Unlawful and Unfair Practices

1. Unlawful and Unfair Practices

1.1 Unlawful and Unfair Practices Introduction

- The NAIC publishes model laws that the states can use so that regulations stay fairly uniform from state to state
- NAIC's Unfair Trade Practices Act is widely used throughout the United States
- In this chapter you will become familiar with unlawful sales practices
- For a PDF of the full law, see "Course Files" tab under Resources section

The National Association of Insurance Commissioners (NAIC) works to coordinate state laws so that regulations can stay pretty much the same from state to state. Part of the way that it does this is by publishing model laws, which the states can choose to adopt and modify as each sees fit. The Unfair Trade Practices Act is one of these model laws.



Every state in the union (and almost every US territory) has laws regulating insurance trade practices, and most use a version of the NAIC's model law. You can find the official Unfair Trade Practices model law in the "Course Files" tab in the Resources section of this course. The PDF contains the 2021 and the 2008 versions of the law, both of which are used throughout the United States.

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In this chapter, we will go over some of the most commonly used sections of the NAIC's Unfair Trade Practices Act, and give some examples of unlawful and unfair trade practices.

Focusing on the types of behavior to avoid should give you an even clearer idea of how an insurance professional ought to act.

1.2 Misrepresentation

Misrepresentation
Misleading the public about the insurer or its policies

An insurer and its representatives must not:

- Make untrue or misleading statements about the insurer or its policies
- Omit relevant facts about a certain product
- Lead the public to false conclusions about another insurer or its products

The first practice in the NAIC's model law—and the most general practice forbidden by all state laws—is misrepresentation. An insurer may not misrepresent itself to any member of the public, nor can it make misleading statements about its insurance policies.

Making untrue or misleading statements about an insurer, omitting or failing to disclose relevant facts about a certain product, or intentionally leading

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the public to false conclusions about another insurer and its products, are all examples of illegal misrepresentation.

For example…
If an applicant asks an XYZ Insurance agent about the company's policies, the agent cannot reply, "unlike our competitors, we pay out on 97% of our claims" if, in fact, the agent has no basis for this claim.

Such a statement causes consumers to believe that they would be more likely to file a claim successfully with XYZ Insurance than they would with its competitors, when, in reality, this is not necessarily the case.

1.3 Lying on Applications

Misrepresentation in Insurance Applications
Involves knowingly doing the following in order to obtain a commission or other benefit:

- Making a false statement on or about an application or negotiation for an insurance policy
- Making a material omission while comparing a replacement policy with the policy it replaces

Both insurance agents and applicants alike must be careful to avoid misrepresentation in insurance applications.

This includes knowingly making a false or fraudulent statement or representation—written or oral—on or about an application or negotiation

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for an insurance policy, for the purpose of obtaining a commission, money, or other benefit from any insurer, agent, broker, or individual.

Simply put, it means being dishonest in any way when dealing with insurance contracts and applications.

This also includes knowingly omitting pertinent facts when comparing a life, health, or Medicare supplement insurance policy with a replacement policy, in order to get a commission, fee, or any other benefit from an insurer, broker, agent, or individual.

For example…
An agent is trying to sell a replacement health insurance policy, but fails to advise the insured of a preexisting condition clause in the replacement policy.

1.4 Twisting

Twisting
Using misrepresentation to trick a policyholder into giving up an existing policy, so that you can sell her another

It is also unethical for insurers to induce policyholders to cancel or let lapse existing policies in order to sell a new policy.

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“Twisting” means intentionally tricking a policyholder into lapsing or forfeiting her policy so that she can purchase a new one. Agents and brokers may be tempted to do this in order to increase their own income.



While the NAIC’s model law does not specifically mention twisting, it describes this practice under the umbrella of misrepresentation, and many states do explicitly forbid it.

It can be easy to deceive a consumer, since one agent’s idea of good coverage might be different from a previous agent’s. Either way, if the sales pitch involves any form of misrepresentation, it is illegal.

1.5 Defamation

Defamation of Other Insurers

Insurers and their agents must not:

- Speak poorly of other insurers
- Air criticisms of other insurers or agents before the public

Defamation of other insurers is also illegal. This means that insurers are not allowed to make false, maliciously critical, or derogatory statements about other insurers or their representatives in order to benefit themselves.

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For example…

XYZ Insurance and its representatives cannot discourage potential clients from purchasing a policy with ABC Insurance by telling them that ABC Insurance “is going broke,” “doesn’t pay its claims,” or “doesn’t care about its policyholders.”



Insurers may not make such claims to individual persons or insurance applicants, nor can they use such statements in any form of advertising, promotion, or public relations.

1.6 False Information

False Information/False Advertisement

Making untrue or misleading statements about an insurance company or its services through any media channel

False Information vs. Misrepresentation:

- False Information is a lie
- Misrepresentation is leaving out the whole truth
- Both are illegal!

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False information and false advertising means making untrue statements about the insurer or its products through any media channel. This is another unethical sales practice.

For example…

XYZ Insurance cannot advertise a $30,000 auto insurance policy for $2.99 a month, when it does not in fact offer such a policy. This would be false information.

If the company did offer such a policy, but failed to mention that the policy has a $10,000 deductible, then this would be an example of misrepresentation.



1.7 Kickbacks

Kickback

Any compensation given to someone (e.g. a contractor or insurance broker) in order to gain favorable treatment in an insurance transaction or interaction

Insurers may NOT provide kickbacks:

- To insurance brokers for pushing consumers into policies they may not need or desire
- To corporate reps, contractors, or vendors for low-balling damage estimates

Rebating

Giving or promising to give something of value in order to convince someone to purchase an insurance policy

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A kickback is any kind of compensation given as a reward or motivation for favorable treatment in an insurance transaction or interaction.

> ***For example…***
> An insurance specialist for Materials Inc. may take a $5,000 kickback from ABC Insurance to ensure that Materials Inc. will only buy policies from ABC Insurance.

Insurers are not allowed to provide kickbacks to insurance brokers for pushing consumers into certain policies they may not need or desire.

It is also illegal for insurers to provide kickbacks to contractors or vendors for “lowballing” damage estimates or repair costs.

Similarly, it is unlawful to give or promise to give a person or a business something in return in order to induce them to buy an insurance policy, perhaps promising to give back a portion of the premium. This practice, called rebating, is not allowed.

1.8 Boycott, Coercion, and Intimidation

> **Boycott, Coercion, and Intimidation**
> An insurance company may NOT participate in activities that coerce consumers into buying its products

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When it comes to selling insurance, insurers may not participate in boycotts or use coercive or intimidating trade practices.

For example…

An XYZ Insurance agent cannot make a deal with a car dealer to approve a consumer's auto loan only on the condition that the consumer purchases her car insurance from XYZ Insurance.

Similarly, ABC Insurance may not strike a deal with a real estate company forcing home buyers to purchase their policies from ABC Insurance as a condition of buying the home that they want.



1.9 Discrimination

Unfair Discrimination

Discrimination is illegal in regards to:

- Underwriting
- Premiums
- Settlements, etc.,

unless it is based on actual statistical differences in risk.

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When charging premiums, making settlements, or accepting applications, insurers may not discriminate on the basis of age, race, gender, religion, language, or disability, unless these factors have some direct bearing on the risks covered by the insurance policy.



For example…

An insurer may only charge different premiums based upon age if there is evidence of a statistical difference in the number of claims. Since younger drivers have statistically been shown to drive more recklessly and cause more accidents than middle-aged drivers, it is not considered discrimination to charge them a higher premium.

1.10 Penalties

Penalties suggested by NAIC Unfair Trade Practices model law:

- Fines
    - up to $1,000 per violation, $100,000 total
    - if violations were brazen, $25,000 per violation, $250,000 total
- License suspension or revocation

Every state, of course, has laws that govern how unfair trade practices should be punished. The NAIC's Unfair Trade Practices model law lays out some guidelines for disciplining those who commit unfair trade practices:

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First, the commissioner should set up a hearing to decide if the person really did commit the unfair practices. If the commissioner decides that she did, he can impose a penalty on her. The penalties listed in the model law are:

- Fines of up to $1,000 per violation, up to $100,000 total
- Fines of up to $25,000 per violation, up to a total of $250,000, if the person committed the acts on purpose and in open defiance of the law
- And, finally, suspension or revocation of the person's license

1.11 Review: Unlawful Sales Practices

Insurance professionals must carefully avoid unethical sales tactics.

Unethical Sales Practices include:

- Misrepresenting insurance products
- Lying on an applications for insurance
- Twisting
- False advertising
- Providing kickbacks
- Defaming other insurers
- Coercing consumers to buy insurance
- Unfair discrimination

To review, insurance professionals must avoid all unethical behavior when they sell insurance.

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Unethical sales practices include misrepresenting insurance products so that they seem better or cheaper than they are, lying on insurance applications, using false advertising, intimidation, or coercion to sell insurance policies, providing kickbacks to increase sales, and misrepresenting a competitor's products to discourage consumers from buying them.

We have focused here on the unfair trade practices that are most commonly adopted by state laws across the nation. However, the NAIC’s model law does include more items, and we encourage you to go to our course resources section to review the full document.

Back to top

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