



CODE & ETHICS 2009 Supplement

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The California Department of Insurance introduced substantial changes to its prelicense course objectives on November 3, 2008. This supplement highlights these changes.

IMPORTANT: EXPECT NEW QUESTIONS ON THE STATE LICENSE EXAM STARTING JANUARY 2009. THIS SUPPLEMENT WILL HELP PREPARE YOU. STUDY THIS SUPPLEMENT WITH CARE.

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INSURANCE CONTRACTS

An Insurance Contract Does NOT Need . . . see 7-8

Information that DOES NOT need to be communicated in an insurance policy is:

- Known information
- Information that should have been known
- Information which the other party waives
- Information not material to the risk

Insurer Ratings see 7-3

The financial rating of an insurer (A+, B, C, etc) is not required to be specified in an insurance policy.

Legal World: see 7-6

A representation in an insurance contract qualifies as an ***implied warranty***.

What is misrepresentation? see 7-10

Materiality of concealment is the rule used to determine the importance of misrepresentation, i.e., someone is considered to have misrepresented an answer on an application if the concealment is considered material. A fact is said to be material if it has influenced someone, put them at a disadvantage or affected the risk being insured or insurability.

Withdrawing a representation see 7-4

A representation made by an applicant for insurance may be altered or withdrawn before the insurance goes into effect, but not afterwards. A representation is considered false when the facts fail to correspond with its assertions or stipulations.

Rescission means the same as revoke or remove. An insurer could legally rescind an insured's policy if: see 7-7

- There's been intentional or unintentional concealment
- There's been an intentional and fraudulent omission
- A misrepresentation comes to light after a policy has gone into effect
- A material warranty or a material policy provision has been violated

Insurance Distribution see 2-11

There are many ways insurance is distributed or sold:

- A. Direct** Writers (or Direct Response), companies that market by mail, phone, and /or the internet with their own employees.
- B. Exclusive** or Captive Agency, companies whose agents represent only one company.
- C. Independent Agency** -- agents represent and are appointed with several companies.
- D. Managing General Agent (MGA)**, any person, firm, association, corporation, or partnership who manages all/part of an insurer's business. MGAs act as an agent and can underwrite up to 5% of the insurer's annual policyholder surplus and may adjust or pays claims in excess of an amount determined by the Commissioner as well as negotiate reinsurance on the insurer's behalf.
- E. Home Service**, also known as "debit" companies, sell small face amount policies and "industrial" insurance.

Transacting Insurance . . . see 3-5

The CIC defines "Transact" when applied to insurance as any of the following:

- Solicitation
- Negotiations preliminary to execution
- Execution of a contract of insurance
- Any dealings before/after the execution of an insurance contract, or any matters arising from the contract

Unlicensed? see 3-23

Any person who transacts insurance without a valid license is guilty of a misdemeanor punishable by a ***fine not exceeding \$50,000*** or by ***imprisonment*** in county jail for a period not exceeding ***one year***, or both.

Agent vs. Broker vs. Solicitor see 3-3

California law defines and insurance agent as someone authorized by an insurer to transact all forms of insurance except life insurance . . . that would be a task reserved for a life-only agent. "Insurance broker" means a person who, for compensation and on behalf of another ***person***, transacts insurance other than life with, but not on behalf of, an insurer. Know that there is ***NO life broker or NO health broker***.

An **Insurance Solicitor** is a person employed to aid an insurance agent or insurance broker in transacting insurance other than life.

Title 18 Violations . . . see 3-9

Title 18 is federal code that prohibits people engaged in the business of insurance, whose activities affect interstate commerce, from knowingly making false statements, with intent to deceive, regarding the value of insured properties, reports to any insurance regulator, or material fact in interstate insurance transactions. The penalties and fines for violating Title 18 are severe:

- Criminal Penalty– Not more than **5 years** in prison
- Civil Fine – not more than **\$50,000**

In addition, any person convicted of a felony under Title 18 is to be known as a ***prohibited person***.

Prohibited Persons . . . see 3-9

Prohibited persons, such as felons, must request written consent from the Commissioner, pay a fee, provide all documentation, and receive consent prior to engaging in any business. It is a criminal offense, punishable by civil penalty up to **\$50,000** for each violation, and imprisonment for up to **5 years**, to employ or permit prohibited persons to participate in the business of insurance without consent. The Commissioner may require additional information in some cases.

Company Appointments see 3-10

In general, a producer hasn't been appointed or affiliated, they can't legally transact insurance, even if they're licensed. However, a life or health agent can present a proposal and transmit an application to an insurer he is not appointed with. If the insurer issues the policy, the agent is considered to be appointed. If all of an agent's appointments are terminated by his insurers, his license is considered inactive.

License Termination see 3-11

A licensee may surrender a license for cancellation by delivery to the Commissioner, or by written notice of the intent to cancel. A license terminates upon the death of the licensee. If an organization is the licensee and it ceases to exist or is dissolved by its partners, the right of that entity to transact insurance is also terminated, unless a surviving partner, if any, files, within 30 days, an application to continue transacting insurance.

Errors & Omissions Insurance see 1-8

Like many professionals, insurance agents should carry E&O insurance. This is valuable protection for both you and your clients.

There is no standard errors and omissions policy. Most policies are written on a ***claims-made*** basis rather than on an ***occurrence basis***. Claims made means the insurer is ONLY responsible for claims filed while the policy was in force. So, if a claim is made against you after you retire and cancel your E&O policy, it will not be covered.

A typical E&O policy will cover your cost of defense and monetary and perhaps punitive awards you must pay to an offended party. Limitations in coverage can occur due to limits of the policy, gaps, caps and deductibles. In addition, there are many other important coverage ***exclusions*** an agent must consider, such as: insurer insolvency, receivership, bankruptcy, liquidation or financial inability to pay; acts by the agent that are dishonest, fraudulent, criminal, malicious or committed while knowing the conduct was wrong; promises or guarantees as to interest rates or fluctuations of interest rates in policies sold, the market value of any insurance or financial product or future premium payments, etc.

Prohibited Acts see 3-12

Except when performed by a surplus line broker, the following acts are misdemeanors in California:

- Acting as agent for a non-admitted insurer to transact insurance
- Advertising a non-admitted insurer to transact insurance
- Aiding a non-admitted insurer to transact insurance

Free Insurance see 4-5

Agents/producers/insurers are not allowed to offer free insurance, e.g., give someone a free life insurance policy if they buy an annuity or homeowners policy. The exception allows free insurance written in connection with newspaper subscriptions or general circulation but not insurance issued to credit unions or members of credit unions.

License Applications...see 3-1

When someone applies for an insurance license, the insurance commissioner may conduct an investigation and based on it's outcome deny (without hearing) an application for issues such as a poor business reputation, lack of integrity, previous license suspensions, previous false statements, fraudulent practices, wrongful acts, misrepresentation, etc. If an application is approved, it can later be revoked or suspended for these same offenses.

Fiduciary Responsibilities see 3-25

All funds received by an insurance agent, broker, or solicitor, life agent, life analyst, surplus line broker, special lines surplus line broker, motor club agent, bail agent, permittee, administrator, or solicitor, as premium or return premium for any policy of insurance, are held in a fiduciary capacity. Any person who diverts or appropriates those fiduciary funds to his or her own use is guilty of theft and punishable for theft as provided by law.

Fiduciary Defined see 3-25

A fiduciary is someone who has undertaken to act for and on behalf of another in a particular manner which give rise to a relationship of trust and confidence.

Continuing Education see 3-17

Upon renewal, these licensees must comply with the following continuing education requirement:

- Life-Only Agents -- A minimum of **24** hours per license period (every two years) following the date of the original license issuance.
- Accident and Health Agents -- A minimum of **24** hours per license period (every two years) following the date of the original license issuance.
- Fire and Casualty Agents (4 years or more in business) -- A minimum of **24** hours per license period (every two years) following the date of the original license issuance.
- Fire and Casualty Agents (less than 4 years in business) -- A minimum of **25** hours per year following the date of the original license issuance.
- Life-Only and/or Accident & Health PLUS Fire and Casualty Agents (less than 4 years in business) -- A minimum of **25** hours per year following the date of the original license issuance.
- Life-Only and/or Accident & Health PLUS Fire and Casualty Agents 4 or more ears in business) -- A minimum of **24** hours per license period (every two years) following the date of the original license issuance.

- Personal Lines Agent -- A minimum of **20** hours per license period (every two years)
- Limited Lines Automobile Agents -- A minimum of **20** hours per license period (every two years) following the date of the original license issuance.

Special CE Requirements see 3-19

- **Ethics:** Every licensed agent must complete a minimum of four hours in specially-approved courses in ethics every renewal period. Personal Lines and Limited Auto agents need only complete two hours. NOTE: This requirement is PART OF not in addition to the continuing education hours required and discussed above.
- **Annuities:** Every life agent who sells annuities shall complete an **annuity eight hour certification** course BEFORE soliciting or selling clients. Thereafter, **four hour certification refresher annuity training** must be taken **every two years** prior to license renewal. NOTE: This requirement is PART OF not in addition to the continuing education hours required and discussed above.
- **Long Term Care:** Every agent that solicits or sells long term care insurance must complete an long term care **eight-hour certification course** BEFORE soliciting or selling long term care insurance. Thereafter, an **eight-hour certification long term care course** must be taken each renewal period. However, if the agent has been in business **less than 4 years, he must take** an eight-hour long term certification care course every year for the first 4 years in business in order to be certified to solicit and/or sell long term care. This does not increase the total continuing education hours required and discussed above.
- **California Partnership for Long-Term Care (PR):** Fire and casualty broker-agents and life-only and accident and health agents who wish to solicit individual consumers for the California Partnership product must (prior to being authorized); complete one specifically designated LTC training course (2004 LTC) and one specifically designated PR course.

Authority to solicit individual consumers for the Partnership Product requires:

- An **8**-hour specifically designated LTC training course (2004LTC) each year and must be accompanied by either a **4**-hour Partnership course every **12**-month period or an **8**-hour Partnership course every **2**-year license term.
- **Worker's Compensation:** Any life agent who wishes to sell **24-hour coverage** shall complete a course, or seminar of an approved continuing education provider on workers' compensation and general principles of employer liability. Satisfactory completion of this requirement is by proctored examination, administered or approved by the department.

Code of Ethics see 4-18

The California Insurance Code and other California laws may identify unethical or illegal practices, but they are NOT a complete guide to ethical behavior. Following are acceptable codes of behavior found in major industries that can be adapted to insurance agents:

- Place the customer's interest first.
- Know your job and continue to increase your level of competence.
- Identify customer's needs and recommend products and services that will meet those needs.
- Accurately and truthfully represent products and services.
- Use simple language
- 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.

A Special Note About Seniors see 4-19

The insurance commissioner has special ethical concerns when insurance agents do business with senior citizens. Specifically, the use of ***pretext interviews*** (whereby an agent misrepresents the purpose of a meeting as a free seminar when it is really a ploy to collect financial information and "sell" a product) are prohibited. With certain insurance products, seniors must also be given 24 hours notice before simply stopping by their home. And, state that the purpose of in-home meetings is to discuss insurance.

Insurance Company Organization see 2-10

Fraternal organizations provide charitable and benevolent activities. Fraternal offer insurance ONLY to their members and beneficiaries and are not for profit. Examples are the Knights of Columbus, Modern Woodmen of America, etc.

Stock Insurers sell shares of stock to shareholders to raise the money necessary to operate the business. Stockholders receive dividends and share in profits and losses. Policyholders, however, do not, i.e., their policies are ***non-participating***.

Mutual Insurers are funded by policyholders. They become the owners and receive non-taxable dividends. Mutual company insurance policies are ***participating*** policies. ***Demutualization is a process whereby a mutual insurer becomes a stock company.***

REGULATION

Changes in the California Insurance Code see 2-1

The Commissioner of the California Department of Insurance (DOI) is the ***elected*** official responsible for administering and enforcing the laws of the California Insurance Code, and the California Code of Regulations

It is important to note that the Insurance Commissioner may *not* make changes to the Insurance code or California Code of Regulations. ***Only*** the state legislature may make those changes. However, the Commissioner *may* review the Insurance Code and issue recommendations for changes.

The Unfair Practices Act see 4-2

This is federal legislation designed to regulate unfair methods of competition or deceptive acts. We go into greater detail in Chapter 4, but the focus is as follows:

- Prohibits misrepresentation of policy terms or company financial condition.
- Prohibits the circulation of false information about another insurance company.
- Prohibits discrimination between individuals of the same class and equal expectation of life.
- Prohibits agents discussing the State Guaranty Fund to “sell” the security of any insurance company.
- Prohibits delays, unequal handling and negotiation of client claims.
- Prohibits an agent from not answering policy questions.

Penalties for violation these acts are not more than ***\$5,000*** for negligence and not more than ***\$10,000*** for willful violation.

Privacy Legislation see 4-20

The Gramm-Leach-Bliley Act (1999) concerns consumer financial privacy and financial safeguards: ***Financial Privacy*** -- Requires financial institution to provide each consumer with a privacy notice explaining what information is collected about the consumer, where the information is used and how it is protected. Any changes must be disclosed. Prohibits the sharing of nonpublic information with a non-affiliated third party unless consumers are given an opportunity to opt-out. ***Financial Safeguards*** -- Requires financial institutions to develop a written security plan describing

how the company is prepared for and plans to protect consumer nonpublic information, even if the consumer is no longer with the financial institution.

The California Financial Information Privacy Act (2003) adds to the financial privacy provisions of Gramm-Leach Bliley by requiring that consumers **opt-in** PRIOR to any sharing of nonpublic information among financial institution non-affiliates. Consumers can **opt-out** for any sharing of information among affiliates of the financial institution.

Insurance Information and Privacy Protection Act (2003) provides that personally identifiable information supplied to an insurance agent or broker in order to apply for insurance must be protected. Agents must provide consumers with a privacy Notice explaining how and with whom this information will be shared and the consumer right to **opt-out** from having personal information shared.

Health Insurance Portability and Accountability Act (HIPPA) assures that an individual's health information (medical records) by establishing national standards for health providers, billing services and health information companies. Requires covered entities to take reasonable steps to ensure confidentiality of communications, notification of record use and document privacy policies and procedures.

Conservation: If an insurance company refuses to submit its books, refuses to observe an order of the commissioner, transfers assets without consent and/or represents a hazard to its policyholders, the commissioner has the ability, through a process called **conservation**, to take possession of the company, and as conservator, run its business or dispose of its assets. It is a misdemeanor to refuse to deliver any books, records, or assets to the Commissioner. See 2-7

Insolvent Insurer see 2-7

The definition of an insolvent insurer is either:

- Any impairment of minimum "paid-in capital" for the class of insurance being transacted.
- An inability to meet financial obligations when they are due.

An insurer cannot escape insolvency by simply being able to provide for its liabilities. It must also have sufficient "paid-in capital" (value of its assets in excess of losses, expenses taxes and debt) to meet code requirements at the time.

FRAUD & CLAIMS

Common Circumstances of Insurance Fraud see 2-13

- Make or cause to be made a knowingly false or fraudulent material statement or material representation for the purpose of obtaining or denying any compensation
- Present or cause to be presented a knowingly false or fraudulent written or oral material statement in support of, or in opposition to, a claim for compensation for the purpose of obtaining or denying any compensation
- Knowingly assist, abet, conspire with, or solicit a person in an unlawful act under this section.

Combating Fraud see 2-13

The Department of Insurance, Division of Enforcement, has created the Fraud Division to enforce the provisions of the Code and to identify and **combat insurance fraud**.

The following ***False and Fraudulent Claims*** statement is required on all claims forms in California: "Any person who knowingly presents false or fraudulent claims for the payment of a loss is guilty of a crime and may be subject to fines and confinement in state prison." In addition, if an insured signs a fraudulent claim form he may be guilty of ***perjury***.

"Shall and May" and "Persons" and Notice by Mail

Throughout the California Insurance Code the word "shall" means its ***mandatory*** while "may" means its ***permissive***. The word "persons" means any person, association, organization or corporation. Any notice required to be given any person by any provision of the insurance code shall be sufficiently delivered if such ***notice is by mail*** to the person's residence or principal place of business. 2-2

Claims

File and Record Documentation see 4-8

Every licensee's claim files shall be subject to examination by the Commissioner or by his or her duly appointed designees. These files shall contain all documents, notes and work papers (including copies of all correspondence) which reasonably pertain to each claim in such detail that pertinent events and the dates of the events can be reconstructed and the licensee's actions pertaining to the claim can be determined.

Duties upon Receipt of Communications see 4-8

Upon receiving any written or oral inquiry from the Department of Insurance concerning a claim, every licensee shall immediately, but in no event more than twenty-one (21) calendar days of receipt of that inquiry, furnish the Department of Insurance with a complete written response based on the facts as then known by the licensee.

Standards for Prompt, Fair and Equitable Settlements see 4-9

Claimant is any person who asserts a right of recovery under a surety bond, an attorney, any person authorized by operation of law to represent the claimant.

Notice of legal action means notice of an action commenced against the insurer with respect to a claim, or notice of action against the insured received by the insurer, or notice of action against the principal under a bond, and includes any arbitration proceeding.

Proof of claim means any evidence or documentation in the possession of the insurer, whether as a result of its having been submitted by the claimant or obtained by the insurer in the course of its investigation, that provides any evidence of the claim and that reasonably supports the magnitude or the amount of the claimed loss.

Standards for prompt, fair, and equitable settlements by insurance companies include the following:

- No insurer shall discriminate in its claims settlement practices based upon the claimant's age, race, gender, income, religion, sexual orientation, ancestry, physical disability, etc.
- Insurers must accept or deny an insured's claim as quickly as possible, and no later than **40** calendar days notify the claimant if more time is required and/or settle the claim by making a reasonable offer—insurers can't make an offer that's unfair or unreasonably low
- Insurers must pay any approved claims no later than **30** calendar days