certificates of Insurance, leading his clients to believe that coverage was in place. Unbeknownst to numerous commercial clients, X also knowingly obtained fraudulent performance bonds from a bogus off-shore surety company, thereby exposing his clients and numerous governmental agencies to uninsured losses.

As a result of the CDI investigation, the Department issued an Order of Immediate Suspension, which prohibited X from conducting any type of business related to

insurance, including the collection of premiums. X also surrendered his insurance license.

B. Professionalism

Producers are required to perform in a professional manner at all times.

Professionalism can be defined as a person in an occupation requiring an advanced level of training, knowledge, or skill.

Being professional means placing the public's interest above your own in all situations. Any deviation could result in a penalty.

A professional agent can meet his or her ethical responsibilities to an insured or **policyowner** by fulfilling the customer's needs and providing quality service. Service is a primary function of the insurance industry. The way that service is provided often determines the agent's future, since clients are a good source for future sales and references.

In addition to quality service, the agent owes the policyowner the same degree of loyalty that he or she provides to the insurer. The agent is also responsible for ethical behavior regarding full **disclosure**, confidentiality, the timely submission of all applications, and prompt policy delivery.

C. Suitability and Needs-Based Selling

An insurance agent has one principal reason for calling on a prospect: to offer a product or service that will benefit the prospect in some way. An agent must sell the kinds of policies that will best fit the prospect's needs in amounts that the prospect can afford to pay. No one profits — not the insurer, not the agent, and especially not the **policyowner** — if an individual is coerced or misled into buying too much insurance or purchasing coverage that doesn't suit that individual's specific needs.

Because of the various uses of insurance products, agents should always assess how well a recommended product will meet the applicant's needs and resources. In other words, agents assess the **suitability** of a product. It is a producer's responsibility to evaluate the consumer's suitability information, which includes

- Age
- Income
- Financial situation and financial experience
- Needs and objectives
- Risk tolerance
- Tax status

Before an individual becomes a policyowner, he or she is a prospect. The transition from prospect to policyowner—and ultimately from policyowner to client—comes when an agent follows two basic rules:

- Make sure the product matches the needs of the client (i.e., determine suitability).
- Provide continued service to the client.

Fortunately, most agents recognize that selling to fit needs is the best approach to the products and services that they represent. They know that specific types of insurance policies are designed to meet specific needs, so matching policies to the appropriate needs produces the maximum benefit to the policyowner. They also know that needs selling involves problem analysis, action planning, product recommendation, and plan implementation. This requires two important commitments on the agent's part.

- A commitment to obtaining and maintaining the knowledge and skills necessary to carry out those tasks
- A commitment to educating the prospect or client about the products and plans that may be implemented

1. Commitment to Knowledge and Skills

The relationship between the professional insurance agent and the **applicant** or **policyowner** is usually built upon the policyowner's trust in the agent's knowledge and skills. The policyowner relies on the agent to provide informed options and trusts that the agent's recommendations for insurance are in the client's best interest.

An agent thus has an obligation to ensure that this trust is justified. This means that an agent has the ethical responsibility to obtain the necessary knowledge and skills needed to evaluate and service the insurance needs of clients. Indeed, the term "professional" implies that the individual possesses knowledge and skill. If the agent feels that he or she is not properly trained to perform the needed service, then another professional should be called in to assist.

An agent must also keep his or her base of knowledge and skills current. To this end, the agent must be committed to a program of continuing professional education. He or she must also stay informed of the latest developments affecting a client's interests. In recent years, there has been an increasing trend toward insurance professionalism. Agents should be competent professionals with a high degree of technical knowledge so that they consistently match a prospect's need with the appropriate solution.

PENALTY BOX: CONTINUING EDUCATION

Staying abreast of new developments in the insurance industry is not just an ethical practice, it is a requirement in every state. The NAIC recommendation is for each producer to complete 24 hours of continuing professional education in each biennial license renewal period, with at least 3 of those hours being in Ethics. (Many but not all states have adopted this standard.)

Failing to complete continuing education can result in penalties and fines including suspension of a producer license.

Texas Enforcement Actions:

Order Number: 110416

Action Taken: Fined \$2,000; Must complete 4 hours of continuing education

Violation: Failed to comply with continuing education requirements

Order Number: 110299

Action Taken: Fined \$2,500; Must complete 4 hours of continuing education

Violation: Failed to comply with continuing education requirements

2. Commitment to Educating the Prospect/Client

Client trust must be earned, nurtured, and constantly reinforced. The agent who remembers this basic rule is the agent who communicates to his or her client the reasons he or she is recommending a particular **insurance policy** or program and how it will serve the client.

Individuals who understand what a particular insurance plan or policy will do for them are more likely to buy, more likely to be satisfied with their insurance, and more likely to keep their business on the books. This communication and education continues

long after the particular policy or program is sold and becomes part of the overall insurance program designed for that client. As noted earlier, the professional agent has established his or her clients insurance program based on needs. These needs should be reviewed annually and supported by explanation and communication of the programs put in place to meet those needs.

Chapter Complete

© 2020 ExamFX All rights reserved.

[Contact Us](#) | [Privacy Statement](#) | [Terms Of Use](#) |
[Terms and Conditions](#)

Study Chapter

Sales Practices and Sales Presentations

Producers are subject to the same rules for fair advertising practices as insurance companies, but these days just about every advertisement used by a producer needs to be approved first by the home office marketing department, so those requirements are discussed later.

However, the actual sales presentation given by the producer is also heavily regulated. Deceptive sales presentations have probably generated more complaints of unethical agent behavior than any other activity.

What constitutes a deceptive sale? Any presentation that gives a prospect or client the wrong impression about an [insurance policy](#) or plan is deceptive. Any presentation that does not provide complete [disclosure](#) to a prospect or client is deceptive. Any presentation that includes misleading or inconclusive product comparisons is deceptive. Even if the deception is unintentional, the agent has done the consumer a great disservice.

Deceptive sales presentations can be blatant. *For example*, if a producer makes a comparison of a term policy and a whole life policy that is based only on premium rates without disclosing that one type of policy builds cash value and the other does not, this comparison is obviously misleading and incomplete. But deception does not have to be so apparent to be unethical.

What if a producer describes a personal life insurance policy as a “tax shelter,” but he/she fails to mention that premiums are not [deductible](#) and that surrendered cash values may be subject to tax? What if the producer recommends a certain kind of health policy, but he/she does not explain the [conditions](#) under which the policy could be canceled or the premiums could be increased? While any of these ploys might help make the sale, they are all misleading and unethical.

Of all the concerns surrounding the marketing and the sales of life insurance, none resonate so loudly as those over the use and misuse of policy illustrations. Insurance policies have changed over the years and emphasized the growth, return, and investment aspects of permanent plans, the “unbundling” of a policy’s accumulation and protection elements, and the flexibility of premium payments. As these changes occurred, insurers and agents discovered that one of the best ways to demonstrate the complex mechanics of a policy was through the use of the computerized policy illustration.

Unfortunately, these illustrations have also been used to “predict” a policy’s potential and its future performance based on assumptions that may or may not be realized. Vanishing premiums, huge cash values, in-force lifetime benefits — all of these things have been extolled to sell a life insurance policy, without the explanation that they are based on nonguaranteed numbers projected into the future. Consumers who have seen these illustrations often did not understand the values they were being shown would materialize only if the underlying assumptions came true.

The negative consequences of illustration-based selling became apparent in the early 1990s. Individuals who purchased life insurance policies in the mid-1980s (when interest rates were high) with the expectation that they would pay premiums for only seven or eight years then found out that their policy’s accumulated values were sufficient to “vanish” but were charged against the policy’s value. Others bought plans believing that premiums of a few hundred dollars a year would produce values of a million dollars by the time they were ready to retire. These individuals then discovered that they were far from their goals.

Consumer groups, politicians, and journalists declared that life insurance buyers were misled by policy illustrations that did not distinguish between guaranteed and nonguaranteed benefits. For some agents and companies, the allegations led to lawsuits. Regulators responded with stricter requirements for how policy illustrations may be used in the sales process.

The bottom line is the agent has an ethical obligation to let his client have any information that can directly affect the client’s possible welfare. If the agent has access to information that may help the client to make a more educated decision, it is the agent’s duty to disclose that information to the client.

A. Ethical Responsibilities at Policy Application

In securing coverage for a client, the producer’s main responsibilities are to adhere to all ethical obligations the producer has to the insurer and to see that the prospect completes the [application](#) accurately and completely.

The insurer is relying upon the agent for full [disclosure](#) of all pertinent information regarding the applicant. However, the agent also has an ethical responsibility to educate the prospective insured to make sure that he or she fully understands the nature of the application process. This includes making sure the applicant understands

- Why the information is required
- How it will be evaluated
- The need for accuracy and honesty in answering all questions
- The meaning of terms such as “waiver of premium,” “automatic premium loan,” “nonforfeiture options,” and “conditional receipt”

1. Conditional Receipt

Because the conditional receipt is occasionally a source of misunderstanding with applicants, let’s clarify what it is and how insurance agents should explain it.

A **conditional receipt** is normally given when the applicant pays the initial premium at the time the [application](#) for a policy is signed. This means that the applicant and the company have formed what might be called a “conditional [contract](#),” which is a contract contingent upon [conditions](#) that existed at the time of application or when a later medical examination is completed. In other words, a conditional receipt provides that the applicant is covered immediately from the date of application, as long as he or she passes the insurer’s underwriting requirements. If a medical examination is subsequently required, the coverage is effective once the applicant passes the medical examination.

This information regarding the conditional receipt should be made clear to the applicant. Many applicants accustomed to homeowners or automobile insurance — where coverage is available immediately upon issuance of the binding receipt — assume that their life insurance coverage is also effective upon submitting the application and premium. It is your ethical responsibility to explain that the applicant is covered on the condition that he or she proves to be insurable (and passes the medical exam, if required).

2. The Importance of the Application

All of the information submitted on an insurance [application](#) has a direct bearing on whether the policy will be issued as requested, whether the application will be rejected, or whether another policy will be offered by the insurer. An agent who knowingly or unknowingly fails to provide all the necessary information about a prospect is not serving anyone’s best interest.

Consider the following scenario: Imagine that you visit a prospective client in his home. You ask if he has any dangerous hobbies, and he says that his most dangerous activity is serving as an armchair quarterback for his favorite football team. As your client is filling out the application, you notice a picture on the wall that shows your client with a group of people on a mountain hiking expedition. When you mention this, your client remarks that he climbs mountains as a hobby, and leads rock climbing expeditions to Mount Everest. This is definitely more dangerous than serving as an armchair quarterback.

You are afraid that your client will not be issued an affordable policy if this detail is mentioned, so you advise him to omit it from the application. The policy is later issued.

But what happens if, a year later, the insured is killed in a mountain-climbing accident? It’s quite likely that the insurer will contest or deny the [claim](#) by citing [concealment](#). Rather than getting the policy proceeds, the family receives a return of premiums paid. What benefit did this policy provide? What kind of service did you render?

This example illustrates why precision and accuracy in completing the application are in the best interest of both the insurer and the prospective insured. It is vital that an agent understands this and explains the need for full [disclosure](#) to each applicant.

On the other hand, the agent must make sure that the submitted application is not only **accurate**, but also **complete**. Incomplete applications may delay the underwriting process, and consequently, policy issue. Any unanswered questions need to be answered before the policy is issued. If the insurer receives incomplete applications, they need to be returned to the applicants for completion. If a policy is issued with questions left unanswered, the [contract](#) will be interpreted as if the insurer waived its right to have an answer to the question. They would be later barred from any right of denying coverage based on any information that the unanswered question might have developed.

3. Replacement

Replacement is defined as the purchase of one [insurance policy](#) to replace another. Replacement can be disadvantageous to consumers, especially in regard to life insurance. Therefore, it is heavily regulated.

Policy replacement can be costly to the policyholder because premiums may be higher, the [applicant](#) may need to re-establish [insurability](#), a new commission must be paid on the sale, and new waiting periods may be imposed for incontestability, pre-existing [conditions](#), suicide, etc. When engaging in a replacement transaction, the agent must comply with additional requirements that include obtaining a signed statement from the applicant and a list of all policies to be replaced. The agent must also adhere to additional recordkeeping and [disclosure](#) requirements. Insurers must maintain a replacement register, and patterns of unnecessary replacements will result in fines and penalties by the state regulators.

Each **producer who initiates** the [application](#) must submit the following to the insurance company with or as part of each application.

- A statement signed by the [applicant](#) as to whether replacement of existing life insurance or annuity is involved in the transaction.
- A signed statement as to whether the producer knows replacement is or may be involved in the transaction.

Duties of the producer:

- Present to the applicant a **Notice Regarding Replacement** that is signed by both the applicant and the producer. A copy must also be left with the applicant.
- Obtain a list of all existing life insurance and/or annuity policies to be replaced, including the policy numbers and the names of all companies being replaced.
- Leave the applicant with either the original or a copy of the written or printed communications used for presentation to the applicant.
- Submit a copy of the replacement notice to the replacing insurance company, along with the application.

Duties of the replacing insurance company:

- Require from the producer a list of the applicant’s life insurance or annuity contracts that are to be replaced and a copy of the replacement notice provided to the applicant.
- Send each existing insurance company a written communication advising each of the proposed replacement within a specified period of time from the date that the application is initially received in the replacing insurance company’s home or regional office.

Replacement Questionnaire

A replacement questionnaire should be employed to help agents determine when replacement is in the client’s best interest. Below are some questions that would be used in a typical replacement questionnaire.

Q1. Will the new life [insurance policy](#) replace an existing life insurance contract?

Q2. If the answer to the above question is ‘yes’, please give details about your current policy.

Policy number: _____ Policy name: _____ Insurer _____

Q3. Did the agent present you with the relevant sales material?

Q4. What kind of insurance is the new policy?

Q5. What is your expected insurance coverage for death benefit?

Q6. Please describe the purpose of adopting a new insurance policy.

Q7. Please describe the source of funds for the new insurance policy.

a) Current earned income

b) Net worth

c) Amount of liquid assets

d) Others _____

Q8. In regards to your decision to replace your insurance policy, how important is the cost of the new insurance policy on a scale of 1 to 5 where 1 is the most important and 5 is the least important?

I have examined my financial objectives including my existing policies and I find the new insurance or annuity contract appropriate to achieving my financial goals.

Signature: _____

Date: _____

PENALTY BOX

Common Producer Violations Related to the Application:

- [Making or permitting a fraudulent statement on an insurance application](#)
- [Misrepresenting the terms of a proposed insurance contract](#)
- [Submitting an application for automobile insurance that contained fraudulent driver information](#)
- [Misrepresenting information pertaining to a driver’s history and auto accidents resulting in lower premiums being charged](#)
- [Falsifying an application in order to avoid a higher rate](#)

B. Explaining the Underwriting Process

Another ethical responsibility that is owed to the [applicant](#) is to briefly explain the underwriting process that the [application](#) will undergo. Although many insurance policies are issued on the basis of the application alone, others require additional information. No prospect should ever be surprised that he or she could be subjected to further underwriting. Therefore, the explanation of the underwriting process should include a description of the checks and balances that apply to underwriting a risk, such as the Medical Information Bureau, the inspection report, and the credit report.

The **Medical Information Bureau (MIB)** serves as a clearinghouse of medical information concerning applicants and helps to disclose cases where an applicant conceals or submits misleading medical information. A life [underwriter](#) can check the MIB for information on an applicant’s past medical history. This possibility should be explained to your applicant when you ask for his/her signature on the MIB form.

An **inspection report** provides details on an applicant’s lifestyle, finances, and [exposure](#) to abnormal hazards. An inspection report is usually ordered on applicants who apply for large amounts of insurance. It’s conceivable that the prospect’s friends and/or employer may be contacted for purposes of an inspection report. The purpose of this report is to provide a picture of an applicant’s general character and mode of living.

A **credit report** is ordered when there is reason to question the applicant’s ability to pay the premiums and to determine whether he or she may be a poor credit risk. Applicants who have questionable credit ratings can cause an insurance company to lose money. Applicants with poor credit standing are likely to allow their policies to [lapse](#) within a short time, perhaps even before a second premium is paid. Again, the purpose of this report should be explained when you ask the applicant to sign the authorization form.

1. Privacy

In the course of qualifying a prospect, completing a financial questionnaire, analyzing needs, or working on an estate or business plan, insurance agents are privy to a client’s personal and financial information. Ethics requires that the agent respect the sensitive nature of this information and keep it confidential. Personal information about a client should never be released without proper approval from the client. The privacy requirements of the Gramm-Leach-Bliley Act require the protection of client’s nonpublic personal information through the use of physical and electronic safeguards.

The Gramm-Leach-Bliley Act stipulates that in general, an insurance company may not disclose nonpublic personal information to a nonaffiliated third party except for the following reasons:

- The insurance company clearly and conspicuously discloses to the consumer in writing that information may be disclosed to a third party.
- The consumer is given the opportunity, before the time that information is initially disclosed, to direct that information not be disclosed to the third party.
- The consumer is given an explanation of how the consumer can exercise a nondisclosure option.

The Gramm-Leach-Bliley Act requires **2 disclosures** to a customer (a consumer who has an ongoing financial relationship with a financial institution):

1. When the customer relationship is established (i.e. a policy is purchased); and
2. Before disclosing protected information.

The customer must also receive an annual privacy disclosure, and have the right to opt out, or choose not to have their private information shared with other parties.

2. Disclosures

Insurance agents have a duty to fully disclose to the insurer all material facts concerning an [applicant](#) or [policyowner](#), or situations involving both. This must be done so as to help the insurer make any decision regarding a particular case. At the same time, an agent has the ethical responsibility of full [disclosure](#) to a prospect or client.

In this context, full disclosure means informing the prospect or client of all facts involving a specific policy or plan, so an informed decision can be made. Full disclosure allows the insurance agent to help the client to do all of the following.

- Select the most appropriate policy to meet his or her needs.
- Understand the basic features of life insurance.
- Evaluate the relative costs of similar plans offered by a competitor.

To assist agents with disclosure, there are published documents available to help the consumer understand the intricacies of a life [insurance policy](#). Many agents use the forms not only as an educational tool, but also to help them in their sales presentations. These forms include the NAIC Buyer’s Guide and Policy Summary.

The NAIC Buyer’s Guide

The Buyer’s Guide was developed by the National Association of Insurance Commissioners (NAIC) as an aid to consumers who are contemplating the purchase of life insurance. Most states require that agents make the Buyer’s Guide (or similar document) available when they solicit insurance sales. This guide explains life insurance in a way that the average consumer can understand. It speaks of the concept in general and does not address the specific product or policy being considered. Included in the Buyer’s Guide is an explanation of the surrender cost indexes used in the Policy Summary.

The Policy Summary includes two types of cost indexes.

1. The life insurance surrender cost index
2. The life insurance net payment cost index

The surrender cost index is useful to applicants who want to compare the death benefits of policies.

The Buyer’s Guide and Policy Summary are especially helpful to agents who want to explain the features and benefits of the life [insurance policy](#) that they are presenting. These forms also provide needed guidelines for the comparison of two or more policies.



Illustrations

The term **illustration** means a presentation or depiction that includes nonguaranteed elements of a policy for individual or group life insurance over a period of years. A life insurance illustration must distinguish between guaranteed and projected amounts.

- **General Rules and Disclosures** — An agent may use only the illustrations of an insurer that have been approved and may not change them in any way.
- **Not Part of Contract** — An illustration must clearly state that it is not a part of the [contract](#).
- **Values Not Guaranteed** — Values that are not guaranteed must be identified as such.

Chapter Complete

Powered by
ExamFX - Online
Training &
Assessment

Select Chapter ▼



Study Chapter

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

© 2020 ExamFX All rights reserved.

[Contact Us](#) | [Privacy Statement](#) | [Terms Of Use](#) |
[Terms and Conditions](#)

Powered by
ExamFX - Online
Training &
Assessment

Select Chapter ▼



Study Chapter Practice Question

Quiz

Insurance Company Responsibilities to the Public and Regulators

A. Role of Insurers

Insurance companies operate with many different departments and divisions. Among them are 4 principal departments responsible for the major functions: Marketing or Sales, Underwriting, Claims, and Actuarial. These departments each have a specific purpose within the structure of an insurer, and each can have an impact — positive or negative — on the profitability of the company.

The **marketing department** is responsible for advertising, promoting, and distributing an insurer's products to the public. This department also sells the products, trains the producers, and develops any materials related to the marketing process. Agents are field representatives of the marketing department, responsible for putting the company's products and services in the hands of clients. Monitoring compliance with the various laws relating to the conduct of agents and the transacting of contracts may also be handled within the marketing department. The marketing department is also responsible for watching consumer trends and then researching and developing or modifying products and services to meet the needs or demands of the marketplace.

The **underwriting department** is responsible for receiving applications for insurance and then evaluating them according to established guidelines. Applications are either approved or declined. Those that are declined do not meet the company's guidelines, but not all approved applicants are equal either. Many present risks that, although the company is willing to insure them, are greater than average risks the company expects to insure. Those particular risky applicants will be classified as **substandard**. There will also be some applicants whose risks are more favorable than average, and those will be classified as **preferred**.

The underwriting department's main objective is to prevent **adverse selection**, which is an imbalance of risks, or the selection of poor risks (in other words, too many substandard risks compared to preferred and standard risks). If the underwriting department approves too many poor risks, the statistical predictions of the actuaries may not hold up, and the company will not have the level of profit it expected, or could even suffer a loss.

The **claims department** is responsible for receiving claim requests, evaluating them in light of the actual contract, paying those claims which are covered by the terms of the contract, and rejecting those which are not. The claims department may employ or contract with adjusters or other investigators to assist in the evaluation of claims, or to seek evidence of false or fraudulent claims. If the claims department does not settle

claims promptly or fairly, or makes payments for claims that are not actually covered by the contract, the profitability of the company can be affected.

The **actuarial department** is where the science of statistics is put into practice. Insurance company actuaries are persons who study mortality and morbidity statistics, the nature of claims and actual claims experience, and even factor in the potential for fraudulent claims and the financial impact of those claims, including investigating fraudulent claims and payments. The actuaries must also account for the ordinary expenses of doing business, including the payment of claims, as well as make a conservative estimate of earnings from invested reserves — premiums received by the company but not currently needed to pay expenses. After all the analyses and calculations have been made, the actuaries publish the rates that must be charged for each line of business the company insures. The intent of their work is to achieve profitability.

1. Insurance Company Responsibilities to the Producer

The relationship between the agent and the principal is a two-way street. The duties of an insurer to the insurance agent are also established under the concept of agency. This concept is tangibly represented by the agency **contract**, which both parties agree to and sign. The principal also owes certain duties to the agent. A rule of agency law is that the principal is responsible for all of an agent's acts when he or she is acting within the scope of his or her authority. This responsibility includes fraudulent acts, omissions, and misrepresentations. Ethical insurance companies provide their producers with:

- Clear compliance directives
- Training and education
- Supervision and oversight of sales activities

A Compliance Procedure Manual should include all of the following.

- *General standards of conduct*
- *Licensing requirements*
- *Product compliance*
- *Training*
- *Advertising rules*
- *Compensation*
- *Underwriting*
- *Claims*
- *Field communications*
- *Complaint handling*
- *Reporting of misconduct*
- *Monitoring and enforcement*

The principal must carefully select honest, loyal, and hard-working agents to protect itself from potential liability. In return, the principal gives the agent all of the following.

- Compensation, or payment, for the business that the agent has given to the principal
- Employment (the principal must specify a reasonable period of time during which the agent is expected to produce a certain amount of business)
- Indemnity (the principal is obligated to reimburse the agent for any damages or expenses incurred in defending against claims that the agent may be held liable for in the course of fulfilling his or her agency obligations)

Agency Agreements should clearly establish

- *Fiduciary expectations*

- *Binding Authority*
- *Premium remittance procedures*
- *Cancellation procedures (if the agency agreement is terminated)*
- *Processing and recordkeeping requirements*
- *Any requirement to carry errors and omissions coverage*
- *Compensation and indemnification arrangements*

2. Insurance Company Responsibilities to the Insured

Fair Sales and Marketing Practices

The potential for deceptive advertising or promotion by companies and agents alike is significant, and the consequences to the consumer can be quite grave. Accordingly, all states have enacted laws regulating insurance advertising. The basis for many of these state statutes is the NAIC's model Unfair Trade Practices Act, which expressly cites false advertising as an unfair trade practice and prohibits it. In this context, the term "advertising" is quite broad. It includes print and radio material, descriptive literature, sales aids, slide shows, prepared group talks, brochures, sales illustrations, policy illustrations, and TV commercials – in short, almost any kind of communication or presentation used to promote the sale of an [insurance policy](#).

The purpose of the NAIC model act is to establish guidelines to ensure that insurance companies and their agents promote their products properly and accurately without exaggerating the benefits or minimizing the drawbacks. Advertising and sales literature must provide full and fair [disclosure](#) of all material information. The act forbids any misrepresentations of the benefits, terms, [conditions](#), or features of any insurance policy, including dividends. The act also bars any misrepresentation of an insurer's financial condition or its [legal reserve](#) system, and it prohibits names or titles of insurance policies that do not represent their true character.

ETHICAL ADVERTISING STANDARDS

- *Advertising may not be obscure, ambiguous, deceptive, or misleading and may not use jargon or terminology that is confusing for a person unfamiliar with insurance coverages.*
- *An advertisement may not imply that an insurer or a policy has been endorsed by an individual or group unless true*
- *Statistical information used in advertisements must be accurate, reflect all material facts, and disclose the source of the data*
- *Advertisements may not use language that exaggerates benefits or fails to disclose policy [exclusions](#) and limitations*
- *Advertisements may not mislead the public with regard to the purpose of the policy, benefits included (for example a life policy where the primary purpose is providing a [death benefit](#) may not be characterized as an investment product with returns).*
- *Life insurance advertising may not imply that policy dividends are guaranteed*
- *Testimonials must be applicable to the policy being advertised and must disclose whether the person giving the testimonial is being paid or otherwise compensated.*

Some states have enacted regulations that separately address life insurance and health insurance advertising. Life insurance advertising, for instance, cannot use the terms "investment," "savings," or "profit" in a misleading way. Health insurance advertising must disclose provisions regarding renewability, cancellability, termination, or modification of benefits.

Generally speaking, the burden of complying with state insurance advertising law rests on insurance companies because most advertisements or promotional pieces,

regardless of the writer or presenter, are considered to be the responsibility of the insurer whose policies are being advertised. In practice, most of the advertising and sales literature that an agent uses is prepared by the insurer under the careful eye of its legal staff. For an agent, then, the ethical issue isn't necessarily the material itself but instead how the material is used and the deceptive sales presentation that may result.

SOCIAL MEDIA AND ADVERTISING

A newly emerging area of concern is the use of social media sites such as LinkedIn and Facebook to make the public aware of insurance products and services. The absence of specific regulations around such communications does not mean they are unregulated.

Insurance rules that are generally believed to apply to social media include

- *Advertising rules*
- *Record Retention*
- *Licensing and jurisdiction*
- *Complaint records*
- *Compensation and referrals*

Regulators hold the insurer responsible for supervision of communications posted to social media sites, including those posted by representatives and employees. Because the dynamic content of Internet postings is so difficult to control and retain, many insurance companies have resorted to a "ban" on such activities. Companies and producers must identify applicable regulatory and compliance issues and establish policies for both the business and personal uses of social media.

In New York, the use of a Linked-In profile page or a similar website for the promotion of insurance, insurers, insurance agents, or brokers constitutes an advertisement, announcement, or statement under the New York Insurance Law. OGC Opinion No. 10-11-07.

Regulators in New Jersey have begun asking companies about their policies, training, monitoring, and timely communications with consumers. Regulators are looking at consumer complaints to detect patterns of noncompliance.

Privacy

The collection of nonpublic personal financial information about individuals (both customers and consumers) requires the insurer to do all of the following.

- Provide notice to individuals about the insurer's privacy policies and practices by no later than the time an **insurance policy** is delivered and at least annually afterwards. If information about individuals is collected from a source other than the **applicant** or public records, notice must be given to the individuals at the time the information is collected.
- Describe the **conditions** under which a licensee may disclose nonpublic personal financial information about individuals to affiliates and nonaffiliated third parties. If the insured requests or authorizes a transaction in connection with servicing, processing, or maintaining an insurance product, the insurer is exempt from the requirements of **disclosure**.
- Provide methods for individuals to prevent a licensee from disclosing such nonpublic personal financial information. An **opt-out notice** must be provided to allow the consumer a choice to limit disclosure of personal information.

For health insurance, the insured's identity, financial information, and medical information may not be disclosed except as necessary to conduct the transaction,

unless permitted or required by law. All parties to the transaction must comply with privacy protections required by federal law. If the laws of the state provide for greater confidentiality than public health law requires, the regulations of the state govern.

Under the Privacy Rule for the Health Insurance Portability and Accountability Act (HIPAA), protected information includes all "*individually identifiable health information*" held or transmitted by a covered entity or its business associate, in any form or media, whether electronic, paper, or oral. This is called **protected health information**. *Individually identifiable health information* includes demographic data that relates to past, present, or future physical and/or mental health or condition(s), or payment information that could easily identify the individual. A covered entity must obtain the individual's written authorization to disclose information that is not for treatment, payment, or health care operations.

Unfair Trade Practices

The Unfair Trade Practices Act has been adopted by every state and includes both Unfair Marketing Practices and Unfair Claims Practices. In each state, statutes prohibit the following practices.

- **Misrepresentation** — It is illegal to issue, publish, or circulate any illustration or sales material that is false, misleading, or deceptive as to policy benefits or terms, the payment of dividends, etc. This also refers to oral statements.
- **Boycott, Coercion, or Intimidation** — It is illegal to be involved in any activity of boycott, coercion, or intimidation that is intended to restrict fair trade or to create a monopoly.
- **Defamation** — This occurs when an oral or written statement is made that is intended to injure a person engaged in the insurance business. This also applies to statements that are maliciously critical of the *financial condition* of any person or company.
- **Discrimination** — It is illegal to discriminate in rates, premiums, or policy benefits for persons within the same class or with the same life expectancy is illegal. No discrimination may be made on the basis of marital status of an individual, race, color, national origin, creed, or ancestry unless the distinction is made for a business purpose or required by law.
- **False or Deceptive Advertising** — Advertisements cannot include any untrue, deceptive, or misleading statements that apply to the business of insurance or anyone who conducts it. The violation of this rule is called false advertising.
- **False Financial Statements** — It is illegal to make any financial statements that are intended to deceive public officials or the general public about the financial condition of an insurer. This often occurs when an important fact about the financial status of an insurer is deliberately withheld in order to present the company in a more favorable light.
- **Rebating** — This is defined as any inducement offered to the insured in the sale of insurance products that is not specified in the policy. Rebates include money, reductions in commissions, stock, bonds, securities and their dividends or profits, special favors or advantages in benefits, and personal services. Both the offer and acceptance of a rebate are illegal.
- **Twisting** — This is a form of **misrepresentation** in which an agent persuades an insured/owner to cancel, **lapse**, or switch policies, even when doing so is to the insured's disadvantage.

If, after a hearing, the department of Insurance determines that a producer or an insurer has committed an unfair trade or competition practice, the Department may issue an order requiring the person to cease and desist from engaging in the method of competition, act, or practice, and/or impose penalties for violation of insurance laws.

Fair Credit Reporting Act

The **Fair Credit Reporting Act** established procedures that consumer-reporting agencies must follow in order to ensure that records are confidential, accurate, relevant, and properly used. The law also **protects consumers** against the circulation of inaccurate or obsolete information.

The acceptability of a risk is determined by checking the individual risk against many factors directly related to the risk's potential for loss. Besides these factors, an **underwriter** will sometimes request additional information about a particular risk from an outside source. These reports generally fall into two categories: Consumer Reports and Investigative Consumer Reports. Both reports can only be used by someone with a legitimate business purpose, including insurance underwriting, employment screening, and credit transactions.

Consumer Reports include written and/or oral information regarding a consumer's credit, character, reputation, or habits collected by a reporting agency from employment records, credit reports, and other public sources.

Investigative Consumer Reports are similar to consumer reports in that they also provide information on the consumer's character, reputation, and habits. The primary *difference* from regular consumer reports is that the information is obtained through an investigation and interviews with associates, friends, and neighbors of the consumer. Unlike consumer reports, these reports cannot be made unless the consumer is advised of the report in writing within 3 days of the date the report is requested.

The consumers must be advised that they have a right to request additional information concerning the report, and the insurer or reporting agency has 5 days to provide the consumer with the additional information.

The reporting agency and users of the information are subject to civil action for failure to comply with the provisions of the Fair Credit Reporting Act. A person who knowingly and willfully obtains information on a consumer from a consumer reporting agency under false pretenses may also be fined and/or imprisoned for up to 2 years.

An individual who **unknowingly** violates the Fair Credit Reporting Act is liable in the amount equal to the loss to the consumer, as well as any reasonable attorney fees incurred in the process.

An individual who **willfully** violates this act enough to constitute a general pattern or business practice will be subject to a penalty of up to \$2,500.

Under the Fair Credit Reporting Act, if a policy of insurance is declined or modified because of information contained in either a consumer or investigative report, the consumer must be advised and provided with the name and address of the reporting agency. **The consumer has the right to know what was in the report.** The consumer also has a right to know the identity of anyone who has received a copy of the report during the past year. If the consumer challenges any of the information in the report, the reporting agency is required to reinvestigate and may need to amend the report if warranted. If a report is found to be inaccurate and is corrected, the agency must send the corrected information to all parties to which they reported the inaccurate information within the last 2 years.

Consumer reports cannot contain certain types of information if the report is requested in connection with a life **insurance policy** or credit transaction of less than \$150,000. The **prohibited information** includes bankruptcies more than 10 years old,

civil suits, records of arrest or convictions of crimes, or any other negative information that is more than 7 years old. As defined by the act, *negative information* includes information regarding a customer's delinquencies, late payments, insolvency or any other form of default.

B. Underwriting and Claims Settlements

It is an **unfair trade practice** to make any statement that an insurer's policies are guaranteed by the existence of the Insurance Guaranty Association.

Insurance companies are expected to be financially solvent, maintain capital and reserves sufficient to meet their liabilities, follow their own underwriting rules, pay claims when due, and provide good policyholder service. Home office personnel need to know how companies operate and how to provide necessary support to agents, policyowners, and management. Claims representatives need to understand the obligations of the parties to the insurance **contract**, as well as how to deal with claimants.

To make sure that insurance companies are executing all of their responsibilities to the public, state insurance departments provide oversight and regulation. The primary purpose of state insurance regulation is consumer protection.

Insurance commissioners have the authority to investigate any insurance company or agency transacting insurance in the state in order to determine if the company/agency is complying with state insurance laws and regulations. If the commissioner believes a violation of those laws and regulations has taken place, a hearing may be scheduled to establish the facts. If a violation is found, the commission can issue a cease-and-desist order. Violations of a cease-and-desist order may result in severe fines (usually \$10,000 but the amount can vary by state), in addition to loss of license.

Insurance companies generally have an entire Compliance Department devoted to ensuring that the firm remains in compliance with all state and federal rules. Creating a "culture of compliance" and fostering an ethical business climate will help an insurance company stay out of trouble with the regulators, but again, compliance with the letter of the law is not necessarily the same thing as ethical behavior.

C. Solvency

Ultimate regulatory responsibility for insurer solvency rests with each state insurance department and the state insurance commissioner. State insurance departments are assisted by the NAIC, which is a voluntary organization of the commissioners of the state insurance departments. The NAIC's overriding objective is to assist state insurance regulators by offering financial, actuarial, legal, computer, research, and economic expertise to state regulators.

It is primarily through the states' adoption of NAIC model laws and model regulations that uniformity is achieved in the financial regulation of insurance companies. Once a state has demonstrated that it has met a wide range of legal, financial, functional, and organizational standards, it can achieve accreditation. (All 50 states and the District of Columbia are currently accredited.) The purpose of the accreditation program is for state insurance departments to meet minimum, baseline standards of solvency regulation, especially with respect to regulation of multi-state insurers.

1. The NAIC and Solvency Regulation

U.S. Insurance Financial Solvency Framework

The US Regulatory Mission is to protect policyholders/claimants/beneficiaries while also facilitating an effective and efficient marketplace for insurance products. Effective regulation requires that regulators have appropriate regulatory authority over insurers, operate independently of insurer and political interference, maintain an adequate staff of sufficiently trained personnel, and treat confidential information appropriately.

Seven “Core Principles” of US Insurance Financial Solvency

1. Regulatory Reporting, Disclosure and Transparency

Insurers are required to file standardized annual and quarterly financial reports that are used to assess the insurer’s risk and financial condition. These reports contain both qualitative and quantitative information and are updated as necessary to incorporate significant common insurer risks.

2. Off-site Monitoring and Analysis

Off-site solvency monitoring is used on an ongoing basis to assess the financial condition of the insurer as of the valuation date and to identify and assess current and prospective risks through risk-focused surveillance. The results of the off-site analysis are included in an insurer profile for continual solvency monitoring.

3. On-site Risk-focused Examinations

U.S. regulators carry out risk-focused, on-site examinations in which the insurer’s corporate governance, management oversight, and financial strength are evaluated, including the system of risk identification and mitigation, both on a current and prospective basis. The reported financial results are assessed through the financial examination process, and a determination is made regarding the insurer’s compliance with legal requirements.

4. Reserves, Capital Adequacy and Solvency

To ensure that legal obligations to policyholders, [contract](#) holders, and others are met when they come due, insurers are required to maintain reserves, capital, and surplus at all times in such forms so as to provide an adequate margin of safety. The most visible measure of capital adequacy requirements is associated with the risk-based capital (RBC) system. The RBC calculation uses a standardized formula to benchmark specified level of regulatory actions for weakly capitalized insurers.

5. Regulatory Control of Significant, Broad-based Risk-related Transactions/Activities

The regulatory framework recognizes that certain significant, broad-based transactions/activities affecting policyholders’ interests must receive regulatory approval. These transactions/activities encompass licensing requirements, change of control, the amount of dividends paid, transactions with affiliates, and [reinsurance](#).

6. Preventive and Corrective Measures, Including Enforcement

The regulatory authority takes preventive and corrective measures that are timely, suitable, and necessary to reduce the impact of risks identified during on-site and off-site regulatory monitoring. These regulatory actions are enforced as necessary.

7. Exiting the Market and Receivership

The legal and regulatory framework defines a range of options for the orderly exit of insurers from the marketplace. It defines solvency and establishes a receivership

scheme to ensure the payment of policyholder obligations by insolvent insurers subject to appropriate restrictions and limitations.

D. Marketplace Regulation & Penalties

Simply defined, **market regulation** is how insurance companies conduct themselves in the insurance marketplace. (Financial regulation, or the ability of an insurance company to pay its liabilities, is a separate regulatory function.)

Insurers must comply with certain established procedures, and failure to comply will result in penalties. Some of the areas that market conduct regulations cover include (but are not limited to) the following.

- Sales and marketing practices
- Underwriting and issuance of insurance products
- Policyholder service
- Complaint handling
- Claims handling
- Policy termination practices

Market conduct examiners take the long view of a company's general conduct in the marketplace when determining whether a company has violated the state's trade practice regulations. Evidence that a violation is a "general business practice" is more likely to result in penalties than isolated incidents of noncompliance.



The NAIC Market Regulation and Consumer Affairs Committee

The National Association of Insurance Commissioners (NAIC) is the U.S. standard-setting and regulatory support organization that is created and governed by the chief insurance regulators from the 50 states, the District of Columbia, and five U.S. territories. Through the NAIC, state insurance regulators establish standards and best practices, conduct peer reviews, and coordinate their regulatory oversight. NAIC members, together with the central resources of the NAIC, form the national system of state-based insurance regulation in the U.S.

The mission of the NAIC Market Regulation and Consumer Affairs Committee is to monitor all aspects of the market regulatory process. This includes overseeing

- *The collection of market data,*
- *The Market Information Systems automated applications*
- *The use of desk audits, examinations, interrogatories, investigations and other resources for monitoring market activities*
- *The analysis of data relevant to market issues.*

In addition, the committee will help identify and develop uniform regulatory standards and solutions to problems related to market issues. As part of this function, the committee will facilitate interstate communication and coordinate collaborative state regulatory actions. The committee will also review and make recommendations regarding the underwriting and market practices of insurers and producers as those

practices affect insurance consumers, including availability and affordability of insurance.

Market Conduct Examinations

"The California Department of Insurance conducts examinations of insurance companies to be sure that the companies are in compliance with the California Insurance Code (CIC) and the California Code of Regulations with respect to rating, underwriting and [claim](#) practices. These are called market conduct examinations. Exams can be scheduled based on consumer [complaint](#) activity, special requests, or at regular intervals.

Market conduct examination reports document the findings of our examiners. The reports identify the size of the policy sample or claim sample that was reviewed by the examiners and indicate any alleged violations of the law discovered during the exam. The reports also summarize actions taken by the insurers to correct the alleged non-compliant practices. The public reports of examination available here contain alleged violations of CIC Section 790.03, Prohibited Acts, and the Fair Claims Settlement Practices regulations. In some cases, the examinations serve as the basis for a formal legal enforcement action against an insurer."

PENALTY BOX

Common Violations by Insurers (from the Texas Enforcement Files):

- *Paying a valuable [consideration](#) to unlicensed persons for the referral of potential customers based upon the purchase of an insurance product*
- *Charging and receiving a premium on [insurance policy](#) not in accordance with applicable rate filing*
- *Failing to respond to a TDI request for information in a timely manner*

E. NAIFA Code of Ethics

The National Association of Insurance and Financial Advisors (NAIFA) is one of the oldest and largest trade organizations in the insurance field. Its mission is to advocate for a positive regulatory environment and promote professionalism and competence among insurance and financial professionals. One of NAIFA's main goals is to promote the ethical conduct of its members. Insurance agents and financial advisors have professional duties not only to the companies they represent, but also to the client. NAIFA Code of Ethics was designed to address these dual obligations and to help agents strike an ethical balance as they perform their professional duties.

Learn these principles, and live by them in your professional practice.

"I Believe It To Be My Responsibility

- *To hold my profession in high esteem and strive to enhance its prestige.*
- *To fulfill the needs of my clients to the best of my ability.*
- *To maintain my clients' confidences.*
- *To render exemplary service to my clients and their beneficiaries.*
- *To adhere to professional standards of conduct in helping my clients to protect insurable obligations and attain their financial security objectives.*
- *To present accurately and honestly all facts essential to my clients' decisions.*
- *To perfect my skills and increase my knowledge through continuing education.*
- *To conduct my business in such a way that my example might help raise the professional standards of those in my profession.*
- *To keep informed with respect to applicable laws and regulations and to observe them in the practice of my profession.*

- *To cooperate with others whose services are constructively related to meeting the needs of my clients."*

F. For Florida Producers Only

Unauthorized Entities:

An entity that is required to be licensed or registered with the Florida Office of Insurance Regulation, but that is operating without the proper authorization, is identified as an **unauthorized insurer**. All persons have the responsibility of conducting reasonable research to ensure they are not writing policies or placing business with an unauthorized insurer. Any person who, directly or indirectly, aids or represents an unauthorized insurer can lose his or her licenses, or face other disciplinary sanctions. Lack of careful screening can result in significant financial loss to Florida consumers due to unpaid claims and/or theft of premiums. Under Florida law, a person can be charged with a third-degree felony and also held liable for any unpaid claims and refund of premiums when representing an unauthorized insurer. It is the person's responsibility to give fair and accurate information regarding the companies they represent. *(Please see section 626.901, Florida Statutes, to read the laws.)*

G. Course Recap

1. Exam Breakdown

The Exam Breakdown should be used to see where to focus your valuable study time. Each test is weighted per chapter, so concentrating your efforts will benefit you when taking the actual exam.



Ethics & Insurance - Final Examination 25 Questions - 2-hour time limit

Chapter	Percentage of Exam
Ethics Defined	12%
Producer's Ethical Responsibilities	12%
Producer's Responsibilities to the Insured	12%
Sales Practices and Sales Presentations	24%
Producer Responsibilities - Other Related Concepts	16%
Insurance Company Responsibilities to the Public and Regulators	24%

2. Key Concepts

This course provided an overview of ethical insurance practices, as well as standards and regulations for insurers and producers. Let's recap some of the major points. Make sure you refresh the following key concepts before taking the final exam.

ETHICS DEFINED	
Ethical Behavior - The Golden Rule	<ul style="list-style-type: none"> • The Golden Rule: treating others with the same regard as you would expect for yourself • Maintaining ethical attitude, ideas and beliefs

The Ethical Balance Sheet	<ul style="list-style-type: none"> • The ends do not justify the means (moral dilemma: production numbers vs. service) • Putting the greater good of others before one's own interests • Rationalization vs. ethics
Ethics as a Legal Force	<ul style="list-style-type: none"> • Legal vs. ethical practices • Legal actions can be unethical • The law sets minimum <i>standards</i> of behavior; ethics sets <i>goals</i> for behavior
Insurance and Industry Ethics	<ul style="list-style-type: none"> • Ethical standards: industry Code of Ethics • Living by ethical standards may not guarantee profitability
The Ethical Bottom Line	<ul style="list-style-type: none"> • Assuming personal responsibility for actions • Doing the right thing
PRODUCER'S ETHICAL RESPONSIBILITIES	
The Role of Agents/Producers	<ul style="list-style-type: none"> • Agents have ethical responsibilities to <ul style="list-style-type: none"> ◦ <i>Insurer</i>: acts of an agent are deemed to be the acts of the insurer; fiduciary duty; loyalty ◦ <i>Insured</i>: disclosing information about the insured's policies; not deceiving or coercing the applicant into buying policies ◦ <i>Public</i>: care and skill ◦ <i>Regulators</i>: legal actions; proper licensing and business transactions
Producer's Responsibilities to the Insurer	<ul style="list-style-type: none"> • Fiduciary duty: position of trust and confidence in handling another person's financial affairs • Express authority: expressly stated in the contract • File underwriting: disclose material information about the applicant to the insurer
PRODUCER'S RESPONSIBILITIES TO THE INSURED	
Fiduciary Duty	<ul style="list-style-type: none"> • Remit and return premiums; maintain funds separate from any other accounts • Managing general agent: <ul style="list-style-type: none"> ◦ Appoint insurer's agents ◦ Accept risks ◦ Collect funds from agents
Professionalism	<ul style="list-style-type: none"> • Advanced level of training, knowledge, and skill • Always placing the public's interest above one's own: quality of service • Loyalty and full disclosure: to the insurer and the customer
Suitability and Needs-Based Selling	<ul style="list-style-type: none"> • Suitability of product: evaluate customer's profile (age, income, financial situation, needs and objectives, risk tolerance, and tax status) • Products must be matched to the customer's needs • Communication and education must continue as long as the insured is the customer
SALES PRACTICES AND SALES PRESENTATIONS	
Ethical Responsibilities at Policy Application	<i>Conditional receipt</i> : explaining when the coverage begins

	<p><i>Unanswered questions on the application:</i></p> <ul style="list-style-type: none"> • Return to applicant for completion • If a policy is issued, unanswered questions are interpreted as if they insurer waived its right to have an answer <p><i>Replacement:</i> must be suitable for the insured</p> <ul style="list-style-type: none"> • Duties of the producer: <ul style="list-style-type: none"> ◦ Notice Regarding Replacement to the insured (submit a signed copy to the insurer) ◦ Obtain a list of existing policies ◦ Provide copies of communication records regarding replacement to the insured • Duties of the replacing insurer: <ul style="list-style-type: none"> ◦ Obtain a list of policies being replaced from the producer ◦ Send notifications to existing insurers about replacement
Explaining the Underwriting Process	<ul style="list-style-type: none"> • Gramm-Leach-Bliley Act: protects private customer information (nondisclosure of nonpublic personal information) • Disclosure statements: help consumers make informed decisions • Buyer's guide: allows consumers to compare the costs of different policies (generic information)
PRODUCER RESPONSIBILITIES - OTHER RELATED CONCEPTS	
Policy Delivery	<ul style="list-style-type: none"> • Agent's responsibility: promptness and policy delivery • Policy delivery in person: ensures that the policyowner fully understands all aspects of the contract
At Claims Time	<ul style="list-style-type: none"> • Agents should be familiar with the insurer's claims procedures • Agents should not be giving legal advice regarding payment of claims • If fraud is suspected, refer to the insurer's special investigative unit (SIU)
Providing Continued Service	<ul style="list-style-type: none"> • Service before, during, and after the sale • Educating the client • Loyalty
Producer Responsibilities to the Public	<ul style="list-style-type: none"> • Provide honest and fair explanation of available policies that would serve the public's needs
Producer Responsibilities to Regulators	<ul style="list-style-type: none"> • Avoiding unfair marketing practices • Controlled business: insurance on one's own life or property, or that of the agent's family or business associates <ul style="list-style-type: none"> ◦ Commissions cannot exceed a state-mandated maximum amount for the year ◦ License cannot be used to write only controlled business
Special Ethics Concerns	<ul style="list-style-type: none"> • Pretext interviews: pretending to be someone else to obtain information <ul style="list-style-type: none"> ◦ Illegal in many states unless for claims investigation

Regarding Senior Citizens	<ul style="list-style-type: none"> High-pressure tactics and cold lead advertising are prohibited
Penalties	<ul style="list-style-type: none"> Interstate commerce: <ul style="list-style-type: none"> Knowingly making false material statements or reports will result in a fine, imprisonment, or both If an agent has a conviction involving dishonest or breach of trust, a written consent from insurance regulatory authority is required before the agent will be allowed to work in the business of insurance affecting interstate commerce (1033 waiver)
Agent Errors and Omissions	<ul style="list-style-type: none"> Professional liability insurance Protects against: <ul style="list-style-type: none"> Agency's or producer's negligence Failure to render reasonable duties or services Does NOT protect from liability resulting from criminal acts or unfair trade practices
INSURANCE COMPANY RESPONSIBILITIES TO THE PUBLIC AND REGULATORS	
Role of Insurers	<p>4 divisions of insurance companies:</p> <ul style="list-style-type: none"> Marketing: advertising, promoting, and distributing insurer's products Underwriting - evaluating and accepting risks Claims - receiving, evaluating, and paying claims Actuarial - developing mortality and morbidity tables (statistics) <p>Unfair trade practices: know them and avoid them</p> <p>Fair Credit Reporting Act:</p> <ul style="list-style-type: none"> Protects consumers against the circulation of inaccurate or obsolete information Consumer has the right to know the information in the consumer report
Underwriting and Claims Settlements	<ul style="list-style-type: none"> Guaranteeing policies by the existence of the Insurance Guaranty Association is an unfair trade practice
Solvency	<ul style="list-style-type: none"> Core principles of insurance financial solvency: <ul style="list-style-type: none"> Reporting, disclosure and transparency Off-site monitoring and analysis On-site risk-focused examinations Reserve and capital adequacy Control of significant, broad-based risk-related transactions Preventing and corrective measures and enforcement Exiting the market and receivership
Marketplace Regulation & Penalties	<ul style="list-style-type: none"> Market conduct: code of ethics for producers and insurers NAIC Market Regulation and Consumer Affairs Committee
NAIFA Code of Ethics	<ul style="list-style-type: none"> Purpose: <ul style="list-style-type: none"> Advocate for positive regulatory environment Promote professionalism and competence among insurance professionals

H. Bibliography

<http://www.naifa.org/about/ethics.cfm>, *Role of Agents/Producers*

<http://www.acli.com/Pages/DefaultNotLoggedIn.aspx>, *American Council of Life Insurers (ACLI) Life Insurers Fact Book*, 2011

The American College - The Center for Ethics in Financial Services, *Code of Ethics and Procedures, Including the Professional Pledge and the 8 Canons*

<http://www.insurance.ca.gov/0400-news/0100-press-releases/2011/release064-11.cfm>, California Department of Insurance, *News: 2011 Press Release*

<http://www.tdi.texas.gov/commish/actions.html>, Texas Department of Insurance, *TDI Enforcement Actions*, 2011

<http://oci.wi.gov/>, Wisconsin Department of Insurance, *Administrative Actions*

www.naic.org, National Association of Insurance Commissioners, *Life Insurance Buyer's Guide*

www.naic.org, National Association of Insurance Commissioners, *The United States Insurance Financial Solvency Framework*, 2010

www.naic.org, National Association of Insurance Commissioners, *The NAIC Market Regulation and Consumer Affairs Committee*

<http://www.insurancejournal.com/news/national/2011/11/22/225032.htm>, Insurance Journal, *Agency E&O Survey*, 2011

<http://www.insurancejournal.com/news/national/2011/11/22/225032.htm>, Insurance Journal, *MVR Compliance Manual for Agents and Brokers*, 2011

<http://www.ftc.gov/os/statutes/031224fcra.pdf>, The Federal Trade Commission (FTC), *The [Fair Credit Reporting Act](#)*, last amended in 2004

Chapter Complete

© 2020 ExamFX All rights reserved.

[Contact Us](#) | [Privacy Statement](#) | [Terms Of Use](#) | [Terms and Conditions](#)