Ethics 4-Hour Training Course

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ETHICS

Ethics involves the struggle of how to live one’s life, both personal and professional. Throughout recorded history, this has occupied the thoughts of many people. The study of ethics involves one of the oldest systems of guiding human behavior, one that goes back to the very beginnings of our civilization.

Self-interest and self-preservation are the driving forces within human beings. Human beings, like all other animals, are born with primary survival instincts, such as the desire to obtain food, shelter and safety, which develop long before they think about ethical behavior. Without these instincts the human race would not survive.

In the earliest days of mankind, human beings lived in small groups, first the family, and then the clan or tribe. Over time, clans and tribes united to form larger units, either for protection or for social and economic reasons. Once the larger unit existed, a division of responsibilities occurred. Some responsibilities remained with the individual, while others, such as defense, were taken over the group. At the same time that some responsibilities were assumed by the larger group, a code of behavior for all members of the group also came into existence.

From the beginning of time, when humans began living together, ethics was a system of unwritten rules that were necessary for survival. These unwritten rules were established so everyone would benefit from each other. The rules established the way in which others were to be treated. Those that worked lasted - those that didn’t were replaced by others.

Ethics are the rules, values, standards and principles that guide our actions in day-to-day issues. There are two sides to ethics. One side defines improper conduct, things people should not do. Ethical persons seek to avoid doing things such as lying, cheating, stealing, revealing confidences, abusing others. The other side specifies what people should do. The individual committed to living a more ethical life must be constantly aware of both the negative and positive sides of ethics and try to live up to both.

Two areas that an individual must emphasize in order to move toward a more ethical life are to cultivate ethical virtues such as honesty, truthfulness, and faithfulness and ability to make ethical choices. Ethical decision-making skills can help people more effectively eliminate improper options and choose among conflicting ethical obligations. People interested in living an ethical life should work at both developing ethical values and improving the choices they make.

Many of the decisions people make depend upon their personal ethical code. They are made after a process in which they weigh all the factors and decide whether or not, in this situation, the end justifies the means. Sometimes taking the most ethical path means people must give up something else that is important to them. There is often a price to pay for leading a more ethical life; fortunately, in the long run, the rewards are also greater.

Personal ethical codes come into being when people are very young and continue to develop as they grow and mature. Personal ethics are different from, though they may reflect or include, the laws of society or the regulations of a church. They normally have much more force in influencing and guiding people’s decisions than religious rules or laws. When the chips are down, even people who might ignore certain laws or disobey the regulations of a church often stick to their own ethical code.
Setting down priorities determines goals in life. Ethics help people set goals that will bring about pride in themselves and their achievements. Regardless of their personal circumstances, it is always possible to have a moral code (a code of ethics). Even in dire circumstances, many people, such as those on the Titanic, members of the Donner Party and Jews in Nazi concentration camps, chose to live their lives with a moral basis.

**How Ethics is Learned**

Most ethical behavior is learned during childhood and adolescence. That is why ethical parenting is so important in the outcome of children's lives and of our society as a whole. Currently, with so many families needing two incomes in order to survive financially, there isn't as much time to teach children ethics and parents are counting on them to learn it elsewhere.

Children learn what they see and hear. They imitate the behavior they see, especially that of the adults that are close to them, such as parents and teachers. As a result, parents who set good moral or ethical examples are teaching their children to do the same. Unfortunately the reverse is also true. In homes where prejudice, racism, sexism and other behaviors are practiced by the parents, children are very likely to act in the same manner. In fact, researchers say that as much as 80 – 90% of an individual's ethics are developed by the time they enter school; and well before they can read or write. Most of it comes from their parents, as well as other family members, church or Sunday school, preschool and day care providers.

Most people are loyal to their families above everything else; this same kind of loyalty is found in groups that have taken the family's place. And the glue that binds families and other groups together is their behavioral code -- the code that sets limits of behavior, rewards for observing the limits, and penalties if they are broken or overlooked.

People's values may change and shift as they grow older. In fact, people often adopt certain behaviors or beliefs that are in conflict with their own personal values in order to belong to a particular group.

Personal ethics are an accumulation not only of what people learn, but also of what they failed to learn. Individuals also learn ethical behavior as a result of their life experiences. A dramatic or tragic occurrence often teaches the fundamentals of ethics or moral behavior.

Moral or ethical conduct is continually learned and refreshed. People continue to learn as new ideas are presented and new experiences encountered. Unfortunately, those who have been poorly educated on ethical conduct might be faced with unlearning bad conduct as well.

**The Components of an Ethical System**

Ethics is about making moral choices and the values that lie behind those choices. It influences actions and affects decisions about what people ought to do, and how they should live.

- **Values** are what people believe in, what they believe is important.
- **Ethics** is what people do.

Many people do not realize the connection between values and ethics. Leading an ethical life requires that people establish their values carefully and then work every day to ward those values.
**Ethics and Success**

The most obvious reason for avoiding unethical behavior is not fear of punishment; it is that personal and professional success are determined in large part by beliefs, values, character and ethics. Being ethical isn't just a matter of knowing what's right or wrong; it's a matter of doing what's right and avoiding what's wrong.

Some people would argue that today's fast-paced, competitive society prevents people from being ethical all the time. Every insurance agent faces competition from other agents when soliciting, servicing and renewing accounts. From time to time most agents feel compelled, in the interest of their clients, insurers or themselves, to practice some form of unethical behavior when negotiating with clients or their own insurance companies. They may feel pressured to make misstatements, conceal pertinent facts or exaggerate a situation to persuade clients to purchase insurance coverage.

Ethics is not incompatible with business success; after all, most businesses are formed to make profits and profit is a good thing. In fact, in the long run, good ethics is good business since clients prefer to work with an ethical insurance agent, someone they can trust. A recent study suggested that ethical people are generally more successful than unethical people. When people find a businessperson with high ethical standards, they tend to do more business with that person.

**How We Define Success**

In the United States and many other countries, success is usually measured by wealth. Unfortunately, society has become used to hearing about businesspeople who have earned their wealth through unethical, questionable or illegal activities.

Ethics sometimes requires tough choices. Choices between right and wrong are not always easy to identify. Individuals must make what they perceive to be the best choice. Even good people will be tempted when in certain situations. How people react to temptation says a great deal about who they are ethically. Businesses must follow ethical guidelines even if it means a lost sale with lucrative potential.

Unfortunately, society isn't always critical of wrongdoing and tends to accept that business is inherently corrupt. In fact, many people feel that the only way to succeed in business is by cheating clients and competitors.

This tendency to emphasize personal financial gain is a common way many businesses including those in the insurance industry, motivate their employees. Financial gain is often held out as the primary measure of success while ignoring professionalism and ethics.

Certainly, agents should expect to be adequately rewarded for success, however, the agent should remember that his or her own rewards must not be earned at the expense of the insurer, clients or general public.

**Long Term vs. Short Term**

Americans have become a nation of buyers where they were once a nation of savers. Pleasure today is promoted over financial security tomorrow. Without a system of values, individuals may come to feel that society owes them a comfortable living and retirement. This
rationalization allows people to spend today without worrying about tomorrow. Self-discipline and self-control have given way to self-fulfillment and material consumption.

Things often look different in the long run than they do in the short run. One of the most frequent causes of unethical behavior is the continuous pressure for immediate results. When people are under extraordinary pressure to meet deadlines, to attain short-term goals, or to focus totally on either profits or cost reduction they are forced to make choices that are often destructive over the long run.

An ethical person must often sacrifice short-term benefits to achieve long-term advantages. They must all be prepared to sacrifice physical or material gains for abstract intangibles like self-esteem, respect of others, reputation, and a clear conscience. Agents must also work at creating win-win solutions.

A high level of professional ethics may sometimes cause a professional to avoid certain actions and to forgo an opportunity for business growth and compensation. It is not always possible to maximize short-term growth or compensation while adhering to ethical business practices.

**Beliefs**

A belief system is formed by a person's interpretation of, and response to, various life experiences. People's beliefs influence their choices, their decisions and their life directions.

**Honesty**

Honesty relates to a person's integrity and truthfulness. Someone who is honest takes care not to deceive others, either by what they say or what they fail to say. Honesty also means making sure others receive what they are entitled to.

Unquestionably, honesty is one of the ethical pillars of insurance. Honesty is vital for insurance to be available and used.

Insurance viability in the long run requires that the number of insured losses suffered by the insured group in any one period be small relative to the total number of exposure units in the group. Otherwise, the premiums required to cover the losses become larger than consumers will be willing to pay and insurers would be forced to withdraw from the market.

Dishonesty leads to an increase in the number and average size of insured losses. Insurance is highly vulnerable to cheating by claimants as well as virtually anyone else in a position to influence the insurance transactions.

Honesty is essential to creating the trust in the agent-client relationship that allows consumers to make an affirmative buying decision. Consumers aren't going to buy insurance from an agent they think has been dishonest with them, nor will they refer friends or associates to that agent. Consumers are eager to work with agents who handle themselves in an honest and professional manner.

Honesty also means that sales professionals do not mislead their prospects, clients, employers or business associates. Ethical sales professionals clearly identify who they are, what companies they represent, their purpose for meeting with individuals, and what products and services they sell. When making recommendations to clients, sales professionals demonstrate their honesty by using presentations and illustrations that are easy to understand, and
explaining the associated risks, benefits and assumptions so that clients can make an informed decision.

Agents who have high standards of honesty and personal integrity may be unable to compromise them, even if their agency or client asks them to do so. It is easy to behave ethically when others will be observing them. The difficult part comes when there will be no recognition for their convictions, when they may even be unpopular or have to confront another who is acting illegally or unethically.

Rationalization

Often times, people do not act ethically because they want to meet other goals. To make themselves more comfortable with their actions, people often revert to rationalizations. Rationalizations make it easier to live with themselves when they do the things they want to do, rather than those things they know they should be doing.

ETHICS IN MODERN SOCIETY

Enron, WorldCom, Arthur Andersen are examples of corporate greed and an utter disregard for the principles of fairness and ethical practices. Although they have become well known for their significant ethical and legal lapses, these companies are not unique.

In today's society, there are also many examples of an increasing emphasis on the ethical aspects of an issue. Some people feel the moral and ethical fiber of society is deteriorating rapidly. Most people agree on the importance of maintaining a high ethical standard for a society to survive and prosper.

Many feel that it is even more important to maintain a high ethical standard in the insurance industry. The unique aspects of the insurance industry demand such a high ethical standard. Both individuals and businesses depend on insurance to provide essential services and to protect them from financial disaster.

Health insurance provides access to quality medical care. Life insurance proceeds support families, educate children, and assist in the perpetuation of a business. Property coverage is an integral part of every mortgage contract. Casualty contracts such as automobile and workers’ compensation are often required by law and protection families and businesses from financial devastation in modern society, insurance has become a necessity.

Ethics are never a separate part of life. They are part of everything people do and everything they say. Ethics determine how people feel the moral and ethical treatment of strangers. Ethics determine a person’s actions in financial and public matters. Ethics belong in every profession and are especially important in some, including insurance. Agents must understand that their peers, their company, their prospects and clients all rely on them to make ethical choices every time.

The Individual and Society

Moral truth is relative to culture, personal ideals, legal aspects, and one's economic situation can have a bearing on their perception of what is ethical.

Some types of ethics tend to be universal and apply to all people in all countries. Sometimes however, people or cultures do not agree on what is ethical behavior. What one culture or
society may consider ethical another may not. Even within the same culture or society, people may disagree on what is and is not ethical. These differences often exist between religions as well.

Since ethical behavior may not be the same everywhere or even from culture to culture in the same country, society must mandate certain behavior when cultures do not conform to what the majority of the citizens desire. Ethical standards, which are enforced by social pressure make no attempt to actually determine what is right or wrong morally. They simply define what is right or wrong according to the given culture. Americans have many opinions as to what is ethical because of the varied population with a varied background.

**Religion & Ethics**

Ethical people often have some form of religion in their lives. In fact, the Bible and other religious texts include many rules for ethical behavior. Religious doctrines are probably the best known source of sound ethical advice. Many religious philosophers have argued that ethics cannot exist without religion.

**Laws Versus Ethics**

An insurance producer's legal and ethical responsibilities to the state in which he or she is licensed are set forth in statutes and regulations. Essentially, each state creates a code of ethics by defining and codifying what is not legal. If the state or federal government says something is illegal it usually is unethical as well. At a minimum, ethical behavior requires that insurance or financial services professionals have to conduct business in accordance with state and federal laws.

However, it is wise not to confuse laws with ethics. Ethics goes beyond the letter of the law and entails not only what someone must do but also what they should do. While laws set the minimum standard by which producers are expected to behave, a person's personal values or ethics provide a guidance system to help him or her choose the right answer or alternative to ethical dilemmas when several choices are available.

Some people feel simply that if it is legal that’s good enough. For these individuals, as long as they are not breaking the law, any behavior is deemed acceptable. Many salespeople do not realize that simply following the laws is the minimum acceptable level of ethical conduct. It is up to the business organization to set the actual ethical code of conduct that they require. Ideally, that will be higher than is actually mandated by law. Of course, each individual must also set their own personal standards of conduct, which may be higher than that of either the law or their agency or company.

A wise insurance agent will certainly follow state and federal regulations, but ethics goes beyond what is simply mandated by state or federal authorities. Ethics define who we are. A person, in any line of work, must realize that their daily actions or inactions defines who they are.

An insurance agent who is unethical will quickly earn a reputation as such. From the legal standpoint, unethical behavior may also mean legal action against an insurance agent, their agency and the insurance company.

**Ethics is Hard Work**
Being an ethical person is hard work. Most people must make a continuous effort daily to maintain ethical behavior. Those who view ethics as a top priority in all aspect of their lives also value others who are ethical. Honesty and caring for others are an important part of the insurance industry.

Ethics is also hard work because being unethical can often be more financially rewarding. Many people become followers instead of leaders. It is easy for the individual to simply go along with the group, even when a person knows something is not right, but no one else is saying anything. People should do what is right all of the time, no matter what others are doing or thinking.

Toughness is also necessary to succeed in sales. An insurance salesperson that cannot take repeated rejection will not last in the insurance industry as a salesperson. Toughness that is coupled with a code of high ethics promotes productivity and efficiency which contributes to economic success.

**Ethics and Character**

Ethics is not just a matter of how people think and act, but also a matter of their character. Many factors come together to form a person’s character and they must all be taken into consideration. Culture, background, values, morals, passions, and many other factors all contribute to who they are. Character is also defined as the combined principles, values, and beliefs of a person.

The decisions people make form their character, which in turn impacts what they will be tomorrow. Those who lie, cheat or steal, even in small amounts will become desensitized to more serious acts such as perjury, fraud, unfaithfulness, and embezzlement. Conversely, those who choose to be honest take a step toward building a stronger character.

No one gets anywhere in the insurance business without personal integrity. Those who lack integrity don’t last very long in the business. Producers who are involved in illegal schemes or who accept kickbacks as part of writing business do so because they opt for short-term profits at the expense of long successful insurance careers. Because confidential information from the insured is usually required in order to provide the needed insurance protection, the agent's or broker's relationship with the insured is similar to the confidential relationship between an individual and his or her physician, lawyer or accountant. The prospect or client must believe that the agent or broker can be trusted with that confidential information.

**ETHICAL DECISION MAKING**

Ethical decision making is a process of evaluating and choosing among alternatives. The goal is to eliminate unethical options and select the best ethical alternative. To consistently make ethical decisions, one must accomplish two, fundamental things:

- Evaluate alternative courses of conduct based on ethical principles.
- Choose the action that best advances those principles.

Ethics and values play an important role in the decisions that are made every day and those decisions that have a profound effect on our own lives and those of others, including our clients.
Ethical Sales Decisions

Insurance agents face difficult ethical questions every day, many of which have no right or wrong answer. In answering many ethical questions it is important to remember that each and every situation is different. The agent has a duty to both the insurance company and the client. The agent must be honest with the company, giving them all necessary information, but they must also keep their promise to their client.

Ethics must be a part of each and every sale. There simply is no reason not to act ethically. Ethical behavior can actually be a successful sales technique.

The professional must consider every aspect of a recommendation and its possible and probable effects on the client and others. Furthermore, the client must be given full disclosure of all the material facts that bear on his or her making an informed decision. Those facts must include the effects on the client and others of implementing the recommendation.

Taking responsibility for their thoughts, values and actions gives people tremendous freedom in the choices they make. Responsibility, is key in maintaining ethical behavior, because it means there is no one else to blame for their failures and mistakes. Assuming responsibility gives people control over their lives.

Every professional should conduct him or herself in a way that improves their client’s situation. Improvement, of course, is specific to each client and each situation. It could mean that risk is transferred, that income is increased, that taxation is reduced or that other goals of the client were met.

A PERSONAL CODE OF ETHICS

Ethics are synonymous with a person’s own personal behavioral code. Everyone has a code of ethics, even if they do not realize it. This code is the most important factor for an individual agent in dealing with ethical challenges. The person looking back at them in the mirror is the best judge of what should be done in a given ethical situation. Family and friends can provide support and insight to help resolve ethical conflicts, as can the agency manager or principal, but it is still the individual agent, using his or her standards of proper ethical behavior, who must respond to the ethical challenge.

Personal integrity and confidence help build client relationships in business. People want to buy insurance from an agent who feels confident about what they are doing. Self-esteem and self-worth are very important in all aspects of life, though unfortunately without knowledge and hard work they alone do not guarantee success.

Most ethical people don’t deem themselves better than other people. Ethical people treat others with a sense that they are valued and respected. This promotes honest communications and strengthens relationships with clients and peers. No one likes being around someone who looks down on them or doesn’t respect them.

Respect and politeness are part of ethical behavior. Courtesy is a trait that is intentionally developed. Words, like "please" and "thank you" can make routine tasks more pleasant. An ethical person is happy about the success of others and doesn't feel envy or jealousy.
Communication is key in all types of professions. It is important to work on communication skills to communicate effectively with clients, coworkers, and others.

When personal and professional value systems conflict, one can experience a great deal of inner conflict and stress. People who have high personal and professional standards of ethics must find a way to achieve success at work without compromising their personal and professional values.

If a sale can't be made with honesty, fairness and objectivity, it must not be made at all. An opportunity for personal gain that comes at the expense of another must be ignored. The ethical agent:

- Learns very early the difference between right and wrong in business and sales practices and acts accordingly. He or she develops high ethical standards through training with experienced professionals and association with industry groups.
- Consistently adheres to his or her values and maintains this integrity throughout his or her sales career.
- Resists conflicts of interest in all business dealings. Ethics emphasize the interests of clients and company over their own interests.
- Willingly assumes the obligation to perform his or her duties in a way that reflects the highest degree of dignity on the industry and best serves the interests of the client or prospect even if that means putting ethics above sales.

Ethical Agents put someone else's interests ahead of their own. They set aside their own interests and concentrate on doing what has to be done to help their client or prospect. In the long-term this will pay off in both material and non-material ways.

**STANDARDS OF ETHICAL BEHAVIOR**

**CORE ETHICAL VALUES**

**Responsibility**

To be responsible is to be reliable and trustworthy. An ethical agent considers consequences and accepts responsibility for actions and inactions; doesn't shift blame or make excuses. This is an essential element for the professional insurance agent because the insurance business is built on trust. The insurance agent possesses specialized knowledge of needs and products which is not easily accessible to the average consumer. As a result, clients must rely on agents for their professional expertise. Insurance agents have an ethical obligation to accept and fulfill their responsibilities to the best of their abilities.

At all times, insurance agents must remember that what they do affects the very lives of their clients -- their health, their property, their homes, their education, and their jobs. It is a very serious responsibility that must not be taken lightly.

**Integrity**
Integrity is the state of being of sound moral principle. An ethical agent is honorable; has courage of conviction; stands up for beliefs and puts principle over expediency. They are not hypocritical, weak, or dishonorable. Professional ethics is built on integrity. Integrity is being willing to risk anything and everything for the sake of being honest. It is incorruptible no matter what the temptation to be dishonest. A person who has integrity does the right thing regardless of the consequences.

A professional insurance agent makes certain that every act he or she performs is performed with personal integrity of the highest order. Not only does such an agent observe all prohibitions, but he or she bends over backward to avoid the slightest appearance of unethical practice.

**Caring**

Caring is the motivation behind the work of the professional insurance agent. An ethical agent is considerate, kind, sharing, and charitable. They are not selfish, manipulative or controlling. No amount of money or recognition is reward enough for the challenges that insurance agents must face day after day and year after year in their careers.

Caring also enables professional insurance agents to act in their clients' best interests. If agents care about their clients, they will do for their clients what they would do for themselves if they were in the clients' situation.

**Selflessness**

Selflessness is the opposite of selfishness. Selfishness is a concern only with oneself and a disregard for others. The insurance business is no place for the selfish. Insurance agents have to put others first. Because the purpose of the insurance business is to be of service to others, insurance agents succeed by putting others first. By directly serving others' best interests, they indirectly serve their own interests.

An ethical agent is generous. Successful insurance agents find that the more they give to their clients, the more their clients give back to them.

**Courage**

It takes courage to be ethical. The right thing may always be the best thing in the long term, but in the short term there may be a price to pay. To be ethical, agents may find that they have to stand up to a customer, or to an esteemed colleague, or to a superior, or even to their families who don't want to risk the material loss that holding to the ethical line might bring. It takes courage to stand up to those persons, whose expectations we are ordinarily eager to meet. Courage is the quality that converts ethical intention into ethical action.

Courage is a universally admired trait. When individuals demonstrate that they have the courage to stand up for principle, they win the respect of their peers, their superiors, their customers, and their family. Individuals who at first feel alone when faced with an ethical situation requiring courage often end up finding a great deal of support for having done the right thing.

One situation that takes courage for an agent is refusing to work with an individual who is unethical. Better to give up a sale than to try to build a career out of ethically compromised
actions. It's easier and more profitable for agents to work with ethical people who will appreciate the value of their services as well as their ethics, and who will refer them to more people whose values they share.

**Excellence**

Excellence means being the best one can be. In the insurance business, ethical behavior and excellence go hand in hand. A part of that excellence means agents must spend part of their time continuing their education and staying up to date with the latest developments in insurance.

**THE GOLDEN VS. THE PLATINUM RULE**

Throughout history philosophers and religious leaders have expressed the need for humans to treat one another fairly and honestly. Most people are familiar with the Golden Rule: “Do unto others as you would have them do unto you.” Most people learned it as children and have taught it to their children. It’s hard to go wrong by following the Golden Rule.

To paraphrase, it says, "Treat others as you would like them to treat you." People who fail to apply the Golden Rule end up with two separate standards of ethics. One standard is how they treat others; the second is how they expect others to treat them.

A corollary to the Golden Rule is the Platinum Rule, which states: “Do unto others as they would like you to do unto them.” It means: "Treat others the way they would like to be treated." The Platinum Rule is more appropriate than the Golden Rule. When people apply the Platinum Rule in their dealings with clients, they do not force their values upon others. They genuinely listen to the other person’s needs and then strive to meet those needs.

**PROFESSIONALISM**

A career in insurance is more than just another job. It's a profession. It is a field upon which our society is depending more and more for both accumulation of wealth and protection from financial disaster. Insurance agents have a professional and ethical responsibility to their own clients and to all other members of the insuring public, to the company, to themselves and even to their competition.

Agents that are professional is not enough: they must behave in a professional manner. The public expects certain things of those who call themselves professional.

**Primary Characteristics of a Profession**

Many people have tried to clearly define the characteristics that distinguish a profession from other occupations. Many feel that those individuals who practice the desirable characteristics such as high ethical standards, concern for the welfare of others and mandatory education and training, should be considered professionals.

In the earliest professions two basic characteristics tended to differentiate them from the other vocations were, (1) a life dedicated to the needs of others, and (2) the possession of specialized knowledge together with a practical application of this knowledge in the form of technical skills or abilities.
One of the main differences between a profession and an occupation is the amount of formal education required. Until recently a person could get into the insurance business with little, if any, formal education and basically learned on the job. Although some agents resent the prelicensing and continuing education requirements of all states today, these increased requirements not only keep unqualified persons out of the business but also help to elevate the stature of the insurance agent or broker as well.

The Hallmarks of Professionals include:

- A commitment to high ethical standards
- A prevailing attitude of altruism
- Mandatory educational preparation and training
- Mandatory continuing education
- A formal association or society
- Independence
- Public recognition as a profession

The public expects all these hallmarks from any occupation which proclaims itself to be a profession. They expect members of that profession to put the customer's welfare first, and to instruct them about matters essential to that welfare. They expect members of that profession to keep any information they may have about the client confidential.

And they expect members of that profession to be aware of limitation to their education and experience. Insurance agents should get help and advice in situations which are beyond their education and experience.

Groups and associations of Insurance Agents have developed codes of ethics, which incorporate the principles of commitment to high ethical standards; concern for the welfare of others; mandatory licensing and training; formal association or society; and the ability to act with integrity and objectivity.

**A Carefully Conceived Code of Personal Ethics**

A code of ethics is essential to a profession since it provides each member of that profession with a benchmark so the agent can check it against his personal conduct and daily decisions to see how well they are measuring up to the standard of conduct adopted by the profession as a whole. (More about his later.)

**Altruistic Attitude and Behavior**

A profession is altruistic in nature which means that each member is guided by and dedicated to the principle of service rather than personal gain. It is true that a professional must make a living but this is secondary or incidental. The income from professional pursuits simply follows as the result for performing acts of public service. Professionals focus maximum attention on providing unselfish and dedicated service to others with the faith that adequate payment for this service will follow automatically.
An agent must place the customer's best interests ahead of his or her own. In the insurance business. That standard is particularly important to an agent's long-term success. Rarely do agents build a successful career out of making one-time sales. Agents need referrals and repeat sales to build successful lifetime careers. And referrals and repeat sales only come when a relationship of trust has been established between agents and clients.

True professionals are more concerned with the welfare of others than with personal financial gain. Sometimes this is a difficult to practice because our society often defines a person's business success by the amount of money he or she earns, regardless of that wealth was accumulated. Many businesses, including the insurance industry, use financial rewards to motivate their employees. Incentives such as trips or bonuses based on production may influence decisions made by an agent or broker.

The insurance business is unique in that it sells promises to perform at a future date. A great deal of trust is necessary when purchasing a product that cannot be tested in advance and that may not be used until sometime in the distant future, if at all.

**Mandatory Licensing and Education Training**

All states have laws requiring insurance agents, brokers and producers to be licensed. The various state insurance departments administer these laws with the objective of permitting only competent and honest producers to represent insurance companies. The standards for licensing vary from state to state.

Professional insurance agents understand the need for mandatory licensing and education, and knows that continuing education in the field is essential if he or she is to serve the public with skill and competence.

**REQUIREMENTS OF PROFESSIONAL ETHICS**

Many people in the insurance industry have made a personal commitment to professionalism. While defining professionalism is difficult, everyone agrees that a high ethical standard is an integral part of it.

**Skill and Competence**

Many ethical problems agents face can be traced to a simple lack of skill and competence. For example, failure to identify prospects' needs and recommend appropriate products or the inability to provide competent service. These problems would not exist if agents were knowledgeable and competent. A thoroughly trained, knowledgeable, competent agent would not fail to identify a prospect’s needs nor would the agent make mistakes or misrepresentations due to their lack of competence in insurance.

The title of professional carries a reasonable expectation that the individual will have a certain minimum level of competence. Prospects and clients have a right to expect that any professional seeking to do business with them is properly skilled, licensed and credentialed. Competence comes from training and experience. A competent agent or broker provides a wide variety of services that are essential to proper insurance coverage.

As part of their competence, ethical sales professionals are timely in responding to clients, and provide accurate information in a consistent manner. When service falls below a client's
expectations, the ethical sales professional seeks to take whatever steps are needed to remedy the situation.

Insurance agents or registered representatives are ethically required to perform their professional duties with a level of skill commensurate with the experience, training and credentials they possess.

When working with senior or disabled clients, the duty to perform with skill and care may be heightened for several reasons, including the possibility that some clients may be more trusting and therefore more vulnerable, or may have physical or cognitive limitations that impair their ability to comprehend and understand information.

Insurance products have become more and more complex, so there is ample opportunity for consumers to be confused. Most consumers lack a clear understanding of how insurance works, and commonly do not understand what is covered by their own policies. Only a handful of people actually read the policy or even the sales literature provided with the policy and even then most do not fully understand it.

Ethical sales professionals continually seek to increase their skills and knowledge through continuing education. They do not claim to have skills or credentials they don’t actually possess. There are many specialized areas of knowledge in insurance selling. Beyond a basic level of competence, agent knowledge will vary. Not even the most advanced agent is an expert in every area. Agents should seek help from more experienced agents, their managers, or home office support personnel when they find themselves in a situation where they lack the competence to serve their clients’ needs properly.

Continuing Education (CE)

Continuing education is one of the hallmarks of a profession, both through formal training and informal study on one’s own.

Every state, and the District of Columbia, require that licensed agents obtain a specified number of continuing education hours prior to the agent’s license renewal date. The number of hours of continuing education required varies from state to state. It is the responsibility of each agent to know and understand their state’s requirements. Failure to comply with continuing education requirements will result in the license not being renewed.

Agents are both legally and ethically bound to meet state continuing education requirements. Professional agents are ethically bound to assess their own needs for continuing education and engage in ongoing improvement of their knowledge and skills, whether or not required by law.

Many agents also pursue education that is not required by the state. The insurance industry has many opportunities for education and advancement, even college-level programs.

Insurance agents need to view education as one of their primary responsibilities. Agents possess information the average person needs and typically does not understand. It is important for an agent to be ethical, honest, and truthful in the insurance business. But an agent must also be knowledgeable and skillful in their trade to be successful. Education plays an important role in making an ethical sale.

It is common to hear agents and agencies alike complain about the educational requirements of their state. Some agents look for the shortest or easiest educational course to simply get the
requirements out of the way. Why should a consumer have confidence in an agent that does not consider education important? An agent who must be forced into being responsible about his or her education cannot be considered ethical or professional.

Continuing to learn, regardless of the number of years in the profession, characterizes a true professional who realizes that there is always room for growth. Each agency is responsible for stressing the value of education for their agents. It is the agents’ responsibility to acquire the mandated credits prior to their license renewal date.

A competent, educated agent can educate the public about insurance and help consumers make informed buying decisions about insurance. To do so, the agent must be knowledgeable about a broad spectrum of insurance products and should be able to explain the advantages and disadvantages of different types of policies, costs and terms, provisions, coverages, exclusions, limitations, etc. It is the mark of a poor agent to consistently recommend the same policy solution to every client. Unscrupulous agents use the consumer’s lack of knowledge to sell inappropriate coverages. They often rationalize “some coverage is better than none at all.”

In the insurance business, increased knowledge equals greater competence. Many agents today work or plan to work in specialized markets. In these specialized markets there are many insurance policies available to meet clients’ needs. The agent must be aware of any new policies with new features that are introduced.

Insurance agents have to understand the features of these policies, their benefits, limitations and exclusions. In addition, agents also have to know how these products compare to other policies their insurer offers as well as how they compare to products of other insurance companies.

One of the most common elements of professionalism is ethics training. Unfortunately far fewer hours are spent in ethics training than in sales training. Not only should ethics training be afforded the same status as sales training, it should be afforded the same level of investment to insure it is effective. Insurance companies invest heavily on sales training to motivate and educate agents. Insurers who are serious about ethics, need to similarly invest in the development of effective ethics training.

All states now require that agents complete courses in ethics as a part of their continuing education requirements.

Agency managers, agent supervisors, and persons in positions of responsibility in insurance company home offices also have an ethical obligation to assure that agents are being trained properly and that agents are offered and encouraged to participate in appropriate continuing education experiences. The responsibility for training and supervision includes an obligation to monitor agent behavior on an ongoing basis for both competence as well as ethical practice.

An agency should not resent or attempt to curtail the time an agent spends to acquire education, because ultimately the agency also benefits. It is very difficult to get all that is available out of a course, whether a live seminar or a home-study program, if the agent must rush through it in order to meet a deadline. An agent that gets 30 hours of CE credit in a few hours on the last day before their renewal cannot possibly absorb much of the content and will probably forget much of what they learned soon after.

**Formal Association or Society**
Another characteristic of a profession is the existence of a formalized body of members, sometimes known as a society or an association, which is designed to achieve more effectively, as a group, the individual goals, objectives and ideals of each of the members.

The two principal functions performed by professional societies are to (1) establish and police high standards of ethical behavior and practice among the members, and (2) establish and maintain high standards of technical performance through programs of continuing education sponsored by the society, improving the ethical behavior and technical performance of each member.

A formal association recognizes a sense of fellowship, which brings together individuals who share common interests, goals and educational backgrounds and who tend to speak the same technical language that is part of their chosen profession.

**Ability to Act with Integrity and Objectivity**

The agent must consider the needs of the client before his or her own commission or fee. An insurance professional should serve clients by carefully analyzing their insurance needs and selling them only the coverages that are needed. However, because an agent's income is often based entirely on commissions, he or she may be tempted to sell too much coverage or the wrong kind of coverage to clients.

**Public Recognition as a Profession**

The title of professional is one for which many individuals and occupations strive. It lends an aura of respectability and suggests specialized knowledge and high ethical standards. For the sales professional, that has many positive aspects, including an enhanced public image and a sense that the individual can be trusted. These qualities often lead to higher levels of success and compensation.

Most people do not consider all occupations to have the same prestige or value. The worth of a career or profession is often judged by the ethical standards to which its members are held.

Although insurance companies have determined the agency system is an expensive way to sell insurance, it continues to exist because it is still the most effective system. However, some insurance companies and brokers are experimenting with alternate ways to deliver insurance products to the consumer, without using agents.

Insurance companies will move quickly to less expensive alternative distribution systems unless agents, brokers, registered investment representatives and other financial services practitioners become more professional and the public perceives a greater benefit from the practitioner's participation in the sale. Ethical business practices are one of the best competitive advantage a sales professional has to demonstrate the need for agents to consumers.

**Seeking Other Professional Resources**

The public also expects professionals to be aware of limitations to their education and experience. Insurance agents should get help and advice in situations which are beyond their education and experience. Those who lack the experience needed can find help from more experienced colleagues or a company underwriter. The ethical violation occurs when agents
pretend that they have skill and knowledge when, in fact, they do not, or if they ignore the need to complete the education and training necessary to properly identify, analyze and treat a risk.

It is essential that insurance agents not hold themselves out as having skills or professional credentials they do not really possess. To do so is unethical, probably illegal, and will also result in the insurance agents being held to the standard of the professional that they claim to be if a lawsuit ensues.

Agents to limit their advice and services to areas of professional competence, and to seek the support of other professionals in areas outside their own including a(n):

- Attorney
- Accountant
- Trust officer
- Appraiser

Insurance agents who fail to seek the services of other professionals for their clients such are exposing themselves to significant liability, doing a disservice to clients and missing an opportunity to further develop their contacts with other professionals.

Unauthorized Practice of Law

One area where agents must be especially aware of their limitations is in regard to the unauthorized practice of law. Every state requires an individual to be properly licensed as an attorney in order to practice law, with violations punishable as contempt of court. The American Bar Association has distinct opinions about what is ethical and unethical behavior for insurance agents in this regard:

- Non-lawyers may determine, analyze, and organize the assets of a client to take care of the needs of the living and of survivors after a death, and may also present general information about laws that affect asset use.
- Non-lawyers may not do legal research; draw up legal documents, such as a trust on will; put advice in specific legal terms; or use legal principals to define the client's particular needs.

No violation arises from the sharing of legal knowledge which is either general information or common knowledge. Providing advice involving the application of legal principles to a specific situation, however, is clearly the “practice of law”.

The non-attorney should not, however, answer “difficult” or “complex” questions of law. When basic legal principles are applied to specific and actual facts or the resolution of controversial or uncertain questions of law is required in an actual case, the practice of law is involved.

The preparation of instruments and contracts by which legal rights are secured constitutes an invasion of the attorney’s authority. The non-attorney who drafts a will or a trust for a client is guilty of the unauthorized practice of law.

Normally, agents will work together with a client's attorney and accountant to come up with an estate or risk management plan. Agents may also be called upon to review indemnification
agreements and insurance requirements in wills, trusts, leases and contracts but should not go further in interpreting or suggesting modifications in the wording of such contracts or other documents.

Insurance agents also behave unethically when, they try to steer business to a particular attorney, or when they try to talk clients out of seeking legal advice. Fee-splitting with attorneys is unethical and in some cases it is also illegal. In most states, agents are not allowed to pay or to receive referral or finders fees or to split commission with any unlicensed persons. Agents should refer to their state’s laws.

An attorney should also not be “practicing” insurance unless they are also a licensed agent or broker. The client is best served if the attorney and non-attorney work together to formulate, implement, qualify, and maintain a plan which suits the client’s needs and objectives.

Agents should not rely on the fact that they are performing these services without pay. Courts have found violations where clients relied on advice or were provided with legal services regardless of whether or not fees were charged.

Fairness

The term “fairness” has many possible meanings including “just and impartial. The ethical mandates with respect to selling in the insurance market are complete disclosure, balanced recommendations and an avoidance of anything that may mislead. The objective of the sales process is to make the prospect fully informed and capable of making an appropriate buying decision.

The Value and Price of Being a Professional

Being considered a professional in the eyes of the client and society generally carries with it certain benefits such as a heightened public image, a greater measure of trust and often, increased success and compensation.

This recognition as a “professional” comes at a price, however. The consequences of being considered an insurance professional, as opposed to simply a sales person, include:

- The imposition of higher standards of conduct and service, and
- A greater potential liability imposed by the courts

PROFESSIONAL CODES OF ETHICS

Every major profession has adopted some form of a Code, Canon, or set of guidelines as to what the profession expects of its members. Professional Codes of Ethics have been developed to provide professionals with working guidelines that go beyond the minimum that is required by law. A professional code of ethics can accomplish a number of things, such as:

- Offer a professional a series of guidelines for work-related decision making.
- Standardize the expectations of both the public and the professional.
Serve as an aid for the professional in reaching the level of trust which the public has come to expect.

Professional organizations need codes of conduct for several purposes:

- To create standards by which conduct can be measured both by the member and by the group itself.
- To acknowledge an obligation to society, to the professional group, and to the client.
- To assure the profession will be governed by high standards.
- To examine priorities and building a tradition based on integrity.
- To limit power. The insurance agent, and other professionals know things the client does not. This special knowledge gives the professional power over a layman who must put great faith and trust in the accuracy and appropriateness of what he is told.
- To provide guidance when people are confronted with a new or unfamiliar situation.
- To maintain trust between an insurance or a financial services professional and the clients he or she serves.
- To provide guidance beyond just doing what is legal or regulated practices

Codes of ethics should clearly define the purpose of the organization, what it hopes to accomplish and how it plans to achieve those goals. Such codes are frequently included in personnel policy manuals and often reference activities such as conflicts of interest, proper use of company assets and property, compliance with the law and maintenance of a high standard of ethical conduct.

In order for codes of ethics to be effective, however, involvement and support must come from the top management of the organization in the form of time, money and resources. If corporations expect their employees to follow certain codes of conduct, then management must lead by example. They should extend empathy, respect, fairness, loyalty and equity to their employees as well as their clients. In a best case scenario, the corporation will find a balance between the needs of its employees and the needs of the company.

Many businesses have a written code of ethics which is rarely discussed or invoked. This makes it difficult for employees to follow it. However, some companies actually hold ethic training classes or seminars that teach proper ethical behavior.

A written code of ethics that is buried in a company manual, but seldom discussed, is not likely to be taken seriously by the employees of the company. This is especially true when management does not appear ethical themselves. When ethical codes are clearly stated and demonstrated by management, staff persons are more likely to behave ethically themselves because they know it is expected. Employees certainly want to be recognized, so it simply makes sense for management to recognize ethical behavior. Such recognition will promote ethical behavior among the employees, which will benefit the company itself. On the other hand, if top management seems only to recognize sales without any concern as to how they are achieved, that message will be clear to the sales force as well.
Sometimes ethical behavior is aided by advancing technology. People may act more ethically simply because they realize that their chances of being caught in unethical actions are greater today than in the past. Today, with the aid of computers, information is much more available to a greater number of people almost instantaneously. In other cases it may be easier to be unethical when dealing with a person by phone or the internet since the agent doesn’t have to face them in person.

In the insurance industry there are a variety of organizations dedicated to professionalism. Each has its own code of ethics which bolster the efforts of the NAIC and state government to regulate areas of the insurance industry that are key in its ability to serve the public fairly.

Here are some of the points commonly included in codes of conduct for members of professional insurance organizations:

- Place the customer's interest first
- Know your job - and continue to increase your level of competence
- Identify customers' needs and recommend products and services that meet those needs
- Accurately and truthfully represent products and services
- Use simple language; talk 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 public's trust and confidence is enhanced by an insurance agent's adherence to a code of ethics provided by a professional association or organization. When insurance professionals strive to live by these ethical guidelines, they strengthen the status and standing of all insurance professionals in the eyes of the public.

**ETHICS AND THE INSURANCE INDUSTRY**

Some people today feel that ethics and business cannot coexist, especially in the insurance business. A goal of all businesses is to be profitable. As long as these profits are achieved ethically, ethics and business definitely can coexist. Being successful is not unethical. It is obviously vital for all businesses to be profitable to be successful. However, this success should not alter the ethical standards within the company.

Many people believe that the primary cause for unethical behavior in the insurance industry is the fact that most agents are paid by commission based on sales. They believe that commission sales cause agents to feel that they must do whatever it takes to make the sale.
Commission sales are ethical as long as they are structured properly. Profits, commissions and ethics can all coexist. The problem is the people and companies that abuse the system.

While most companies do believe good ethics and good business go hand-in-hand, they don't always acknowledge or reward ethical behavior with the same emphasis they reward high sales volume. Ethical behavior should be recognized and rewarded. This in turn leads to more ethical behavior which benefits everyone, including the company. When the only behavior that is rewarded is sales volume, employees will learn quickly to make a sale by any means.

Statistics show that one out of every five employees in the insurance industry is aware of at least one ethical violation by their peers or managers over the past two years. Working in the insurance industry, people often model behavior that happens around them. When their peers and people around them do not consider ethics important, they will eventually lose sight of ethics and its importance.

If company leaders don't exhibit the behaviors and decisions of high integrity, the company's employees aren't going to do the right thing. Leadership is critical to build an ethical organization, however, for an industry to make significant strides ethically each person, individually, must commit to doing what is right. Not just in order to meet compliance regulations, but because it is good business and more important, because it is the right thing to do.

The insurance industry also depends upon the consumer to act ethically when disclosing personal information, it depends upon the agent to relay that information correctly to the underwriters and it depends upon the insurer to keep their promises in the contracts. The claims process is especially dependent on ethical behavior. Many fraudulent claims are submitted each year, which drives up the costs for insurance protection. Many ordinarily law-abiding consumers feel it ok to file false or inflated claims.

PUBLIC EXPECTATIONS AND THE INSURANCE INDUSTRY

Negative Perception of the Insurance Industry

The insurance industry has suffered many image problems in recent years, some deserved and some undeserved. In public opinion polls, insurance agents routinely end up at the bottom of the list. The unethical and misleading sales practices of some of the largest insurance companies and brokerage houses has significantly affected the public image of the insurance and investment business. As a consequence, consumers do not feel that insurance companies and their representatives consider ethics to be a high priority. Many consumers feel that ethical behavior in the insurance industry only exists because, and to the extent that laws mandate it.

For decades, the insurance industry was one of the most trusted financial institutions in the nation. In the 1930s and 1940s, the public's confidence in the securities industry was shaken by the stock market crash of 1929 and the long depression that followed. During that period, when people lost their life savings due to a number of banks and savings and loans folding, insurance companies remained financially sound.

Offering that kind of stability and service enabled the insurance industry to enjoy tremendous growth. Whether the insurance industry can maintain that rate of growth will depend to a large
extent on whether it can continue to earn the public's trust. Continued adherence to the highest ethical standards is essential.

When insurance policy owners are asked about their own agent, most have favorable comments. However, when asked about insurance agents in general, most people feel that the majority of insurance agents are inclined to put their own interests ahead of the people they are supposed to serve.

A relatively few individuals who act with little regard to ethics can damage the reputation of the entire sales force of the insurance industry. Each individual agent's actions are extremely important to the public perception of the industry. By being scrupulously honest in all their dealings, agents can establish the necessary relationship of trust with their clients.

The field of insurance is one where public expectation and opinion are extremely important to everyone involved. Many people look to insurance to provide them with a sense of security and assurance. When they buy insurance many people think, “Now I don’t have to worry; everything will be taken care of.” Insurance is only a partial solution, however, for the uncertainties that the world presents. Many ethical and legal concerns with insurance exist because of this gap between consumer expectations and genuine insurable risk.

People are often disappointed, angry or disillusioned to find that the insurance they have been paying for does not cover a particular situation. This can leave consumers feeling that insurance is a “rip-off”. Not meeting a customer’s expectations can be frustrating and dissatisfying to both the clients and the agent. Because of this difference between what people expect and what insurance provides, insurance is one of the most highly regulated industries in the U.S. It is one of the few industries that is primarily regulated at the state level with 51 different sets of laws and regulations governing insurance (including the District of Columbia).

**Insurance is an Essential Product – A Necessity**

Insurance is a formalized way for people to come together and help each other. In today's society, both individuals and businesses depend on the insurance product to provide essential services and protect them from financial disaster:

- Health insurance provides access to quality medical care.
- Life insurance proceeds support families, educate children, and assist in the perpetuation of a business.
- Property coverage is an integral part of every mortgage contract.
- Some casualty policies (automobile and workers' compensation, for example) are required by law. In modern society, insurance has become a necessity.

Very few people would have surgery, ride in an airplane, get on an elevator, eat in a restaurant or drive cars, if there was no insurance in place. In many cases, without insurance they could not enter into business. Without insurance one mistake could bankrupt a business and shatter customer confidence. Insurance not only provides protection to the consumer, but also allows people to conduct business offering important products and services to consumers.

Insurance alone cannot save a life, but it can pay for the medical treatment that will. Insurance can help keep families together. It can permit a widowed mother to raise her children without
taking a job. It can replace the income of a disabled breadwinner, send a son or daughter to college, or pay for quality medical and legal care.

Insurance cannot eliminate liability or prevent lawsuits, but it can protect the owners of homes, automobiles, and businesses from the adverse effects of lawsuits. Without insurance it might not be feasible to face the risks involved in owning a home, operating an auto, or running a business.

Insurance does not prevent property from being damaged or destroyed, but it can replace a dwelling destroyed by fire or windstorm so that a family will have an adequate place in which to live. It can, protect the individual, the family and the business from financial ruin.

**Trust**

All business transactions are based to a certain extent on trust. People don't like to have their trust violated. Businesses become successful by providing value and taking care of their customers. That's especially true in the insurance business. The success of the insurance industry depends on individuals who are both knowledgeable and ethical. People want to do business with someone whose integrity is unquestioned.

The insurance “product” is basically an uncertain promise that the insurer may never be called upon to fulfill. The value of the promise is based on the trust of the policyholder in the insurer. However, Gallup polls since 1977 have consistently ranked insurance sales persons among the lowest in terms of perceived honesty and ethical standards.

There's much more at stake with an insurance policy compared to most purchases. If a travel agent does not do a professional job planning a vacation, he or she may ruin a week or two of their client’s life. If an insurance agent does not do a professional job, their client's may never recover financially.

In addition, a tangible product like a car can be physically inspected, but with an intangible product like an insurance policy, a consumer is buying a promise that may not need to be fulfilled for years in the future. It takes a lot of trust to trade today's dollars for that kind of product.

Trust is an important factor in the purchase of insurance. Although modern insurance contracts are easy-to-read, they are not easy-to-understand. Few insureds read their policies and those who do, seldom understand what they are reading. Most people buy their coverage based on trust. They trust the agent to recommend and procure appropriate coverage. They trust the insurance company to pay claims. It is imperative that individuals, working in the insurance industry, maintain a high ethical standard.

Insurance is a complex product. Consumers are generally not in a position to evaluate their own needs and choose an appropriate solution. The customer trusts the agent to assure that the product meets their needs. Customers depend on the agent's specialized knowledge and skills, and agents shouldn't take unfair advantage of that trust.

Clients must reveal a great deal about themselves to their insurance agent, everything from the state of their health to their financial worth. Insurance agents know more about their clients than do many of their friends, and trust is essential for the relationship to work.
It is the potential abuse of power that ethics are designed to prevent or limit. The limitations and restrictions on the agent must not be so great as to be unenforceable, unrealistic, and impractical as to prevent the agent from performing their duties to the client.

The potential for abuse of power and knowledge led to the development of rules which are often called ethical standards. Sometimes, these ethics are written standards, which may be mandated by law on either a local or federal level. The premise upon which these laws and ethics must be based, is that power must be exercised in the interest of the clients and not solely in the best interest of the professionals themselves.
ETHICS FOR INSURANCE PRODUCERS

In this section we are going to look at some of the legal and contractual relationships of the insurance business. We will be studying the unique role that insurance producers play and the part ethics plays.

TYPES OF INSURANCE PRODUCERS

Insurance agents, brokers, and solicitors are categorized by their function in the industry, as well as the line(s) of insurance they are licensed to sell.

Some producers are licensed in more than one capacity and for more than one line of insurance. In this case, an agent must be careful to follow the rules for the specific activity they are performing. For example, a person licensed as both a life agent and a property-casualty agent can bind coverage for auto or homeowner’s coverage but not life insurance.

Line of Insurance

Life and Health (L&H)

Life and health agents represent the insurer to the buyer with respect to the sale of life and health insurance products. The agents are appointed by the insurer and usually the agent’s authority to represent the insurer is specified in the agency agreement (contract) between them. Life and health insurance agents generally do not have the authority to issue or modify insurance policies, but are authorized to solicit, receive, and forward applications for the contracts written by their companies.

The agent may collect the first premium due with the application, but usually not subsequent premiums (except for industrial life insurance). The insurance company approves and issues the contract after receiving the application and premium from the applicant through the agent. The agent cannot bind coverage. This means that a life and health agent cannot commit to providing insurance coverage on behalf of the insurance company.

Property and Casualty (P&C)

Producers in the property-casualty field may be one of two types: (1) those who have the authority to bind the companies they represent; or (2) those who cannot bind coverage or issue policies because they do not represent insurance companies. Some states also have licenses for solicitors or limited agents who must usually work under the authority and supervision of a licensed agent or broker.

Function & Authority

Agents vs. Brokers

It is difficult for most insureds to tell the difference between an insurance agent and an insurance broker or to understand how that difference impacts them or the sale. Basically, an agent acts under specific and delegated authority from the insurer while a broker acts on behalf of the insured.

Insurance agent
An insurance agent is someone who solicits insurance or who aids in the placing of risks, delivery of policies or collection of premiums on behalf of an insurance company. Property and casualty agents are appointed by property and casualty (liability) insurance companies. Usually P&C agents may bind or commit their companies by oral or written agreement. A binder is a temporary contract, usually providing coverage for a short period of time (commonly 10 to 90 days, depending on the state) pending the issuance of a policy. Coverage under a binder usually ends when coverage begins under a policy. To avoid any dispute, the agent who gives an oral binder should immediately record the effective date of coverage, the terms of coverage, and the names of the parties (insurer and insured).

Property/casualty agents may sometimes inspect risks for the insurance company and collect premiums due, and may be authorized to issue some types of insurance contracts (policies) from their own offices.

The acts of agents are binding upon the company only to the extent specified in their contracts or that they are otherwise authorized to do so. Agents cannot delegate their rights or powers unless expressly authorized. Agents act in a fiduciary capacity and occupy a position of special trust and confidence in handling or supervising the affairs or funds of another.

**Insurance broker**

Unlike an agent who represents an insurance company, an insurance broker legally represents the insured or applicant. A broker acts as an independent contractor and does not have the authority to bind the insurer. In some cases, brokers are also licensed as agents who have the authority to bind the companies which have appointed them as agents and may attempt to place business with more than one company. A broker is paid commissions by the insurers where the business is placed.

Brokers must be licensed and their routine activities and functions are similar to that of agents. Brokers solicit applications for insurance, may collect the initial premium, and deliver policies.

A broker's primary responsibility is to his or her client. Brokers serve their clients by finding the appropriate insurance coverages to meet the clients' needs. The broker is prohibited from engaging in any marketing practice that involves unfair competition or a deceptive act. Like agents, in most states brokers are required to take continuing education (CE) to remain knowledgeable and current in areas that pertain to insurance principles, coverages, laws and regulations in order to retain their license.

**Insurance solicitor**

A solicitor is a salesperson who works for an agent or a broker, most commonly in the property and casualty insurance field. Depending on the state, the solicitor may be required to obtain an agent's or broker's license, or may hold a special solicitor's license. Solicitors normally have a working agreement with a single agent or broker specifying that the solicitor's primary functions are to solicit insurance, collect initial premiums and deliver policies. Solicitors cannot usually bind coverage.

**Insurance Consultant or Analyst**

A relatively small group of insurance professionals are licensed as insurance consultants or analysts. Generally they are not paid by commission for the sales of insurance policies.
Instead, they work strictly for the benefit of insureds and are paid a fee by the insureds they represent. In most states, it is illegal to charge a fee and represent oneself as a consultant, analyst, advisor or other similar title without holding the proper license. This differs greatly from one state to another.

**Excess or Surplus Lines Brokers (E & S Bokers)**

An Excess or Surplus lines broker is a person licensed to place coverage which is not available through insurers licensed in his or her state through insurers not licensed to do business in the state where the broker operates (non-admitted insurers). These individuals specialize in lines that are difficult to write, due to high loss frequency or severity potential. In some cases, brokers dealing with these hard-to-place risks will use markets such as Lloyd's of London or coverage may be placed with non-admitted insurers. Most states require excess or surplus lines carriers to be specially licensed and to follow strict rules.

**General Agents and Managing General Agents**

Although no special license is required, an agent who hires, trains and supervises other career agents within a specific geographical area, is referred to as a general agent (GA) or managing general agent (MGA). The MGA is compensated by commissions earned on business he or she sells as well as overrides on the business produced by the other agents managed by the general agent. An MGA may receive additional compensation for administrative and service functions performed for policyholders.

**Agency Relationship**

The extent of any agency relationship between the agent and insurer beyond collecting the premium and delivery the policy is governed only specific agency agreement or binding authority.

**Exclusive vs. Multiple-Company Representation**

Whether an individual represents one insurer or works with a number of insurers; from the agent's point of view, they have an ethical obligation not to take any action that might impute liability to any company they represent. Agents serve their own best interests in avoiding liability for their companies, since they become liable to their companies for any damages that they cause. Approximately one fourth of all E&O claims filed are those where an insurance company is suing their own agent- usually for exceeding the authority given them in their agency contract.

Multiple-company representation may create questions about which insurer is responsible for an agent's activities. The situation is not at all clear when an agent represents more than one company. For this reason it is extremely important for agents to document any transactions for clients and show which insurer they are finding coverage with.

For many years, exclusive representation was the norm in the life insurance industry and to a large extent it still is, especially for new agents. However, multiple-company representation is more common than it used to be even in the life side of business. Agents may represent more than one company in order to offer a wider range of products to their prospects and clients.
Property and casualty insurance is marketed by independent agents, exclusive or captive agents, and brokers. Exclusive agents sometimes offer insurance at a lower cost, due to lower commissions and reduced expenses resulting from centralization of underwriting, policy issuance and claims processing. Independent agents and brokers offer insurance consumers the most options, because they work with multiple insurers. The agents have a wider choice of coverages, prices and services for their policyholders. Historically, independent agents have been the predominant producers in the property-casualty field.

**Exclusive or Captive Agents**

Exclusive or captive agents represent only one insurance company or one group of companies. These agents are paid a salary, commission or a combination of both. Under restrictions imposed by the insurer, the insured is considered to be the company's client rather than the agent's. Companies using captive agents own and control the account, policy records and renewals. If the agency relationship or employment of a captive agent terminates, the agent loses all rights and interest in the renewal business and related commissions.

These agents are sometimes referred to as career agents. Most often, these captive or career agents are compensated by commissions. New agents may also be paid a training allowance for several months which serves as a salary for a limited period of time during which the new agent is being trained. Most companies will require that the career agent validate this training allowance by producing a certain amount of new business each month. In some cases this is referred to as a 'draw' which is actually a loan taken against future commissions.

The contract an agent has with his or her company may require the agent to give the company "first right of refusal" on all of the agent's business. If the company does not wish to insure a particular applicant, the agent may then be free to submit the business to another company.

In addition, a captive agent has the ethical obligation to inform his or her company about any other related service he or she provides and for which payment is received including. The insurer can then determine if there is a conflict of interest.

**Independent Agents**

Independent agents are independent businesspeople who represent several insurance companies, pay all their own agency expenses and make all decisions about how their agency operates.

Independent insurance agents sell their clients the policy that fits their needs best among the many insurers they represent, and are paid a commission for each sale. The independent agent owns the expirations of the policies he or she sells, meaning that that agent may place that business with another insurer at renewal if in the best interest of the client.

Although the independent agent is free to place business with the insurer who best meets the prospects needs, conflicts of interest may arise because independent agents usually must place a specified amount of business with each insurer in order to maintain their appointment. For example, assume an agent must write ten new homeowners policies with a particular insurer each month. To assure that this quota is met, the agent may be tempted to only offer new clients a quotation from that company rather than "shopping" around with several companies. In some cases, the client might be better served by another insurance company that offers more or different coverages. However, if the agent loses the appointment with that
insurer, all of the policyholders covered with that company may have to be replaced with other companies that do not meet their needs as well.

Although the agent represents the insurer, he or she must also attempt to serve each client by providing the best coverage at the most competitive premium. The agent may feel torn between serving the insurance company and the client because generally an agent cannot act as an agent for both parties in a transaction. Conflicts can be avoided if the independent agent follows the guidelines that apply to 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, in claims settlement or other insurer-related activities.

- The agent represents his or her client only during the process of helping the client select the insurance plan best suited to the client's needs. It is up to the agent to see that the policy is written properly so that coverage applies where and when needed.

**Direct Writers**

A direct writer is an insurance company that sells its policies through employees. These agents usually receive a salary, or a salary plus commission for the business they produce. Most commonly policies are solicited and sold through the mail on the phone, or over the internet. A direct writer maintains complete control and ownership of its policies and renewals and no ownership rights exists for the agent.

**AGENCY LAW PRINCIPLES -- THE CONCEPT OF AGENCY**

The relationship between an insurance agent and his or her company is governed by the concept of agency. Agency is a relationship in which one person is authorized to represent and act for another person or entity. An agent is a person authorized to act on behalf of another person, who is called the principal. An insurer appoints licensed insurance agents to represent its interest to the insurance buying public. Insurance agents, acting for the insurer, establish insurance contracts with the general public on behalf of the insurer. In the insurance field, the insurer (the principal) authorizes agents to carry out certain activities which are then legally binding upon the principal.

The agent's actions are considered by law to be those of the principal when the agent is acting within the scope of his or her authority. Both the principal and the agent may be individuals, corporations or partnerships. Since an insurance agent acts for the insurer/principal, in the minds of clients the insurance agent often becomes the company and the agent has a serious ethical responsibility to do nothing which will cause harm to the principal.

**THE THREE TYPES OF AGENCY**

There are three ways to form an agent/principal relationship:

- Appointment
- Estoppel
- Ratification
Agency by Appointment

When a principal and an agent wish to enter into an agreement to create, modify or terminate contractual relations with a third party, they usually enter into an explicit contract for that purpose. A contract defines the specific authority the principal gives to the agent to use on its behalf. In most cases, the contract will be in writing, but it is not always legally necessary to do so. This is the usual way in which agency is created.

Agency by Estoppel

In some cases, an agency relationship may be created without an express agency contract. Although an individual or legal entity acting on behalf of a principal does not in fact have the legal authority to do so, the principal has allowed a situation to develop in which innocent third parties assume the agent does in fact have proper authority and enter into a contract with the principal. The principal may then legally be estopped (barred) from claiming that the agency did not in fact exist.

In order for agency by estoppel to exist, three things are required. First, the principal must act in some way to create the appearance that an agency relationship exists. Second, an innocent third party must have been misled by the principal's actions and made to believe that an agency relationship exists. Finally, the innocent third party may be injured by acting in the belief that an agency relationship exists.

Agency by Ratification

Agency may also be created by ratification. This describes a situation in which someone acts as though he or she has a principal’s authority to act on its behalf, when no such authority actually exists. But if such an individual performs an act that is seen as beneficial to the principal, the principal may ratify that act, and the presumed authority behind it. Basically, ratification results when the principal later formally sanctions the previously unauthorized actions of an agent. Ratification of unauthorized acts of an agent can be sufficient in some cases to release the broker/agent from liability to the principal.

AUTHORITY OF AN AGENT

The concept of authority is related to the concept of power. Before an individual can act as an agent and establish contracts between the principal and third parties, he or she must have the power, or authority, to do so. In the case of an insurer and an agent, this power is granted through an agency contract. Naturally, there are limitations on an agent’s authority. The ethical significance is that an agent must, first and foremost, serve the insurer, live up to the contract and operate within the scope of his or her authority.

When agents act within the scope of their authority, the acts of the agent are considered to be the acts of the principal. Under certain circumstances, companies can be held liable for illegal or other unauthorized actions taken by an agent.

If an agent's unauthorized actions end up costing the company money, the agent can be liable to the company for the amount of the loss. For this reason, it is in both the company's and the agent's best interests for agents to be careful not to take any actions that would impute liability to their companies.
From a legal standpoint, agents are considered to have three types of powers:

- Express authority
- Implied authority
- Apparent authority

**Express Authority**

Express authority refers to those particular actions the agent can and cannot perform for the principal. Agents are given expressed powers in a written agency contract and in written underwriting instructions from the company. These expressed powers specifically authorize certain actions on the part of the agent.

Insurance agents normally have the express authority to solicit applications; describe various coverage/policies to clients; discuss the process by which coverage is purchased; collect premiums and service policies once placed. Some agency agreements give the agent express authority to issue policies; cancel policies; retain a commission from the premiums collected.

It is very important for an agent to know the limitations of their agency contract and to operate within those limits. To do otherwise could place the agent in a position of personal liability. The agent must constantly be alert to the consequences on the insurance company of his or her actions and words.

**Implied Authority**

Implied authority refers to actions that are associated with the actions that are expressly authorized. These powers are implied by the requirements of their agency contract, though these implied powers are not specifically expressed or written.

To show that an action was taken by the agent under implied authority, the agent must show that the act they performed was directly related to, and necessary because of, an act that they are expressly authorized to do by the insurer.

**Apparent Authority**

Apparent authority is the authority the agent seems (appears) to have because of certain actions undertaken on his or her part. This action may mislead applicants or insureds, causing them to believe the agent has authority which he or she does not, in fact, have. An insured may rely on powers the agent seems to have, although those powers are actually outside the scope of the agent's expressed or implied authority. The principal may add to this assumption by acting in a manner that reinforces the impression of authority.

If a company supplies an individual with forms, manuals, and other materials (known as signs and evidences of authority) that make it appear that he or she is an agent of the company, a court will likely hold that a presumption of agency exists. The company is then bound by the acts of this individual whether or not he or she has actually been given this authority.

**Limitations on Authority**
Rarely, if ever, is an agent's authority to act for a principal unlimited. In most agency relationships, an agent's activity is restricted to some extent. Typically, the limits to an agent's authority are spelled out in the agency contract, and it is within those limits that an agent must act. For example, while an insurance agent is authorized to solicit applications and may even bind coverage in some cases, the final decision to accept or reject the risk lies with the insurance company's underwriter. Also, the amounts and types of insurance the agent can bind will he solicit to limits as well.

In addition, an insurance agent cannot modify a contract or waive exclusions, unless that authority is granted under the terms of his or her agency contract, and most state laws specify that this is a "nondelagable duty," something that only the insurance company can legally do, and only in writing. An insurance agent also cannot adjust premium rates. This act is reserved for the company.

SELECTING INSURANCE COMPANIES TO REPRESENT

As agents and the general public have become more educated on the variety of options available, the perception of insurance has changed. While price has always been considered, additional elements are now commonly looked at as well. Consumers want to know if the company they are considering can manage its expenses, and investment returns in a way that allows the company to make good on the promises made in the contract in the future.

Agents are expected to place coverages for their clients with financially sound insurance companies. In spite of the fact that agents are not actuarial experts, agents are increasingly being expected to monitor the continuing financial solvency of the companies with whom they have placed business.

An agent has a duty to act with a degree of care that a reasonable person would exercise under similar circumstances. This prudent person rule states that persons engaged in activities that can result in harm to others or their property must exert reasonable care in the exercise of their duties.

The reasonable care standard requires agents that take into account the factors in their clients' lives that might affect their ability to handle their own affairs effectively and efficiently, and deal with other matters arising from the coverage they have bought.

DUE DILIGENCE IN BUSINESS

One area of ethical behavior that should not be overlooked deals with due diligence. Professional agents prefer to deal only with financially sound companies, but many agents may not know how to evaluate companies.

For the agent, due diligence is the analysis of a particular company's products, performance and financial standing. Insurance makes long-term promises to clients. It is vital to those clients that the company be able to keep those promises. Due diligence is the agent's analysis of whether or not the company can, in fact, keep their promises.

In the public's view, the level of service and quality of the advice given are linked directly to the insurance company and that company's performance. Practicing due diligence protects the agent, as well as the consumer. When an agent takes the time to investigate his companies (and document that investigation), he or she is protecting their own financial future along with
that of his or her client. Due diligence is, of course, an ongoing process since companies can and do change over time.

It is common for an agent to go to work for an agency and simply accept whatever companies the agency is appointed with. While we would like to assume that an agency has done their homework, this may not always be the case. In addition, it is possible that the agency viewed the companies and products only from a point of view of how much commission and other compensation they pay. An agent who bases his or her company affiliations on commission levels, leads provided, or where the next convention will be held, may very well be in trouble down the road.

In recent times, agents are being told that due diligence is their responsibility. Often the result of court actions, it is now being legally determined that individual agents are responsible for the recommendations they give, the products they sell, and the companies they represent.

In the property, casualty and liability fields, major disasters, such as earthquakes and hurricanes, can cause company failures if financial resources are not adequate. Insureds who are not sold enough or the right kind of insurance may never recover from a business or personal property of liability loss.

For the insurance company, due diligence is an ongoing process which insures that pricing objectives are being realized, and that integrity and consistency of internal procedures are being maintained. It is working with the agents and agencies, as well as their policyholders, to preserve fairness in all parts of the operation. For the company, due diligence also means making investments that are sound and prudent.

There are many ways that an insurance company can get into trouble. Usually it is a combination of problems; seldom one problem alone. Perhaps losses greatly exceed gains and capital and surplus are consumed. When money goes out faster than it comes in, no business or individual can run efficiently. When this happens, policyholders may begin to withdraw their money, which only intensifies the existing problems. This downward spiral is what caused the eventual collapse of many savings and loans in the 1980's and '90's.

**FINANCIAL STRUCTURE OF INSURERS**

It has become increasingly difficult to predict the amount of loss reserves that an insurer must hold in order to maintain financial security. This is especially true for property and casualty companies because of liberalization of insurance contract interpretations by the courts and the expansion of tort liability. Insurance companies have the potential of much larger losses in today's world than was present in the past when the policy was priced and the premiums were collected.

**FISCAL STABILITY OF INSURER**

An insurer’s fiscal stability rests upon its ability to accurately calculate the monetary amount of the risks it assumes through the policies it issues and to charge rates which balance that sum, all within the rating regulatory framework governing the industry. The carelessness of agents in dealing with applications and premiums could harm a company and in turn its insureds. Agents have an ethical responsibility to the insurer to be aware of the effects their activities may have upon its fiscal stability.
The life insurance industry has become increasingly complex with the advent of investment oriented life and annuity products, interest rate volatility, the reduced certainty of future cash demands and growing policyowner and public perception. The banking systems financial problems have added additional stress as policyholders feel less secure about major institutions, including insurance companies. All of these factors have affected the credibility of even well-established insurance companies.

Gathering Company Information

An agent must begin his due diligence process by gathering information on the major components of the company from as many sources as possible. This would include seeking information directly from the company, talking to their immediate manager or regional manager, the home office (especially the underwriting department), and even the company's competition.

An agent can often learn a lot from simply asking other agents who have been with the insurance company for a relatively long period of time. Find out about the speed of the company's claim service since this is often an indicator of company solvency problems. Find out if commission checks seem to be consistent, correct and on time.

Statutory Financial reports

Each year insurers are required to file a statement with the Commissioner describing their financial condition and affairs as of the previous year. The statement must show the insurer's capital stock and paid-in capital, if any, its assets, liabilities, income, expenditures, reinsurance, and premiums. It must include a balance sheet of all business. The Commissioner may also request that insurers file additional reports during the year. These reports are available to the public in most cases.

The agent should collect the financial statements of his or her insurers and study them. Does the company seem to be making excessive profits or does it company seem to be making too little profit to ensure survival? Compare the company's surplus in relation to the amount of business being produced to see if it falls within acceptable guidelines. Ask the state Insurance Department to see if there are any watches or cautions outstanding. Check the number of consumer complaints the company has experienced in the past year as well as in a three year period to see if any pattern seems apparent. The agent may also want to watch for any shifts or may exodus in the management of the company which can change the philosophy of the company and even show that there are problems when the “rats start leaving a sinking ship.”

Insurance Company Rating Services

Several organizations rate the financial strength of insurance carriers, based on an analysis of a company's claims experience, investment performance, management, and other factors. These organizations include A.M. Best Company, Standard & Poor's Insurance Rating Services, Moody's Investors Service, Duff & Phelps Credit Rating Company, and Weiss Ratings. These ratings are one of the most widely used indicators of financial health (or the lack of it) in the insurance industry.

The objective of the rating services is to evaluate the factors which affect the overall performance of the insurance companies. By doing so, they provide their opinion of the company's financial strength, operating performance and ability to meet its obligations to the
policyholders. The procedure includes both quantitative and qualitative evaluations of the company's financial condition and operating performance.

Each firm uses a different methodology for evaluating the financial strength of insurance companies and the firms don't all do business in the same way.

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<th>Firm</th>
<th>Scale, Highest to Lowest</th>
</tr>
</thead>
<tbody>
<tr>
<td>Standard &amp; Poor's</td>
<td>AAA, AA+, AA, AA-, A+, A, A-, BBB+, BBB, BBB-</td>
</tr>
<tr>
<td>Duff &amp; Phelps</td>
<td>BB+, BB, BB-, B+, B, B-, CCC, CC, D</td>
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<tr>
<td>Moody's Investors Service</td>
<td>Aaa, Aal, Aa2, Aa3, A1, A2, A3, Baal, Baa2, Baa3, Bal, Ba2, Ba3, Bl, B2, B3, Caal, Caa2, Caa3, Cal, Ca2, Ca3, Cl, C2, C3</td>
</tr>
</tbody>
</table>

A given rating is meaningless, even misleading, if it is not viewed within the context of the scale. For example, an "A+" rating sounds like it belongs at the top of a scale, yet it is a top rating only if the rating service it comes from is Weiss. If it comes from A. M. Best, it is the second highest rating. If it comes from Standard & Poor's or Duff & Phelps, it is the fifth highest rating. Similarly, a rating of "A1" sounds like it could be the top of the scale. But it is the fifth highest rating from Moody's Investors Service.

In addition, it is helpful to know what percentage of the companies rated by a given service earns that service's top rating. A.M. Best and Weiss both rate hundreds of companies. For A.M. Best, fewer than 10% of those companies earn its top rating of A++. For Weiss, less than 1% of companies earn its top rating of A+. Standard & Poor's, Duff & Phelps, and Moody's, the fee-based services, rate only a fraction of the companies rated by A.M. Best and Weiss. For Standard & Poor's, about 30% of companies earn its top rating (AAA), and for Duff & Phelps, a little over 20% earn the top rating (also AAA). For Moody's, 15% of the companies it rates earn the top rating of Aaa.

Agents have an ethical duty not only to disclose facts, but to make sure that clients understand what those facts mean. In addition, since ratings from two or more services are available for many insurance companies, agents should disclose all the ratings of which they are aware, not just the most favorable ones.

If a financial rating changes after a client has purchased a policy agents may have an ethical obligation to disclose the change. If the change in rating is a sign of a material risk to the client, agents would have an ethical obligation to disclose the change. If it is serious enough that the agent himself or herself would be concerned about it, then the agent should provide that information to clients.

Guaranty Associations

Protection against insurer insolvency is one of the principal concerns of regulators in the insurance industry. Insurance insolvency regulations govern areas such as the organization and ownership of a new company, capital and surplus requirements, reserves, accounting,
investments, annual statements, and the rehabilitation and liquidation of impaired insurers. In addition to these areas of regulation, insurance departments in many states have adopted regulations for the establishment of guaranty associations in the event that an insurer does, in spite of regulations and precautions, become insolvent.

State Guaranty Associations are organized to protect claimants, policyholders, annuitants and creditors of financially impaired or insolvent insurers by providing funds for the payment of claims and other related policy benefits. The Associations are composed of the insurers authorized to transact a particular line of insurance business within the state. Member insurers are assessed certain sums of money (usually based on the percentage of premiums each insurer writes in the state) to cover the Association's operating expenses. If an insurer insolvency does occur, each member insurer is assessed additional fees to cover the insolvency.

Most states prohibit insurance agents from referring to the existence of Guaranty Associations during the insurance advertising or sales presentation, in order to prevent misunderstandings on the consumers' part that their insurance policies are "guaranteed" or "insured" in the same way that bank deposits are insured by the FDIC. Agents must walk a fine line between accurately disclosing the existence and purpose of a guaranty association without in any way implying that the insurance product being sold is a "safe investment" because of the existence of the guaranty association.

**Unauthorized Insurers**

By law, only insurers that have been authorized or admitted by a state may issue policies in that state. Consequently, an agent must make sure that the insurers he or she represents are licensed to do business where solicitation is made. State guaranty funds provide a means for paying at least part of an insured's losses if his or her property-casualty insurer becomes insolvent and is unable to meet its obligations to its policyholders. The amount of reimbursement is subject to both a deductible and a limit of liability, depending on the state. Generally speaking, a state's guaranty fund only covers the liabilities of authorized (admitted) insurers, so anyone purchasing policies from unauthorized or non-admitted companies would be at risk if those insurers could not meet their claims. Some states hold the agent or broker personally liable for any insurance contract he or she places with a non-authorized insurer.

**Commissions**

The commission structure that has been set up by the insurance companies has been blamed as one of the primary cause for many of the ethical problems within the industry. The whole insurance sales compensation system revolves around commission earnings. The agent makes a sale and earns a commission. The sales manager may earn an override on the agent's commission. The measuring device for success is the number of sales made and the commissions earned.

Agent commissions are generally based on the amount of the premium. At the inception of the policy, the premium is largely unearned. It isn't until the end of the year that the annual premium is fully earned by the company. Yet on some policies the agent's commission is paid on the full, unearned premium collected at the beginning of the policy period.

By paying higher commissions up front for new business companies effectively give agents an incentive for violating ethical rules such as those prohibiting unnecessary policy replacement.
Insurance companies who use a level commission structure report improvements in both policy persistency and agent recruitment and retention.

The commission structure of most companies places the agent in the ethical dilemma of selling "higher commission" products in lieu of policies which may better serve the client's needs. For example, whole life with a higher commission may be sold in smaller amounts instead of larger quantities of lower commission term insurance. Property and casualty lines also involve incentives to use one company over another on the basis of commissions, bonuses, and other compensation.

Another ethical problem can arise because agents are compensated only if an applicant is approved for the insurance and a policy is issued. The agent may be tempted to alter or omit material information on the application or simply not tell the truth so that the policy will be approved.

Disclosure of commissions is a topic of continuing discussion in the insurance industry. It is a difficult issue, since there are good reasons both for and against requiring agents to disclose commissions to clients.

Some consumer groups wonder whether the insurance industry has something to hide. Commission disclosure seems to be reasonable since the amount of commission may give some indication of how much the agent expects to benefit from the transaction. In addition, disclosure of commissions and acquisition costs is a standard requirement in other areas of the financial services industry.

Required commission disclosure might cause changes in commission structures, especially in the life insurance industry. Instead of high first-year commissions, products might be designed to pay level commissions for a period of five or ten years, or deferred commissions, a portion of which would be forfeited if the policy did not stay on the books for a certain number of years. Some believe that such a commission structure would make agents more service-oriented, which would be of benefit to the public.

At this point, agents aren't legally or ethically bound to disclose their commissions, but some agents do so voluntarily. It demonstrates to clients that the agent is being straightforward about all aspects of the transaction. Clients appreciate being able to evaluate for themselves the extent to which the agent may be operating out of self-interest or out of a concern for the best interests of clients. More often than not, clients are surprised at how little commission agents actually make, especially in property-casualty insurance.

Being successful is not unethical. It would be unethical to the owners or stockholders of a business to avoid profits. Being profitable, however, should not alter other ethical concepts within the business. Just as profits and ethics can work together, so can ethics and commissions if other ethical concerns are also considered?

While "good" insurance agents are more concerned with their customers' needs and not focused on their own compensation, part of the problem is that an agent's livelihood and potential for career advancement hinge on the ability to sell and meet sales quotas.

Unfortunately sales are often made at the expense of the buyer's needs and objectives. The agent may conduct poor or incomplete fact finding and needs analysis. Out of financial desperation, an agent might resort to an unethical practice in an effort to make a sale and earn
commissions. When making sales becomes the priority, without any other aspects considered, integrity can certainly suffer.

A good deal of unethical behavior is initiated because clients are shopping for insurance based on price with little or no understanding about the difference between policies and coverages. Due to advertisements on television urging people to shop for a cheaper rate with no mention at all about coverage on quality, many agents feel that they must do whatever is necessary to provide the lowest rate, even if they have to cut corners on the coverage to do so.

Selling a lower amount of homeowner’s coverage in order to keep the premium down is dangerous. In the recent California fires over half of all homeowners were underinsured and could not afford to rebuild their homes. Agents and insurers had failed to properly determine the client’s needs. Clients shopping for the lowest price, were sold policies which failed to cover them properly when needed.

Several state insurance departments have also turned their attention to agent commission structures. Various state laws limit commissions paid on replacement policies, especially for insurance sold to seniors (such as Medicare supplement and long term care insurance).

It has been argued that eliminating the current commission structures and substituting a salary might attract a more dedicated, committed individual to the insurance business. This type of financial arrangement might also provide for better retention among agents and lower costs and expenses to the insurer.

**Capital & Surplus**

Insurers must have capital in order to cover unexpected losses. Insurers set their premiums at a level sufficient to cover expected losses. Naturally, all expected losses do not occur as soon as premium is earned, so insurers’ earned premium is in excess of claims paid out. This excess is called 'surplus,' or 'earned surplus'. If earned surplus is more than sufficient to cover future expected losses and to finance company growth, the company's directors may decide to give some portion of surplus back to policy owners in the form of a policy dividend.

Insurers are required by law to maintain certain minimum amounts of capital and surplus. If an insurer's assets minus its liabilities equals less than the sum of its minimum capital and surplus amounts, the insurer is considered "impaired" and may eventually be deemed insolvent.

**Investment of assets**

Insurers are restricted in the type of investments they can make with their general account assets (these restrictions do not apply to separate accounts funding variable contracts). Insurers may invest their minimum paid-in capital only in U.S. government obligations; U.S. Post Office obligations; Canadian or Puerto Rican government securities; state, county, municipal, road division, and school district bonds; insured mortgages; collateral trust bonds secured by authorized obligations; farm loan bonds; home loan securities; and bank or savings & loan accounts. Funds in excess of minimum capital may be invested in any of the preceding plus common stock, corporate bonds, real estate, limited partnerships, and other investments, subject to certain restrictions.
The History of Insurance Regulation

Insurance has been regulated by the states since the beginning of the industry's history in this country. Since insurance was not considered to be commerce it was not subject to regulation by the Federal Government (Congress). The status of insurance as commerce was, however, tested in 1869 in a landmark case tried in the U.S. Supreme Court, Paul vs. Virginia. The Court ruled that insurance was not commerce, and this opinion held until 1944.

In 1944 the Supreme Court, ruling in the U.S. vs. the South-Eastern Underwriters Association, said insurance was commerce, and therefore subject to regulations by the federal government. The Southeastern Underwriters case threatened to throw the insurance industry into turmoil. In response, the U.S. Congress enacted Public Law 15, better known as the McCarran-Ferguson Act. This law, passed in 1945, reserves the right of the federal government to regulate insurance in certain areas such as fair labor standards and antitrust matters. All other insurance regulation is reserved to the states.

As such, the states carry the major burden of regulating insurance affairs, including the ethical conduct of agents licensed to conduct business within their borders. Regulation of an insurance agent's ethical conduct is usually conducted through an insurance commissioner's or director's powers to oversee the marketing practices of both agents and insurance companies in that state. Many of these regulations governing ethical conduct are derived from model legislation developed by the National Association of Insurance Commissioners (NAIC).

Today there is joint federal and state supervision of the insurance industry, with the federal government exerting control in matters that are, or should be, uniform across state lines such as Medicare Supplement policies and Long Term Care Insurance. The federal government conducts insurance programs in areas where commercial insurers are unable or unwilling to provide insurance, such as federal flood insurance, FAIR plans, federal crime insurance and federal crop insurance. All other regulation is handled at the state level.

THE NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS (NAIC)

All state insurance commissioners, regardless of the title they hold in their respective states, are voluntary members of the NAIC. The organization has standing committees and works regularly to examine various aspects of the insurance business.

The NAIC has four broad objectives:

- to encourage uniformity in state insurance laws and regulations;
- to assist insurance officials in administering these laws and regulations;
- to help protect the interests of policy owners; and
- to preserve state regulation of the insurance business.

NAIC Model Laws

To promote uniformity among the various states in insurance regulation, the NAIC formulates and drafts what is called "model legislation." This term includes representative bills or statutes.
presented to the individual state legislatures for consideration and passage, creating insurance law for that state.

STATE AND FEDERAL LAWS GOVERNING INSURANCE

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." Other states refer to it as "unfair trade practices." All states have established a code of ethical standards for insurance agents through laws defining what an agent can and cannot do. These laws differ from state to state.

State laws governing insurance fall into several broad categories. Laws defining Unfair Trade Practices are most relevant to ethics. Insurance commissioners in each state are charged with:

- Investigating claims of unethical or unlawful behavior
- Overseeing the issuance of licenses
- Levying penalties for violations of ethical practice (including fines, suspension, or revocation of the agent or company to do business in that state)
- Ensuring that penalties are carried out

State insurance departments, divisions or boards operate under the direction of a commissioner, a director, or a superintendent of insurance, who may be elected or appointed. Duties and operations of the various state departments of insurance include the following:

- issuing rules and regulations;
- licensing insurers, agents and brokers;
- suggesting laws to their legislators;
- examining insurance companies' financial operations;
- approving policy forms and insurance rates; and
- overseeing advertising and marketing practices.

Although insurance companies are subject to strict government regulation, many consumer groups advocate even stricter controls over the ways in which insurers are permitted to do business. The insurance contract is extremely complicated to understand. Without regulation, unethical agents and insurers could say almost anything about their own products and those of the competition without the prospect/insured being able to determine the truth of the matter. Some have misrepresented the benefits of their policies and have refused to pay benefits which are legally due the insured.

And, because most people buy an insurance policy, stick it in a drawer and rarely look at it again, the lapse of time between the sale and the claim can work to an unethical agent or
company's advantage. Abuses may be discovered too late for any remedy to be made. For all of these reasons, regulation of the insurance industry is required.

**Laws Regulating Agent Activities**

States have passed a number of laws outlining agent responsibilities in the areas of fiduciary duty, licensing and continuing education, unfair trade practices, policy delivery, policy illustrations, replacement, disclosure, etc. Court decisions help refine the standards to which agents and brokers are held.

**Licensing of Agents**

Licensing of agents is a major method by which states regulate the insurance industry. Licensing laws require that insurance companies have a license or certificate of authority allowing them to do business in the state. And, the agents of the company must also fulfill licensing requirements before they are allowed to act for the insurer in the state.

One of an agent's most important responsibilities is to be legally and properly authorized to sell the insurance products he or she is selling. This means not only obtaining and maintaining as current the required license for the lines of insurance being sold, in all of the states in which the agent does business, but also possessing the knowledge and expertise to sell those lines of insurance, holding the proper appointments, and meeting all other legal requirements such as nonresident licensing, countersignature, bonding, etc., as set out in state law.

Any agency employees that solicit insurance business will probably need to be licensed in accordance with state law. This usually includes anyone who:

1. Takes applications for insurance
2. Receives or delivers insurance policies for a company
3. Examines or inspects risks
4. Receives, collects, or transmits insurance premiums

Agency employees who are regularly salaried clerical and administrative employees are usually not usually required to obtain an insurance license. Agents can check their states licensing laws for details.

Companies must keep accurate copies of agent licenses and other required forms, and keep accurate reconciliation records and may be penalized if their agents are not in compliance with the licensing and Continuing Education requirements of the state. The most common violations (and the most common reasons for companies receiving fines and penalties) include:

- Paying commissions to unlicensed agents
- Accepting applications from unlicensed or non-appointed agents
- Failure to notify the insurance department of appointment and termination of agents
- Paying commissions without having a copy of the agent/agency's license on file
Failure to maintain agent licensing records
Failure to hold the appropriate license or appointment, and selling coverages without proper authority are among the most common agent-related violations. If an agent was not appointed at the time of sale, the department of insurance will not hesitate to sanction both the agent and the company.

There are common state requirements for agent licensing, education, examinations, appointment, renewal, and termination, which insurance companies are expected to monitor. State licensing regulations commonly include:

- Who is eligible or ineligible to become an insurance agent
- How to apply for an agent license
- Who must take and pass a qualifying examination
- Who is exempt from the examination
- Types of licenses required
- Educational requirements
- How to maintain an insurance license
- Conditions for suspension, revocation, or nonrenewal of the license

Eligibility for License

To be eligible for a license as an agent, broker or solicitor, an individual typically must usually meet the following requirements depending on the state:

- Be at least 18 years of age
- Be a citizen of the United States, or have applied with the U.S. Department of Immigration for permanent residence with the intent to apply for citizenship
- Have been a bona fide resident of the state in which application is being made
- Be trustworthy, have a good reputation, and not have been convicted of a felony or a crime involving moral turpitude
- If applying for a brokers license, have filed any bond which may be required and demonstrate to the insurance department the necessary competency or experience
- Comply with any required prelicensing education laws and pass the required licensing examination
- Intend to actively engage in the insurance business with members of the public, and not use the license principally for transacting controlled business

Application for License
Licenses are issued upon proper filing of the application, satisfaction of statutory requirements, and payment of the appropriate fee. Applications usually require personal information including the identity, personal history, business record, and insurance experience of the applicant, along with a statement about the purpose for which the license will be used. Applications frequently include the following questions:

- Whether or not the applicant was ever previously licensed to transact any kind of insurance in any state
- Whether or not any license was ever refused, suspended or revoked
- Whether or not the applicant is indebted to any insurer or general agent
- Whether or not the applicant has ever had an agency contract cancelled

If a firm or corporation applies for an agent or broker license, similar information is required with regard to the firm or corporation, as well as the names of all members, officers, and directors of the firm or corporation. Each person who is to exercise agent or broker powers must be identified and must furnish the same personal information required of an individual applicant.

Incredibly, some of the biggest problems encountered by state regulators involve misrepresentations on the initial agent license application.

**Continuation/Expiration/Renewal of License**

Subject to continuation of the appointment and payment of the renewal fee, licenses are renewed. Appointments generally remain in effect until the agent's license is revoked or terminated or until the agent and/or insurer no longer wish to do business together. Late charges may be added to the fee if a filing of license renewal is late.

**License Authority**

It is generally assumed that anyone quoting premiums or discussing terms of an insurance contract should be licensed. However, insurance departments across the country have expanded the definition of who should be subjected to licensing as an insurance producer. Many agency principals have licensed almost all staff members, regardless of what the functions they perform. The staff of insurance companies are exempt from producer licensing while performing a wide variety of service functions.

Temporary licensing can be requested when the agency principal or owner dies to allow a surviving family to conduct business with existing clients. These licenses are usually limited in duration. Each state may have different rules.

**Notice of Appointment**

In addition to license requirements, states generally require a notice of appointment be filed with the insurance department. This document is executed between the agent and insurer and authorizes the agent to transact one or more classes of insurance business. An agent may be appointed with several insurers. Upon termination of all appointments, an agent's license becomes inactive. While inactive it can usually be renewed and reactivated by the filing of a new appointment.
Each insurer appointing an agent is typically required to file the appointment with the insurance department in writing and pay the specified appointment fee. The filing specifies the kinds of insurance to be transacted by the agent.

**Termination of Appointment**

Subject to an agent's contractual rights, if any, an insurer may terminate any of its appointed agents at any time. The insurer is required to give prompt written notice of the termination to the insurance department as well as the agent, and must file a statement of facts related to the termination and reasons for it.

The agent's license is with the state and the agent's contract and appointment is with an insurer. Depending on the state, loss of an appointment does not necessarily mean that an agent has lost his or her license. It simply means that the agent may no longer represent that particular company although he or she may still be licensed with the state. Usually upon the termination of all company appointments, an agent's license usually becomes inactive and can be reactivated by filing an appointment.

**Issuance of License**

Once the individual has met all the qualification, application, examination, and other legal requirements, a license is issued which states the name of the licensee, issue date and expiration, kind(s) of insurance covered, and any other conditions which apply.

Insurance companies have more discretion in appointing agents than the state regulators do in licensing them. If an applicant for an insurance license has met all of the qualifying criteria, the state has no choice but to issue the license. And once an agent license is issued, it can take many months of administrative process at the state level in order to have the license revoked.

Agents are supposed to report any out of state disciplinary actions to the resident state insurance department. Similarly, agents are expected to report disciplinary actions to their appointing company(ies) at the time of the violation, or no later than at license renewal, but this rarely happens. Insurance companies have found themselves in the embarrassing position of giving sales awards to an agent whose license is being revoked for violations of insurance law.

**LICENSE SUSPENSION/TERMINATION**

Licensing laws specify the rules and procedures for terminating the license of agents who show themselves to be untrustworthy or incompetent. Whether a license is suspended or revoked the state is the final authority of who may and who may not sell insurance within its borders. The director or commissioner of insurance has the authority to revoke or suspend any license or certificate of authority that he or she issues to companies, agents or brokers.

**Disciplinary Actions**

An agent or broker may lose his or her license by engaging in misleading or unethical marketing practices. State laws differ on what constitutes grounds for denial, suspension, revocation, or nonrenewal of an insurance agent's license. An unethical act can have severe repercussions because what most states consider unethical, is also illegal. In most states, an agent's license can be suspended or terminated for any of the following unethical actions:
• Making a materially untrue statement in the application for an agent's license;
• Violating or failing to comply with insurance laws in other states;
• Using fraud to obtain a license;
• Misappropriating funds;
• Misrepresenting the terms of a contract;
• Being convicted of a felony;
• Being convicted of an unfair trade practice;
• Having a license suspended in another state; or
• Engaging in fraudulent, coercive or dishonest practices, or being incompetent, untrustworthy or financially irresponsible.

• Any cause for which the original license or any renewal would have been refused
• Willful violation of or noncompliance with any insurance statute, lawful rule or regulation
• Misrepresentation or fraud in obtaining or attempting to obtain an insurance license
• Misappropriation or conversion to personal use, or illegal withholding, of monies belonging to policyholders, insurers, beneficiaries or others and received during the conduct of insurance business
• Suspension or revocation of an insurance license in any jurisdiction
• Conviction by final judgment of a felony involving moral turpitude
• Conduct of insurance affairs showing the licensee to be incompetent or a source of injury and loss to, or repeated complaints by, the public or any insurer

The license of a firm or corporation also may be suspended, and the revocation or suspension of an agent or broker license will automatically revoke or suspend the licenses of all solicitors appointed by that agent or broker.

Most agent licenses are suspended or revoked based on fiduciary misconduct (such as commingling, misappropriation, or improper withholding of client funds, and failing to remit return premiums due), charging of additional fees, felony convictions, etc.

Insurance departments have investigative units that follow up on complaints of wrongful conduct on the part of insurance agents. Insurance departments have the power to investigate, review, hold hearings, and, if necessary, suspend, not renew, or revoke the insurance agent's license and may impose civil penalties in the form of fines and jail sentences based on the violations uncovered.

In most states, an agent or broker whose license has been revoked may not apply for a new license for at least one year, often 3 years. Further, in many states, the insurance director or
commissioner may stipulate that, as a condition of relicensing, the agent maintain a bond protecting the citizens of the state for at least five years.

When agents are terminated for cause, the insurance company is supposed to notify the department of insurance. In practice, companies may be reluctant to call attention to their internal disciplinary actions.

**License Domicile**

Agent domicile (the state in which the agent resides and has a primary place of business) is a rapidly changing area of law. Currently, many states will grant non-residents a producer license. Agents and brokers of insureds with exposures in several states must be licensed in those states before they can collect a commission for the coverage they have written.

Other rules and regulations enacted in some states require that insurance policies be countersigned by licensed resident agents of the insurer, regardless of where the contracts are made or the residency of the insureds usually a countersignature fee is charged which can often be higher than the commission the agent earned for the sale. Many states require proof of continuing education credits for non-resident agents in those lines of insurance they are licensed or physically go to the state and pass a test before renewal or relicensing.

**Display of License**

Most states require that an issued license be prominently displayed in the agent's office or available for inspection by the public. Where the business entity is a "fictitious name", that name should be registered with the insurance department and status have strict rules as to what types of names can be used so the consumer is not misled.

Many states require that an agent print his or her insurance license number on his or her business card, in advertisements, and on other materials given to the public. Many states also have a website where consumers can look up the status of an agent's license. Whether they are in fact properly licensed, and in good standing; if they are up to date on their continuing education (including which courses they've taken); and if they have been subject to any fines, penalties, suspensions or revocations. This makes it easy for consumers, insurers and prospective employers to obtain this information in a timely fashion.

**State Insurer Regulation of Policy Provisions**

States also regulate insurance policy contract provisions. Standardized policies or provisions in some lines help meet the criteria of uniformity proclaimed by the NAIC. State law may require that certain terms be defined in a particular way. Other laws state that policies be easy to read, written with clear and simple wording. States may also forbid certain provisions from being included in a policy.

States require that any insurance policy to be sold in that state be submitted for review and approval before it is offered to consumers. States have the power to reject policies which do not conform to their regulations and laws.

**Rates Are Regulated by Law**
Rates are also regulated by law, with companies in most states having to file rates assigned to their policies with the state insurance department for review. There are three main areas that insurance commissioners review in regard to rates:

- Rates must not be so low that they do not cover the insurer’s anticipated losses and administrative expenses; nor must they be lowered to establish an unfair advantage over other companies.
- Rates must not be so high that they exceed anticipated losses and administrative expense, thus placing an unnecessary expense on consumers.
- Rates must be fair, in that insureds with the same risk must be charged the same for the same coverage.

**Insurance Commissioners Investigate**

Insurance commissioners also have the legal right to investigate and examine companies operating within their states. They may conduct examinations when they have reason to suspect that the company is in violation of insurance laws, and they are required to examine all domestic insurers at periods set by law.

The most obvious reason for taking this action against an insurance company would be the insurer's failure to limit the amount of new business it writes in comparison to the amount of its policy owners' surplus. In general terms, policy owners' surplus is the difference between a company's assets and liabilities. In property/casualty insurance, the insurer can safely write $2 of net new premiums for each $1 of policy owners’ surplus in order to offset any substantial underwriting or investment losses.

When insurance companies become insolvent, an investigation will often reveal that officers of the company have used false financial statements to conceal the company's shaky condition. Filing false financial statements is a serious offense, punishable by both fines and imprisonment.

**UNFAIR TRADE PRACTICES**

The Unfair Trade Practices Act, first introduced by the NAIC in 1947, has been continuously updated and adopted by the states. The Act which, is generally divided into two parts - Unfair Marketing Practices and Unfair Claims Practices, defines and prohibits certain trade and claims practices which are unfair, misleading and deceptive, including sales and marketing practices, discrimination in rating and underwriting, policy cancellation and nonrenewal, and claims investigation and settlement. While most of these laws are directed mostly towards insurance carriers, many of the requirements apply specifically to insurance agents.

This section includes a brief summary of the prohibited unfair practices that relate to agent behavior that most states have adopted. For more detailed information about what is required by a particular state, refer to that state’s unfair practices laws and regulations. Keep in mind that any act can be considered an unfair practice upon investigation by the insurance department, regardless of whether the practice is specifically defined or prohibited by law. If the commissioner believes an agent or insurer is engaging in an unfair method of competition, act, or practice, a hearing may be called to investigate further.
Although certain practices may be unethical largely because of the situations in which they occur, while other practices are unethical irrespective of the situation.

**Unfair Marketing Practices**

Agents or brokers found guilty of an unfair marketing practice or unfair method of competition may be fined and have their license suspended. Whatever the case, the agent must cease and desist from continuing such practices. Repeated violations will likely result in license suspension or revocation. Agents should pay particular attention to the responsibilities they have in the following areas:

**Concealment**

- Concealment is neglecting to communicate what the agent knows or should know to be true.
- Whether concealment is intentional or unintentional the injured party is entitled to rescind the contract or policy.
- Communication that is generally considered exempt from concealment includes:
  - Matters which the client/insurer waives (refuses or declines to discuss)
  - Matters which are not material and matters which, according to the "prudent man theory," the other party ought to know.

**Fraud**

If an agent intentionally misrepresents any information in an insurance transaction, he is guilty of fraud. An agent found guilty of fraud may be subject to fines and/or imprisonment.

**Failure to Remit Premiums**

It is unacceptable for an agent to hold a premium for an unreasonable length of time. An agent should submit premiums collected to the insurance company at the earliest opportunity. They must also remit refunds to the insured within a reasonable period. Many states have published rules or regulations specifying how long this period is.

**Deceptive Sales Practices**

Any communication—either face-to-face, on the telephone, via e-mail or through the postal service—with a client or prospective client shall not mislead and needs to:

- Properly identify the professional and the company he or she represents
- Clearly identify the products and/or services the professional provides
- Truthfully state the purpose of the communication

**Using Euphemisms for "Agent" and “Insurance”**

The phrase "insurance agent" means "salesperson" to some. Salespeople play a vital role in our economy by helping customers evaluate their needs and by providing specialized
information on products and services that can meet those needs. But the general public doesn't always keep this aspect of the salesperson's role in mind.

Prospects may resist a sales appointment with an agent. To get around this resistance, some agents attempt to disguise the true nature of their business and the products they sell by calling themselves financial planners, financial consultants, estate planners, risk managers, etc., rather than insurance agents.

An insurance agent is NOT a risk manager, financial advisor, financial planner, financial consultant, retirement planner, pension specialist, or investment counselor. Agents must be very clear to identify themselves as representing insurance companies and make it clear that they sell insurance products. Also agents must be sure to identify the insurer(s) being represented.

Most agents who avoid calling themselves agents don't do so out of an intent to deceive prospects. However, from an ethical standpoint, it is the behavior itself and not the individual's good intentions that count. If one is licensed as an agent, then the only acceptable way to identify oneself is as an agent. Anything else is unethical.

For example, an insurance agent who speaks to a prospect with the objective of securing a sales appointment should identify him or herself early in the conversation as an agent for the insurance company he or she represents. The agent should make it clear to the prospect that he or she intends to discuss certain insurance products and services.

Often the company's lower level sales managers, whose pay is based on the sales production of the agents they supervise, encourage deceptive sales practices. Sales materials and techniques developed in the field may not be authorized and may in fact be in violation of company policy and state law. Agents who were dismissed for using deceptive sales practices protested that the sales pitches they used were taught to them by company managers.

Considering how unfamiliar consumers are with the principles underlying insurance contracts, even a technically accurate product description may be too confusing for the average buyer. If the customer misunderstands the provisions, coverages, exclusions, and limitations of his or her policy, the sales practice used may be considered misleading. For example, a proposal presented to a customer that is titled "Retirement Funding Proposal" or "Private Pension Plan" might be ruled misleading if the "plan" proposed is actually a life insurance policy.

No single piece of sales literature or statement made by the agent needs to be incorrect in order for the sales process to be considered deceptive. If the net result of a sales practice is a pattern of customer misunderstanding, then the entire sales process can be viewed as deceptive.

**Misleading Terms**

Because ethics in the insurance and investment business requires full and complete disclosure of everything that is material to the sale, the sales person needs to avoid any terms that might tend to confuse the facts. Unfortunately terms that are used to help describe and clarify the product at the time of the sale may actually mislead the insured.

Because certain terms have a high likelihood of being misleading when used to describe features of insurance products, the ethical sales person should avoid them. Some of the terms that are most likely to get in the way of properly communicating with prospects are:
### Terms That Are Misleading…

<table>
<thead>
<tr>
<th>Terms That Are Misleading…</th>
<th>When Discussing…</th>
</tr>
</thead>
<tbody>
<tr>
<td>Account, plan, private pension, program or strategy</td>
<td>Policy</td>
</tr>
<tr>
<td>Contribution, deposit, investment or payment</td>
<td>Premium</td>
</tr>
<tr>
<td>Earnings, profit or return</td>
<td>Dividends</td>
</tr>
<tr>
<td>Account or savings</td>
<td>Cash value</td>
</tr>
<tr>
<td>Mutual funds or funds</td>
<td>Variable life or Annuity Separate accounts</td>
</tr>
<tr>
<td>Vanishing premiums</td>
<td>Using dividends to pay premiums</td>
</tr>
<tr>
<td>Tax-free</td>
<td>Tax-deferred</td>
</tr>
</tbody>
</table>

Do not use inappropriate analogies (something is “similar to” or “very much like” something else) to explain financial products because it often leads to misunderstanding by the prospect or client. In many cases, the prospective client remembers only the analogy and may believe the investment or insurance product is the same as the product to which it was compared. Eventually, the prospect may discover that the product is not identical to the product used in the analogy. Frequently he or she then feels that it has been misrepresented and that he or she has been misled.

**Sale of Life Insurance as a Retirement Plan**

The living benefits of cash-value life insurance add a great deal of sales appeal to the product. However, trouble can arise when living benefits because the main reason for purchase. The life insurance death benefit should be the center of any sales presentation. If a prospect isn’t sold on the need for a death benefit, he or she generally won’t be sold on the need for life insurance. Regardless of how good the living benefits of the plan are, there is almost always a less expensive method to attain the living benefits if the death benefit is not needed.

Even if all the information the agent provides about the living benefits provided by the plan is true, if the agent fails to tell the prospect that the plan is life insurance, he or she has omitted a fact that is material to the prospect’s purchase decision. Such omissions are illegal, misrepresentations. Such omissions are also unethical, since they are not in the best interests of the client.

**Private Pension**

The term “private pension,” used when referring to a life insurance policy, is also unethical and has gotten many agents and insurers in trouble. The phrase “private pension” obscures the true nature of the product since the product being sold was a life insurance policy rather than a pension plan.
**Premiums**

An unethical agent who wishes to disguise the fact that the product was life insurance might choose to refer to premium in some other way. Some of the other terms that are used to refer to premiums and obscure the nature of the insurance product include:

- Investment
- Deposit
- Contribution
- Payment

The use of these terms obscures the facts and is unethical.

**Vanishing Premiums**

A concept that often results in charges of unethical sales practices involves the payment of life insurance premiums through the use of policy dividends. This concept has frequently been called “vanishing premiums.” Since premiums really don’t vanish, but are simply being paid by dividends and the cash value of surrendered dividend additions, the use of the phrase as misleading. To make matters worse, premiums may have to be paid out of pocket when dividends are diminished. The ethical agent must avoid using the term “vanishing premium.”

**Cash Values**

Referring to life insurance cash value accumulations "investments" has gotten many agents in trouble, and in fact is expressly prohibited by many state laws. Even variable insurance products should always receive primary representation as insurance. In many instances the problem has been that life insurance hasn’t been described as life insurance. Life insurance must always be described as being primarily an insurance (protection) product rather than an investment or savings product.

Cash values should never be referred to as equity, savings, passbook savings, liquidity accounts, emergency accounts, or earnings. Agents should never imply that tax-deferred means tax-free. The word "guaranteed" should be used with care, since life insurance buyers do not easily understand which elements of the policy are guaranteed and which are not.

**Insurance vs. Investments**

In life insurance, there are distinct and definite prohibitions when it comes to describing life products. Topping the list of things agents should never say are phrases about investing and investment returns.

Agents must keep in mind the reason that life insurance has traditionally been afforded favorable treatment under the tax code is that life insurance is the only method to mitigate the catastrophic and irreversible financial consequences of death. In other words, life insurance owes its tax advantages to its death benefit – the living benefits are a side effect of the death benefit.
While some government programs, such as Social Security, provide benefits to qualified survivors in the event of a covered individual's death, such programs provide only a minimal benefit, usually only adequate for the basic necessities of life. The tax benefits accorded to life insurance are meant to encourage people to provide for additional financial security through private means. By allowing families to maintain their lifestyles and businesses to continue their operations, life insurance proceeds contribute to the stability of our society.

It would be tragic if the life insurance tax advantages were lost. Provisions that would eliminate some or all of the tax advantages of life insurance are continually included in proposed new tax legislation, though so far the major tax advantages of life insurance have been preserved.

In any life insurance sale, it is essential to establish the prospect's need for the death benefit that the policy will provide. It is then appropriate to evaluate how the living benefits and tax advantages of the policy compare to the features offered by other financial vehicles. Agents must always be sure that clients understand that they are proposing the purchase of a life insurance policy, the primary purpose of which is to provide a death benefit.

**Misrepresentation**

A misrepresentation is a written or oral statement which is false. Generally, in order for a misrepresentation to be grounds for voiding an insurance policy, it must be material to the risk if the party to whom the misrepresentation was made would have made a different decision had they known the truth, then it is material.

Agents may say something about a product to a consumer that isn't true, not out of an intent to mislead, but simply out of ignorance. Because they lack intent, such misrepresentations are not fraudulent, but they are still illegal and subject to severe penalties.

Misrepresentation has been the basis of many of the legal problems in the insurance industry. Although in most cases misrepresentations happen unintentionally, the agent's ignorance is not a defense against liability arising out of this unintentional misrepresentation. Existing laws hold agents responsible for misrepresentation based on the premise that agents have an ethical duty to know what they are selling and to present policies in an honest and thorough manner.

To avoid misrepresentation, an agent must thoroughly understand the product he is selling so that he can explain it accurately to a prospect. To further protect the consumer, many states require agents to deliver a Buyer's Guide to prospects when certain products are being sold, such as life insurance, annuities, long-term care insurance and Medicare Supplement insurance.

An agent, broker or solicitor must not misrepresent any material fact concerning the terms, benefits or future values of an insurance contract, including:

- Misrepresenting the financial condition of an insurance company
- Making false statements on an application
- Disclosure of State Guaranty Fund backing of insurance contracts (some states)
- Making false statements or deceptive advertising designed to discredit an insurer, agent or other industry group
• Making agreements that will result in restraint of trade or a monopolizing of insurance business, etc.
• Misrepresents the terms, benefits, advantages or conditions of any insurance policy
• Misrepresents the dividends or share of surplus to be received on any insurance policy
• Makes any false or misleading statements as to the dividends or shares of surplus previously paid on any insurance policy
• Misrepresents or is misleading as to the financial condition of any person or the legal reserve system upon which any life insurer operates
• Uses any name or title of any insurance policy or class of policies that misrepresent the true nature of the policies
• Misrepresents any material fact for the purpose of inducing or tending to induce the lapse, forfeiture, exchange, conversion, replacement or surrender any insurance policy (this illegal practice is known as twisting)
• Misrepresents any material fact for the purpose of effecting a pledge, assignment, or loan on any insurance policy
• Misrepresents any insurance policy as being a share of stock

**FALSE OR MISLEADING ADVERTISING**

In every state it is unlawful for an agent or any other person to formulate or use an advertisement or make a statement which is untrue, deceptive or misleading regarding any insurer or person associated with an insurer.

State regulators have concluded that the use of misleading advertising and sales materials demonstrates an inadequate control by the company over the content, form, and method of distribution of its advertisements. Many home offices have now prohibited the use of any sales and marketing materials unless they have first received approval from the home office. Many companies allow only the use of preapproved sales materials, and may provide agents with sample preapproved letters and brochures on agent letterhead. Approved documents receive control numbers with expiration dates.

Agents should not assume that documents provided by the company in the past are still approved for use; agents should verify the approval status of any document about which they are not completely sure.

Responsibility for compliance is being redefined. The standards by which individuals and companies are being held accountable have changed. Increasingly, insurance companies are being held responsible, especially financially for the actions of their agents, and agents are being held responsible for their conduct through license revocations and in some cases, criminal prosecution.

**NAIC Guidelines for Insurance Advertising**
• All insurance advertisements must be truthful and not misleading in fact or implication. Words or phrases that are clear only through familiarity with insurance terminology cannot be used.

• All information required to be disclosed (i.e., exceptions, limitations of benefits, exclusions from coverage) must be printed conspicuously next to the statements to which the information related and displayed in such prominence that it’s not minimized, confusing or misleading (no fine print).

• Deceptive words, phrases or illustrations may not be used to describe a policy, its benefits, the losses to be covered or premiums payable.

• Testimonials must be genuine, represent the current opinion of the author, be applicable to the policy advertised and accurately reproduced.

• Disparaging remarks or statements about another insurer, agency or agent of another insurer, their products and services may not be used in any advertisement.

• The identity of the insurer must be clear in all advertisements, as well as the name, address and phone number of the agent placing the advertisement.

**FALSE FINANCIAL STATEMENTS**

It is a violation for any person to deliberately make a false financial statement regarding the solvency of an insurer with the intent to deceive others. An agent could be found in violation for telling an applicant that the insurance company with whom the coverage is being placed is financially stable when in fact its financial condition has been downgraded or declining steadily.

When insurance companies become insolvent, an investigation will very often yield the information that officers of the company have used false financial statements to conceal the company’s shaky condition.

In some cases officers of insurance companies have raided the company treasury, often transferring the funds to offshore banks.

**REBATES AND INDUCEMENTS**

Another practice that most people in the insurance business consider to be unethical, as well as illegal in most states, is rebating. While the giving of gifts to customers takes place in many industries, this practice is generally forbidden in the insurance and investment businesses. Rebating involves the giving or promising of a valuable consideration intended to be an inducement to the buyer to purchase an insurance policy or investment. The inducement may be cash or any other item of value. Generally, any gift greater than a nominal one could be considered a valuable consideration and a violation of rebating rules. Some states specify a dollar amount while others simply refer to a nominal amount.

Rebating is also considered a violation of the Unfair Trade Practices Act in most states (Florida and California are exceptions). Rebating includes any of the following activities when used as an inducement to the purchase of insurance or annuities, whether property & casualty or life & disability:
• Making agreements that are not plainly expressed in the policy
• Paying or giving directly or indirectly a rebate (kickback) or other consideration of the required premium payment not specified on the contract
• Giving any special favor or advantage in dividends or other benefits
• Giving any valuable consideration not specified in the contract
• Sharing or splitting commission with the applicant
• Giving, selling, offering or promising any shares of stock or other securities, or any dividends, returns or profits on such securities, or any advisory board contracts

The subject of rebating commissions elicits strong emotional responses, both positive and negative. Rebating occurs when the buyer of an insurance policy receives any part of the agent's commission or anything of significant value as an inducement to purchase a policy.

Some agents believe they should be able to voluntarily relinquish part of their commission if it will help them close a sale, while others believe that allowing rebates encourages unethical behavior.

Rebating is illegal in most states because unregulated rebating can be detrimental to consumers as a form of discrimination in the sale of insurance. In the states where rebating is legal (Florida and California), agents who offer rebates must be careful not to violate the anti-discrimination statutes. California's anti-rebate provisions were repealed when the controversial Proposition 103 was passed. Florida permits rebating in certain situations, under a rebate schedule which must be filed by the agent and which must be applied "uniformly" to those purchasing a policy from the agent.

Some companies have a policy against rebating even where it is permitted by law. They may include an anti-rebating clause in their agency contract. Even in states where it is legal, and their insurers allow it, many agents decline to offer rebates and find that their ethical clients generally do not expect kick-backs.

**Gifts are Rebates**

During any insurance transaction, and when advertising, agents must not offer a free gift, bonus, or anything of value outside of the policy or contract, which is an inducement to buy or as an inducement to refer clients since the payment of rebates is illegal in most states and the payment of referral fees or gifts is illegal in ALL states. State laws differ on how "anything of value" is defined.

Most insurers do not permit their employees to accept or provide any gifts or favors which might influence decisions involving business transactions. Even a nominal gift might appear to be influential with regard to business transactions (and could be construed as a violation of laws). Included in this compliance function, are prohibitions against gifts of value to government officials of both this country and foreign countries. Many insurance companies will not even allow agents to take an underwriter out to lunch and pick up the tab.

**Exceptions**
There are exceptions to the provisions concerning discrimination and rebates. The payment of policy dividends, retroactive rate adjustments, and reduced premiums that reflect the savings of direct payment to an agent or home office are not usually considered to be rebates.

**Referral Fees**

Similar to, and often confused with, rebating, the payment of referral fees is unethical as well as illegal in all cases. Even in states where rebating is legal, paying referral fees is not. The reason for this is that it amounts to payment of (or splitting) omission to an unlicensed person which is illegal. For example an agent may offer a cash or other type of inducement to clients to refer their friends to them. Another agent might pay a fee to other sales persons for referring clients to the agent for auto insurance or to real-estate agents for referring home buyers needing homeowner’s policies.

Many insurance agents pay referral fees to attorneys, accountants, auto dealers, financial planners and others for referring clients for insurance. This is illegal and must be avoided by agents. This includes non-cash payments or gifts including tickets to sporting events, vacations, gift certificates, etc.

It is also unethical and illegal in most jurisdictions for an agent to receive a referral fee as well, such as from a doctor, lawyer, accountant or body shop or other repair service in conjunction with repairs including claims of their clients. For both the person paying such a fee and for the person accepting such a fee, this represents a conflict of interest and is unethical and usually a violation of the law as well.

**LOWBALLING**

Lowballing occurs when an agent intentionally misquotes premium information to the consumer and accepts a low deposit just to get the business (and undercut the competition). The consumer is eventually billed by the insurance carrier for the difference- the correct price of the coverage.

Sometimes when an agent fears he or she is losing a sale due to the amount of the premium, figures may be incorrectly stated for the benefit of the sale. Such situations may be merely misunderstandings. Premium amounts may also be misstated simply because the agent is inexperienced in using premium tables or software.

In many cases the agent is betting that the insured won’t notice the difference by the time the policy is insured, especially if the premium is being paid in installments. Agents who practice “low balling” often misquote the full premium but accurately quote the down payment and installment which is all that many insureds remember or pay attention to anyway.

**BOYCOTT, COERCION, AND INTIMIDATION**

It is a violation of the law for any person to commit (or agree to commit) any act of:

- boycott,
- coercion, or
- intimidation
Resulting in or tending to result in an unreasonable restraint of (or monopoly in) the business of insurance.

**Boycott**

The act of refusing to transact insurance business dealings with another until he or she complies with certain conditions or concessions.

**Coercion**

Agents and brokers are prohibited from acting in any manner that would lead the insurance prospect to believe that he or she must purchase from a particular agent, broker or company.

**Defamation**

Any false, maliciously critical or derogatory communication, written or oral, that injures another's reputation, fame or character is considered defamation. Individuals and companies both can be defamed. Unethical agents practice defamation by spreading rumors or falsehoods about the character of a competing agent or the financial condition of another insurance company. These actions are illegal in most states.

**Unfair Discrimination**

Unfair discrimination exists when two people of equal risk are charged different rates because of a difference in race, religion, national origin or where they live (redlining). Property and casualty insurers may charge different rates based on territory or protection class. Underwriting standards may also be based on actuarially sound principles (such as statistical proof that women live longer than men, or that younger drivers are higher risk than older drivers, thus affecting the level of risk). These differentiations are based on company loss statistics and are not considered unfairly discriminatory.

Neither the insurer nor the agent may cancel, limit, or refuse to insure or renew insurance coverage based on unfairly discriminatory standards. Primary responsibility for compliance with this law falls with the insurance carrier. Agents and brokers should be familiar with the anti-discrimination laws and should refuse to comply with insurers engaged in discriminatory sales or underwriting.

Consumers have the right to be treated fairly by an insurer's underwriting guidelines. This means that the guidelines used for underwriting a company's insurance policies should have a sound actuarial basis, be relevant to the risks being insured, and be applied uniformly to people of the same class.

Insurance companies have the right to be discriminatory; they just can't be unfairly discriminatory. Many states prohibit the use of underwriting criteria based on:

- Marital status of the applicant, insured, or other person residing in the household
- Length of time at the address
- Employment status (including length of time employed)
- Level of education of the applicant or insured
• Failure of applicant or insured to purchase an additional policy which he or she did not request,
• Applicant’s status as a member of the armed forces

Such groupings would be considered unfairly discriminatory if they are not actuarially supported, not relevant to the risk, or are based directly or indirectly on race or ethnicity.

**Redlining**

The practice of redlining occurs when a company literally or figuratively "draws a red line" around a specific geographical location and refuses to insure properties located within its boundaries. Many insurers argue that they need to control potential losses and that they should be permitted to limit coverage or even refuse to write property coverage in areas where losses have been frequent or severe. However, under the provisions of the Fair Housing Act, a licensed individual or company may not refuse to provide homeowners or renters insurance solely on the basis of the geographical location of the insured's property.

When coverage is issued in a redlined area, other forms of discrimination take place such as charging higher premiums for comparable policies and charging higher rates for inferior policies. The U.S. Department of Housing and Urban Development (HUD) prosecutes insurance companies that intentionally engage in practices that have the intent and effect of denying, limiting or restricting homeowners insurance for people living in minority neighborhoods throughout the United States.

The NAIC's Unfair Trade Practices Act was amended in the 1970s to prohibit unfair discrimination based on the geographic location and age of a residential property (except actuarially sound discrimination). Allegations of redlining come up most often in urban, poor, minority, and/or rural risks.

Studies show that urban residents have limited access to limited coverages from a limited number of companies, for which they pay higher-than-standard premiums and are subject to more frequent policy cancellations and nonrenewal.

**Fee Based Compensation**

In most occupations professionals set their own fees. The marketplace determines if those fees are appropriate. Although a professional’s fees, if any, should be fair and reasonable, the most significant ethical issue with respect to fees is that they must be clearly disclosed. This disclosure must fully outline the scope of the work to be accomplished and disclosure must be made before any work is done to enable the prospect or client to make an informed decision with respect to hiring the professional.

The compensation of agents should be in proportion to the time and effort it takes to sell and service insurance policies and meet regulatory requirements for underwriting and policy delivery. Some agents and agents groups have advocated fees instead of commissions. In this way agents can be paid based on the amount of work they do for a client instead of on the amount of premium paid by the client.
The increased sophistication of insurance consumers demands more information and service from the agent. This, combined with reduced commission levels from insurance companies, is leading agents to consider charging fees for service.

Some agency contracts limit or prohibit the charging of unauthorized fees because it can get both the agent and the insurance company in trouble. One reason is that fees can be includible in the insurance company's premium tax liability, so the insurance company must be notified and give written consent. It is considered safest if brokers/agents either charge a fee or accept a commission payment, but not both. Any "discounting" of established fees could be viewed as a violation of rebating restrictions.

Most states allow fees to be charged only after the broker/agent has received written permission in advance from both the insurance company and the client. Other states require producers who want to charge fees to file a request with the insurance department. Some states require a separate license in order for an insurance professional to charge a fee. For example, California prohibits life agents from receiving fees unless they are licensed as and acting in the capacity of, a life insurance analyst.

In many states agents must disclose not only fees but all compensation received from their transactions for that client including commissions, bonuses, prizes, fees, etc. For example, broker fees are permitted in California, but unethical and abusive practices have prompted full disclosure and limits on the amount that can be charged.

**Collecting Both Fees and Commissions**

Insurance advisers or insurance counselors are persons who provide advice on insurance matters to clients in return for a fee. The value that clients must receive from the adviser in return for the fee is an objective analysis of the client's insurance needs and a recommendation regarding which products will best meet those needs. In most states a license is required to act as an insurance counselor, advisor, or to otherwise charge a fee for insurance advice, and this license is different from an agent or broker license. In many states an individual is not allowed to hold both types of licenses at the same time due to possible conflicts of interest.

There is a conflict of interest between the role of an agent, who will earn a commission for selling the products of only one or more companies, and the role of an insurance counselor or adviser, who must be objective about the benefits offered by the products of many companies. The ability to receive a commission on a sale could easily influence the recommendation an adviser might make.

For these reasons, agents are prohibited from charging fees altogether in most states. In many other states, collecting both a fee and a commission in connection with the same insurance policy is prohibited. In some states, collecting both a fee and a commission is permitted. In certain of those states, specific requirements must be met in order to do so.

A client should be able to obtain a recommendation to purchase a policy from an agent in return for only a commission. A substantial additional benefit must be provided for a fee to be charged.

It is generally illegal for an agent or broker to charge fees in addition to the policy premium for services which are not "truly" extra. In many states, it is illegal for any person or insurer to collect premiums or make charges which are "not specified in the insurance contract".
Additional charges may not be made for services which a producer would normally be expected
to perform in connection with the sale of an insurance policy (such as evaluating the applicant’s
needs, recommending coverages, and processing the application).

Extra services for which additional charges may be permitted are those which are not in the
scope of the producer's regular duties. These may include special research activities, or
services performed as a convenience to the insured where the producer incurs extra additional
expenses which are to be passed on to the insured. Usually, if an agent or broker is going to
perform and charge for an extra service, the service and the amount to be charged must be
specified in a written agreement, and it must be approved by the applicant or insured prior to
performance of the service.

Unfair Claims Practices

Unfair Claims Practices are considered part of the Unfair Trade Practices Act, and are
important for agents to understand as part of the insurance company’s responsibilities towards
policyholders.

Agents and agency employees are usually the first to be notified when a client experiences a
loss. Claims are easier to settle when agents provide guidance to the policyholder throughout
the claims process. Consumers are less apt to file complaints when they feel their claims are
being handled properly. An agents responsibilities at claims time are relatively straightforward,
yet very important.

Regardless of the type of insurance, the insurer will usually require a written notice of loss or
claim and supporting documents. Most insurance policies contain loss provisions or a section
spelling out the insured's duties when loss occurs. By helping the policyholder submit a timely,
detailed, and accurate claim, the agent can minimize settlement delays and misunderstandings.
At times it may be necessary to follow up on claims, and to exert a special effort to speed relief
for loss victims who may be experiencing unusual hardships.

Depending upon the type of loss, a variety of special requirements may apply: for a life
insurance claim, a death certificate may be required; for an accident or disability claim, a
medical examination may be required; for a claim involving theft of insured property, the
insurance may not apply if the insured has failed to notify the police of the loss. Property
insurance coverages usually require the insured to protect property from further loss. Liability
coverages may require that the insurer be notified of claims and suits, even if the lawsuits are
groundless. There may be a time limit on when a claim can be filed so that the insurer may
conduct an investigation before paying a claim.

Various provisions may affect the amount of insurance coverage. For example, in property
insurance, a coinsurance clause and the amount of coverage written may determine whether a
loss is paid on an actual cash value or replacement cost basis. Many property insurance
policies include an appraisal clause, which establishes a way to set the value of property if the
insured and insurer cannot agree on the value or the amount of loss. Automobile insurance
policies contain an arbitration clause, which establishes a way to settle an uninsured motorist’s
claim if the insured and insurer cannot agree on the amount of loss or whether a person is
entitled to payment.
Agents should go over the insured's claim obligations as specified by the insurance policy, and the client should be told what to expect next from the insurance company, when they will be contacted by a claims adjuster, etc.

Notice of loss provided to the insurance agent is considered notice to the carrier, so the agent should transmit notice to the carrier as quickly as possible. If the agent receives notice of a claim but fails to forward it to the company for several weeks, a delay in claims payment could result. Since many state laws require that claims be acknowledged and the appropriate forms be provided to the claimant within 15 days of notice, if agents fail to forward timely notice of claim, the insurance company could face stiff penalties.

Agents should not assure the policyholder that the loss will be covered unless they are absolutely sure the circumstances of the loss are within the policy's scope of coverage. Agents should also not provide legal advice, or make unauthorized decisions on behalf of the insurance company. In most cases agents are forbidden to affirm or deny coverage or amounts payable for a specific claim and must forward all such inquiries to the company's claims department.

**UNFAIR CLAIM SETTLEMENT PRACTICES ACT**

Most consumer complaints involve claims such as a company's refusal to pay a claim or its dispute about the amount payable to the claimant. State insurance codes offer some protection to insurance consumers in this important area and such complaints are often resolved in favor of the consumer.

The claims settlement practices of insurers are regulated, in the public interest, for two main reasons:

- Insurance companies collect policyowner's money for the purpose of settling claims
- When insureds' claims are denied, or claim payments are delayed or altered, the consequences can drastically affect the insured's financial situation

The Unfair Claims Settlement Practices provisions of the Unfair Trade Practices Act (a model NAIC Act which has been adopted in all states) are designed to protect the insureds and claimants from any claims settlement practices which are unfair, deceptive or misleading.

- Attempting to settle claims for less than the amount for which a reasonable person would believe one was entitled, based on written or printed advertising material accompanying or made a part of an application.
- Compelling insured to institute suits to recover amounts due under its policies by offering substantially less than the amounts ultimately recovered in such suites brought by insureds
- Attempting settlement of claims on the basis of applications that were altered without notice to, the knowledge of, or consent of insureds.
- Making claims payments without including a statement of the coverage under which the claim is being paid.
Failing to promptly provide a reasonable explanation of the basis relied on in the insurance policy in relation to the facts or applicable law for denial of a claim or for the offer of a compromise settlement

Making known to insureds or claimant that the company has a policy of appealing arbitration awards in favor of insureds or claimants in order to compel them to accept settlements or compromises less than the amount awarded in arbitration.

Delaying the investigation or payment of claims by requiring an insured, a claimant, or the physician of either to submit a preliminary claim report, and then requiring the subsequent submission of formal proof of loss forms, both of which contain substantially the same information.

Failing to promptly settle claims under one portion of a policy for the purpose of influencing settlements under other portions of the policy.

Not attempting in good faith to make prompt, fair and equitable settlement of claims in which the insurer’s liability has become reasonable clear.

Failing to acknowledge with reasonable promptness, communications pertaining to claims.

Misrepresenting pertinent facts or insurance policy provisions relating to coverage at issue

Failing to adopt and implement reasonable standards for the prompt investigation of claims arising under insurance policies

Refusing to pay claims without conducting a reasonable investigation based upon all available information

Dissuading a claimant from filing a claim

Failing to affirm or deny coverage of claims within a reasonable time after proof of loss statements have been completed

Failing to inform and forward claim payment to a client or a beneficiary

Specifically advise a client not to seek an attorney when seeking claim relief

Misleading clients concerning time limits or applicable statutes of limitation concerning policies

Some states have added another provision which makes it an unfair claim practice to offer a settlement or payment in any manner prohibited by law.

**Penalties for Agents**

An agent found guilty of unfair trade practices by the Insurance Commissioner can lose his or her license, or have it suspended for a period of time. A license can be suspended or terminated if an agent:
• makes a materially (significant; substantial) untrue statement when applying for an agent's license
• violates or does not comply with other states' insurance laws
• obtains a license fraudulently
• misappropriates funds;
• misrepresents a contract's terms;
• is convicted of a felony;
• is convicted of an Unfair Trade Practice;
• license in another state is suspended;
• engages in fraudulent, coercive or dishonest practices; or is incompetent; untrustworthy; or financially irresponsible.

False Application Statements

It is illegal for any person to make false or fraudulent statements or representations on or relative to an application for insurance coverage for the specific purpose of gaining a commission, a fee, money, or some other benefit from any agent, broker, insurer, or individual. This would apply to an applicant who, through false statements, will obtain coverage that would have been rejected were the truth known.

Unfair Trade Practices of Lienholders

Because many mortgages or loans are made only on the condition that life insurance to pay off the loan be assigned or purchased, there are specific trade practices relating to these transactions.

All individuals who lend money and/or extend credit, and those who solicit insurance covering real or personal property, are required to state in writing that the borrower may purchase insurance relative to the loan/credit from an agent or insurer of the borrower's choice.

Disapproval by a lender of an insurance policy provided by a borrower shall be deemed unreasonable if it is not based solely on reasonable standards uniformly applied, relating to the extent of coverage required and the financial soundness and services of the insurer. Such standards may not discriminate against any particular type of insurer, nor call for disapproval of a policy because it contains coverage in addition to that required by the creditor.

No person who lends money or extends credit shall solicit insurance on real or personal property after a person indicated interest in securing a first mortgage credit extension, until the person has actually received a commitment in writing from the lender as to a loan or credit extension.

Agent Integrity
While many agents believe that "integrity" is a characteristic of choice, many state laws set minimum agent responsibilities to follow, such as:

**Qualifications**

Insurance Commissioners have been known to suspend or revoke an insurance agent if it is determined that he or she is not properly qualified to perform the duties of a person holding the license. Qualification may be interpreted to be the meeting of minimum licensing qualifications (age, exam scores, etc) or beyond.

**Lack of Business Skills or Reputation**

Licenses have been revoked where the agent is not of good business reputation, has shown incompetency or untrustworthiness in the conduct of any business, or has exposed the public or those dealing with him or her to danger of loss.

Agent licenses have been revoked or suspended for activities where the licensee:

- did not actively in good faith carry on as business the transactions permitted by law,
- avoids or prevents the operation or enforcement of insurance laws,
- knowingly misrepresents any terms of the effect of a policy or contract, or
- fails to perform a duty or act expressly required of him or her by the insurance code.

**Activities Circumventing Laws**

Agent licenses have been revoked or suspended for activities where the licensee (1) did not actively and in good faith carry on as a business the transactions that are permitted by law; (2) avoids or prevents the operation or enforcement of insurance laws; (3) knowingly misrepresents any terms or the effect of a policy or contract; or (4) fails to perform a duty or act expressly required of him or her by the insurance code.

**Agent Dishonesty**

Agents have lost their license because they have engaged in fraudulent practices or conducted any business in a dishonest manner. A licensee is also subject to disciplinary action if he or she has been convicted of a public offense involving a fraudulent act or an act of dishonesty in acceptance of money or property. Furthermore, most Insurance Commissioners will discipline any licensee who aids or abets any person in an act or omission which would be grounds for disciplinary action against the persons he or she aided or abetted.

**Catchall Category**

In addition to the specific violations above, most states establish agent responsibilities that must not violate "the public interest". This is an obvious catchall category that has been used where agents have perpetrated acts of mail fraud, securities violations, RICO (criminal) violations, etc.

**Records**
Agents should maintain a record-keeping system that will provide a sufficient "paper-trail" to identify specific insurance transactions and dates. At a minimum, such record systems should track the name of the insurer, the insured, the policy number and effective date, date of cancellation, premium amounts and payment plans, dates premiums are paid and forwarded or deposited to the insurer or trust account, commissions (and who gets them). Where an agent trust bank account is used, agents should maintain all bank statements, deposit records and canceled checks. Most records should be kept for a total of 5 years after the expiration or cancellation of the policy. Some states require that records be maintained "on-site" for one year after expiration or cancellation or stored off-premises but available within two business days.

Agent Files

While agent files may not be required by law in certain states, every policy transaction should be separately filed and include a copy of the original application for insurance or a memo that the client requested coverage, all correspondence between agent/client and agent/insurer, notes of client meetings and phone conversations, memorandums of binders (oral or written) and termination/cancellation dates with proof of notification.

Reporting Changes

Agents are often contractually required to report any changes of home or business address immediately to the carrier(s) with whom they hold an appointment, as well as to all regulatory authorities such as the state insurance department. Statutes usually specify this notice should be made "immediately," "within 30 days," or "within a reasonable time".

Penalties

Following an investigation and a hearing, if the state insurance department finds that an insurance company has engaged in any unfair trade or unfair claims practice, the commissioner may issue a cease and desist order prohibiting the individual or company from continuing the practice. Failure to comply with a cease and desist order can result in a substantial fine (usually $10,000, but these amounts differ by state). In addition, fines and loss of license may also be imposed for any company or person guilty of violating the Unfair Trade Practices Act.

A PRODUCER’S DUTIES AND RESPONSIBILITIES

Insurance producers must fulfill certain duties toward their prospects and clients, and also toward the companies they represent. Insurance is a contract of "utmost good faith" between an insurance company and an insured. The parties involved in the contract must deal with one another honestly and fairly.

Agents’ ethical duties to the public and their prospects are quite demanding. In addition to the attributes that most consumers expect from their agents, (skill, competence, professionalism and moral integrity), there are other ways in which agents can impact the public's perception of insurance and the insurance industry.

As representatives of insurance companies through their agency contracts, agents may be granted wide authority to inspect risks, to immediately bind an insurer by oral or written agreement, to issue various types of contracts, to collect premiums due, to settle some claims and so on. Consequently, the agent is obligated to do the best job possible for the insurer and the client. If the agent makes improper promises or representations that induce the client to act
on those representations, the agent may be held liable to either the client or the insurer, or both, for any damages that result.

**Communication**

Insurance agents represent their insurer to the general public and prospective insureds. Their actions help shape the public's perceptions of the insurance industry. The agent's primary ethical duty to the public and each prospective insured is to provide accurate information regarding insurance policies and benefits in a fair and unbiased manner. That information should be complete in every way, providing the prospect with the details of any policy deductibles, conditions, limitations, exclusions or requirements. An audit of a prospect's or client's current insurance policies should be done to determine if they are up to date and in proper order, provide the type of protection needed and provide the best protection in the most economical way.

A prospect's lack of understanding of precisely what coverage an insurance policy will and will not provide is usually the result of poor communication. Sometimes this problem occurs when an agent attempts to sell a product without fully understanding the policy's features and benefits. This brings us back to the importance of spending time on product knowledge as well as training in communication skills.

**CONFLICTS OF INTEREST**

A conflict of interest arises in any situation where an agent's self-interest competes with their duty to act in the best interests of another. Conflicts of interest involve the danger that individuals may violate their ethical duties toward others.

Insurance agents face numerous situations that may involve a conflict of interest. Agents in the insurance and financial services industry have an obligation to identify and disclose any conflicts of interest.

An inherent conflict of interest arises in the case of any person who, for a fee, is expected to provide an objective, unbiased financial plan for the client, while also offering financial products for sale. The conflict of interest results from the sales person's interest in the sale of a product, which may affect the unbiased nature of the financial planning recommendation.

While agents should make recommendations based on the client's needs, they need to sell in order to earn commissions and make a living. In the short-term, the benefit to the agent is maximized by selling the largest possible amount of the product that pays the highest commission in the least amount of time.

When a situation clearly involves a conflict of interest, the agent is required to set aside his or her self-interest and act in the best interests of the prospect. If agents conduct themselves properly in these situations, they will earn the trust of their clients. However, if conflicts of interest are mishandled, many different types of problems can arise ranging from loss of license, to loss of company appointments, to loss of clients to civil and/or criminal penalties.

**THE AGENT AS A FIDUCIARY**

A fiduciary is an individual whose position and responsibilities involve a high degree of trust and confidence. Insurance agents automatically have a fiduciary responsibility to both the insurer
they represent as well as to their clients. Serving in a fiduciary capacity demands high ethical standards and performance. In fact, fiduciaries are held to a higher standard of conduct than is required in the usual course of events.

An insurance agent must understand the fiduciary nature of his or her responsibility to clients. Insurance is about money, value, and worth. It is a way of paying for the loss of something before that loss occurs. And when clients purchase a policy, they are concerned, primarily, with three things:

- The value of the thing to be insured
- The cost to insure it
- The benefit if a loss occurs

When going over the policy, agents should concentrate on those three things. Agents must also be sure that clients understand their responsibilities such as paying the premium on time, updating coverage amounts when circumstances change and their duties in the event of a claim.

A client depends upon the agent to sell him or her a policy that will meet the client's needs within the limitations of what the client can afford to pay. Making sure the client understands how the policy works, avoids trouble later.

One of the duties of an insurance agent is to make certain that the client is familiar with the particular insurance company's record for financial stability and payment of claims.

**AGENT RESPONSIBILITY**

An insurer places a great deal of trust and confidence in its agents; consequently, an agent must act 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:

- soliciting applications for coverage;
- describing coverages and policies to prospects and applicants and explaining how such policies can be purchased;
- collecting premiums (or in some cases, only initial premiums with subsequent billings being issued and sent by the insurance company); and
- providing service to prospects and the insurer's policyholders.

While the provisions of the agency contract tell agents what acts they are authorized to make, how they go about those tasks is usually left to their own judgment and discretion. However, both an agent's actions and judgments are held to fiduciary standards.

*Reasonable Care*
An agent has a duty to carry out his or her actions with the utmost care and skill. The fiduciary relationship is a special relationship of trust and confidence that requires a high degree of care and integrity. As the insurer's authorized agent, the agent represents the company to the public and must act accordingly. In some cases, this means the agent must refer the business to others who are more qualified if the agent does not have the skills to handle it.

**Provide Information and Follow-up**

An agent has the obligation to act promptly in all matters regarding the insurer's business, including the responsibility to transmit completed applications and notice of bound coverages as quickly as possible. The insurer cannot begin the process of underwriting and issuing insurance until it has received an application. If the applicant has not been given a binder, he or she remains at risk until a policy is issued. On the other hand, if an applicant is given a binder at the time of application, the insurer is obligated to provide coverage, until and unless the application is formally rejected. In either event, a delay by the agent in turning over an application may place the applicant or the insurer in jeopardy.

**Acting As a Trustee**

Agents are sometimes asked by their clients to act as trustee of a life insurance trust or a qualified plan. However, if an agent has sold or will sell a policy to a trust or plan, he or she should not accept any other role in relation to the trust. If an agent has assumed a role as trustee or adviser to a trust, he or she should not sell a policy to the trust.

Under the law, a trustee who accepts any bonus or commission for any act performed by him or her in connection with the administration of the trust, has violated his or her fiduciary duties.

**ETHICAL SELLING**

An ethical insurance agent that goes out of business because he or she could not bring in the earnings necessary to pay their bills will not do the consumer much good. Therefore, the agent must be both ethical and skilled in his or her trade. In fact, the financially successful agent will probably find it easier to be ethical since there will be less stress involved to make the sale at any cost.

**Ethical Sales Concerns**

The important points are:

- The sales professional owes certain ethical duties to clients and employers
- The primary ethical duty owed to prospective clients involves open and honest communication of all material information so that he or she may make an informed decision
- Certain acts may be ethical or unethical due to their context; other actions such as churning, twisting, forging signatures and the willful failure to obtain complete client information are unethical, regardless of their context.
- Misleading terms must be avoided at all costs
Insurance replacement should be recommended only when the replacement coverage is clearly superior to the coverage being replaced.

Sales professionals must take special care to communicate accurately, clearly and completely in all phases of the sales process when working with physically or cognitively impaired clients.

**Agent Duties**

In the financial sales relationship, there are duties owed by the sales professional to both the client and the sales person’s employer or principal. These duties give rise to ethical and, sometimes, legal obligations.

**Agent’s Responsibilities to the Client**

The ethical duties that the sales person owes to his or her client generally include the duty to:

- Provide a balanced presentation
- Hold client information confidential
- Avoid conflicts of interest
- Perform tasks with skill and care
- Fully disclose all material information
- Complete any transactions undertaken

Agents have a responsibility to know the differences in products they are selling, and they have a duty to explain policy options that are reasonably priced and widely available for the policy suggested.

In some cases, agents are responsible to see that a policy continues to meet client needs. The more that the clients depend on the agent for their insurance needs and the longer they do business with them, the higher the standard of care is in selling and serving them.

**Reasonable Client Expectations**

It is not only the actions of sales professionals that determine their ethics. Prospect or client expectations are also involved, as long as those expectations are reasonable. Following are three reasonable expectations that clients have:

- Recommendations from the sales professional that meet the clients’ needs in ways that are suitable and appropriate for their needs and goals
- The maintenance of proper coverage for their needs
- Clear and specific information and communication

**Meeting the Client’s Needs in a Suitable Way**

Financial sales professionals are ethically obligated to make recommendations that are
reasonably capable of meeting the prospective client’s needs, and suitable for him or her. The failure to obtain agreed-upon coverage for the client often results in charges of unethical practices, particularly in property and casualty insurance.

Maintaining Proper Coverage

In the insurance business, the agent’s failure to maintain proper coverage is another area in which agent ethics is often based on the client’s reasonable expectations.

Communicating Clear and Specific Information

All clients have a reasonable expectation that they will receive clear and unambiguous information concerning products recommended to them. In addition, they expect that they will be informed of all material facts before making a buying decision.

Unfortunately many policies are sold on the basis of assumed facts or misconceptions. The agent may not have outwardly misled consumers, however, they allowed the consumer to make assumptions that were incorrect. Some misconceptions may cause serious legal problems.

A policyholder that knows a specific claim will not be paid is not likely to be upset, but a policyholder that thought a specific claim would be paid will be very upset when the claim is denied. That policyholder will probably feel the salesperson misled them or failed to fully disclose the conditions and limitations present in the policy.

The Changing Role of the Sales Professional

The role of the salesperson has changed dramatically as well as the concept of selling. At one time, the buyer was responsible for ensuring that any purchase made was suitable and appropriate for the use to which it was to be put. If the buyer purchased an inappropriate, defective or otherwise unsuitable product, the problem was his or hers rather than the seller’s. Any recourse required that the buyer prove the seller was at least grossly negligent or that they acted with an intent to defraud.

A far more ethical role envisions the sales person as a professional who assists the client in making decisions that will help to better ensure the client’s health, safety and financial well-being, rather than an adversary, around whom the client needs to be wary.

Ideally both the sales person and the client should be jointly focused on the client’s interests. This has contributed to making the sales professional-client relationship a fiduciary one, requiring sales professionals to make decisions involving their clients that are consistently ethical.

SELLING TO NEEDS

The most important duty of an insurance agent to a prospect is to be honest in his or her analysis of the prospect's valid needs. Companies and agencies should stress needs analysis for the various types of insurance. Agents must make sure they continue to follow the procedures they have been taught.

Doing a ‘needs analysis’ is a fairly cut-and-dry process. However, when the human factor is brought in, needs analysis can be a challenge to an agent's ethical code. Faced with a client who simply doesn't want to think about possible loss, an agent may write a policy that represents an amount of insurance the client is willing to pay for, rather than coverage that
meets the client's needs. When the person dies or becomes disabled, or when their house burns down and they are underinsured they will feel that the agent failed to do their duty.

Parents of children with physical, mental, or emotional problems may not want to face the fact that they must make provisions for the child after they are gone. Denial may take the form of pretending that the child will one day be able to take care of itself. But an ethical agent must find a way to see that this very significant need is dealt with and met.

In the conduct of business or professional activities, an agent should not engage in any act or omission of a dishonest, deceitful, or fraudulent nature. An agent must not allow the pursuit of financial gain or other personal benefit to interfere with the exercise of sound professional judgment and skills.

Because the agent has specialized knowledge about insurance that the prospect does not possess, and because the agent is licensed and regulated by government authority in order to protect the public interest, the agent has assumed a duty to act in the best interests of the prospect. To act in the best interests of the prospect, the agent must take the time to evaluate the prospect's needs and recommend a product that best meets those needs and is affordable to the prospect.

By putting their client’s best interests first, they also serve their own best interests over the long-term. Not only do clients receive the products and service that truly meet their needs, but agents build the kind of clientele that will make them lifelong successes in the life insurance business.

**Suitability**

Suitability means that the purchase recommendations made by the insurance agent are based on reasonable grounds that are "suitable" for the customer. The National Association of Securities Dealers (NASD) defines suitability as "purchase recommendations that are based on information furnished by the customer about the customer's financial situation, needs, and investment objectives." Similarly, the Securities and Exchange Commission defines suitable recommendations as "those made on the basis of the client's needs, financial circumstances, and investment objectives."

Several states have begun applying suitability considerations to life insurance and annuity sales. Such suitability requirements making it illegal for agents to sell products that are inappropriate for a client's financial needs, would impose a degree of care (and liability) on agents that has until now merely been implied.

References to "suitability" especially appear in laws having to do with sales of insurance products to senior consumers, such as Medicare supplement and long-term care insurance. The regulations generally specify that the agent selling the insurance must have "reasonable grounds" for believing the recommendation is "suitable" for the customer, based upon the customer's circumstances, risk tolerance, need for insurance, and existing insurance already owned. For example in California, agents soliciting seniors for long term care and Medicare supplement insurance must make "reasonable efforts to determine whether the purchase is appropriate for the client."

Determining the suitability of a particular insurance product for a particular client is probably the most important service the agent provides. Needs-based selling and ongoing client service are
among an agent's primary responsibility to the customer. A needs-based analysis is the only way to ensure that the customer gets the insurance product that is most appropriate to his or her goals and needs.

Agents should give the client sufficient information about how the insurance product being recommended meets the client's specific needs, and should always document the final outcome with a letter to the client that summarizes what was discussed, what was recommended, and what the client decided to do. Such follow-up letters can save an agent many headaches (not to mention errors and omissions problems) down the road. In fact, an agent probably should document all client meetings with a follow-up letter, and should make notes on any conversations with the client or the carrier with regards to the client.

Agents must recognize that specific types of insurance policies are designed to meet specific needs, and matching the policy to client's needs produces the maximum benefit to the policyowner. This requires that an agent spends the time to learn all they can about the various types of policies, how each one works and the needs that each one is least able to satisfy. They must also work on their presentation and communication skills so that they can convey this knowledge to their prospects in the most easily understood manner.

Client trust must be earned, nurtured and constantly reinforced. The agent must communicate to his or her client the reasons why a particular insurance policy or program is being recommended and how it will serve their needs. 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 renew or retain their policies.

**Service After the Sale**

Agents also have an ethical obligation to provide exemplary service to their clients. This includes staying in touch with customers and conducting periodic reviews of coverage and needs to assure that customers are adequately covered. In addition, agents should be aware that they are in possession of considerable private information about their customers. They should take care to protect the confidential relationship they have with their clients.

The agent also has a responsibility to keep clients informed of any changes in insurance instruments or laws/regulations affecting the coverage, as well as new policies or enhancements that might apply to the insured's needs.

**The Professional Sales Process**

In securing coverage for the client one of the main responsibility of an agent is to adhere to their ethical responsibilities to the insurer and see that the prospect completes the application accurately and completely.

During the application process the agent is responsible for obtaining full and accurate information necessary for analyzing the risk and the hazards and exposures involved in order to determine the prospect's needs accurately. Remember that the insurer is relying upon them for full disclosure of all pertinent information regarding the applicant.

The sales process is the heart of any company's distribution system. The sales process—from initial introduction to delivery of the product—may involve multiple meetings, and has four steps.

- **Approach**
• The opening and fact-finding interviews
• Recommendations and close
• Implementation and follow up

Selling is not something that a salesperson does to someone else; instead, it is something that the professional does for and with a buyer that results in an exchange of value. Basic to the success of the sales process is the salesperson’s ability to develop trust and create rapport with a prospect. Sales people’s ethics and values contribute more to the success of the sales process than any sales techniques or strategies they might use.

**Working with Seniors or Disabled Clients**

Although individuals may suffer cognitive or other impairments at any age, sales persons working in the senior marketplace are more likely to encounter clients with such impairments. Working with the impaired client requires that the sales professional take special care to communicate in all phases of the sales process.

The sales professional must take particular care when working with the impaired client in:

• Obtaining information
• Making recommendations
• Implementing plans

**Ethical Concerns in the Approach**

During this step, the two most ethically sensitive issues are:

• The way sales professionals represent themselves
• What is discussed between the sales professional and the prospect

The purpose of the approach is to develop rapport with prospects to cause them to come to perceive the financial sales professional as someone with whom they may want to do business. During the approach step of the sales process, the important ethical issue is that, at no time, was the prospective client misled in any way.

As a result of the approach step in the sales process, the prospective client should have a clear understanding of the identity of the sales person, the products or services being offered for sale and the company or companies the sales person represents.

**How Sales Professionals Represent Themselves**

The principal ethical concern is that sales persons must fully disclose who they are, what company or entity they represent and that the purpose of this meeting is to sell insurance or other financial products, and not state or imply that he or she has skills, experience or credentials that are not possessed.
If sales professionals represent a particular company, their status as representatives of that company must be disclosed. In addition, if sales professionals are registered representatives, they must identify the company and broker/dealer, and provide addresses and telephone numbers.

Insurance agents, and other financial services practitioners, because of the personal nature of their business, must be viewed as both competent and credible before the prospective client will share financial information. Therefore, there is enormous pressure on financial sales professionals to appear knowledgeable and experienced.

For most financial sales professionals, this need for credibility and competence causes them to obtain professional education and experience. When that occurs, both the professionals and their clients benefit. However, if the need to appear competent causes sales people to misrepresent their credentials, experience or skills, it is a serious ethical problem.

A sales person who states or implies the possession of skills actually not possessed may result in his or her liability for failing to perform in the manner of someone who possesses such skills. If the sales person represents or implies that he or she has certain skills, failure to provide that level of service could make the sales person liable for any damages the client sustains as a result.

Using professional designations such as CPCU, CLU, CFP, ChFC or CPA is improper and deceptive unless individuals have earned them and is still in good standing, having satisfied the program’s continuing education requirements or other requirements. Another unethical situation is the acquisition of a supposed ‘professional designation’ which does not require advanced knowledge, examination or experience to qualify. There are literally hundreds of so-called designations out there available to anyone who pays the price. Unfortunately the consumer can be easily mislead into thinking that these ‘letters’ after the agent’s name on their business card represent a higher level of knowledge and an increased ability on the part of the agent that doesn’t really exist.

Some sales professionals use a trade name. While using a trade name is certainly acceptable, its use by sales professionals as a way of identifying themselves without also identifying the company being represented would be misleading. To the extent that it misleads, it is unethical. Any implication by the sales person that he or she is affiliated with the government, any governmental agency or other organization in an attempt to suggest its approval of the sales person or his or her products is unethical and illegal in most jurisdictions.

Sales professionals must not represent themselves as financial planners, investment planners, consultants or advisors when, in fact, the practitioner is a life insurance agent or registered representative. Such a statement suggests to the prospective client that the practitioner provides unbiased analyses of client financial situations, with no conflict of interest. The selling of financial products clearly creates such a conflict. These titles are misleading and unethical and may even be illegal in certain jurisdictions.

The tools that the financial sales professional uses could also lead the prospective client to the wrong conclusions. Using a data-gathering form which is entitled Financial Planning Form will lead clients to a conclusion that the sales person is in the business of providing financial advice. The sales professional has the responsibility to avoid anything that could reasonably be expected to mislead the prospect, and to correct any misperception of which he or she becomes aware.
How Sales Professionals Represent their Products

One of the ethical requirements is that the information provided to prospects is balanced and complete and enable them to decide whether to work with the sales person based on truthful information. Any product discussion should result in complete understanding by the prospect.

The real nature of the product as insurance should never be hidden or disguised. For example, the terms “plan,” “program” or “private pension” when referring to a life insurance policy is unethical, and in some cases illegal, because those terms obscure the true nature of the product, life insurance.

If the initial approach is made by telephone the sales person should usually avoid discussing specific products, because an adequate explanation with the limitations of the telephone is difficult. An attempt to discuss a complex financial product in this setting often results in misunderstandings and is more likely to cause confusion, rather than understanding.

Whenever interacting with a prospective client, care must be taken to ensure that the agent doesn’t inadvertently lead the prospect to believe that they are providing services not actually provided. If the sales person becomes aware of any such misunderstanding on the prospect’s part, he or she is under an ethical obligation to correct it as soon as possible.

Ethical Concerns in the Opening and Fact-Finding Interviews

In the opening interview, the agent will normally begin to develop rapport with the prospective client and begin to identify benefits that the individual would receive by proceeding to allow the agent to collect data to establish needs and formulate a plan to treat those needs.

It is common for insurance companies to use the services of celebrities and other prominent people for advertising purposes. Testimonial letters from satisfied clients are also used to motivate the prospect. It is important that any testimonial letters actually reflect the writer’s current opinion. Testimonials used in advertising must be applicable to the policy advertised and be given accurately. Such testimonials must indicate if the person giving the testimonial is being compensated or has any financial interest in the company.

An insurance agent may choose to use visual or graphic material to inform the prospective client about the potential advantages and benefits of a product. When using graphics or other illustrations, it’s important to make sure that they are accurate, up to date, that they do not mislead the prospect, and that the material matches the prospective client's level of understanding. Most insurers prohibit agents from using any materials unless they have been reviewed and approved by the insurer (and sometimes even the state) before use.

The agent must obtain sufficient information about the prospective client to develop a recommendation that is suitable to his or her situation, and consistent with his or her objectives and tolerance for risk.

This presents the insurance agent with an ethical and legal duty to make a diligent effort to determine all the client's circumstances that are relevant to his or her financial situation, including the prospective client’s current finances, as well as his or her desires and aspirations.

Obtaining Information from Seniors
The requirement that recommendations be suitable increases as the prospective client ages or becomes impaired. However, ensuring suitability may be somewhat more difficult when the prospective client has an impairment that affects his or her ability to hear, read or understand.

The sales person must be able to communicate adequately with, and obtain needed information from, the prospective client. Prospective clients with cognitive disorders present the greatest challenge to the sales person. Individuals whose hearing or vision is severely diminished, also require special care. Some impaired individuals may be uncomfortable admitting their limitations which presents the sales professional with even greater difficulty.

Ethically, the sales professional working with an impaired individual must make every reasonable effort to ensure that he or she is understood. Often, the sales person must confirm the prospective client’s understanding.

If the sales person knows or suspects that the prospective client is not fully in possession of his or her mental faculties, or has difficulty hearing or seeing the sales person working with an impaired individual should:

- Confirm that the prospective client understands the questions. Confirming understanding may require that the sales person not only explain the questions verbally, but also provide them in writing.

- Document the prospective client’s responses by writing them in a pre-printed form. When the data-gathering session is concluded, the sales person should present the completed data-gathering form to the prospective client and recap the questions and answers. When the sales person and the prospective client agree that the information on the data-gathering form is correct, the sales person should ask the prospective client to sign or initial the form so indicating. (A copy of the form should become a permanent part of the client file.)

- Request, if appropriate, that other individuals who have no vested interest in the sales process or its results accompany the prospective client, such as caregivers, family members or other trusted advisers, the individual’s accountant, attorney, financial planner, pastor, etc.

**Ethical Concerns During the Recommendations and Close**

The final step of the sales process is when agents make recommendations based on their assessments of prospects’ needs, and seek decisions from the prospects to purchase the recommended products. The principal ethical issues here are:

- Recommendations must provide complete disclosure to the prospect of all material elements. All information that could reasonably effect the prospect’s buying decision must be disclosed.

- Recommendations should be balanced and identify both the advantages and disadvantages.

- A proper recommendation will include the benefits to be gained by the prospect, the costs involved and risks that would be assumed by the prospect.
Insurance products are complicated and require careful explanation. Any products or services recommended should be clearly identified and explained to the prospect. The explanations used for insurance products should avoid comparisons to other similar, but not identical, products or services. Also, any comparisons with competing products and services must be accurate, complete and fair.

Products or services recommended must meet a need acknowledged by the prospect and be suitable for the prospect with respect to his or her age, condition, financial situation and psychological disposition. When the prospect has a limited comprehension of the basic insurance products and concepts, the agent should suggest that a family member or trusted adviser be a part of the meeting.

Insurance agents often use statistics as part of their recommendation. Any statistics employed in making a recommendation should be both accurate and complete to enhance rather than obscure the prospect’s understanding.

Any material that must be provided by the agent to prospects by law—buyer’s guides, prospectuses, etc.—must be provided in a timely fashion, before the sale is made. Supporting materials used in presenting the recommendation to the prospect or client must inform without misleading, and must:

• Enable the prospect or client to render a more informed decision with respect to the recommendation

• Be complete and balanced by disclosing both the advantages and disadvantages of the recommended course of action

• Clearly identify those elements of the recommendation that are not guaranteed, and those that are based on assumptions that may not be realized

Making Recommendations to Seniors

Although many seniors continue to function well mentally, emotionally and physically well into advanced age, for others impairment may be an unwelcome companion of becoming older. When impairment results in diminished cognitive abilities or a loss of vision or hearing, it places even greater ethical responsibility on the sales professional to ensure that recommendations are fully understood.

In a meeting with an impaired prospective client in which recommendations for purchase are to be made, the sales person should suggest that any family members or trusted advisers be present.

Begin the meeting by reviewing the completed and signed data gathering form used to discover the client’s needs and develop the recommendations being presented.

Next distribute and review a written copy of the recommendation being made including how the recommended product will satisfy each of the prospect’s needs.

Ethical Concerns in Implementation and Follow Up

Many ethical issues arise out of the sales professional’s conduct following the sales interview. Principally, these are the two critical problem areas:
• Failure to obtain proper coverage. One or more of the following usually causes the failure to obtain coverage:
  • A failure to properly analyze the client’s situation and the risks involved
  • Failure to request the proper coverage
  • A delay in requesting any coverage for a period of time
  • Not receiving the proper coverage from the insurer
  • Failure to maintain proper coverage; Failing to maintain coverage usually occurs because of the insurance agent's failure to:
    • Renew coverage on a timely basis
    • Notify the insured of the deadline for renewing coverage non-renewal

Keeping in Touch After the Sale
The hardest policies to replace are those of an agent that keeps in touch with his or her clients. Aside from the business retention standpoint, an agent’s ethical duties regarding service after the sale often depends partly upon the arrangements made between the agent and his or her agency or insurance company. Some companies have a separate servicing staff so that the selling agent is not expected to do any further service work. Most agents, however, are probably expected to do any necessary service work personally. Even if the selling agent is not expected to provide service, most professionals find that referrals and additional sales result from close client contact. In addition to that aspect, everyone likes to feel that they were more than a commission to a salesperson.

Consequences of a Breach of Responsibility to Clients
An agent who breaches his or her ethical responsibility to clients will be exposed to two types of consequences:
  • Personal
  • Legal

The legal consequences for unethical conduct can include suspension or revocation of the agent’s license, as well as lawsuits in criminal or civil court. Agents can, by their unethical and illegal behavior, put themselves and their insurers and clients in jeopardy.

Implementing Plans for Impaired or Disabled Clients
Chief among the considerations in implementing a chosen plan for an impaired client is communicating with both the client and his or her advisers.

Implementing a recommendation could take several months or longer and may involve several different professionals. The sales person needs to remain involved in the process, even after the product is purchased, to ensure that each required step is accomplished and appropriately communicated.
When ongoing premium payments or investments are required to complete or maintain the implemented plan, ensuring that those subsequent premium payments or investments are made is critical. Since the impaired client may forget to make needed payments or additional investments when required, it is important to provide premium notices to others such as family members, caregivers or professional advisers so they can take remedial action to ensure that payments are made.

**PROVIDING SERVICE TO CLIENTS**

Selling to needs is only part of what an agent must do to meet the ethical responsibilities he or she owes to a policyowner. Service, during and after the sale, is just as important.

In all instances, the agent is responsible for:

- maintaining accurate records about his or her clients
- maintaining complete and accurate written records of all business transactions
- keeping informed about changes in markets, new coverages and products availability that might expand coverage for a client or provide potential for additional sales to prospects or clients;
- assisting clients with their service needs, such as changes on policies, premium payment, etc.;
- assisting clients in filing claims and by following up on the status of open claims; and
- contacting clients before renewal dates to: (1) review existing policies and their values and limits in light of any changes in exposures and needs that may have occurred; and (2) recommend suitable changes in coverage as necessary.

Things are continually changing in insurance financial services. The client's situation is also changing. As time passes, people develop different financial needs. Marriage, divorce, children born, and children moving out on their own are just a few of the life changes that clients may experience, all of which may have a substantial impact on their financial needs.

An agent assumes a duty to meet a client's financial needs not just at a single point in time, but over the client's lifetime. A commitment to ongoing service is not just an ethical demand, it is also good business and creates the opportunity for additional sales. Periodic reviews of a client's coverage may reveal a need for additional coverage. In addition, the agent will be rewarded through referrals obtained from that satisfied client, and by the renewal of that policy over the lifetime of the insured.

Agents and their clients must understand that changing circumstances require modifications and adjustments to the life insurance policy over time. The client may need or be able to afford more coverage, his or her protection goals may change, interest rates and values may not be performing as projected; all require ongoing monitoring and reconsideration. Current life insurance commission structures, however, do not support that level of continuing customer service.
First year commissions in life insurance are higher than renewal commission in recognition of the sometimes lengthy application process. These higher commissions in life insurance sales also are intended to help new agents survive the early, difficult years in the business and give them the incentive to prospect for new business. Their undesirable effect, however, is to place all of the focus on new sales rather than on service.

**Lapsed or Cancelled Policies Are Costly**

Lapsed or cancelled policies are costly to the agent, but even more so to the insurer. Some agents write policies they are fairly certain will lapse in order to make their monthly sales total look good. The insurance company's administrative costs can be heavy including handling the applications, the underwriting process, issuing the policies, and collection and lapse/cancellation procedures. Of course in some cases claims are submitted during this short period further adding to the cost to the insurer without the usual number of policy premiums to balance out the claim cost.

**MARKETING AND ADVERTISING**

The insurance agent is key to the sale, marketing, underwriting, and delivery of insurance policies. Insurance agents and brokers remain the principal contacts for insurance consumers, and are expected to fulfill certain legal, professional, and ethical obligations toward their clients. As a marketing representative of the insurer, it is the agent's responsibility to represent and market the insurer's products in an ethical and professional manner. This requires knowledge of various insurance products, learning about the prospect's insurance needs and problems, and how to treat these needs with the proper insurance products. Agents can be a valuable resource, providing helpful guidance on the most appropriate use of a family’s assets and allowing them to achieve financial goals such as risk management, retirement planning, death protection, health care, asset protection, etc.

All states have laws prohibiting agents from engaging in unfair or deceptive acts or methods of competition with respect to selling and servicing insurance policies. The basis for many of these state laws is the NAIC's model Unfair Trade Practices Act, which expressly cites false advertising as an unfair trade practice and prohibits it. Under this provision, the term "advertising" is quite broad including almost any kind of communication or presentation used to promote the sale of an insurance policy.

The burden of complying with state insurance advertising laws rests on the insurance companies, since most advertisements or promotional pieces, regardless of the writer or presenter, are considered the responsibility of the insurer whose policies are being advertised. Most of the advertising and sales literature an agent uses is prepared by the insurer under the careful eye of its legal staff. For an agent, the ethical issue is not the material itself, but how the material is used and the deceptive sales presentation that may result.

**Sales Tools**

Insurance professionals use a variety of tools and methods to create interest in purchasing or keeping the products or services they sell or provide to people. Sales tools include almost everything that professionals use to communicate with prospects and clients, including presentations, sales and seminar scripts, brochures and product illustrations. Every communication designed to influence a decision to purchase a product by prospects or clients should be considered a sales tool.
Insurance companies have become much more concerned about the sales process, especially the sales materials used in the field. Many companies now require home office approval before any sales materials may be used. In some cases they must also be approved by the state before use as well.

**Advertising and Sales Literature**

The purpose of state laws governing advertising and sales literature is to provide full and fair disclosure of all material information. Ethical advertising, regardless of its origin, is the responsibility of the insurer. Advertising information must not be obscure, ambiguous, deceptive, or misleading and must be truthful and accurate.

States usually specify that advertising and sales material may not omit information or use statements which are misleading to potential buyers. Advertisements cannot use jargon or terminology that would be confusing for a person not knowledgeable about insurance coverages. An advertisement cannot use language which exaggerates benefits or fails to disclose policy exclusions or limitations. In fact, most states require the insertion of specific wording for consumer protection.

Other ethical advertising standards include the following:

- It is misleading for an advertisement to imply or state that an insurer or a policy has been approved or endorsed by an individual or, a group, unless it is in fact true.

- Statistical information used in advertising must accurate and reflect all material facts. Usually, the source of the statistical information must be disclosed.

- It is unethical and misleading if advertisements mislead the public with regard to the purpose of the policy, benefits to be derived from the policy or falsely identifying the type of policy being advertised. For example, referring to a life insurance policy as an investment product or retirement plan.

- Life insurance advertising must not imply or state that policy dividends are guaranteed. Nor may any sales literature or proposals combine guaranteed policy values (such as the cash value) with dividends which are not guaranteed.

Many states require the company to keep a record of advertisements used in the state; this would include advertisements used by agents. An interesting question arises with regard to independent agents who represent several companies and advertise under their own names. In many states an agent cannot advertise a product under their name alone. Any advertisement must contain the name and sometimes the logo of the insurer as well as that of the agent.

Companies must establish clear lines of communication, control, and responsibility over the dissemination of advertising and promotional materials by company officials whose compensation is not linked to sales.

**Advertising and Other Communications**

The objective of an ad or direct mail piece is to generate the maximum interest possible in the products and services advertised. However, ads, direct mail and other types of mass
communication may cause ethical problems. Special care must be taken to present the material in a clear and honest way that prospects and clients can readily understand.

“Advertising includes advertising in print and other media, such as:

- Direct mail
- Flyers and handouts
- Personal brochures
- Posters
- CDs
- Websites
- Internet advertising

Electronic advertising and other communications such as e-mails and websites may present special ethical challenges, especially for insurance or financial sales professionals. The viewer must not be misled in any way by the ad or communication.

Sales people sometimes attempt to motivate readers to act immediately by stating the product or service is available, or is at a particularly low price, only for a limited time. While there is nothing ethically wrong about such a claim if it is true, however, the use of this language in an advertisement or sales literature when it is not true is dishonest and unethical. All advertising pieces and sales literature that the professional uses must be examined to ensure that any exaggerations and ambiguities are removed or clarified.

**Motivation of Prospects and Clients**

It is also unethical to attempt to motivate prospects and clients by using fear, guilt or other negative emotions. Ethical sales professionals seek to help prospects and clients to accurately identify their real needs and goals. Agents must conduct an objective and comprehensive effort to gather facts and information. Only then are sales professionals in position to determine what products and services to ethically propose to prospects or clients.

**Words to Avoid**

The advertising industry has long been aware that many consumers are conditioned to more quickly recognize certain words, such as best, biggest, greatest and other superlatives -- while ignoring the meaning of other important words. For this reason, words such as the following should be scrupulously avoided, unless there is clear evidence that their use is accurate and appropriate:

- Special
- Full
- All Risk
• New
• Comprehensive
• Unlimited
• Best
• Generous
• Low cost

‘Puffing’ occurs when a sales person presents a product in an exaggerated manner by describing a product as new, best, unique or revolutionary. These and other superlatives, such as lowest cost, lowest risk, safest and similar words could mislead the reader. Legally and ethically, this language must be scrupulously avoided, unless its truth can be verified.

Other terms that are potential ethical breaches are tax-free, tax-favored, and tax-advantaged or words that point to the tax benefits of life insurance or other products that offer special tax treatment should not be used without additional qualifying language that advises readers to check with their tax advisors for applicability in their specific situations. Because of the lack of space and time to provide complete disclosure in advertising and direct mail pieces, it is a good idea to avoid discussing specific products or features in them.

**Modifying Sales Tools and Methods for Seniors or Impaired Persons**

Based on statistics from the U.S. Bureau of the Census, the number of U.S. residents over age 65 has grown substantially and continue to grow rapidly. Furthermore, the fastest growing segment of the population is made up of those individuals age 85 and older.

The senior market is projected to double in the next 30 years. This is the result of the aging of the huge numbers of baby boomers as well as the discovery of drugs and medical treatments that can prolong life.

The senior market is often viewed as a potentially lucrative one for sellers of financial products and services, due to a concentration of wealth. However, the senior market is marked by a disproportionately large percentage of members with limitations, both cognitive and physical that need to be taken into account during sales and service. Because of that deceitful individuals target the senior market more frequently than any other age group.

The tools and methods used by professional sales people may need to be modified to better serve specific markets such as seniors or disabled persons. As people age, their vision and hearing often diminish, and their ability to reason may be adversely affected. Because of these limitations, certain prospects may experience difficulty in reading material with smaller type sizes or be unable to follow a particular line of reasoning in a sales presentation.

Changes may need to be made in the sales professional’s stationery, business cards, advertising, etc. to ensure that they are readable and understandable by prospects with age-related limitations. In addition, the methods that the sales professional employs in the sales process may require modification to meet the special needs of seniors.

**Stationery and Business Cards**
How sales professionals identify themselves on their business cards or letterhead is important because these are typically the first pieces of sales material received by prospects or clients. States often have very specific laws regarding stationery and business cards used by insurance professionals. Some companies may have additional requirements. At a minimum sales professionals’ letterhead and business cards should include:

- Sufficient information to adequately identify themselves and the company they are representing without misleading the public.
- The fact that they are insurance agents and their insurance license number
- The address and telephone number of the sales person’s local office

**Complete and Honest Presentation**

The insurance buyer can suffer because of a misunderstanding about a policy's terms and conditions. If a loss goes uncovered because the agent or broker did not fully understand the risk, the buyer suffers, and the industry suffers. The agent must fully understand the insurer's policies and forms and also be aware of its underwriting, pricing and claims settlement practices. An agent's duty is to present each policy with complete honesty and objectivity, pointing out any limitations, exclusions or drawbacks the product may have, along with its features and benefits. In all cases, a simple, straightforward explanation of the policy and how that policy will help fit the prospect's needs is always the proper ethical course.

Any presentation that gives a prospect or client the wrong impression about any aspect of 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 committed an unethical and possible illegal act.

Helping clients to understand how the insurance policy they buy is tied to their particular needs is an important responsibility for an agent. Educating the client begins with the application process. In many cases, the client will be required to sign authorizations for:

- Medical Information Bureau reports
- Inspection reports
- Credit reports

While some people sign these authorizations with no objection, many people feel that such reports are an invasion of their privacy. It is up to the agent to explain the necessity of such reports in the underwriting process, and also to stress the confidentiality of the information thus obtained.

The application process also offers opportunities for unethical behavior on the part of the agent. An ethical agent may exclude negative information in the hope that questionable risk will be placed or that they will obtain a lower premium than what should be paid. If a claim happens, however the policy may not pay, because they concealed information vital to the underwriting process.
The average insurance buyer knows very little about insurance and therefore relies on the advice and recommendations of the insurance agent. By the time a consumer discovers that a particular policy does not meet his or her needs or does not live up to the agent's promises, it is probably too late to purchase another. The potential for deception by companies and agents alike is significant and the consequences to the consumer can be catastrophic.

**DISCLOSURE**

Insurance agents have a duty to fully disclose to the insurer all material facts concerning an applicant or policyowner, or situations involving either, in order to assist the insurer in making any decision regarding a risk. At the same time an agent has the ethical responsibility of full disclosure to a prospect or client.

The sales professional is ethically obligated to disclose any and all information that may be material to the prospective client to allow him or her to make an informed decision. A sales professional should document the file showing the information given to the prospect. The sales person should provide any material information in written form, even if it is not legally required.

Material information is any information that can reasonably be expected to affect a prospective client's buying decision including:

- Benefits of the recommended plan
- The costs involved in the recommendation, including any that may not be obvious.
- The risks and consequences of the recommended purchase

In the old days, sales persons where expected to simply show prospects the benefits they could expect to receive by purchasing a product or service. It was up to buyers to discover any disadvantages attached to the transaction.

Today not only are sales professionals ethically called upon to disclose the benefits of the purchase, they are also required to disclose any fees or risks associated with it. The objective is to enable the prospective purchaser to make an informed decision, understanding both the advantages and disadvantage of the purchase.

To the extent that any material facts are withheld, or are presented inaccurately, the responsibility shifts from the prospect to the agent. If the prospect makes a purchase decision while not in possession of all the material facts, and things later do not turn out to the prospect's satisfaction, the agent can be held liable.

Agents must disclose to clients any hidden conflicts of interest that might be perceived to affect the recommendations the agent might make. If a conflict of interest remains hidden at the time an agent makes a recommendation, it casts doubt on the agent's motives. By disclosing conflicts of interest, agents show that they are being completely straightforward and allowing clients to evaluate all aspects of the transaction.

An agent is obligated to fully disclose all information that may affect the insurer and its ability to conduct business. Full disclosure is most important during the application and claims handling processes. An agent must complete all applications and claims forms as accurately and completely as possible. Failure to do so could lead the insurer to follow a course of action it
would not otherwise take (such as issuing a policy to an applicant whose bad driving record had been concealed). It is the agent's or broker's responsibility to see that the answers to questions on the application are recorded fully and accurately.

Between agent and insurer, the obligations and duties of both should be:

- Fully disclosed in the agency agreement,
- Fully disclosed in the general agency agreement, or
- Explicitly detailed in other written documents.

**STANDARDIZED DISCLOSURE MATERIALS**

**Disclosure Letters and Disclosure Forms**

In disclosing the benefits of an insurance policy, an agent must describe the risks as well. Agents must present fair comparisons of products. It is best to keep explanations clear and understandable and to use written disclosure forms and disclosure letters to protect all parties - agent, consumer, and carrier - from misunderstandings.

A disclosure form describes the product being sold and how it applies to the consumer's needs. This form, which is signed by both the agent and the client at the conclusion of the actual sales presentation, ensures that all relevant disclosures have been made during the sales presentation. This includes:

- Information about the insurance company
- A full description of the policy(ies) presented (including exclusions, limitations, and conditions
- The "free look" period (for life and health policies)
- The Policy Summary (or Outline of Coverage)
- Buyers Guide and other mandatory guides or pamphlets required by state or federal law.
- Any illustrations used (and a statement that illustrations are estimates and not guarantees of future results)
- A Prospectus (if a variable product was presented)

If the policy is a replacement policy, the disclosure form should state that all replacement procedures were properly followed and that all replacement forms were reviewed and completed.

A disclosure letter can be mailed to the consumer following a sales presentation. It should summarize what was discussed at the presentation, what types of insurance products the agent proposed to the prospective client, and what final decisions were made. It is important to include documentation of the risk assessment performed, the reasons for the recommendations
made, any product comparisons that were made, details about the policies recommended, and discussion of any illustrations used.

Disclosure letters and forms help establish that the agent has explained all product features as required by state law. They give the client the opportunity to confirm that he or she understands what has been presented and what has been purchased. They also reduce the possibility that the client will later claim that he or she did not understand what was being purchased.

Using standardized disclosure materials helps agents assure that the disclosures made to clients are consistent, accurate, and complete. In some cases, standardized disclosure materials may be required by state law.

The benefits of providing complete disclosure to clients include the following:

- It builds trust and strengthens the agent-client relationship.
- It makes the agent's work easier, more enjoyable, and more profitable.
- It minimizes the chance of misunderstanding and future conflict.
- It makes the client responsible for the purchase decision, reducing the agent's potential liability for errors and omissions.

**Telephone solicitation**

Federal and state laws regulate solicitations conducted by telephone. Agents who make telephone solicitations must, early in the conversation, identify themselves as insurance agents and identify the insurer they represent.

**ONGOING DISCLOSURE**

As long as an individual remains a client, the agent has an ethical obligation to disclose material information to that client, including a periodic reassessment of the client's needs as well as updates on the performance of policies in force. Ongoing service and ongoing disclosure transform a single sales transaction into a lifelong relationship.

**SPECIFIC DISCLOSURE ISSUES IN LIFE INSURANCE MARKETING**

A number of the issues have a disclosure-related aspect. For example, consider the following.

- Policy illustrations in sales presentations
- Replacement.
- Conflicts of interest

**Adverse Tax Consequences**

Agents must be sure to disclose any adverse tax consequences involved in a life insurance purchase. Such consequences are material to the prospect’s decision and must not be omitted.
Modified Endowment Contracts (MECS)

One example would be the funding of a life insurance policy with a large premium in any of the policy's first seven years, which could cause the policy to be treated as a Modified Endowment Contract (MEC) for tax purposes. The tax treatment of policy loans and surrender proceeds from a MEC differs significantly from the treatment of loans and surrender proceeds from a life insurance policy.

The agent should make sure that the client understands these potentially adverse tax consequences before purchasing any life insurance policy whose proposed funding pattern would cause it to be considered a MEC.

Using Policy Loans to Create Tax-Free Income

One of the unique tax advantages of cash-value life insurance is that policy loans are not considered to be taxable income to the policyowner. If the insured dies while a policy loan is outstanding, the policy loan is repaid with a portion of the death proceeds and none of the amounts borrowed from the policy ever become income taxable to the policyowner. Under these circumstances, it is possible for a policyowner to use policy loans from a cash-value life insurance policy as a source of tax-free income.

As long as the client has a need for a substantial death benefit, the secondary benefit of using life insurance policy loans as a source of tax-free income may be worth the risk of the adverse tax consequences. To the extent the client does not have a need for a substantial death benefit, the tax risks outweigh the tax benefits. In any case, it is up to the client to decide. If an agent proposes that a life insurance policy be used as a source of tax-free income, he or she must be sure to point out the potentially adverse tax consequences as well as the potential tax benefits.

Pension Maximization

Pension maximization is a technique for making life insurance sales to persons covered by an employer-sponsored pension where they work. If those persons are married, at retirement they will have a choice of obtaining a benefit payable for as long as they live (single life), or for as long as either they or their spouse lives (Joint-and-survivor).

The benefit based on the joint-and-survivor benefit may be anywhere from 10% to 30% lower than the benefit based on the single life. If these individuals take the lower joint-and-survivor benefit and their spouse dies before they do, they generally are still locked into the lower payment for the remainder of their life. However, if they take the higher single life benefit, these individuals risk leaving their surviving spouse with nothing if they die before their spouse does.

In some cases, these individuals can resolve this dilemma by insuring their life for an amount adequate to provide their spouse with a benefit equal to the survivor benefit provided by the pension plan. With their spouse provided for in the event of their death, these individuals are then free to elect the higher single life benefit from the pension plan.

Pension maximization can be a great concept, but agents have an ethical obligation to do thorough fact finding and to fully disclose the elements that may affect the results of a pension maximization proposal for a particular client. Agents who use pension maximization must always make sure that the amounts of coverage they recommend will meet the needs of their...
clients. They have an ethical and legal obligation to completely and accurately disclose the costs and benefits of the proposed pension maximization plan.

**Property/Casualty Insurance**

Disclosure on property-casualty (PC) accounts is more difficult that for life insurance. The first reason is that PC policies have so many more options, exclusions, endorsements and conditions. In life insurance there is only one claim whereas a PC policy may be subject to many claims over the lifetime of the contract.

Another big difference is that life insurance policies are not subject to cancellation or nonrenewal whereas PC policies are.

Perhaps the most important market conduct responsibility for property/casualty agents is disclosure. Property/casualty agents create coverage for clients based on the client's exposures. Such agents are advised to recommend the broadest possible coverage and anticipate future events. If the insured declines a particular coverage or endorsements which the agent has recommended, agents should be sure to get the declination in writing from the insured.

The agent must clearly explain policy provisions such as who is insured and who is not, what is covered, what is excluded, etc. by each policy sold, to ensure that there are no misunderstandings at claims time.

**Presentations, Illustrations, and Quotes**

It is illegal and ethical to induce a client to purchase or replace a policy by using

- presentation materials,
- illustrations, or
- quotes that are materially inaccurate.

**Presentations**

Insurance policies are often complex and difficult to understand. Most agents' presentations include some standard information regarding premiums, benefits, agent services and information regarding the company. Usually premiums are the biggest concern of the consumer and unfortunately the discussion concerning premiums often takes up a majority of the agent's presentation.

However, the majority of the E&O claims filed against an agent are related to the policy coverages and benefits, and how they were explained to the client, particularly the exclusions and/or limitations in the policy. This is one area where most agents need to do a better job.

The insurance contract is often confusing and intimidating to most clients. It is technical, complex, and rarely read fully by the insurance agent or their client. This is where many misunderstandings take place. It is important for the agent to stress to the client not only what claims the company is willing to pay, but also the conditions and limitations in the policy.
When replacing an existing policy the eligibility of an applicant (and their dependents) is always a concern. Continuity must be taken into consideration when replacing any type of policy. The existing plan should not be replaced until the new one is in force. The new policy should be thoroughly reviewed before the existing plan is dropped.

The presentation is a critical step in the sales process, since it presents the prospective client with a solution to a need that he or she has. It is the matching of an insurance or investment product to the prospective client’s requirements.

The presentation of a policy is very important, since many consumers do not understand the insurance business and the terminology involved. It is important that the agent discusses all options with the client and makes sure the client totally comprehends the concepts discussed. This is why communication skills are extremely important in the insurance industry.

If the product being recommended is a stock or bond, the sales professional needs to identify it as such. If it is a mutual fund or a life insurance policy, the prospective client must be informed. Referring to the recommended product by a name that disguises its true nature to the prospective client is unethical, illegal and indicates a lack of competence.

Agents should not use analogies to explain the unknown in terms of what the prospect already knows. Analogies should not be used to explain how a particular financial product works, since they have a high probability of misleading the prospect. The ethical concern is that the analogy often omits important information leaving the prospect with an incomplete and erroneous understanding of the product. Many clients confuse the statement “is similar to” with “is the same as.” For example saying that a variable annuity “is similar to” a mutual fund is a common, but unethical misrepresentation made by agents and other financial services representatives.

Recommendations

The principal ethical issue is that recommendations can easily be misleading to prospects and clients. Insurance recommendations should be based on a needs analysis done for the prospect. The agent customarily provides a written proposal and a product illustration. The illustration may be based on a series of assumptions that may or may not be realized. If those assumptions do not come to pass the results shown on the illustration will not be attained.

The prospect must be able to properly assess the product and its suitability for meeting his or her need. This information is necessary to better inform the prospective client so he or she will be able to make a fully-informed decision. A fair and balanced comparison that details the pros and cons of each product, along with a detailed examination of their similarities and differences, is the only ethical way to do that.

Life insurance illustrations show hypothetically how the policy would perform under a given set of financial assumptions. A copy of any product illustrations shown to prospective clients should be provided to them for their files, the sales professional should make it completely clear that the assumptions upon which the illustration is based may not be true in the future. Life insurance dividends, costs and interest rates will almost certainly be higher or lower than shown. The non-guaranteed nature of any element in an insurance product or investment must be clearly explained to any prospective client before any sale takes place.

Balanced
A balanced comparison is one that compares all the important features of the products, including the advantages and disadvantages of each. It should be obvious that an intentional misstatement concerning a competing company or product is unethical but it may be less obvious that the omission of material information would also be unethical and possibly illegal. The seller must point out to the potential buyer any negative features of the product.

An unbalanced illustration is one that presents the advantages and benefits of a product or strategy without giving equal attention to any costs or disadvantages. Another type of unbalanced illustration would be one that unfairly compares the features of one company’s products to another.

**Risk Disclosure**

Prospects and clients vary substantially in their level of comfort with risk which applies to the products they prefer and to the strategies they are willing to implement. When discussing strategies or products that involve risk, the key ethical consideration for the financial salesperson is appropriate risk disclosure.

The competent insurance agent or registered representative should fully understand the risk involved with a proposed strategy. The salesperson’s failure to advise the prospective client of the risks inherent in any recommended strategy is unethical and possibly illegal as well.

**Vanishing premium**

A life insurance policy in which policy dividends pay the entire premium at some point in the future is often called “vanishing premium”. The use of such a term, however, is misleading and should be avoided.

Consumers can be led to believe that premiums will "vanish" after a short period (such as 10 years). Many agents have used "current" values rather than the values guaranteed by the policy (which are much lower) to illustrate possible future performance of a policy.

Life insurance agents who propose “vanishing premium” life insurance should illustrate how the policy would perform if the dividends or interest is actually lower than illustrated. To do that, agents would be required to run the illustration with a conservative dividend or interest.

Life insurance agents are ethically required to explain that the premiums do not really stop. Instead, premiums continue, but are simply paid by policy-generated dividends or excess interest, whose use in that way will reduce the policy’s total cash value. Furthermore, sales professionals need to explain that premium payments might resume if the declared dividends or credited interest rate is lower than that shown in the illustration.

**Tax-advantaged Products**

A statement that an insurance policy offers income and estate tax advantages could easily mislead prospective clients. Complete disclosure requires that any mention that any insurance product is tax-advantaged must include a full explanation of the conditions required to qualify for those tax advantages.

**Illustrations**
Life insurance agents customarily use illustrations to sell insurance products. An illustration has considerable potential for ethical lapses. The illustration may be used to show the possible growth of cash values, dividends and death benefits of a life insurance policy or it may show the historic growth of a security. Regardless of its intent, the important ethical principle is that the information provided must enable the prospect to make an informed decision.

Product Illustrations Provided by the Insurer

Insurer-provided product illustrations usually present few if any ethical problems, because the insurer that provides them ensures that needed disclosures and explanations are included. Ethical issues usually arise when the illustration is created by an outside vendor, or by the insurance agent. Insurers often prohibit the use of any illustrations, unless the sponsoring company has created or approved them in advance.

Agents should use only the computer illustrations and sales materials provided by the insurers for each specific product. An agent should not, under any circumstances, use illustrations or other materials created by the agent, unless the insurer has reviewed and approved them. Insurance agents have an ethical and legal duty to those companies they represent and could be held liable for their acts by virtue of the law of agency. In addition agents must be careful to follow all laws regarding advertising in each respective state. In some cases advertisements must be approved by the state before they can be used by agents.

Ethical Issues Surrounding Illustrations

An important ethical issue in the life insurance industry is the appropriate design and use of life insurance policy illustrations. Concern over this issue has been voiced by a wide range of persons and entities: from individuals at all levels of the life insurance industry, and from persons outside the industry as well as inside it.

During the 1980s, the proliferation of computer technology made policy illustrations quickly and easily available to agents. Running a policy illustration became an automatic part of every sales proposal for many agents. Running a policy illustration for every proposal is not a recommended sales practice.

As agents got comfortable using policy illustrations, they moved away from the traditional life insurance sales process of identifying customer needs and then selling a product to meet those needs. In needs selling, the death benefit of the life insurance policy takes center stage, and cash values play an auxiliary role. Prospects are naturally attracted to cash values more than death benefits, so a lot of life insurance sales began to be made on the basis of those cash values rather than on the death benefit.

There is nothing unethical about pointing out the living benefits of cash value life insurance, but it must be done in conjunction with a discussion of the policy's death benefit. Death benefits should take center stage in an agent's sales approach because the primary purpose of life insurance is to provide a death benefit. Talk about life insurance cash values is generally unethical until the need for a death benefit has been established.

In addition to needs selling, agents must make sure that they accurately represent what the figures in a life insurance policy illustration mean. Agents won't get into trouble if they illustrate only guaranteed values.
Consumers often do not understand that policy illustrations are estimates of what might happen based on the continuation of a given set of assumptions. Too many assume the numbers used in sales illustrations are a promise or guarantee of the policy's future performance. And although sales illustrations are traditionally accompanied by strong cautionary language indicating that numbers shown are estimates only, consumers often fail to read or understand such language. Other agents exacerbate the problem by telling their clients not to worry about the low figures in the guaranteed column since their policy is certain to perform better – more like the non-guaranteed column.

Modern technology has pushed this abuse to new levels since it is now possible for agents to sit down at their personal computers and produce their own illustrations without company review. Some agents have even gone so far as to exclude the guaranteed column altogether from their illustrations.

There is a wide range of opinions regarding how the life insurance industry should approach the use of policy illustrations.

- Show Guaranteed Values Only
- Base Non-Guaranteed Values on Actual History
- Prescribe the Assumptions Upon Which Illustrations May Be Based
- Promote More Extensive Disclosure

A few states require that agents obtain the applicant's signature on a statement attesting to the fact that the non-guaranteed elements shown in a policy illustration were explained by the agent.

**NAIC Model for Policy Illustrations**

Concerned that companies and agents were using overly aggressive assumptions in creating their illustrations, in December 1995 the NAIC adopted a model regulation that provides illustration formats, prescribes standards to be followed when using life insurance illustrations, and specifies the disclosures that are required in connection with illustrations. The goal of the regulation is to make illustrations more understandable, and to make sure that illustrations are not misleading to purchasers of insurance.

According to the NAIC model, insurance companies must notify the commissioner of insurance whether a particular policy will be marketed with or without illustrations. If there will be illustrations, an illustration must be delivered to the prospect, and both the agent and prospect must sign a statement indicating they have discussed and understand that non-guaranteed elements of the policy are subject to change and actual results could be higher or lower.

The illustration must include the name of the insurer, agent, proposed insured, underwriting or rating classification on which the illustration is based, generic policy name, initial death benefit, and dividend option or application of nonguaranteed elements. The model regulation also imposes requirements on the insurer to develop more realistic scales for projecting the growth in non-guaranteed elements and cash value, and these scales (current and disciplined) must receive annual approval from the insurance department. The agent may not use illustrations that project more favorable results than those provided by the insurer.
Agents are prohibited from representing the policy as anything other than a life insurance policy (such as calling it an investment product or retirement plan). Agents must take particular care to describe the non-guaranteed elements (such as dividends) clearly. Incomplete illustrations are prohibited. Agents may no longer use terminology such as vanishing premium to imply the policy becomes paid up or that the policyholder can use non-guaranteed elements to pay future premiums.

The prospective insured must sign the illustration used during the presentation and copies must be provided to the insurer and the applicant. Even if no policy illustration is used, both the agent and the applicant must certify in writing to that effect.

The model also requires the insurance company to provide the policyholder with an annual report on the status of the policy, and notify the policyholder of any changes that would have a negative effect on policy values.

Agents should check with their insurers and their state Departments of Insurance to see whether this model law has been adopted by their state and if it has been modified.

Advice to Agents

Besides adhering to state laws and abiding by the Golden Rule, there are ways for agents to keep out of trouble. Compliance skills should be learned along with basic product knowledge and sales skills. Field offices and agencies may establish their own "code of ethics" to be used in the course of business. Agencies may conduct regular meetings for staff regarding market conduct and compliance. Agents can also take industry ethics courses to learn more about their legal and ethical responsibilities.

Agents should communicate frequently and thoroughly with their companies' compliance departments, underwriting, and claims departments. Direct contact with their departments of insurance is also recommended.

Agents must take special care to follow strict procedures (and train all employees to do the same) in taking applications, placing coverages, explaining coverages, collecting premiums, submitting changes to policies upon an insured's request, and preparing claim forms.

Agents are encouraged to review their own agency practices, sales materials and sales practices, and determine whether they are in compliance both with state laws and home office guidelines. Agents should maintain a file of sales materials that are used and discard any older sales materials that may be out of compliance with current requirements. (Anything that has been used as an advertisement or sales material may need to be retained for at least three years as part of state recordkeeping requirements.) Everything should be reviewed, from pre-approach letters, advertisements, business cards, brochures, etc. to telephone presentations, data collection (fact finders), illustrations, policy descriptions, receipts, newsletters, annual policy reviews, and all correspondence with the applicant/policyholder.

Once the agent has identified which materials are out of compliance, he or she should take immediate steps to revise them. Agents can seek guidance from the home office on questionable materials, or may decide to use only materials from the insurer's list of approved sales materials.

EXPLAINING POLICY BENEFITS AND LIMITATIONS
Most presentations involve a few set items, including premium rates, benefits, agent services and company stability. Of these, the premium amount should be the least important.

In many ways, life insurance policies are more easily understood than other types of insurance. You buy, you die, and it pays! In a health or long-term-care policy, there may be numerous limitations or conditions of payment that the consumer (policyholder) has difficulty understanding. They contain such things as co-payments, stop-loss provisions, elimination periods, plus a variety of other confusing and easily misunderstood clauses.

The most extreme example of confusing policy language is found in property-casualty policies. There are often dozens of coverages and coverage options, coverage triggers, exclusions, limitations, and conditions. In one section coverage is provided but in another section it is limited or removed. Any contract can be confusing to the consumer and any contract can cause a misunderstanding.

Full disclosure is always necessary in any type of policy being suggested to a client. Where different interpretations are possible between a brochure or outline of coverage and the actual policy, the policy is always the final authority. A brochure is simply a selling too. An agent who has not read the policies he or she is selling, is an agent waiting for a lawsuit to happen.

Whether dealing with a property, casualty, health, disability, or life insurance policy, make sure that the questions on the application are clearly understood and answered correctly. Sometimes an agent simply is not aware of existing conditions. If the applicant does not fully understand a question, it may be incorrectly answered. It is the responsibility of the agent to present the questions in a way that is understandable. A policy may be rescinded by the insurance company for incorrect or undisclosed information. Since these types of misunderstandings can easily happen, an alert agent will closely monitor the questions and answers on applications.

Some agents are extremely knowledgeable, but they are unable to present their knowledge in a way that is understandable to the layperson. An ethical agent will put a priority on client understanding, taking time to learn better communication skills along with product knowledge.

The Agent’s Responsibilities to the Insurance Company

Clearly, an agent's duties to the insurance carrier extend beyond the mere fulfillment of the strict terms in the agency agreement. As in all business dealings, the agent must:

- Display utmost good faith, honesty, and integrity in dealing with the carrier
- Follow the carrier’s reasonable instructions (within the confines of the law)
- Avoid conflicts of interest in representing multiple carriers
- Solicit business that will be profitable both to the agent and the principal

Some responsibility falls to the consumer, as well, to seek out alternate sources of information, make appropriate inquiries, shop with a few different agents or companies before making a purchase, and not blindly trust the advice of a single agent. One of the biggest problems is that consumers have been taught over the years to shop for insurance based on price alone. Just as you can’t compare a four star resort to Motel 6 on price alone, it’s impossible to compare insurance policies or companies solely on price. Consumers need to learn what other factors
are important in order to make the best decision overall. Price won’t matter if the coverage isn’t there when a claim happens. One of the problems, however, is that competition and advertising based on price has literally taught insured that there is no difference between agents, companies and policies except price.

Most agents are familiar with the term fiduciary duty. Fiduciary duty of the agent prevents him from competing with the principal or from making a "secret profit" other than what is stipulated or agreed to.

Areas of additional concern include clerical mistakes, erroneous policy limits, omissions of endorsement, misappropriating premiums, failure to disclose risk, failure to cancel or notify cancellation, authority to bind, premium financing activities and unfair trade practices.

The duties of an insurance agent to his or her insurer are established by the concept of agency. This concept is represented by the agency contract, which both parties agree to and sign. As representatives of insurance companies, agents may be granted wide authority. Within the scope of that contract, the insurance agent owes to his or her insurer the duties of honesty, good faith and loyalty. He or she also is obligated to reveal to the insurer all material facts concerning the agency relationship.

In carrying out his or her duties, the insurance agent is the direct representative of the insurer. His or her day-to-day activities are a direct reflection on the insurer's image within the community. Consequently, the agent is obligated to do the best job possible, with sincerity, integrity and technical competency. If the agent makes mistakes, then the agent may be liable either to the client or the insurer for any damages that result.

An agent must ethically give the insurance company all facts considering the insured that are pertinent to the issuance of the policy, but on the other hand, the agent also owes it to his or her client to give them all the pertinent facts regarding the insurance company. The agent has an ethical duty to both the insurance company and the policyholder.

In a legal sense, insurance agents or registered representatives must act in the best interests of the principal. Sales professionals owe certain duties to their employers, which include:

- Careful solicitation
- Loyalty and full disclosure of any material information
- Proper accounting for funds

**Careful Solicitation**

An agent has the ethical duty to protect the insurer's interests by exercising reasonable care in soliciting quality business.

The agent has a duty to solicit business carefully meaning that:

- Any insurance or securities recommendation must be suitable in relation to the prospective client's financial situation, objectives and tolerance for risk
- Any risk submitted to an insurer must be consistent with its published underwriting standards and philosophies
Loyalty and Full Disclosure

Loyalty is the basis of a relationship between a principal and an agent. Loyalty means adhering strictly to the lines of authority the principal has given the agent, and acting with absolute integrity in carrying out the principal’s business. Loyalty precludes agents from conspiring with competing principals to take business away from the agent’s current principal. And, unless an agent has specific authority to represent more than one company, he or she may not do so. Independent agents and brokers represent several companies, with the full knowledge of all involved.

The agency contract sets limits within which an ethical agent stays. Agents have an obligation to follow their insurers’ lawful and reasonable instructions. Because of the litigious environment, especially where the deep pockets of insurance companies are concerned, this obligation is particularly important. State laws now make insurers responsible for providing thorough instructions about the solicitation of business and the type of advertising and sales materials that agents can use, and seeing to it that the agents follow these instructions.

These instructions are designed both to limit the insurer’s liability and provide a minimum standard against which agents’ conduct may be measured. Agents who choose to ignore the instructions from their insurers may find their contracts terminated, and they may find themselves facing lawsuits from their insurers as well as from their clients, and possibly loss of their licenses as well.

The primary ethical responsibility an agent owes to the insurer is loyalty. This means that he or she must, at all times, act in the insurer’s best interest in every matter involving the insurer's business. An agent cannot act for himself or herself, if contrary to the insurer's interest.

Unless the agent is specifically authorized to do so, he or she cannot represent competitors of the principal. It is quite common, however, for independent insurance agents and brokers to represent several insurers with the full knowledge and consent of the other insurers.

In the insurance business, the duty of loyalty includes an obligation to fully disclose all material facts. The duty of full disclosure is particularly important to insurance companies to adequately underwrite new risks, and appropriately handle claims.

An agent is also charged with adhering to the limits of his or her authority and staying within the guidelines of the agency contract. For example, except for the compensation specified in the agency agreement, an agent cannot earn additional profits from the agency relationship by using the principal's name for personal gain.

Proper Accounting for Funds

By law, payment to an agent is payment to the insurer. The agent has the fiduciary duty to account for all funds he or she receives in connection with the insurer's business, and to turn these funds over promptly. Even if there is no illegal intent, it is unethical to delay or withhold premium payments.

Agents must be particularly honest and ethical in handling any premiums they may collect. Agents frequently collect premiums from insureds and applicants, and receive return premiums from insurers. It is the agent’s duty to make certain that these premiums are submitted to the appropriate party promptly. All insurance related funds received by an agent
are received in a fiduciary capacity and must be held in trust. An agent may establish separate bank accounts for fiduciary funds, or may deposit all such funds in a single account - in either case the agents records must clearly distinguish the amount of funds held for each person. Agents should consult their states laws for legal requirements regarding trust funds and trust accounts.

Agents should never accept cash payments from insureds. Cash makes recordkeeping more complicated, makes commingling of funds tempting, and opens the agent up to claims of wrongdoing if the insured asserts he or she paid the agent more than they actually did. In some cases it is safest to advise clients to use the cash to purchase a money order.

Most agents and brokers are authorized to collect initial premiums from applicants when the application for insurance is completed. Some are also authorized to invoice and collect renewal premiums on behalf of the insurer. In most states, an insured may be billed for insurance coverage in one of two ways: (1) the insurance company may invoice the insured and the premium is sent directly to the company; or (2) the insurance agent or broker may invoice the insured and the premium is remitted to the agent or broker, who deducts his or her commission no and remits the balance to the insurer, often on a monthly basis.

**Commingling Funds**

The agent must account for and pay the correct amounts to insureds, insurers, and others who are entitled to the money. These funds should not be mixed with personal funds. Mixing personal funds with the insured or insurer's funds is an illegal practice known as commingling.

Any agent who uses funds held in trust for personal use is guilty of theft or misuse of funds and will be punished as provided by law. Usually a misuse of funds is punishable by suspension or revocation of license, as well as fines and imprisonment.

Every agent should understand the hazards of commingling funds. While state laws vary, most professionals have an operating account and a trust account. The trust account is used for funds that do not belong to the insurance agent or the insurance agency. The operating account is used for commissions that are due and payable to either the agent or the agency and to pay the operating expenses for the agency. The trust account holds funds "in trust" for either the insurance company or the policyholder. Since these rules may vary somewhat from one state to another, any agent that is not clear on this should contact their state's insurance department for that state's specific requirements.

**CONSUMER PROTECTION**

All states have laws that regulate sales and marketing practices as well as the licensing of brokers and agents. If the agent is incompetent or dishonest, the state insurance commissioner has the authority to suspend or revoke the agent's or broker's license which provides powerful control over the insurance producer's behavior.

Though state laws regulating sales and marketing practices by insurance agents vary, there is a great deal of uniformity in the principle and intent of these laws. All are designed to protect the interests of consumers by ensuring fair and ethical conduct by an agent.
Public perceptions of the insurance industry itself are based on how well—or how poorly—an agent does his or her job. Thus, the professional insurance agent has two ethical responsibilities to the public:

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

**Consequences of Breach of Responsibility to Clients**

An agent who breaches his or her responsibility to clients to behave in an ethical manner will be exposed to two types of consequences, Personal and Legal. Depending upon the seriousness of the breach, the agent may suffer anything from loss of a client to loss of a job, or even criminal and/or civil prosecution.

**Ethics & Competition**

Agents often feel that many of the ethical challenges confronting them stem from two sources: competition and the stress of meeting performance (sales) quotas. The intense competition within the insurance industry as a whole forces management to focus on the bottom line, creating a conflict with business ethics. Furthermore, the practice of measuring and rewarding performance on the basis of production poses a challenge to ethics since the result is considered more important than the means.

Unethical behavior tends to rise as the industry becomes more competitive. Unfortunately some insurance agencies push competitive sales contests and look the other way when activities seem to compromise ethical behavior. When unethical behavior is rewarded (as with prizes or additional commissions) it further erodes ethical standards and when unethical behavior is punished, unethical behavior was deterred.

Many people may compromise their ethical beliefs to achieve success in business when under pressure. Unfortunately an honest and ethical individual can be influenced by unethical pressures especially in the workplace. In today's society, many families need two incomes for support and feel that if they lost their job, they would be unable to survive financially. Under this pressure, many people are inclined to participate in an unethical act just to keep their job. In addition, unethical behavior is often more prominent in industries like insurance which are highly competitive.

The insurance industry is highly competitive. Insurance professionals must often compete with other agents or brokers who are less principled than they should be. For an agent, there is ample opportunity to conduct business inappropriately at the expense of a competitor. These agents may offer false or misleading representations of products or services due to the temptation for financial gain (or other personal benefits).

Misrepresentation or defamation of a competitor’s character reflects negatively on the entire industry. As a duty to his or her insurer and to the industry itself, an agent must resist this temptation. Ethically an agent should acknowledge the worth of other agents and their policies, and compete only on the basis of the value of the products and service he or she can provide.
To succeed in business takes a lot of hard work, knowledge, skills, and self-motivation. Sometimes the pressures of these demands make it tempting for someone to take an ethical shortcut, but the pressure to perform can never justify an unethical act.

An agent might be tempted to resort to unethical actions when his or her production goals are too challenging. Production goals must be based on the assumption that ethical actions will be taken to reach them. If production quotas are set so high that the only way to reach them is by using unethical methods, they should be revised to a more reasonable level.

An agent’s pressure to perform may come from an internal drive to succeed. There's nothing wrong with desiring material success, or setting production objectives. In fact, both production objectives and a desire for success are positive factors in themselves. However success can be reached without violating ethical boundaries.

Ethical trouble may arise when an agent views insurance sales solely from the standpoint of self-interest. There's nothing wrong with earning a commission on the sale as long as they are providing value to the client in return for that commission. The transaction must serve the customer's best interests as well as the agent's. The agent might base a recommendation to purchase a large amount of coverage solely on the basis of his or her commission, rather than on the individual's needs. Or the self-interested agent might recommend a high-commission product when the prospect would be better served by purchasing a product that pays a lower commission.

Taking the ethical path isn't always easy. Sometimes being ethical means taking a risk of losing a sale to a competitor who isn't acting ethically. That's hard to do. If a competitor isn't being ethical, it may be tempting for an agent to "level the playing field" by acting unethically, too. It may seem "fair" to act unethically in such situations, but it certainly isn't right. The best course of action in any situation is to stay firmly within the dictates of ethics and realize that in the long run this will bring success.

**PROMOTING ETHICAL BEHAVIOR**

The more complex society becomes, the more necessary it is to teach ethics to both professionals and to the general population. In the past, ethical behavior was primarily taught to children by their parents and by churches to their congregations. As our families become more complex and spread out, these teachings seem to be diminishing.

Why would anyone want to do business with someone they know to be unethical? Would they do business with someone who knowingly lied to others simply to make a profitable commission? Would they use an insurance broker who was dishonest and misrepresented his or her clients? Ethics are the only element, other than legal mandates, that add an element of trust to many industries.

Ethics creates trust in relationships in all areas of life. Ethics comes from within an individual and challenges them to do the best job they can and helps them maintain high ethical standards with others.

Even though different conclusions may be reached to the same ethical question, it does not mean that one solution is right and another wrong. Ethical questions often have multiple answers, all of which may be correct.
Everyone's interests are tied to the interests of others. Ethical individuals always take into account other people and the effect their decision will have on others. Although everyone must look out for their own interests, this does not mean making unethical decisions. Even commission salespeople are able to make a very good living while still maintaining ethical behavior. In fact, the most successful salespeople are often the most ethical.

The insurance agent who is not ethical will, at some point, find making a living impossible because no client will wish to deal with him. People are better able to achieve their goals when they recognize the goals and interests of others. Unethical behavior is ultimately self-defeating.

The insurance profession has been labeled by many as lacking ethical standards. Unfortunately the few "bad apples" in the industry cause people to think the whole industry is unethical. This is true in many professions.

The part of the insurance industry dealing with senior products has received especially bad publicity. Part of this has to do with the age of the consumer, and because the older population controls most of the nation's wealth.

Everyone, regardless of their occupation, faces ethical issues on a daily basis. However, those in an occupation that has a "public interest," like insurance professionals, are especially prone to ethical issues. Ethics are standards to which an insurance agent or broker must aspire, as a commitment to each client.

The ethical person knows right from wrong and chooses to do the right thing. Ethical individuals believe in doing what is best for all involved. In the insurance industry the ethical agent or broker will work to do what is best for their client whether or not it provides him with a commission. Though insurance is something that all people need for themselves and for their families, many people do not realize the importance of insurance and therefore don't purchase it or don't purchase the right kind or amount. It is important that those working in the insurance business go the extra mile to help others realize the importance of insurance using their education and communication skills with their clients.

The Agency Environment

Insurance representatives are often a reflection of what is going on around them. If they are surrounded by people who are primarily concerned with themselves, it is likely that they will have that same attitude. If the agency in which they were trained stresses sales, without regard to other issues, it is likely that they will lose sight of the role that ethics should play. When ethical behavior is not deemed important by their employers or peers, it is not surprising that ethical problems arise.

Not everyone believes it is in their own self-interest to be ethical in their behavior. An agent who has never considered ethical behavior might begin to do so if the agency where he or she works has a strong emphasis on ethics. Agencies must make the effort to emphasize ethical behavior because there will always be agents who will respond favorably to such efforts. Companies and agencies must be vigilant to ensure that all employees are in compliance with the firm's ethical standards.

It is also important for people to know why they do what they do. For insurance agents, that means understanding why the industry and services are valuable. If their agency has lost sight
of ethics chances are their agents will not understand why they are doing the job beyond making money and ethics can easily be forgotten.

Though agents need to consider who they work for in conjunction with their behavior they also have to take responsibility for their own actions and decisions. If an employer is only interested in obtaining new business and increasing profits ethical behavior is possible regardless of what their employer does.

A business owner must be aware that without employees who are ethical, business transactions could not be trusted. It would certainly cripple a business if employees could not be trusted. On the other hand, employees must also be able to trust their employer to be ethical. Those who own and manage the business must also be trustworthy. Above all, ethical agents stress the need for an agency environment that does not encourage an agent to compromise his or her ethical standards just to achieve sales goals.

Often people are not aware of the influence that their jobs, and those they work with, have on the way they think and act. They think they are capable of maintaining their identity without allowing others to influence them. Even though many thought patterns and work habits are formed over time and may be difficult to change, they are constantly influenced by others, just as they are constantly influencing others. Each person may be highly influenced by what happens to them day-in and day-out in their jobs. That is why it is so important to carefully choose where they work, and with whom they work.

A work atmosphere that is kind and considerate, education oriented, and cooperative can go far in securing ethical behavior practices. However, when an agency is investing heavily in its sales force, it is likely that production is a major criteria for those employed there. Certainly there are agencies that promote both sales and ethics. It is likely that new agents become more ethical just by being exposed to those who work there (just as others will become less ethical in the opposite type of atmosphere).

Unfortunately people may make a job decision based solely on the salary or commission plan offered. Though they need to pay their bills, this is when they may get greedy and ignore certain attitudes and negative feelings about a possible employer and think that a large paycheck will provide job satisfaction and happiness.

Agents may be shown sales techniques and tactics that do not have the client's best interest at heart, but rather are intended to increase sales. They see others rewarded for sales volume, perhaps without regard to quality of coverage or service, which puts a tremendous amount of pressure on them to behave unethically. Since agents work on commission, they must produce or they may not get paid. The financial pressure can cause the most honest salesperson to be tempted to make a sale in any manner possible.

Successful agents are influential in the ethical conduct of other agents. Some people develop by imitating and repeating the actions of those around them. This is why it is so important that insurance agencies make ethical behavior a priority in the workplace. One bad example, however, can cause poor behavior in many others.

A basic question is whether or not insurance companies and management staffs actually value ethical behavior in their field force. While most people feel that practicing good ethics is also practicing good business, many agents feel that there is little, if any, recognition for ethical
behavior or practices. Insurance agencies and companies seem uncertain how to reward, or even recognize, ethical sales practices in their agents.

Underwriters value ethical behavior because it is necessary in order for them to underwrite the policies effectively. When an agent has a reputation for giving solid information, the underwriters are likely to do a better job for that agent in terms of time and judgments. On the other hand, when underwriters know an agent consistently omits needed information or misrepresents the information given, then underwriters are much more likely to question every aspect of that agent's submitted applications. Certainly, this is one way that ethical behavior is rewarded.

The celebration of the ethical behavior of producers should be at least as elaborate as the celebration of their sales production. Just as it is important to celebrate ethical behavior, ethical misconduct should be punished consistently and harshly, regardless of the production performance of the offender.

The activities and policies of a business tell the employees what the firm’s underlying values actually are. Regardless of what is written in the employee manuals or company mission statement, actions reveal more about a business than executive speeches or advertising campaigns. Each employee will judge the company by the way they are treated individually.

People are more likely to voice ethical behavior than follow it. A person's identity is established by what they do and do not do more than by what they say. Seldom are they formed by one single experience although one single experience, if great enough, can change their direction or focus in life. A code of ethics must be a goal that people deliberately choose to follow.

When success in the workplace means compromises in ethics and values, that often means that people are allowing their employees, employer, or coworkers to define who they are rather than defining that role themselves. In an effort to move up the corporate ladder, people occasionally lose track of why they do the things they are doing. To discover the role that ethics or values play in their work, clear and distinct goals are crucial so that they don't lose sight of what's really important in their lives and their work.

It is always a challenge to do the right thing in a competitive environment. But, each time people make a decision to stand for what is right they reinforce their own moral character and influence others. 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.

**Reasons to be Ethical**

To ethical people, self-respect is more important than any reward someone else could offer. Ethical people do the right thing just because it's the right thing to do.

The most important reason to be ethical is that people are a reflection of their lives, their work, their families, their community, and of themselves. Their children will copy them, their families and communities will be affected by their actions and they, themselves, must live with who they are. Those around them, including their coworkers, are affected by their values and ethics. When their character is something they are proud of, it will show in their daily behavior, which includes their work. This will bring self-assurance, which will ultimately benefit them in many ways, including financially. Personal integrity radiates confidence and everyone prefers to deal with people who seem confident.
When an agent understands the important role they are playing in another's life, the responsibility goes hand-in-hand with ethical behavior. Clearly defined goals and purposes are essential for people to understand what their lives in general and their work in particular are really all about.

For some, the very effort to be as ethical as possible brings its own rewards. The work of an insurance agent often impacts the entire financial well-being and future of businesses and families.

**GREED & ETHICS**

When an industry seems to be involved in widespread illegal and unethical behavior the cause is nearly always greed. This affects even the ethical person who simply happens to work in the industry. When an industry is perceived to be dishonest, the ethical individuals often finds themselves tainted by the activities of others.

Most agencies have invested considerable time and money in their agents, so it is important that they succeed. In addition, the future of the agency depends upon the production of their sales force. Promoting a materialistic self-serving method will not only cause frustration for the agents, but it may also side track the agency from attaining its goals.

Those whose job is motivating salespeople often portray greed as something that is necessary, even desirable in a capitalistic society. A person who is motivated only by greed cannot survive long-term. There will always be traces of greed in everyone. When greed becomes a motivating factor, however, it is dangerous to others and ourselves, as well. For companies or agencies to actually promote greed is unethical. Greed and ethics simply cannot co-exist.

It has become commonplace for insurance companies and other industries to shower their salespeople with prizes, plaques and medals for selling their products. Companies seem to believe their employees will work only for material gratification. Financial rewards are essential, but when ethical behavior is not tied to those financial rewards, many negative circumstances can develop.

Too often people have been brainwashed into thinking that material rewards are the goals that they need to achieve in life in order to be happy. When work volume is joined to financial rewards the goal becomes volume of sales and not necessarily determining the best product for the client.

Encouraging financial gain exclusively is also a disservice to clients. When there is no thought given to whether the client can afford the service or product being provided or if the client will benefit from the product, then the company is not behaving ethically.

**THE INSURERS RESPONSIBILITIES TO POLICYHOLDERS**

An insurer's reputation is one of its greatest strengths, and high ethical standards are the cornerstone of that reputation. Each insurance company should attempt to meet its obligations in an ethical manner which earns the respect of policy owners, clients, regulators, employees, business associates, and the community. The insurer’s employees and agents contribute to the high ethical standards of the company and continue to enhance its reputation and image.

To accomplish these goals, the insurer attempts to:
• Conduct its business in a fair, lawful, and ethical manner

• Offer customers those products and services which are appropriate to their needs and provide fair value

• Maintain a climate which encourages agents and employees to be honest and fair in the conduct of their duties

Policyholders may expect the insurer to comply with those laws and regulations pertaining to policyholder service such as fair sales and marketing practices, fair underwriting practices, fair claims practices, and fair notice of policy cancellations and nonrenewals.

Policyholders also have the right to expect the insurer to comply with broader insurance laws, since ultimately violations of these laws result in some impact on the public. For example, an insurer that fails to maintain adequate reserves and becomes insolvent will be unable to fulfill its obligations to policyholders.

If agents are to conduct their business in an ethical manner, then the insurers must adhere to ethical principles and encourage similar conduct from their sales force. Not only do the insurers have an ethical obligation to their agents but they also have a responsibility to the general public as well. It is the duty of the insurer to make certain that its sales force obeys the unfair marketing practices laws, such as misrepresentation, rebating, and twisting. It is equally important for the insurer to see to it that its claims personnel comply with the laws regarding claims settlements.

The insurer must enforce laws which are pertinent to agent conduct and behavior as well as comply with the laws which apply to the insurer itself. Most insurance companies have entire divisions devoted to compliance and are well aware of their obligations towards policyholders. Insurer responsibilities are important for the agent to understand, so that he or she can provide accurate advice to policyholders on what to expect from the insurance company. Also, by knowing what to expect from the insurer, the agent can see to it that the company indeed follows through.

**Due Diligence in Hiring Agents**

The truth is, there are plenty of good agents out there, providing excellent advice and service, clearly explaining the policies they sell, and fairly representing their insurance companies. It's the poorly trained, dishonest, self-serving agents that give the insurance business a bad name.

Insurance companies can be held partly to blame for these problems. Insurance agents are recruited from a wide range of sources, sent through selection and screening processes, trained, licensed, and rushed into the field where immediate sales are demanded. The result is often a staggering turnover. In the life insurance industry, only 20-25% of agents last four years or longer.

Insurance companies owe it to their policyholders to recruit and hire competent insurance agents to represent their products to consumers. Stringent selection standards are in order, particularly in conducting background checks and following up on employment histories and references. Many companies are developing "due diligence" committees that oversee the agent recruiting process.
Recruits who are properly investigated, properly trained, properly motivated, and provided with adequate support systems can succeed. Since insurance companies are being held liable for the actions of their agents they are being much more careful about recruiting, hiring, managing and disciplining their agents now than in the past.

**State Requirements for Background Investigations**

State guidelines for appointing new agents vary, but basically all require the company to certify the prospective appointee's "trustworthiness, suitability, and competency" prior to appointment.

Some states also require companies to certify that an investigation has been completed as to the character and ability of the applicant and certify that the company is satisfied that the applicant is "of good moral character, financially responsible, and trustworthy." Others go so far as conducting their own criminal and/or credit background investigations of new or newly appointed agents.

The Federal Crime Bill of 1994 imposes criminal penalties on anyone who allows a person convicted of a felony, or an act involving dishonesty or breach of trust, to participate in the insurance industry. A national search for background information such as this could cost thousands of dollars per applicant. Just conducting a criminal background check may not be enough. Some insurers report they see a correlation between an applicant’s credit history and future agent behavior.

Carriers use the information from background investigations to help ensure a high-quality distribution force. This not only helps protect companies from regulatory, legal, and other market conduct problems, it helps keep unscrupulous agents out of the business and away from the public.

By conducting background investigations, and gathering information about the potential agents financial history (including bankruptcies), criminal history, civil litigation history, education history, military record, employment or contracting history, insurance licensing history, and securities licensing history, carriers are better able to make informed decisions about appointing their agents. Most agents support the use of background investigations because they help ensure that good agents won't have to compete with unethical or underhanded competition.

**Complaints and Agent Conduct**

In most states companies are required to maintain a complaint register that records all complaints as well as the insurer's response and final disposition of the complaints. Each insurer should have complaint handling procedures that have been clearly communicated to policyholders and to agents. Policyholders should be provided with a telephone number and address for complaints and inquiries regarding their coverage.

Some states compile and release annual consumer complaint ratios by insurance company -- some include this information on their web site. These should be considered only one part of the total picture for an insurer and are not intended for marketing purposes.

Consumer complaints about specific agents or agent practices require special attention from the insurance company. The insurer should respond promptly to the consumer and conduct fact finding, audits, and disciplinary action as necessary to correct any agent misconduct.
Policyholders have the right to expect fair treatment from insurers when it comes to policy cancellations and nonrenewals. State insurance statutes define the amount of advance notice required before certain types of policies may be cancelled or not renewed, and some even restrict policy cancellations by limiting the reasons upon which the insurance company may base its decision to terminate a policy.

**THE INSURER'S RESPONSIBILITIES TO AGENTS**

The insurance company has certain legal, regulatory, professional, and ethical responsibilities to its appointed agents. The company establishes the agent's employment contract, must permit the agent to act in accordance with the terms of the contract, and must recognize all of the provisions of that contract. The agency agreement should clearly establish the relationship between the agent and the company, including:

- Representation and advertising methods
- Fiduciary arrangements
- Status of binding authority
- Procedures for premium payment (emphasizing "no commingling" laws)
- Cancellation procedures if the relationship is terminated
- Processing and recordkeeping arrangements, and
- Any requirement for agent errors and omissions coverage

Since the insurance company operates entirely through the people it employs (especially its agents), the direction and example must come from the company. Companies should maintain visible senior management support for compliance from the home office management and personnel all the way through to agency operations.

In addition, the company must pay the agent the compensation agreed upon in the contract, reimburse the agent for proper expenditures made on behalf of the principal, and indemnify the agent for any losses or damages suffered without fault on the part of the agent but occurring on account of the agency relationship.

**Compensation**

The most important duty that the principal owes the agent is compensation, or payment, for the business the agent has sold for the principal. This compensation is usually in the form of commissions that vary by line of insurance. The commission rate on renewal business may be the same or lower than on new business, depending on the company.

**Employment**

When the agency agreement is signed, the principal must specify a reasonable period of time during which the agent is expected to produce a certain amount of business. The agency agreement usually spells out the type of business, the amount of premium that must be
generated, the amount of commission that will be paid for each line of business and the length of time the contract will remain in effect. If the agent fails to meet the terms of the contract, the principal may terminate the agreement, withhold compensation or reimbursement or, if the agent has realized personal profits in excess of those stipulated in the agency agreement, sue to recover the excess profits.

**Indemnity**

The principal is also 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. However, if the agent is guilty of breach of duty or lack of due care that harms the principal, the insurer may sue and recover monetary damages from the agent.

**Clear Compliance Directives**

An insurance company must provide explicit guidelines for acceptable and unacceptable market practices. Agents should receive initial and ongoing compliance training which defines what is and is not permissible when the agent is in the field. In the past, agents were given great latitude in managing customer relationships without home office oversight, but regulators have made it clear that those days are over. Regardless of whether the company considers its agents to be "independent contractors," the government imposes strict oversight and supervisory responsibilities.

Many insurers have established general guidelines for ethical employee and agent conduct. Commonly those guidelines address confidentiality, conflicts of interest, and legal and regulatory compliance.

Many companies make it easier to comply with legal and ethical trade practices by providing agents with company manuals spelling out compliance policies. Companies have established entire compliance departments which control the creation, review, distribution, and use of all advertising materials. Compliance personnel train agents to educate the consumer, and require them to attend meetings to learn compliance and advertising standards.

**Agent Support and Training**

The insurance company should provide for excellence in the recruiting, training, and ongoing support of its agents not just as part of its obligations to consumers but as part of its responsibilities towards its own agents. Agents deserve a fair chance to succeed in the insurance industry, and in many cases this depends on the quality of training and education provided by the principal. Industry experts have suggested strong mentoring programs as a good step to attracting the best and brightest. Others recommend that detailed training programs that last six months, a year, or even two years are necessary before an agent is ready to work alone.

Agent training often begins as soon as the agent is hired by the company. This training is primarily product and sales training designed to provide the new agent with a sales approach and a general working knowledge of the company's products.

Some companies and agencies strongly support technical and continuing education, even going so far as to reimburse agents who attend continuing education seminars, or who enroll in educational courses and professional designation programs. In addition, the insurer will often
encourage continued professional education through such industry associations as the Life Underwriting Training Council, and the Chartered Property/Casualty Underwriter and Chartered Life Underwriter programs available through the American College and American Institutes.

Most state regulations include agent training requirements as part of the insurance company's responsibilities. It is also the insurer's responsibility to train and develop quality sales managers, who influence and guide the sales force on a daily basis through training and sales supports. Proper agent and management training can produce the desired behavior and ethical conduct expected of the agents by the company and contribute to agent retention and success. Agents who are successful will stay in the business. Adequate training and management programs can enhance the agent's chances for success and survival in the business.

FRAUDULENT AND ILLEGAL ACTIVITIES

Some activities are not only unethical, but are also violations of the law. Any activity that is illegal is also unethical and must be avoided by the professional insurance agent.

Illegal activities reflect badly not only on the individuals who engaged in them, but also on the people who worked closely with that individual and either knew or should have known what was going on. If people know that illegal activities are taking place, or if they are in a position of responsibility and should be alert to illegal activities on the part of those who report to them, they may be considered just as guilty under the law as the persons who committed the illegal acts.

To a large extent, trust is an absolute concept. If people don't trust a company or the insurance industry in general, it makes the marketing of insurance that much more difficult for everyone in the industry.

The image of the insurance industry is everybody's business. Overlooking illegal activity on the part of others is unethical, since it doesn't serve the best interests of the public, and because it makes things harder for anyone involved in insurance marketing.

Ignorance of the law is no excuse, so agents should be sure they are aware of the laws that apply to the area where they do business.

FRAUDULENT CLAIMS

It is unlawful for an agent to submit a false or fraudulent claim to receive insurance loss proceeds. This includes "staging" or conspiring to stage accidents, thefts, destruction of property, damage or conversion of an automobile, etc.

Fraudulent claims, exaggerated claims, or malingering should be reported to the carrier immediately.

Studies show that even individuals who generally consider themselves to be "honest' think there is nothing wrong with inflating insurance claims in order to collect more than they would otherwise be entitled to after a loss has occurred.

One of the most difficult decisions an agent may have to make is when he or she suspects a valued client of submitting a fraudulent or exaggerated claim. Conversely, the agent must be careful not to charge someone with fraud when there is no evidence of fraudulent activities.
Fraudulent claims are investigated at both the state and company level. Many state insurance departments have established fraud investigation units and impose heavy fines and penalties for those caught submitting fraudulent claims. The insurance companies have special investigative units (SIUs) to conduct claims reviews and to help detect and prevent fraudulent claims.

**AGENTS AND UNDERWRITING**

*Post Claims Underwriting*

Life and health policies are issued based upon the applicants responses to questions on the application designed to determine the applicant’s health status. The time to conduct comprehensive underwriting and clear up any questions is before a claim arises, not after.

Postclaims underwriting is the illegal and unethical practice rescinding, canceling or limiting of a policy or certificate due to the insurer’s failure to complete medical underwriting and resolve all reasonable questions arising from written information submitted on or with an application before issuing the policy or certificate.

**Credit Scoring – the Ongoing Controversy**

Credit, and the ability to access it and manage it, is an integral part of everyday life.

Today, credit records affect getting a job, finding a place to live, securing a loan, setting up telephone service and buying insurance. Most consumers benefit from the use of credit information because most people manage their debt well and therefore have good credit histories.

The use of credit information by the financial services industry has been widespread for a long time, and credit has become a key tool for insurers. Commercial insurers have for decades reviewed the credit history of businesses before issuing certain types of policies.

One reason for this is that businesses in poor financial condition might tend to cut back on maintenance and safety, which may lead to more accidents, injuries and claims.

Home and auto insurers use credit information to produce an “insurance score” because it helps them to more accurately assess and price a risk. In conjunction with other information such as years of driving experience, previous accidents, the type of car or home, and where the driver lives and drives, credit-based insurance scores allow insurers to differentiate between lower and higher insurance risks. Many recent studies confirm the strong correlation between credit history and loss in both auto and homeowners insurance.

**Failure to Obtain Full and Complete Client Data**

It is important for the agent to know the underwriting guidelines of each insurer they represent before soliciting business.

In accordance with agency law, information given to the agent is the same as providing the information to the insurer. If the agent knows of anything adverse concerning the risk to be insured, it is his or her responsibility to provide this information to the insurer. To withhold
important underwriting information could harm the insurer's risk selection process. A failure on the insurance sales person's part to obtain full and complete information can also lead to recommending or selling products that are unsuitable for the prospective client.

State law usually requires the agent and the applicant to certify in writing that the applicant has read, or had read to him, the completed application and that any false statement or misrepresentation may result in loss of coverage.

Some agents, usually property-casualty, have the authority to issue policies for the risks they have underwritten. Copies of the application, binder of insurance and the policy are sent to the insurer. Even though a policy or binder has been issued, the insurance company underwriter may send a notice of cancellation if he or she finds that the risk does not meet company guidelines.

The formation of a life or health insurance contract is somewhat different than property-casualty in that the life or health agent usually does not have the authority to bind coverage. The agent can only solicit offers from prospective insureds. The insurance company approves and issues the contract after receiving the application and premium from the agent.

The restricted underwriting authority of the life insurance agent is related to the nature of life insurance contracts. The insurance company is in a much better position than the agent to evaluate the applicant's insurability. Life insurance policies are generally non-cancellable, long-term contracts. A life insurance policy is contestable only for a one or two-year period. Property and casualty insurance, by comparison, involves a short-term contract which can usually be cancelled at almost any time.

Failure to complete an application accurately and honestly could subject the agent to disciplinary action both by the company and the insurance department.

**Field Underwriting**

Field underwriting involves the agent analyzing risks and exposures, taking steps to avoid or reduce risks, considering loss control efforts and submitting risks to the proper markets. However, the agent cannot perform all the needed underwriting services.

Company underwriters are increasingly relying on paramedical exams and blood tests for information in order to accurately evaluate life and health risks. Blood testing is almost universally used to determine cholesterol levels, elevated liver enzymes, and the presence of HIV infection. In many jurisdictions, HIV testing requires informed consent of the applicant, confidentiality of results, and proper notification procedures.

Every agent or broker should engage in the process of screening out unacceptable risks. There is no point in submitting risks that obviously will be rejected by the insurer, because that wastes their time and that of their client. And, if the agent submits poor risks consistently that are accepted, his or her book of business with the insurers will suffer and the agent might jeopardize his or her relationship with them.

A primary objective of the agent as a field underwriter is to help protect the insurance company from adverse selection. When confronted with an impaired risk, it is up to the agent to ask the right questions and submit the proper information to the underwriting department so the appropriate policy can be issued.
Agents have a duty to make known to their companies any information that would impact the underwriting decision. If agents withhold or distort such information, the company will end up insuring risks that it otherwise would not have accepted, or would have accepted only at higher rates. As a result, claims experience will be worse than anticipated, and that will hurt the company's financial performance. That, in turn, may affect the performance of the policies owned by an agent's clients, and it may also affect an agent's competitiveness in the marketplace, if the company finds it necessary to raise its rates generally.

The agent's duty as a field underwriter can conflict with the agent's self-interest regarding the earning of commissions. If the company obtains information which causes it to reject the risk, the agent won't make a sale. Even if the risk is simply "rated up" by the company rather than rejected, the agent may be afraid that the sale would be lost anyway because the prospect may decline.

The Application

It is the responsibility of the agent to be sure to ask the applicant medical and nonmedical questions clearly and precisely and to record the answers the same way. The agent must be careful to present the facts and not his or her interpretation of the facts. If the agent has any suspicions whatsoever, any suspicions should be stated to the underwriting department in the space provided on most applications for agent's comments. The goals of the agent are to get complete and accurate information from the applicant and to detect the possibility of moral hazard.

The Agent's Statement is part of the application and requires that the agent provide certain information regarding the proposed insured. Generally, this includes information regarding the agent's relationship to the insured, data about the proposed insured's financial status, habits, general character and any other information which may be pertinent to the risk being assumed by the insurer.

Agents have a responsibility to provide complete and accurate information about an applicant, and that responsibility extends beyond the items listed on the application form.

Sometimes agents are tempted to withhold or distort underwriting information not so much out of their own self-interest, but instead to serve the applicant's best interests. Agent's obligation to prospects involves making proper coverage recommendations and providing service not concealing or falsifying underwriting data. Misrepresentations on applications can cause coverage to be voided which does not serve the client's best interests.

Applications for life and health insurance generally require detailed information regarding the insured's past medical history, current physical condition and personal morals. Many times, the proposed insured must undergo a medical examination.

In addition, the agent is responsible for providing the insurance applicant with privacy notices and information such as the Notice of Insurance Information Practices, and finally to provide the insurance applicant with necessary receipts for the initial premium collected.

Precision and accuracy in completing the application are in the best interests of both the insurer and the prospective insured. The agent also has an ethical responsibility to educate his or her prospective client so that he or she fully understands why the information is required, how it will
be evaluated, the need for accuracy and honesty in answering all questions and the meaning of insurance terms included in the contract.

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 pertinent information about a prospect is doing both his client and his insurer a disservice.

A signed and witnessed copy of the application often becomes part of the legal contract of insurance between the insured and the insurer, so it is of utmost importance that the application information be accurate and complete, and that the proper signatures are secured. Material omissions or errors might subject the applicant to denial of benefits, voiding of the policy, and even prosecution for fraud.

**Misconceptions**

It is crucial to present policies in a clear manner, with no misconceptions. When agents take the time to fully explain all parts of the policy, everyone benefits. Most consumers do not have the knowledge and understanding of the policies to the extent an agent does. Trying to explain a misconception once a policy has been issued is not only difficult to do, but is damaging to the agent's reputation since the client often thinks that the agent was trying to mislead them.

**Premiums**

Another source of confusion and misconception can occur when policy premiums are discussed. Premiums can be falsely stated to the client in order to get a sale. We are all human and therefore we all make mistakes. Misquoting a premium may result from a mistake, a lack of education, or even inexperience, whereas a deliberate misquote is done on purpose to defraud the client.

**BINDERS AND CONDITIONAL RECEIPTS**

**Submitting the Application & Initial Premium**

Life and health insurance agents are generally encouraged to collect the initial premium with the application. An important point that the agent should make to the applicant is that if the applicant waits to pay the premium, he or she may become uninsurable, or may die before the policy takes effect. When the initial premium is not paid with the application, there can be no conditional receipt, no contract is in force. The applicant is not making an offer to the insurer. He or she is merely inviting the insurer to make an offer by issuing the policy.

Since there is no insurance in force under these circumstances, when the agent delivers the policy and collects the initial premium, there may be additional underwriting requirements which must be satisfied. Most commonly, the insurance company may require that the insured sign a health statement verifying that no change in health has occurred since the date of the application.

**Prompt Submittal of Application**

Agents should also explain to clients that once the underwriting department of the insurer receives the applications, further information may be needed. Anything which delays the issuance of the policy is detrimental to both applicant and agent. It is important that the agent
obtain all possible relevant information from the client before sending in the application. Taking time to ask questions to reveal particular risks affecting the policy will save time later.

Once the agent is satisfied that the information on the application is both thorough and accurate, he or she has an ethical responsibility to the client to submit the application to the insurer as soon as possible. The agent has the further responsibility to deliver the policy as soon as it is issued, and to sit down with the client and go over its contents.

The agent should review all forms for completeness and be sure that they are properly signed. Not only does this make for good relationships with the home office underwriter, but it is extremely important to the applicant. Unnecessary delays in delivering the policy can cause the applicant undue anxiety and result in a loss of confidence in the agent. Since agents are handling money belonging to their clients, it is extremely important that an accurate record of such transactions be kept. It is also wise for the agent to keep copies of applications and other information. This avoids unnecessary delay or other problems if the originals are lost.

Two facets of insurance policies that need particular explanation in order that the client fully understands them are the Binder and the Conditional Receipt.

**Binder**

A binder has the full force and effect of the policy. It is an acknowledgment that coverage is in effect during the time it takes for the company to issue the policy. A binder can be oral or written, but a written binder is preferable to avoid misunderstandings later. Only agents who have been given binding authority by the insurers they represent may issue binders. Usually life agents and property casualty brokers and solicitors are prohibited from binding coverage by law.

All states have laws regarding the issuance of binders including the information they must contain, the length of time they may be issued, and other important details. Agents must be familiar both with these laws and with the binding authority given them by their insurers in their agency contracts. The client, the agent, and the insurer should all receive a copy of the binder.

**Binding Receipt**

A few life insurance companies authorize certain agents to issue an "unconditional" or binding receipt that makes the company liable for the risk from the date of application. Like the property-casualty binder referenced above, his coverage lasts for a specified time or until the insurer either issues a policy or declines the application, if earlier. The specified time limit is usually 30 to 60 days.

With a binding receipt, regardless of the applicant's insurability, he or she is covered for a specific period of time following completion of the application and the payment of the initial premium. This type of receipt for life and health policies is rare.

**Conditional Receipt**

A Conditional Receipt, used in life and health insurance, provides coverage once the initial premium is paid, and before the policy is issued, however, coverage is provided during this period only if the applicant meets underwriting requirements for the particular coverage. Coverage depends upon the insurability of the client.
Agents may give the applicant a conditional receipt if the premium is paid at the time of the application. This receipt makes the coverage effective on the date of the application, if the applicant is found to be insurable under the company's general underwriting rules in effect at the time of application. However, some conditional receipts make coverage effective on the date of application, or the date of the medical examination, whichever is later.

If the applicant were to die before the policy was issued, the beneficiary would receive the face amount of the policy. However, if the applicant was found to be a substandard risk, then the conditional receipt is null and void and no coverage would be effective.

**Altering Applications**

Altering applications for any purpose is illegal and is not to be engaged in, encouraged, or tolerated under any circumstances. Applications have been altered for a number of fraudulent reasons. Sometimes the purpose has been to change underwriting information in order to obtain a more favorable premium rate. In other cases, applications have been altered to switch the type of coverage being applied for, from term or an annuity to whole life, for example, in order to earn a larger commission on the sale. Another fraudulent instance of altering applications has involved adding zeroes to the amount of coverage applied for.

**Signing Someone Else's Name (Windowing)**

Obtaining client signatures on all of the necessary applications and forms is an important part of an agent's job. Every so often an agent simply forgets to obtain a signature from the client. Though this is often simply an oversight on the agent's part, when it occurs regularly it might show that an agent needs to work on their organization skills.

In some cases, signatures might be purposely overlooked as a way to avoid negative aspects of certain disclosures. This is not only unethical, but illegal as well since all forms need to be disclosed to the client.

"Forgetting" to obtain a client's signature may lead to the agent forging the client's signature. Forging a client's signature is much more common in business than most people realize. Forging a signature is not only unethical, but also illegal.

"Windowing" is a term used to describe forging someone else's signature, derived from the illegal practice of holding an authentic signature up to a window and tracing over it on another form. Windowing is not only illegal, but self-defeating, for there is no way it can go undetected forever. Perpetrators may be subject to both criminal and civil penalties as well as loss of their career and reputation. Any form of windowing is blatantly illegal and is not to be engaged in, encouraged, or tolerated under any circumstances.

**Applications and Fraud**

Fraud can be committed:

- By the applicant without the agent's knowledge,
- By the agent without the applicants knowledge, or
- By both working in conjunction.
Agents have advised applicants to omit information to ensure that coverage will be issued, or will be issued coverage at a lower premium. Sometimes agents illegally sign applications or other disclosure forms on behalf of the applicant, in the belief they are helping the client expedite the request for coverage.

If an agent ‘enhances’ an insurance application in order to help the applicant get a lower premium, and the policy is issued, if a claim occurs the insurance company may deny the claim based on misrepresentation.

The carrier has entrusted the agent to collect all the information relevant to accepting or declining a risk. If pertinent facts are concealed, omitted, or understated, the insurer may take on risks it would not otherwise accept, or may collect insufficient premium for the risk. In that case the insurer and the insured may bring legal action against the agent to recover damages.

**Explaining the Underwriting Process**

Another ethical responsibility to the applicant is to briefly explain the underwriting process that the application will undergo. Underwriting is the process of selection, classification and rating of risks. During the risk selection process information is evaluated to determine whether the risk is acceptable, and how the individual or risk will be classified (preferred, standard or substandard). Once this part of the underwriting procedure is complete, the policy will be rated in terms of the premium which the applicant will pay. The policy will then be issued and subsequently delivered by the agent.

**Keeping the Applicant Informed**

The underwriting process for an insurance application can be time-consuming. Delays can occur whenever an underwriter needs additional information from the applicant and relays that request through the agent, or whenever a counteroffer, a different policy or a different rate is proposed to the applicant, again through the agent.

It is an agent’s duty to help ensure that there are no unnecessary delays in the underwriting process. This means checking the application for accuracy and giving careful thought to the information provided and the coverages offered before the application is submitted. Many underwriting delays occur simply because the application is not complete or is not clear.

Applications, binders, pictures, building diagrams, medical reports and other pertinent underwriting information should be submitted to the insurer as soon as possible. The time frame will vary, of course, depending on the type of insurance and the complexity of the risk. An agent must take these factors into account in order to move in an efficient manner. If it appears that the underwriting process may take longer than anticipated, the agent should inform the applicant about the delay.

**Ratings and Rejections**

Most policies are issued as applied for. On the other hand, some policies will be surcharged or rejected because the risk does not meet the insurance company’s underwriting guidelines. When this happens, the agent has two responsibilities:
He or she should personally review the surcharge or rejection to determine if the rating or rejection was proper and to get as much information as possible to be able to explain the higher premium or rejection to the applicant.

Assuming the rating or rejection was valid, the agent has the responsibility to notify the applicant promptly. To withhold this information in an effort to prevent the applicant from seeking insurance elsewhere is a breach of ethics and could actually harm the applicant and his or her family.

**Delivering the Policy**

After the policy is issued and prior to policy delivery, the agent should check to be certain that the coverages, limits, forms, endorsements and so on are contained in the policy as requested.

Legally, the policy is considered “delivered” when it is mailed or turned over to the policyowner or someone acting on his or her behalf. Some companies mail policies directly to policy owners. However, many prefer to have the agent make a personal delivery.

Because some coverages do not take effect until the policy is delivered, timely delivery is critical. The agent should take the time to explain all policy provisions, particularly the exclusions, and any riders that may restrict the coverage given in the policy, review the purpose of the policy and how it fits into the policyowner's total insurance program, reinforce the relationship and good will established with the client, explain the possible need for additional coverage, explain how the agency provides ongoing service (such as annual reviews), and even ask the insured for referrals.

The agent should carefully explain coinsurance, deductible provisions, exclusions (especially on all risk policies) and any other important information in the policies being delivered. Explaining the policy and showing how it meets the policyholder's specific needs, reinforces the sale and helps to avoid misunderstandings. It also serves to build trust and confidence on the part of the client in the agent's abilities and desire to be of genuine service.

With life and health insurance policies, if a conditional receipt has not been previously issued, the insurer may require the agent to obtain a statement of good health at the time of policy delivery. Once the policy is delivered, the agent should wrap up any concluding paperwork and complete the policyholder's files.

**Explain the “Free Look”**

Another practice that is considered unethical is the lack of full disclosure of specific policyowner rights such as the “free look” provision. Most states require the insurer to provide for a “free look” period (usually 10 days and 30 days for some policies) during which a life, health or disability insurance policy holder may review the policy and make a final decision regarding the policy and receive a full refund if they decide not to keep it. The free look period begins on the date of policy delivery, so it is important to fully explain the details of the free-look provision, and to acknowledge any request for a refund promptly.

Agents may withhold this information in an attempt to avoid having the client send the policy back for cancellation. In these cases, however, the policy holder will usually allow the policy to lapse soon after the purchase anyway. The insurance professional's failure to tell the policy
owner his or her rights under the free look provision, or to explain the details of the provision, is unethical, and only postpones the lapse of coverage anyway.

**Controlled Business**

When an agent becomes licensed, he or she must intend to actively engage in the insurance business with members of the public, and not use the license principally for transacting a disproportionate amount of controlled business. Controlled business means insurance on the agent's, broker's, or solicitor's own property or interests, or those of his family, his employer, or any partnership, association, or corporation in which he or a family member has an interest as an officer, director, stockholder, partner or employee.

A certain amount of controlled business is permitted but a licensee may not be permitted to earn commission or compensation from controlled business in excess of a stated amount, depending upon the state, during a stated time period or the producer's license may be revoked or suspended.

**Reporting Misconduct**

Another area of agent responsibility is that agents are being asked to report suspected or confirmed misconduct on the part of other agents or company employees. This is because many times agents are aware that their colleagues are violating fair practices laws but company compliance officers now hold everyone in the company responsible for monitoring compliance.

**Premium & Rates**

The premium is the total cost for the insurance coverage (or limit of liability) purchased, and is calculated from the rate—the cost per particular unit of insurance to be purchased. Base rates have been developed for various risks and these rates are multiplied by an exposure base (i.e., amount of insurance, payroll, sales, and area). In life insurance, for example, the rate applies per $1,000 of coverage; for workers compensation insurance, the rate is applied per each $100 of remuneration (payroll).

Some risks are class rated, which means that the loss history of a class of risks having similar characteristics (i.e., male drivers age 25, jointed masonry buildings in a particular urban area, male non-smokers age 30, etc.) was used to develop the rate. Underwriters usually have the option of applying rating modifications, based on the loss history or special characteristics of a risk. For example, the insured's actual past loss experience plays a major role in the development of the rate. In certain lines of insurance an underwriter may use judgment rates, based largely on the underwriter's knowledge and experience. This type of rating is still subject to the rules against discrimination in rate making.

**POLICY REPLACEMENT**

Unethical activities regarding policy replacement are some of the most common complaints filed against agents.

**Twisting/Churning/Replacement**

Virtually every jurisdiction prohibits the act of twisting or churning and harshly penalizes any offender. The act of "twisting" or "churning" is defined as misrepresentation or comparison of
insurers or policies for the purpose of inducing a client to change, surrender, lapse or forfeit an existing policy. Agent violators may be subject to:

- fines,
- imprisonment, and/or
- license suspension/revocation.

Twisting and churning are forms of replacement that employ the use of misrepresentations to influence the policyowner's decision. The term "twisting" is used to describe the practice of using misrepresentations to induce replacement of a policy issued by an insurer other than the one the replacing agent represents. The term "churning" is used to describe the practice of using misrepresentations to induce replacement of a policy issued by the insurer the agent represents. Whether twisting or churning, the agent's goal in such cases is to earn a new first-year commission for himself or herself and not to serve the client's best interests.

Any action taken to further the agent's self-interest rather than the client's best interests is unethical. Any form of misrepresentation is, of course, illegal and unethical. Twisting and churning are specifically prohibited by law in most states, as well as being illegal under the general prohibition against misrepresentation.

**Twisting**

Twisting is illegally inducing a person to drop existing insurance in order to purchase similar coverage with another agent or company. Misrepresenting a policy or making incomplete comparisons of policies to induce a policyowner to change or replace an existing policy is called twisting. The primary hallmarks of twisting are deceit and misrepresentation--deliberate attempts to make a prospect believe something other than the truth, either by omitting details or by making false statements.

Although twisting applies largely to life insurance policies, most states have regulations in place that require agents and brokers to provide policy owners with enough information to make an informed decision concerning the replacement of any existing policy. These ethical principles apply equally to life, health, auto and homeowners or even commercial property casualty policies. No agent should ever sell their policy to a client to replace the client’s current coverage without fully disclosing how their policy provisions differ from the client's current coverage.

All too often coverage is replaced to save premium but the client isn’t fully aware of the decreases in coverage required to attain the lower premiums. A lower cost policy, whether health, life, property or casualty, isn’t a good deal if the policy does not suit a client’s needs; especially when it is sold to replace a policy that was adequate for the insured.

**Churning**

If an agent convinces a prospect to replace a policy with a new policy from the same company and if the replacement policy is not in the client’s best interest, the agent is guilty of churning. The typical churning "victim" would be someone who has a significant amount of cash value and/or accumulated dividends in an existing policy.
Churning usually has no benefit whatsoever for the client and is forbidden. Financial sales professionals who practice it are acting unethically. The sales professionals must be guided by the client's interest with respect to his or her objectives and financial situation.

**Policy Replacement**

There are situations in which a policy should legitimately be replaced. The unscrupulous act of twisting should not be confused with policy replacement. State laws recognize that sometimes a replacement may be in the policyowner's best interest, and they do not prevent an agent from replacing one insurance policy with another, provided the transaction is handled precisely in accordance with required procedures which include:

- Full and fair disclosure of all facts regarding both the new coverage and the existing insurance. Policyowners who consider replacing policies should be fully aware of how the features of their existing policies are different from the replacement policies. They should also be made aware of any monetary penalties for cancellation or replacement of coverage.

- Proper completion of the appropriate forms by the agent. These forms must be signed by the insured, acknowledging that he or she is aware that coverage is being replaced by the new coverage being purchased. Typically this procedure includes returning the existing policy (or a signed Lost Policy Release) to the current insurer along with proof that a new insurance policy (in the form of a binder or a copy of the declarations page) is in force.

Sometimes a prospect will make the decision to change insurers or drop one policy for another even when the agent advises against this action. If the prospect is capable of making decisions, and if the agent is certain that the prospect fully understands both contracts, then the decision rests with the prospect, and the agent's actions are not unethical. Though it is sometimes necessary to replace a policy, replacing one policy for another simply to earn a higher commission for the agent is always unethical.

One of the major reasons that some types of policies (particularly life and health/disability insurance) are replaced by the writing agent is because, the first year commission was high, but the commissions from the second year on are considerably lower. By replacing their business every year or even just every two years, agents are able to keep their commissions high. This is usually a disservice to the client, especially if preexisting conditions played a part in the replacement.

Another reason an agent might replace a policy has to do with the fact that at times agents will change employers. When an agent chooses to move to a different company or agency they attempt to take the clients that they served in the past often with them. Since insurance policy decision are often made on the perceived trust a client has in an agent, an agent might feel that the client doesn't belong to their former employer but to them. Whether this is ethical or legal is a difficult question to answer and the client's interests should guide any decision to replace an existing policy.

Company stability is another reason for policy replacement. If an agent feels that a company is experiencing financial troubles, they may wish to change the client's policy from that company to try and protect their client.
Replacing policies occurs frequently. Whether it is done for ethical or unethical reasons the consumer has some peace of mind knowing that insurance laws exist to protect them and not the agent.

An agent should always be slow to replace an existing contract of any type. Any time an existing coverage is being replaced with a new policy, continuity must be considered. The old plan should never be dropped until the new plan is firmly in place. The new policy should actually be in hand and reviewed for accuracy before the old policy is dropped.

A complete comparison with respect to a life insurance policy replacement requires that the consequences of any replacement be made clear to the policy owner. It must be explained that:

- The suicide and incontestable provisions begin anew
- The previous policy’s cost basis may be lost
- Adverse tax consequences could result

Legislation has been adopted in certain states concerning life insurance replacement requirements and is expected to be endorsed by the National Association of Insurance Commissioners (NAIC) as model legislation for other states. The legislation is a significant departure from existing replacement regulations that have been on the books for many years. This insurance replacement legislation requires that these steps must be taken for every life insurance policy replaced:

- Insurers must have internal procedures in place to handle replacements and a company officer responsible for monitoring and enforcing them.
- Applicants are given a 60-day period following the replacement sale during which they can change their mind and have their initial premium returned. It is during this 60-day cooling-off period that replacing companies must implement additional disclosure requirements.
- Insurance sales professionals are required to obtain a list of all of the applicant’s existing life insurance and annuity contracts, and must provide the applicant with a form that defines the scope of a life insurance replacement. Both the sales person and the applicant must sign the form.
- If replacement occurs or is likely to occur, the replacing insurance professional must complete a statement disclosing specified information about the new policy and submit it with the life insurance application. An insurer whose agent is replacing existing life insurance must reject any application received that isn’t accompanied by the necessary disclosure forms.

**THE LEGAL ASPECTS OF POLICY REPLACEMENT**

To be legal, policy replacement must generally meet certain procedural requirements. With replacement, as with any other violation of regulatory codes, “ignorance of the law is no excuse.” Agents are responsible for knowing what the law is and for abiding by it. Besides,
even if an agent never engages in any sales activity that involves replacement, the policies he or she has sold may be subject to replacement by other agents.

The specific procedural requirements for sales involving replacement vary somewhat from state to state, but they are similar in many respects. Agents must acquaint themselves with the particulars of the laws for the states in which they do business.

**Legal Definition**

Generally, replacement is defined to include not only cases where existing coverage is dropped in favor of a new policy, but just about any situation in which an existing policy will be reduced in value or used to fund another life insurance policy.

There are usually only a few exceptions from the general definition of replacement. In such cases, certain of the procedural requirements are modified as appropriate. However, agents must still comply with the provisions that require certain disclosures to be made to the client.

**Procedural Requirements**

**Duties of agents**

The first procedural requirement of most replacement regulations is that all life insurance applications contain two statements, one signed by the applicant and one signed by the agent, indicating whether replacement of any existing policy is intended in connection with the purchase of the new policy.

If replacement is intended, the agent must give the client a "Notice Regarding Replacement of Life Insurance." In most states, this notice must be signed by the applicant, the agent, or both. In some states, the notice is lengthy and detailed. In others, a shorter version that covers the same essential information in less formal language is used. Some states have made further modifications to the notice—for example, to include a note to the consumer that he or she should read the notice carefully before signing it.

A sample of the simplified version of the "Notice Regarding Replacement of Life Insurance" follows.

<table>
<thead>
<tr>
<th>Notice Regarding Replacement of Life Insurance</th>
</tr>
</thead>
<tbody>
<tr>
<td>Are you thinking about buying a new life insurance policy and discontinuing or changing an existing one? If you are, your decision could be a good one—or a mistake. You will not know for sure unless you make a careful comparison of your existing benefits and the proposed benefits.</td>
</tr>
<tr>
<td>Make sure you understand the facts. You should ask the company or agent that sold you your existing policy to give you information about it.</td>
</tr>
<tr>
<td>Hear both sides before you decide. This way you can be sure you are making a decision that is in your best interest.</td>
</tr>
<tr>
<td>We are required by law to notify your existing company that you may be replacing your policy.</td>
</tr>
<tr>
<td>You are urged not to take action to terminate, assign, or alter your existing policy until your new policy has been issued and you have examined it and found it acceptable.</td>
</tr>
</tbody>
</table>
Agents are also required to obtain a list of the policies to be replaced and to submit this list to their insurance company with the application. The application must also be accompanied by a copy of the signed "Notice Regarding Replacement" and a copy of any sales material used in the presentation to the client. Usually, a copy of the sales material must also be left with the client.

Duties of Companies

In addition to requiring their agents to comply with the procedures just described, companies must send the issuer of the coverage to be replaced certain information about the proposed replacement. This information may include a policy summary of the replacement policy and a copy of the sales proposals used. Some states have additional requirements, such as sending a policy summary of the replacement policy to the client, or verifying the accuracy of the sales proposals used. In most states, companies must also keep all records pertaining to the replacement on file for a certain period of time, such as three years.

Consequences of Illegal Replacement

The consequences of not complying with replacement requirements, or of twisting or churning, can be severe. Agents can be subjected to investigations or hearings conducted by the insurance department, the result of which may be censure, substantial fines (up to $25,000 in at least one state), and temporary suspension or permanent revocation of the agent's license. In addition, if the insurance department finds that the agent's company knew or should have known about the agent's actions, the company may be ordered to pay fines, reimburse policy owners, and dismiss certain employees. The company and the agent may also be subject to civil lawsuits filed by policy owners, for which they may be required to pay actual and punitive damages. Punitive damage awards can be very high.

Ethical Consequences for Senior Clients

Insurance replacement may have special ethical consequences when recommended for senior clients because:

- Insurance premiums are generally age-related, and for senior clients this almost always involves higher premium costs

- An insurance applicant’s health tends to decline as he or she ages, so the older applicant may be unable to purchase needed insurance or to obtain the replacement insurance at an affordable premium

Particularly for individuals of advanced age or those whose health may be less than perfect before any existing coverage is terminated, replacement coverage must be firmly in place. The application for replacement coverage should be thoroughly scrutinized by the applicant to ensure that any and all health history questions are answered completely and correctly since the policyholder will be subject to a new rescission period.
From an ethical standpoint, replacement can be viewed as a potential conflict of interest, and that as such a replacement sale calls for the agent to put his or her own self-interest aside and act solely in the best interests of the client.

Replacement is both a legal and an ethical issue. When replacement is done illegally, it is always unethical. When it is done legally, the professional life insurance agent must still be careful to make sure that the replacement meets ethical standards, which would include adherence to the agent's duty to disclose all material information and always act in the best interests of the client.

**CONFIDENTIALITY & PRIVACY ISSUES**

Sales professionals owe a duty of confidentiality to prospects, clients, their employer and business associates. With all of the issues concerning identity theft these days, this is one of the most important ethical requirements for agents and other employees in the insurance and financial services industries.

In the course of qualifying a risk, completing an application, analyzing needs or determining appropriate coverages, insurance agents must obtain a client's business, personal, financial and medical information. Ethics require 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.

To obtain such information, agents must earn their clients' trust. To violate that trust would be a breach of ethics as well as a violation of several laws.

Most agents wouldn't deliberately violate a client's trust through the improper use of confidential information. The danger is that the agent might carelessly divulge something that didn't seem important, but about which the client was very sensitive. Other than to provide underwriting information to their company, agents should make it a rule never to discuss business or personal matters of a client with anyone but the client. Even divulging that a person or entity is a client of the agent is unethical, and possibly illegal, without prior permission.

Sales professionals are under an ethical and legal duty to keep all their clients information confidential. They may not ethically disclose any personally identifiable information that relates to a prospect or client, unless such disclosure:

- Is reasonably required to transact the business authorized by the prospect or client
- Must be made in order to comply with legal requirements
- Is required in order for the professional to maintain a defense against charges of malpractice or other wrongdoing

In addition to gaining client information, sales professionals may also come into possession of proprietary information gained in the course of their employment. They are under an ethical obligation to keep such information concerning their employer and/or business associates confidential. Confidential information obtained in the course of employment should never be used for an employee's personal gain or benefit. It is a violation of federal law for an employee or agent to trade in company securities on the basis of inside information which is acquired during the course of employment. There are also new federal and state laws requiring agents...
and insurers to protect the insured from identity theft as well as protecting their personal information from disclosures without their authorization.

That means restricting access to client records to those employees with a legitimate business reason, and documenting office procedures for confidentiality and privacy protection. It is critical that financial and other information on clients is not divulged to anyone in the absence of due legal process or the written consent of the client.

**PRIVACY PROTECTION ACTS**

*The NAIC Privacy Act*

The NAIC Model Privacy Act provides for the enforcement of individual rights. The individual has the right to information concerning himself or herself, and the right to correct inaccurate information, the right to know the reasons for being turned down for insurance, or any other adverse underwriting decision. These rights are those found under the Fair Credit Disclosure Reporting Act.

Authorization forms are required by law to be prescribed and approved by the state insurance commissioner. The disclosure form must be written in accordance with the plain language laws of the state, and dated.

The notice must give the applicant or insured the following kinds of information:

- The people with access to personal information
- The kind of information to be collected
- The kind of information the insurer can receive without the applicant's prior approval
- The sources of information
- The persons to whom information may be disclosed without the applicant's prior authorization

The form must also state the reason information is collected, and how it will be used.

A fine of $10,000, up to one year in jail is the penalty for any person who obtains information that he or she has no legitimate reason to receive.

The applicant's signature on the disclosure form authorizes the insurer to collect and disseminate information in the manner described in the notice. The authorization is only good for a certain period of time. For example, if authorization is given to an insurer to collect information with regard to a claim settlement, the authorization is good for 30 months. At the end of this period another authorization must be obtained. The applicant or insured should be provided with a copy of the authorization form.

Personal information may be disclosed to persons under certain conditions. Among those to whom an insurer may disclose information are agents, other insurers, insurance organizations (such as the Medical Information Bureau) and state insurance departments. This type of third-party disclosure may require authorization, but in some instances authorization is not required, as long as the applicant or insured has received proper notification of the insurer's information...
practices. In some cases information is also passed on to those conducting scientific research, audits, or marketing approaches.

**HIPAA**

Insurance agents are exposed to and trusted with personal medical and financial information from the clients they work with. It has always been good business practice to view this type of information as confidential. In 1996, however, the federal government passed the Health Insurance Portability and Accountability Act (HIPAA) that provides specific rules for how agents must protect personal medical information. It is no longer an option.

**Who is required to comply?**

Three types of organizations are required to comply with the rules outlined in HIPAA.

- **Covered Entities** – A Covered Entity includes health plans, healthcare clearinghouses, and most health care providers. The law considers employer group health plans as Covered Entities.
- **Business Associates** – A Business Associate includes in business or individual who works with a Covered Entity and creates, uses, receives, or discloses protected health information.
- **Employer and Other Sponsors of Group Health Plans** – An Employer and Other Sponsors of Group Health Plans includes all employers that receive protected health information as well as other organizations that sponsor group health plans (for example, a union).

**Protected Health Information**

HIPAA defines Protected Health Information as any individually identifiable health information that is created or received by a healthcare provider, health plan, employer, or healthcare clearinghouse. The definition of Protected Health Information includes a person’s name and address.

**Permitted Disclosures**

HIPAA requires that a group health plan does not disclose this information except for the following permitted or required disclosures:

- To the individual;
- To carry out treatment, payment, or healthcare operations;
- With a valid authorization;
- Under limited circumstances, when the individual has the opportunity to agree or object to the use or disclosure;
- For defined “public good function” and for very limited “marketing” purposes; and
- Group health plans may make disclosures of protected health information to business associates if the plan obtains satisfactory assurance that the business associate will adequately safeguard the information.

**Required Disclosures**

- To an individual seeking to access their protected information;
- To an individual seeking an accounting of disclosures of their protected health information; and
- When required by the Secretary of HHS to investigate or determine the group health plan’s compliance with the regulation.

**Business Associates**

Insurance agents fall under the definition of a “Business Associate;” and are required to enter into a “Business Associate Contract” with the health plans with which they work. These contracts are required to have the following provisions:

- Establish the permitted uses and disclosures of protected health information;
- Provide that the business associate will not use nor further disclose the information other than as allowed under the contract or required by law;
- Provide that the business associate will use appropriate safeguards to prevent the unauthorized disclosure of information;
- Require the business associate to report to the health plan any unauthorized uses or disclosures of the information;
- Ensure that any agents or subcontractors to whom the business associate discloses protected health information agrees to these same restrictions;
- Provide that the business associate will make protected health information available for inspection;
- Provide that the business associate will make protected health information available to amend and that the business associate has the capacity to make amendments;
- Provide that business associates can provide for an accounting all of their disclosures of protected health information;
- Require that the business associate agrees to make its internal practices, books, and records available to the Secretary of HHS for inspection, if necessary;
- Provide that the business associate agrees to return or destroy, if feasible, all information and limit future uses and disclosures to those purposes that make its return or destruction infeasible, and
- Authorize the termination of the contract if the business associate has violated a material term of the contract.
The Gramm-Leach-Bliley Act (GLBA)

Insurance agents also need to be familiar with requirements of the Gramm-Leach-Bliley Act (GLBA) of 1999. This law put into place privacy requirements for the protection of consumer’s non-public, personal financial information. GLBA is specifically designed for and directed at the professionals working within the financial services industry, which specifically includes insurance agents and companies. The types of information protected includes: information that comes from an individual seeking to obtain an insurance product; information that is financial in nature; information that relates to a personal, family, or household product or service; information that is non-public, and information that identifies the individual.

If they receive this type of information, agents must determine if they disclose the information in any way. As an agent doing business in the insurance industry, it is nearly impossible to not disclose this protected information as defined by GLBA. They must determine the appropriate discloser and authorization documents to use within the course of their daily business.

Another portion of this law requires that agents safeguard all information to keep it confidential. This means agents should not leave applications, files, checks, forms, claims or any other information unattended on their desks or in unlocked receptacles (i.e. desk drawers) while they are not personally in control of who can and cannot access them.

Companies and agencies must also maintain security over information stored electronically using password protection on all computers and other EDP equipment. All information to be discarded should be shredded and only employees who need the information to perform their jobs should have access to it.

Each individual state’s government has the job of enforcing the GLBA requirements within the insurance industry. While efforts have been made to promote consistency from state to state, the reality is that each state’s compliance measures can and may be different. Life and health agents need to be familiar with the compliance measures for each state in which they do business.

The information presented in this section is not intended to be a complete description of HIPPA or GLBA. In the context of ethics, this information is intended to provide an overview of this important legislation. As insurance professionals, it is responsibility to conduct our business in accordance with state and federal laws. If, after reviewing this section, you want additional information regarding these laws, please see our course “Privacy – It’s the Law”.

Fair Credit Reporting Act

An insurance company may hire a consumer reporting agency to obtain personal information about an applicant for underwriting purposes before a policy is issued. The Fair Credit Reporting Act is a federal law that helps to ensure confidential, fair and accurate reporting of information about consumers-including applicants for insurance. The Act stipulates that consumer reports may be furnished by consumer reporting agencies only for certain purposes, which include the underwriting of insurance. Applicants for insurance must be advised that such reports may be obtained and, within certain guidelines, consumers may demand to know what information an investigative agency has on file about them and to whom such reports have been made. Consumers also have the right to insist that disputed information be reinvestigated and corrections be made and sent to anyone who received a consumer report about them.
The Inspection Report

Insurance companies usually require an inspection or an appraisal of the property to be insured. An appraisal is an estimate or opinion of value. Value in real estate terminology, is the present worth of future benefits arising from the ownership of real property. Most insurers use professional appraisers to determine the value of the property by calculating the replacement cost of the property based on the construction cost at current prices of similar structures. Insurers require insureds to maintain insurance equal to a specified percentage of the replacement cost of the insured property. The agent should explain that the coinsurance clause is required in fairness to other policy owners who would otherwise be paying more than their share of premiums and in order for the insurer to have adequate premiums to pay for losses.

The Credit Report

Most commercial insurers order a credit report to determine the applicant's ability to pay premiums and to determine whether he or she may be prone to submitting fraudulent claims. Again, the purpose of this report should be explained when the agent asks the applicant to sign the application for insurance.

When an application is submitted to an insurance company, a consumer reporting agency may be used to obtain personal information about the applicant to be used in the underwriting evaluation. To protect the consumer's right to privacy in this situation, the federal Fair Credit Reporting Act includes procedures for consumer reporting agencies to follow in their dealings with businesses to ensure that records are confidential, accurate, relevant and properly used.

Consumer Reports

Consumer reports include written, oral and other forms of communication which a consumer reporting agency has regarding a consumer's credit, character, reputation, or habits, which is used or collected to determine whether or not a consumer is eligible for credit, insurance, employment or other purposes authorized under the Act. Consumer reports may only be issued to persons who have a legitimate business need for the information. Governmental agencies may also be provided with a consumer's name, present and former addresses, and present and past places of employment.

Investigative Consumer Reports

An investigative consumer report includes information on a consumer's character, general reputation, personal habits, and mode of living that is obtained through investigation, i.e., interviews with associates and friends and neighbors of the consumer.

Such reports may not be made unless the consumer is clearly and accurately notified in advance about the report in writing within three days of the date on which the report was first requested. The consumer must also be notified that he or she is allowed to request additional information.

Consumer Reporting Agencies

Consumer reporting agencies collect information on individuals, prepare reports, and make the reports available to persons or organizations having a legitimate reason to receive such information. These agencies may operate for profit; for example, a credit union. Or, agencies
may be nonprofit, such as the Medical Information Bureau (MIB) which is a clearinghouse for confidential medical information on applicants for life insurance.

When the noncompliance is due to negligence, the guilty party must pay the consumer the sum of the consumer's actual damages, the costs of any successful action to enforce liability, plus reasonable attorney's fees.

**Penalties**

The commissioner of insurance has the authority to investigate any insurer, or any agency used by the insurer to collect information, to determine if the company is in compliance with insurance laws. If the commissioner believes that a violation of the Act has taken place he or she can conduct a hearing to determine the facts.

If a violation is found, the commissioner can issue a cease and desist order, but if the violator continues in violation, the commissioner can institute a fine of up to $10,000 for each violation. If the violation is one that happens with such frequency that it appears to be a general business practice, the fine for each violation can be up to $50,000.

If a policy is being renewed, the insured must be given notice by the renewal date. If a policy is being reinstated, the applicant-insured must be given notice at the time the request is made. If an insured is requesting a change in benefits, the insured must receive notice at the time the request is made.

Failure to comply with the provisions of the Fair Credit Reporting Act makes the guilty party liable to the consumer for the sum of actual damages sustained as a result of the noncompliance; punitive damages deemed proper by a court; and the costs of an action which enforces liability, plus reasonable attorney's fees.

**Prohibited Information**

Consumer reporting agencies are specifically prevented from putting information in their reports about bankruptcies over 14 years old; suits and judgments over seven years old or in which the statute of limitations has expired, whichever period is longer; paid tax liens or accounts placed for collection or charged to profit which are over seven years old; arrests, indictments, or conviction of crime reports; and any other adverse information which took place seven years prior to the report. (These restrictions don't apply when the consumer credit report is used in connection with a credit transaction of $50,000 or more, a life insurance policy of $50,000 or more, or when it concerns employment of an individual earning $20,000 or more.)

**Privacy Act of 1974**

The insurance industry is one of the largest collectors and users of personal information. Two federal laws governing the disclosure and use of such personal information are the Fair Credit Reporting Act and the Privacy Act of 1974. The NAIC Model Privacy Act has also had an important impact by helping individual states to enact regulations governing privacy. These Acts protect individuals from misuse of personal information that has been collected about them, prohibit the use of deceptive practices in gathering such information, provide for advance notice to the individual when such information is to be collected, and provide guidelines for correcting inaccurate or otherwise disputed personal information.
It became clear in the 1970s that with the vast numbers of organizations collecting and using personal information, controls were necessary to protect the public from inaccurate, or misused information. The Privacy Act of 1974 was designed to:

1. Minimize intrusiveness
2. Require fair and impartial collection, analysis, and presentation of information and reports
3. Assure the public they can expect personal information to be handled in confidence

**Disclosure Authorization**

Applicants for insurance must be given advance notice of the insurer's practices regarding collection and use of personal information. Notice must be given promptly and in writing. Notice should be given in the following cases and in the following manner:

- If a third party is interviewed, the applicant must be given notice when the collection of information has begun
- If only the applicant is interviewed, the applicant must be given notice when the policy is delivered

**Consumers' Rights**

Consumers who feel that information in their report is inaccurate or incomplete may inform the consumer reporting agency, which then must reinvestigate and record its findings in a reasonable period of time. If the information is no longer accurate or verifiable, it must be deleted. If the dispute is not resolved after reinvestigation, the consumer may insert a brief statement (not more than 100 words) concerning the problem, which then must be noted in any future consumer reports the agency provides on that consumer.

If insurance is denied, or charges are increased, based on information contained in a consumer report, the insurer must notify the consumer and report the name and address of the consumer reporting agency which made the report. If insurance is denied, or charges are increased, due to information obtained from a person or organization other than a consumer reporting agency, the insurer must disclose the nature of that information to the consumer upon request. The insurer is responsible for informing consumers of their right to request this information when the adverse action is communicated (at the time the person is either declined for insurance or is "rated up").

The maximum penalty for obtaining consumer information reports under false pretenses is $5,000, or imprisonment for one year, or both. The same penalty is imposed on officers or employees of consumer reporting agencies who have knowingly and willfully provided consumer information to a person not authorized to receive it.
Anti-Money Laundering Programs

Under two final rules announced 10-31-05 by the Financial Crimes Enforcement Network (FinCEN), certain U.S. insurance companies are required to both establish anti-money laundering programs and file Suspicious Activity Reports. Insurance companies subject to these rules must establish an anti-money laundering program and start filing Suspicious Activity Reports 180 days after the date of the publication of the final rules in the Federal Register.

The final rules apply to insurance companies that issue or underwrite certain products that present a high degree of risk for money laundering or the financing of terrorism or other illicit activity. The insurance products subject to these rules include:

- permanent life insurance policies, other than group life insurance policies;
- annuity contracts, other than group annuity contracts;
- any other insurance products with features of cash value or investment features.

At minimum, insurance companies subject to the rule requiring an anti-money laundering program must establish a program that comprises four basic elements:

- A compliance officer who is responsible for ensuring that the program is implemented effectively;
- Written policies, procedures, and internal controls reasonably designed to control the risks of money laundering, terrorist financing, and other financial crime associated with its business;
- Ongoing training of appropriate persons concerning their responsibilities under the program; and
- Independent testing to monitor and maintain an adequate program.

“These rules represent key steps in ensuring that the Bank Secrecy Act is applied appropriately to these businesses and in protecting the insurance industry from potential abuse by those seeking to launder money or finance terrorism or other illicit activity, said William J. Fox, Director of the Financial Crimes Enforcement Network. “The rules enhance the protection of the U.S. financial system generally, given that the characteristics of financial products, including certain insurance products, can make those products vulnerable to those seeking to launder money or finance terrorism or other illicit activity.”

Anti-Money Laundering Program Requirement for Certain U.S. Insurance Companies

Insurance agents and brokers are not required to have separate anti-money laundering programs. However, as an integral part of the insurance industry given their direct contact with customers, insurance agents and brokers must be integrated into an insurance company’s anti-money laundering program and monitored for compliance. An insurance company’s anti-money laundering program also must include procedures for obtaining relevant customer-related information for an effective program, either from its agents and brokers, or otherwise.

Importantly, an insurance company that is subject to the requirement to have an anti-money laundering program under another provision of the Bank Secrecy Act is not required to establish a duplicate program under this rule. For example, an insurance company may also be
a registered broker-dealer in securities. However, the company should evaluate the extent to which its existing anti-money laundering program should be revised to appropriately address the risks of doing business in insurance products covered by this rule.

Under the USA PATRIOT Act, financial institutions that have an obligation to establish anti-money laundering programs are able to participate in the sharing of information between financial institutions concerning terrorist financing and/or money laundering. Once an insurance company subject to the final insurance company anti-money laundering program rule has established its anti-money laundering program, it may file a certification for purposes of Section 314(b) of the USA PATRIOT Act.

**Suspicious Activity Reports Filing Requirement for Certain U.S. Insurance Companies**

The requirement to identify and report suspicious transactions applies only to an insurance company, and not its agents or brokers. Insurance companies are required to obtain customer information from all relevant sources, including its agents and brokers, and to report suspicious activity based on such information.

A new Suspicious Activity Report form for insurance companies (FinCEN Form 108 – Suspicious Activity Report by Insurance Companies) will replace the procedure of checking the suspicious transaction box on Form 8300 (Report of Cash Payments Over $10,000 Received in a Trade or Business). Consequently, it may be appropriate for an insurance company to file a Form 8300 as well as file FinCEN Form 108 when circumstances surrounding the receipt of cash are suspicious.

Until FinCEN Form 108 is published and effective, insurance companies may use FinCEN Form 101 (Suspicious Activity Report by the Securities and Futures Industries) to report any suspicious transactions. The words "Insurance SAR" should be entered on the first line of the narrative section.

The threshold amount obligating an insurance company to report suspicious transactions that are conducted or attempted by, at, or through the institution is at least $5,000 (whether in an individual transaction or in aggregate) in funds or other assets. This threshold amount is not limited to insurance policies whose premiums meet or exceed $5,000; rather, it includes a policy in which the premium or potential payout meets the threshold. Nevertheless, insurance companies are encouraged to voluntarily file Suspicious Activity Reports, if appropriate. An insurance company that files a Suspicious Activity Report voluntarily is protected from civil liability to the same extent as a company filing a Suspicious Activity Report that is required under this final rule.

FinCEN is also issuing a series of Frequently Asked Questions that are designed to assist insurance companies in establishing their anti-money laundering and suspicious activity reporting programs. FinCEN will continue to issue additional guidance for this industry and will provide outreach and training about these and related issues. Financial institutions may also call the FinCEN Regulatory Helpline at 800-949-2732 for assistance.
ADVICE TO AGENTS

In this course we've discussed a lot of different topics regarding ethics but what it all boils down to is ‘Doing the Right Thing;' consistently making the decision to choose to act ethically.

We need to understand why ethics is so important in life, and especially in the insurance business and use that as the motivation to make ethical decisions. We need to surround ourselves with co-workers and associates who are ethical and to refuse to compromise our values to make a sale.

We need to remember the ethical training we received as children from our parents, teachers, Sunday school classes as so on and combine that with our knowledge of laws and ethics regarding insurance specifically.

Lastly we need to make a commitment to continually improve our product knowledge and communication skills to provide the best service to our clients as well as our insurers.
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